Investment Management
Regulatory, tax and accounting HOT TOPICS
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A snapshot of the changes ahead

1 January – FATCA withholding begins on US FDAP payments on pre-existing accounts of non-documented "prima facie" FFI’s

13 February – ESMA’s consultation on amending trade reporting RTS and ITS closes.

2 March Consultation on draft RTS and ITS closes

12 March ICAV available

13 February – ESMA’s consultation on AIFMD asset segregation*

30 January – AIFMD - ESMA’s Consultation paper on asset segregation closes.

By 2 March – ESMA technical advice on delegated acts concerning MAR

By 2 March – ESMA’s Consultation paper on UCITS share classes

Q2 2015 expected feedback on CP86 Fund Manager delegate oversight

By 2 July – ESMA must deliver to Commission final RTS and ITS on MAR

AIFMD ESMA advice on on-EU passport 22 July

ESMA to submit to Commission final RTS

Q2 New UCITS Regulations expected from the CBI*

1 June 2015 Companies Act 2014 entry into force

MMF Reg – triadogue negotiations April 2015

By 14 October – Deadline for responses to ESMA consultation paper on draft RTS on ELTIFs

ESMA, EBA and EIOPA – Expected to consult on draft RTS on the content, presentation and calculation of info in the KID

14 October – Deadline for responses to ESMA consultation paper on draft RTS for ELTIFs

Q3 2015: Feedback on CP94*

Expected Q3 2015: ESMA’s Consultation on amending trade reporting RTS and ITS

Q4 2015 Capital markets union – Commission expected to deliver their ‘Action Plan’

By 22 October Decision on non-EU passport under AIFMD

Q4 2015 expected from the EU Commission to report to the European Parliament and Council on the possibility of allowing social entrepreneurship funds established in a third country to use the "EuSEF" Regulation

By 1 December – New margin requirements for un-cleared derivative trades to be phased in between Dec 15 and Dec 19

Before end 2015: Fund Management Company Guidance- Third publication

1 January – FATCA withholding begins on US FDAP payments on pre-existing accounts of non-documented "prima facie" FFI’s

First clearing obligations likely, but will be subject to phasing in.

First clearing obligations likely, but will be subject to phasing in.

Expected in Q2 2015: FATCA info for 2014 by 30 September

23 October – Closing date: ESMA consultation on proposed guidelines on sound remuneration policies under the UCITS V Directive and revisions to the guidelines on sound remuneration policies under the AIFMD

* Estimated timeframes subject to change
**Regulatory timeline**

*A snapshot of the changes ahead*

**2016**

- **January 2016** - Implementation of Solvency II on 1 January 2016
- **January 2016** - New FCA and PRA clawback and deferral rules will apply to variable remuneration awarded for performance periods beginning on or after this date.
- **25 March 2016** - ESMA to submit to the Commission final ITS on MiFID II.
- **31 March 2016** - EBA final guidelines on sound remuneration policies under Article 74(3) and 75(2) of the CRD IV Directive and disclosures under Article 450 of the CRR will apply. EU competent authorities are expected to implement them, to ensure that all institutions apply them for the 2016 performance year and beyond.
- **30 June** - End transitional period for implementation of new CBI managerial functions.
- **1 July** - FATCA withholding begins on US FDAP payments on pre-existing obligations of non-documented entities and individual non high-value accounts maintained by an FFI.
- **3 July** – MAR applies.
- **31 December 2016** - PRIIPs KID Regulation applies in Member States (transition for UCITS until 31.12.2019).

**2017**

- **1 January 2017** - FATCA withholding begins on gross proceeds from the sale, redemption, repurchase or other disposition of any property of a type that produces US-source interest or dividends.
- **1 January 2017** - FATCA withholding begins on US FDAP payments by non-intermediaries on certain offshore obligations.
- **1 January 2017** - FATCA withholding begins on payments made by secured party with respect to collateral arrangement, provided that only a commercially reasonable amount of collateral is held by the secured party as part of collateral arrangement.
- **1 January 2017** - FATCA withholding on foreign passthru payments begins on the later of January 1st, 2017 or 6 months after the publication of final regulations defining the term foreign passthru payment.
- **22 July** - EU Commission to review and report to the EU Parliament and Council of the EU.
- **22 July** - EU Commission to commence review of the interaction between the EuSEF Regulation and other rules on collective investment undertakings and their managers.

*Estimated timeframes subject to change*
Investment fund developments
Investment fund developments in Ireland

- Fund structuring options in Ireland
- Loan origination funds
- Fund Management Company Boards (CP86)
- ICAV
- IFIA Corporate Governance Code for Fund Service Providers
- IFIA Corporate Governance Code for Collective Investment Schemes
- Companies Act 2014
- 2015 Central Bank of Ireland’s thematic reviews
# Regulated funds in Ireland

## Fund vehicles

<table>
<thead>
<tr>
<th>Available legal vehicles</th>
<th>Investment limited partnership</th>
<th>Unit trust</th>
<th>Common contractual fund</th>
<th>Variable capital company</th>
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<td>Always required</td>
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<td>Requires trustee certification</td>
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### Legal structure considerations

#### Is risk spreading an issue?

#### Tax treatment

#### Local market requirements/preferences

#### Operational considerations

#### Investors – retail or professional?

*As long as the investors’ interests are not prejudiced.

* * non-Irish resident – no tax due; Irish tax resident – 41% (Indiv) or 25% (company)
# Loan origination by investment funds

## Loan Originating QIAIFs

Since October 2014, Qualifying Investor Alternative Investment Funds (QIAIFs) have been authorised to originate loans (“LOQIAIFs”). The first LOQIAIF was launched in March 2015. This forms part of the CBI’s suite of measures to encourage alternative sources of financing for small and medium enterprises.

| **Eligible Assets** | In addition to originating loans, the LOQIAIF will be permitted to participate in loans, participate in lending and to operations directly arising therefrom, including handling assets which are realised security or when engaging in loan origination as part of a syndication or club deal. LOQIAIFs are prohibited from engaging in other types of commercial business, or from investing in other funds. A LOQIAIF may instead be established as a sub-fund within an umbrella fund, where other sub-funds invest in other asset classes. |
| **Marketing** | As a QIAIF, the LOQIAIF will be available to professional investors to the exclusion of retail investors, and may be marketed across Europe under the AIFMD passport. |
| **Structure** | As the LOQIAIF is required to be closed-ended, it will most likely be established as a corporate vehicle, either a variable capital company or an Irish Collective Asset-management Vehicle. It may be structured as an internally managed vehicle, and will be able to avail of the Central Bank’s 24 hour regulatory approval process. The revised AIF rulebook clarifies that it must have an authorised AIFM rather than a registered AIFM. |
| **Credit assessment granting and monitoring** | The LOQIAIF must establish, implement, document and regularly update a variety of policies and processes for activities including: implementing a risk appetite statement; procedures for assessing, pricing and granting credit; credit monitoring; monitoring collateral. They must also abide by the Central Bank’s Code of Conduct for Business Lending to Small and Medium Enterprises. |
| **Due diligence** | In addition to AIFMD’s requirement that investors be treated fairly, access to information for due diligence must be non-discriminatory. |
| **Diversification** | Exposure to one group or issuer is limited to 25% of net assets within a specified time-frame. |
| **Prohibited loans** | Loans may not be issued to natural persons, other funds, the funds’ service providers or parties related to them, to financial institutions or to their related companies (unless there is a bona fide treasury management purpose ancillary to the primary object of the LOQIAIF), nor to persons intending to invest in equities or other traded investments or commodities. |
# Loan origination by investment funds

## Loan Originating QIAIFs

| Acquiring loans from credit institutions | A LOQIAIF shall not acquire a loan from a credit institution where the credit institution or a member of its group:  
• retains an exposure correlated to the performance of the loan; or  
• provides an administration, credit assessment or credit monitoring service regarding the loan  

unless the LOQIAIF is satisfied that its policies and procedures are sufficient and it has received warranties from the vendor that the vendor will retain a material net economic interest of 5% of the nominal value of the loan as measured at origination; the exposure will not be subject to any credit risk mitigation techniques and the LOQIAIF will have access to materially relevant data on the credit quality and performance of the underlying exposures and on cash flows relating to the collateral supporting the exposures to enable it to produce comprehensive and well informed stress tests on the cash flows and collateral values supporting the exposures. |
| Stress testing | The LOQIAIF shall have a comprehensive stress testing programme, including identifying factors such as possible events which could have unfavourable effects on the LOQIAIF’s credit exposures and assess the LOQIAIF’s ability to withstand such changes. The LOQIAIF must report the results testing to the board of the AIFM at least quarterly. |
| Liquidity | The LOQIAIF must be closed-ended with a determined termination date, but may at authorisation specify pre-determined interim redemption dates within the fund’s life-cycle. The LOQIAIF may only make distributions or redemptions if there is unencumbered cash or liquid assets available and if such actions will not endanger the regulatory compliance or liquidity obligations of the LOQIAIF. |
| Valuation | The Feedback Statement to CP85 confirmed that the AIFMD’s valuation rules suffice. |
| Leverage | The LOQIAIF must not have gross assets of more than 200% of net asset value, resulting in a debt to equity ratio of 1:1. |
| Investor disclosures | The LOQIAIF’s marketing material must include:  
• a prominent risk warning highlighting the unique risks inherent in loan origination, how investment in a loan originating fund is not guaranteed and is subject to the possibility of investment losses and illiquidity  
• information on the fund’s risk/reward profile  
• anticipated concentration levels  
• credit monitoring process  
• confirmation on whether the manager will allow access to records and staff for due diligence  
• a risk warning that the Central Bank may tighten lending standards and leverage limits  
• information that a reasonable investor would consider important in considering investing in the fund.  
• the implications of the Central Bank’s Code of Conduct for Business Lending to Small and Medium Enterprises where loans are made to SMEs.  
• periodic statements must disclose details of the fund’s loan book.  
• submit a list of any undrawn committed credit lines to the Central Bank. |
The Central Bank has issued feedback on its “Consultation on Fund Management Company Effectiveness – Delegate Oversight” (CP86) (the “Consultation”). It has also issued consequential guidance on related subjects: Central Bank Guidance on Organisational Effectiveness and Central Bank Guidance on Directors’ Time Commitments, as well as a timeline detailing upcoming changes to the rules and authorisation processes following CP86.

The original version of CP86 included draft guidance on Fund Management Companies – Delegate Oversight (‘Delegate Oversight Guidance’). The CBI is now inviting submissions on this draft guidance.

The CBI is proceeding to streamline the existing managerial functions from 15 into 6. The content of each role will be proposed in a future consultation on management company guidance.

The six managerial functions comprise:
- investment risk management
- investment portfolio management
- compliance
- distribution
- capital and financial management
- operational risk.
Fund management company boards – CP86

Irish resident directors - number and ‘residency’

Current rules require Fund managers to have at least two Irish resident directors. CP86 proposed two changes to this – reducing the number of Irish resident directors to one, and defining ‘residency’ to mean 110 days per year.

The Feedback to CP86 confirms that funds will continue to require two Irish resident directors. They said that the main reason to retain this requirement was for funds in distressed circumstances. The Feedback also confirms that a director must be in Ireland for 110 working days per year to be ‘Irish resident’. This was based on half a working year excluding holidays.

Guidance on Fund Management Companies – Organisational Effectiveness

One independent director of a fund management company (including the Chair if he or she is independent) should undertake an organisational effectiveness role. They must be on alert for organisational issues and escalate these to the board. Their role is a ‘change leader’, who proposes improvements in effectiveness to the board and drives the implementation of any agreed actions, including replacing outdated or inappropriate organisational arrangements such as:

- monitoring the adequacy of a fund management company’s internal resources against its day-to-day managerial roles;
- reviewing the organisational structure of the fund management company and considering whether it remains fit for purpose;

When all sections of the Central Bank’s fund management company guidance have been finalised, the Central Bank will amend the AIF Rulebook and include in its forthcoming Central Bank UCITS Regulations a rule that the organisational effectiveness role must be performed by an independent director.

Draft guidance on Fund Management Companies - Delegate Oversight

The Delegate Oversight Guidance sets out recommendations regarding good practice for boards of investment companies, UCITS management companies, AIFMs and AIF management companies incorporated and authorised in Ireland.

The focus of this document is on the role of boards where significant tasks are delegated externally. Delegation does not dilute the board’s ultimate responsibility and it must at all time retain and exercise control over the relevant delegate’s management.

The CBI is accepting submissions on the draft Delegate Guidance until 24 July 2015.

See overleaf for more details on this area.

Rationale for board composition

CP86 proposed a new rule, as part of the authorisation process, requiring fund managers to document how a Board’s composition provides it with sufficient expertise to achieve an appropriate balance of skills and competencies on their boards.

The Feedback confirmed that this rule will be adopted. In future, a fund management company must include this rationale in its business plan/programme of operations, and update this plan/programme everything the board constitutions changes.

The new role of ‘organisational effectiveness’ will include keeping the board composition under review and reporting to the Board on this matter.
Fund management company boards – CP86

Guidance on Directors’ Time Commitments

In parallel with their review into the Fund management company delegate oversight, the Central Bank (CBI) also conducted a thematic review to assess the number of directorships held by individuals on the boards of corporate investment funds, fund management companies and AIF management companies. The aim of this review was to determine the impact on governance where directors hold multiple directorships. The Irish funds industry has 2,057 active directors, and the CBI review discovered that 13 of those individuals hold 652 directorships within the Irish funds industry, along with what they described as an ‘extensive level of aggregate professional time commitments’.

It has therefore issued this Central Bank Guidance on Directors’ Time Commitments to assist Boards and directors in complying with requirements.

Central Bank supervision of the time allocation

The CBI considers that a governance ‘risk indicator’ is triggered when an individual holds more than 20 directorships and an aggregate professional time commitment exceeding 2,000 hours annually. The consequences of such high time commitments include:

- The director being contacted by the CBI to ensure their legal obligations and responsibilities are being met.
- The CBI will monitor director’s commitments to prevent any risk of weakening of governance standards.
- The CBI will treat this as a ‘risk indicator’, which triggers additional CBI supervision as appropriate under the CBI’s risk based approach.
- Where a fund is considering appointing a director with such time commitments (including non-Irish fund-directorships and non-fund directorships), the CBI will:
  i. request a letter from each board setting out the proposed time commitment (IFIA Code para 4.5) and
  ii. dis-allow the 24 hour guaranteed corporate QIAIF approval time
- After 1 January 2016, any previously authorised funds with such directors will be given priority consideration for CBI thematic review where board effectiveness is already being considered.

| 2000 hours per director | • based on a 9 hour day and 230 working days per annum.
|                         | • This ‘total’ time allocation should include all professional commitments including other directorships and employments held.
|                         | • Directors must satisfy themselves, and their boards, that they have sufficient time to fully discharge their duties.
| Minimum time allocation for board meeting attendance | • Boards and directors must agree this and record it in the director’s appointment letter.
|                                                        | • Must incorporate sufficient time to allow for preparation, document review and travel time.
| Additional time requirements – in addition to the normal time allocated to each director role | • ‘Buffer’ – incorporate this to allow for ad-hoc queries which arise occasionally.
|                                                        | • Chairperson – extra responsibilities and work require additional time be set aside. This extra time allocation should be agreed with the board.
|                                                        | • Sub-funds – these each require extra time; cannot just account for the umbrella fund alone.
|                                                        | • Type of fund and investment complexity – must consider whether these require extra time.
|                                                        | • Different client relationships – consider the number of such relationships when assessing time commitments.
|                                                        | • Board committees – membership should be regarded as a separate role; must be included in assessing time commitment and availability.
|                                                        | • Designated person role – this is a separate role to that of director and must be considered separately. A separate time commitment should be allocated for each such role, and must be commensurate with any additional work the role requires and remuneration received. Allocated time must incorporate an on-going oversight role, daily availability, report review and onsite visits to delegates.
| Letters of appointment | • Directors - require a letter of appointment.
|                        | • Designated person role for managerial functions – this requires a separate letter of appointment.
|                        | • Both letters must:
|                        |  ➢ include a written contract outlining job specifications; time expectations; fee arrangements
|                        |  ➢ be subject to annual review by the board and made available to the CBI upon request.
| Conflicts | • In cases of multiple directorships, directors must consider:
|           |  ➢ any potential conflicts
|           |  ➢ ‘corporate interconnectivity’
|           | • Where individuals have full-time positions in a service provider to the board, any potential conflicts must be considered and appropriate action taken.
| Expertise | • Must consider the type and complexity of individual funds and sub-funds when assessing the time commitment and necessary expertise to oversee that fund.
| Regulatory and legal obligations | • of differing types of boards and legal structures – consider before appointment.
## Delegate oversight

### A Investment management
The Board of the Fund Manager should seek a report or presentation from the investment manager prior to the issue of the prospectus and launch of the investment fund or sub-fund, and should approve the investment approach which the investment manager proposes to take. Following the (sub)fund launch, the board should oversee the investment manager’s compliance with this approach. The Board is also asked to seek comprehensive annual presentations from the investment manager regarding the investment manager’s performance and investment team. The directors are required to have a good understanding of the investment manager’s business, which may necessitate due diligence visits to their premises.

### B Distribution
The Board are required to review and approve the proposed distribution strategy prior to a (sub) funds’ launch, and to receive regular updates on distribution including patterns of distribution, sales flow and any legal, regulatory or tax issues.

### C Risk management
Although a management company may delegate (internally or externally) many day to day risk management tasks, its board retains ultimate responsibility for risk management. It should adopt a risk management framework, including identifying risks and risk mitigants, confirming the risk appetite, and incorporating appropriate policies for measurement and management of risk. It sets out specific requirements for each of investment risk, operational risk and enterprise risk and business continuity.

### D Operation and administration
When appointing a delegate to undertake operational and administrative tasks, a board should establish that the delegate has sufficient capacity and flexibility to manage varying levels of business, operational resilience and suitable procedures for confidentiality and data protection. It should regularly receive reports on operational matters including depositary reports, administrator reports, performance, and operation of anti-money laundering procedures. The Board should adopt an appropriate valuation policy and a budget for payment exceeding the investment management fee.

### E Support and resourcing
Management companies must have sufficient resources to enable them to carry out their functions properly, taking into account the nature, scale and complexity of their business. The Guidance suggests that matters which may require support include proactive monitoring of developments between board meetings, management of board meetings, a regular review of the management company’s suite of policies and procedures. It also suggests that individual directors may be designated with particular roles in the oversight of certain functions. In that case, the board should ensure that that person is sufficiently experienced and qualified for the role, s/he has sufficient resources to enable them to undertake that role and their nomination for that role does not comprise either their or the board’s independence.

### F Boards of externally-managed companies
This section of the Guidance caters for externally managed investment companies (EMIC) which are not regulated as management companies. It emphasises that the board of an EMIC retains ultimate responsibility for its management including the appointment and oversight of the management company which is its principal delegate. The EMIC Board also remains responsible for issuing the prospectus and publishing audited annual financial statements. It should receive regular reports from the management company describing its compliance with the sections 1 (investment management), 3 (risk management) and 4 (administrative tasks) of the Guidance, developments in the distribution of the funds, and the extent of its delegation of any tasks and its control framework for oversight of the delegates’ performance. The Guidance asks the Board to consider whether it considers it appropriate to receive reports from any of the delegates of the management company.

The Guidance acknowledges that some AIF management companies (AMC) may appoint external AIFMs. These AMCs are not regulated as AIFMs, however, they remain responsible for the AIFs under management, the oversight of the AIFM, issuing the prospectus and publishing audited financial statements. The AMB’s Board is also required to apply the same principles to the oversight of the AIFMD as described above for EMICs. To avoid doubt, the Guidance clarifies that this section (6) is limited to EMICs, to AMCs with external AIFMs, and that it does not apply to other forms of investment fund or management company.
Irish Collective Asset-management Vehicle (ICAV)

No ordinary company

The “Irish Collective Asset Management Vehicle” (ICAV) was launched on 12 March 2015. The first ICAV was launched days later.

Future-proof against company law changes

What makes the ICAV different?

US “check the box” election

No investment diversification requirement

Elect to dispense with AGM

Prepare financial statements for individual sub-funds

Easier process to amend constitutional documents

Checking the box

• The ICAV is a regulated, corporate fund structure that can make a “check the box” election under US tax rules to be treated as a transparent or flow-through entity for US federal income tax purposes.

• This renders the ICAV attractive for US investors as they do not suffer the adverse tax consequences that arise when a corporate vehicle is treated as a “passive foreign investment company” (PFIC).

• Previously, the Variable Capital Company (VCC) was the only corporate fund structure available in Ireland and had to be treated as a “per se” corporation for US tax purposes.

Regulated structure with the usual advantages

• The Irish Collective Asset-management Vehicle (ICAV) is a new corporate fund structure, authorised and supervised by the CBI.

• The ICAV may be established as a UCITS or an AIF and will have the standard fund structure features such as the ability to establish an umbrella, sub-funds and share classes, as well as segregated liability between sub-funds.

• Like other corporate entities, an ICAV has a Board of Directors and Company Secretary and can be listed on the stock exchange.

Simplified compliance

• The ICAV will benefit from standalone funds legislation outside the scope of European and Irish companies legislation. It is therefore immune from amendments these regimes intended for trading companies, which could have caused unintended consequences for investment funds.

• The ICAV’s constitutional documents can be amended without shareholder approval where the depositary certifies that the changes do not prejudice the interests of investors.

• The Board can elect to dispense with the need for an AGM by notifying shareholders.

• The ICAV will not be subject to the risk spreading rules currently applicable to VCCs and can consequently be structured as a single asset fund.

• Financial statements may be prepared at sub-fund level.

• The corporation/registration process will be solely in the CBI, rather than both the CBI and CRO.

Conversion/migration to an ICAV – by way of continuance

• Existing VCCs have the option of converting to an ICAV.

• Overseas corporate funds can migrate/convert to an ICAV under a one-step migration/conversion redomiciliation process.

• Conversion/migration is available for corporate AIFs and corporate UCITS.

• The migration/conversion by continuation enables a fund to maintain its track record by changing the seat of incorporation rather than starting anew.

• A cost/benefit analysis (including a review of tax implications) should be done in advance of conversion or migration.

Conversion/migration to an ICAV

• The ICAV may be established as a UCITS or an AIF and will have the standard fund structure features such as the ability to establish an umbrella, sub-funds and share classes, as well as segregated liability between sub-funds.

• The ICAV is a regulated, corporate fund structure that can make a “check the box” election under US tax rules to be treated as a transparent or flow-through entity for US federal income tax purposes.

• This renders the ICAV attractive for US investors as they do not suffer the adverse tax consequences that arise when a corporate vehicle is treated as a “passive foreign investment company” (PFIC).

• Previously, the Variable Capital Company (VCC) was the only corporate fund structure available in Ireland and had to be treated as a “per se” corporation for US tax purposes.

Mergers

• ICAVs established under the Irish UCITS regulations may merge with any other UCITS using the UCITS merger provisions.

• ICAVs established as AIFs under the ICAV Act may merge with any other fund, under conditions imposed by the CBI.
This initiative by the Irish Fund Industry Association (IFIA) to introduce a Corporate Governance Code for Fund Service Providers (the Code) follows on from the IFIA’s Corporate Governance Code for the Collective Investment Schemes and Management Companies (2012).

The Code’s purpose is to provide the board of directors of Administrators, Custodians and Depositaries authorised and regulated by the Central Bank of Ireland (collectively “Service Providers”), with a framework for good practice of corporate governance and oversight. The Code provides a set of principles and guidance but is not intended to be prescriptive, rather a codifying of existing practice combined with what is seen as good international practice.

Although the Code is voluntary, it is recommended by IFIA. Compliance and the level of compliance with the Code should be disclosed in the Director’s report accompanying the Service Provider’s annual report for years commencing on or after 1 January 2015. The Code is broken into sections, as detailed below.

**Composition of the Board**

The Board must be of sufficient size and expertise to adequately oversee the Service Provider’s operations. The Code recommends a minimum of 3 directors, including 2 Irish resident Directors. 2 Directors must also be reasonably available to meet the Central Bank at short notice. The Board shall specify the time commitment it expects from each Director; Directors shall document their other time commitments, including time devoted to the boards of collective investment schemes, both Irish and overseas. The Board shall review potential conflicts of interest, both personal and professional, when considering potential board members. The composition must be reviewed every 3 years. Appointments require approval from the Central Bank, and departures require notification with reasons for the departure and confirmation that the departure is not linked to issues with the service provider. Administrators shall not share directors with depositaries. Directors shall comply with the Central Bank's ‘fitness’ requirements, disclose all directorships to the board and be aware of all relevant duties, regulations and obligations.

**Chairman**

A board must have a Chairman, who can be either a non-executive director or an independent non-executive director. The roles of Chairman and CEO shall remain separate: a former CEO of an organisation may be appointed Chairman after a three year interval. The choice of incumbent shall be reviewed every 3 years.

**Role of the Board**

The Code requires that the role and responsibilities of the Board must be clearly documented. The Board may delegate activities to committees or management to act on its behalf, but must implement mechanisms for documenting and monitoring the delegation. The Board remains responsible for delegated activities, as well as for any activity outsourced by the Service Provider.

**Appointments**

The Board is responsible for appointing appropriately qualified senior management, including a CEO. The Board shall be constituted so that no on person has unfettered control.

**Meetings**

The Board shall meet as often as appropriate, with at least 2 meetings per half year. One meeting per year must be in person. An agenda, minutes and supporting documentation (including risk, compliance and finance materials) must be circulated in advance. Minutes must detail decisions, actions and discussions. The Board must document a ‘conflicts of interest policy’, and must consider changing the membership of the Board if conflicts continue.

**Reserved powers**

The Board shall document and maintain a schedule of matters reserved specifically to it for decision.

**Committees**

The Board may establish committees, who shall minute their meetings and report to the Board.
### IFIA Corporate Governance code

**Collective investment schemes and Management Companies**

This initiative by the Irish Fund Industry Association (IFIA) introduces a Corporate Governance Code for Collective Investment Schemes and Management Companies (the Code). It aims to provide the board of directors of funds and fund management companies (collectively “FundCos”), with a framework for good practice of corporate governance and oversight. It provides a set of principles and guidance but is not intended to be prescriptive, rather a codifying of existing practice combined with what is seen as good international practice.

Although the Code is voluntary, compliance is recommended by IFIA.

Compliance and the level of compliance with the Code should be disclosed in the Director’s report or in a public medium.

The Code is broken into sections, as summarised here.

<table>
<thead>
<tr>
<th>Chairman and INEDs</th>
<th>The Board must have a non-executive Chairman. The choice of incumbent shall be reviewed every 3 years. Independent Directors (INEDs) shall be clearly identified in the annual report; they must be sufficiently experienced and qualified in collective investment schemes to enable them to contribute effectively.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Composition of the Board</td>
<td>The Board must be of sufficient size and expertise to adequately oversee the FundCo’s operations. It must have a minimum of 3 directors, including 2 Irish resident Directors. 2 Directors must also be reasonably available to meet the Central Bank at short notice. It must specify the time commitment it expects from each Director. Directors must document their other time commitments, both Irish and overseas. There is a rebuttable presumption that directors can sit on a maximum of 8 non-fund boards. The Board shall review potential conflicts of interest, both personal and professional, when considering potential board appointees. The composition must be reviewed every 3 years. Appointments require approval from the Central Bank, and departures require notification with reasons for the departure and confirmation that the departure is not linked to issues with the FundCo. Boards must not have directors in common with the boards of the CIS’s trustee/custodian. Directors shall comply with the Central Bank’s ‘fitness’ requirements, disclose all directorships to the board and be aware of all relevant duties, regulations and obligations.</td>
</tr>
<tr>
<td>Role of the Board and Reserved Powers</td>
<td>The Board is responsible for the effective and prudent oversight of the relevant company, and for ensuring that risk and compliance is properly managed. It shall consider key decisions, including creating/terminating new sub-funds/share-classes; changes in investment policies/objectives, temporary suspension of NAV calculations; AML requirements; financial reporting; corporate governance; Board’s role in the context of FundCos; new entrants to the market; potential takeovers; management appointments; the Code recommends that INEDs take part in at least one board meeting per year. The Board remains responsible for delegated activities, as well as for any activity outsourced by the FundCo. They must be able to explain their decisions to the Central Bank; They must comply with all relevant legislation, including regulation; statutory, fiduciary and common law duties. They are also charged with appointing a depositary and are responsible for valuing the assets and ensuring a valuation policy is in place. The Board must document and maintain a schedule of matters reserved specifically to it for decision, which must be updated and documented in a timely manner.</td>
</tr>
<tr>
<td>Appointments</td>
<td>The Board is responsible for appointing all board members and ensuring they are aware of the relevant policies and procedures, and have received adequate and sufficient training to enable them to discharge their duties. An annual review shall be carried out of the board’s performance and its individual members; with a formal documented review every three years.</td>
</tr>
<tr>
<td>Risk management, audit, control and compliance</td>
<td>The Board shall ensure that internal control procedures of service providers are being monitored for effectiveness. External audit – The Board must keep proper books of account which disclose with reasonable accuracy the company’s financial position, to enable it to ensure the financial statements comply with the Companies Acts. This may be delegated to the Administrator, subject to performance reviews. It must also appoint an auditor, prepare the annual audited financial statements, prepare a director’s report, ensure that the annual and half-yearly reports contain the appropriate information, are sent to the Central Bank and available to investors/public. It must notify the CBI in advance of a change of auditor, and explain why. The Board is also responsible for compliance with legislation and applicable regulatory requirements, for compliance with provisions of the prospectus and constitutional documents. It must ensure that internal control measures complying with CBI supervisory and reporting requirements are implemented. It shall receive compliance reports at least at every quarterly board meeting, and direct reporting of material compliance issues. The Board is also responsible for ensuring that all applicable risks regarding investments are identified and continually monitored, including implementing adequate controls and. It must receive regular reports and be promptly notified of any breaches of risk limits. The Board must ensure apt controls are in place to identify/monitor/manage any risks; it must ensure implementation of sound administrative and accounting procedures as well as control and safe-guard arrangements for data processing.</td>
</tr>
<tr>
<td>Meetings</td>
<td>The Board shall meet as often as appropriate; UCITS at least quarterly; non-UCITS less often if this is justifiable, and must explain this decision. An agenda, minutes and supporting documentation (including risk, compliance and finance materials) must be circulated in advance. Minutes detailing decisions, actions and discussions must be tabled at the next board meeting. All directors must attend and participate (an attendance record will be kept). They must keep a ‘conflicts of interest policy’, and consider changing the Board if conflicts continue.</td>
</tr>
<tr>
<td>Committees and delegates</td>
<td>The Board may establish committees, who shall minite their meetings and report to the Board. may delegate all or part of the management of the FundCo, as long as it has mechanisms to monitor the performance of the delegate; it does not abrogate its overall responsibility; it receives reports on a regular basis (at a minimum at the quarterly board meetings) to assess the performance of the delegate and relevant FundCos.</td>
</tr>
</tbody>
</table>
The Companies Act 2014 became effective on 1 June 2015, with certain chapters subject to an 18 month transition period. It consolidates and radically overhauls Ireland’s company law regime.

**Investment companies**: Ireland’s investment fund companies were PLCs with variable capital, governed by Part XIII of the Companies Act 1990. This regime was replaced and repealed by Part 24 of the Companies Act, which is largely a restatement of the existing law. In addition to Part 24, the following sections of the Companies Act apply to investment companies:

- Parts 1-14 which apply to limited companies, unless dis-applied by either Part 24 dealing with investment companies or Part 17 which governs PLCs.
- Part 17 governs PLCs and therefore encapsulates investment companies also, save for certain exceptions such as the definition of ‘authorised minimum’ and ‘authorised share capital’.
- Certain provision of the UCITS Regulations.
- Schedule 16 provides a very brief template memorandum and articles of association which must be supplemented with operational provisions.

Note - although investment fund companies are not required to re-register, they may nevertheless choose to convert to being an ICAV and to opt-out of future company law changes.

**Fund managers**: Any corporate fund managers currently registered as Private Limited Companies must elect to become either a Company Limited by shares (“LTD”) or a Designated Activity Company (“DAC”) during the 18 month transition period. If no action is taken, the fund manager will at the end of the transition period automatically convert by default to a being a LTD.

Note – the CBI has confirmed that fund service providers and investment companies are not required to re-register as a DAC (unlike some other regulated entities).
Central Bank of Ireland publishes programme of themed inspections

On 26 February 2015, the Central Bank of Ireland (CBI) published its programme of themed-inspections which reflect a number of supervisory priorities for this year. This programme builds on the supervisory work of previous years and also anticipates areas of emerging risk.

The themed-inspections, which supplement day-to-day supervisory activities under the Central Bank’s risk-based supervisory framework (PRISM), are:

- Cyber Security / Operational Risk - Inspection of controls and procedures around system security and access.
- Integrity of Regulatory Returns - Review of firms’ regulatory reporting.
- Treatment of pricing errors for the Calculation of Fund NAVs - Examination of the processes for the treatment of pricing errors and the payment of compensation.
- Depository Oversight - Review of depositary oversight of investment funds including the depositary’s annual report to investors.
- Proprietary trading - Reviewing the governance and control environment for MiFID firms trading on their own account.
- Conduct of Business - Review of selected MiFID conduct of business requirements.
- Suspicious Transaction Reports (STRs) - Follow-up on previous themed-inspection from 2013 related to market discipline in filing STRs.
- Person Discharging Managerial Responsibilities (PDMRs) - Review of policies and practices in relation to notification of relevant trading activity by persons discharging managerial responsibility in listed firms.
- Risk management in UCITS - Examination of the on-going application of risk management processes employed by UCITS.

Director of Markets Supervision, Gareth Murphy said:

‘Investor protection, market integrity and financial stability are at the core of the Central Bank’s mandate. By announcing these themed-inspections, we are highlighting areas where investment firms, funds and market participants may need to raise standards. Following these inspections, we will communicate our assessment of regulatory standards in these areas and, where necessary, we will ensure that specific remedial actions are taken.’
AIFMD

- Recent EU developments and consultation papers
- Implementation overview
- Marketing and private placement
- Transparency – annual report, disclosure & regulatory reporting
- Authorisation and structuring options
- Full compliance – key features overview
- AIFMD in Ireland
## Alternative Investment Fund Managers Directive

### Overview of recent developments

<table>
<thead>
<tr>
<th>ESMA consultation on asset segregation</th>
</tr>
</thead>
<tbody>
<tr>
<td>ESMA published a consultation paper on guidelines on asset segregation under the AIFMD on 1 December 2014.</td>
</tr>
<tr>
<td>ESMA has produced the guidelines in response to questions on whether the assets that can be held in such an account are only those coming from the same delegating depositary or, alternatively, whether the omnibus account can hold assets for AIF clients coming from different delegating depositaries. In the guidelines, which are set out in Annex III to the consultation, ESMA seeks views on two alternative options:</td>
</tr>
<tr>
<td><strong>First option.</strong> The account on which the AIF's assets are to be kept by the delegated third party may only comprise assets of the AIF and assets of other AIFs of the same delegating depositary. Assets of AIFs of other depositaries would be considered as assets of the third party's &quot;other clients&quot; for the purpose of Article 99(1)(a).</td>
</tr>
<tr>
<td><strong>Second option.</strong> A delegated third party holding assets for multiple depositary clients would not be required to have separate accounts for the AIF assets of each of the delegating depositaries.</td>
</tr>
<tr>
<td>The deadline for responses was 30 January 2015.</td>
</tr>
<tr>
<td>EMSA intends to finalise the guidelines and publish a final report in 2015.</td>
</tr>
</tbody>
</table>
Alternative Investment Fund Managers Directive

Implementation

• The new AIFMD regime commenced on 22 July 2013, with a one year transition period which ended on 21 July 2014. 25 of the EEA countries have implemented the AIFMD; Slovenia, Romania, Portugal and Poland have yet to implement it.
• AIFMD rules apply where it is intended to market and/or manage Alternative Investment Funds (AIFs) in the EU.
• AIFs are broadly defined to include virtually any collective investment scheme other than UCITS. See overleaf for a chart summarising the implementation status.

Key compliance areas

<table>
<thead>
<tr>
<th>Key compliance areas</th>
<th>Authorisation</th>
<th>Delegation</th>
<th>Capital</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>Organisational &amp; business conduct</th>
<th>Remuneration</th>
<th>Risk, liquidity &amp; valuations</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>Reporting &amp; disclosures</th>
<th>Distribution</th>
<th>Depositary</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Draft paper</th>
<th>Commission proposal</th>
<th>Parliament &amp; Council</th>
<th>EU trilogues</th>
<th>Adopted</th>
<th>Technical measures</th>
<th>Implemented</th>
</tr>
</thead>
</table>

Key issues

Non-EU passport

• Non-EU AIFMs and AIFs must currently use National Private Placement to market their funds across the EU.
• ESMA considered whether to extend the passport to 6 countries. It found that the USA, Hong Kong and Singapore were not yet eligible. Guernsey, Jersey and Switzerland were eligible for an AIFMD passport, but ESMA suggested that the passport availability be delayed until more countries were eligible.

Remuneration

• Look through to portfolio and risk management delegates unless they are subject to ‘equivalent’ rules.
• ESMA has clarified that delegates subject to CRD rules may be treated as operating under ‘equivalent’ rules for the purposes of AIFMD remuneration rules. The UK’s FCA guidance also allows AIFMs to treat MiFID and CRD remuneration rules as ‘equivalent’ when delegating portfolio or risk management functions.
• The UK has also issued guidance on proportionality. Certain rules (e.g. bonus deferral, payment in units, clawback) may be disapplied subject to various thresholds.

Depositary models

• The depositary remains liable for assets held in custody that are passed from the AIF to its prime broker.
• To facilitate AIFMD’s implementation, depositaries have managed to contractually discharge liability and/or have been willing to accept indemnification from prime brokers.
• The development of new operational models to increase information flows from prime brokers and mitigate risk remains a priority for depositaries.
• Depositary pricing may increase for certain arrangements/assets.

Delegation

The AIFM has to perform functions relating to either PM or RM and must be "closely involved in the decision making of its delegates”.
• Investment management functions cannot be delegated “to an extent that exceeds by a substantial margin the investment management functions performed by the AIFM itself”.
• The Central Bank of Ireland issued a consultation paper (CP86) on oversight of fund managers as part of a review process to ensure delegates are correctly supervised. It also refined the 16 identified managerial tasks down to 6 – see page 16 for more information.
# Alternative Investment Fund Managers Directive

## Implementation overview

<table>
<thead>
<tr>
<th>Country</th>
<th>Transposition</th>
<th>Implementation Date*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>✓</td>
<td>5 July 2013</td>
</tr>
<tr>
<td>Belgium</td>
<td>✓</td>
<td>17 June 2014</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>✓</td>
<td>20 December 2013</td>
</tr>
<tr>
<td>Croatia</td>
<td>✓</td>
<td>1 July 2013</td>
</tr>
<tr>
<td>Cyprus</td>
<td>✓</td>
<td>5 July 2013</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>✓</td>
<td>19 August 2013</td>
</tr>
<tr>
<td>Denmark</td>
<td>✓</td>
<td>16 May 2013</td>
</tr>
<tr>
<td>Estonia</td>
<td>✓</td>
<td>16 April 2014</td>
</tr>
<tr>
<td>Finland</td>
<td>✓</td>
<td>15 March 2014</td>
</tr>
<tr>
<td>France</td>
<td>✓</td>
<td>24 July 2013</td>
</tr>
<tr>
<td>Germany</td>
<td>✓</td>
<td>22 July 2013</td>
</tr>
<tr>
<td>Greece</td>
<td>✓</td>
<td>November 2013</td>
</tr>
<tr>
<td>Hungary</td>
<td>✓</td>
<td>16 March 2014</td>
</tr>
<tr>
<td>Ireland</td>
<td>✓</td>
<td>16 July 2013</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Country</th>
<th>Transposition</th>
<th>Implementation Date*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Italy</td>
<td>✓</td>
<td>9 April 2014</td>
</tr>
<tr>
<td>Latvia</td>
<td>✓</td>
<td>9 July 2013</td>
</tr>
<tr>
<td>Lithuania</td>
<td>✓</td>
<td>1 January 2015</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>✓</td>
<td>15 July 2013</td>
</tr>
<tr>
<td>Malta</td>
<td>✓</td>
<td>27 June 2013</td>
</tr>
<tr>
<td>Netherlands</td>
<td>✓</td>
<td>25 June 2013</td>
</tr>
<tr>
<td>Norway</td>
<td>✓</td>
<td>01 July 2014</td>
</tr>
<tr>
<td>Poland</td>
<td>×</td>
<td>delayed</td>
</tr>
<tr>
<td>Portugal</td>
<td>×</td>
<td>delayed</td>
</tr>
<tr>
<td>Romania</td>
<td>×</td>
<td>delayed</td>
</tr>
<tr>
<td>Slovakia</td>
<td>✓</td>
<td>22 July 2013</td>
</tr>
<tr>
<td>Slovenia</td>
<td>×</td>
<td>delayed</td>
</tr>
<tr>
<td>Spain</td>
<td>✓</td>
<td>13 February 2015</td>
</tr>
<tr>
<td>Sweden</td>
<td>✓</td>
<td>19 June 2013</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>✓</td>
<td>22 July 2013</td>
</tr>
</tbody>
</table>
The Directive provides 3 marketing routes

<table>
<thead>
<tr>
<th>Compliance level</th>
<th>July 2013</th>
<th>2015</th>
<th>2018</th>
<th>2019 →</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU Passport</td>
<td>Full</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>EU only</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private Placement</td>
<td>Limited</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-EU only</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-EU Passport</td>
<td>Full or near full</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-EU only</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

- **EU Passport**: Available to EU AIFMs / EU AIFs only
- **Private Placement**: Available for non-EU AIFMs / non-EU AIFs from July 2013 to 2018
- **Non-EU Passport**: Available for non-EU AIFMs / non-EU AIFs from 2015/6 *
ESMA chose 6 countries to review based on feedback received to its consultation and on the volume of non-EU funds and managers which currently operate within the EU. ESMA gave its feedback on these countries focusing on 4 areas:

1. Investor Protection
2. Market Disruption
3. Obstacles to Competition
4. Monitoring of Systemic Risk

We summarise ESMA’s findings under each of these topics for each of the 6 countries analysed.
Alternative Investment Fund Managers Directive – Article 42

Marketing: non-EU AIFMs marketing EU and/or non-EU AIFs – selected country overview

<table>
<thead>
<tr>
<th>Country</th>
<th>AIFMD implemented?</th>
<th>Is marketing without an EU passport provided for? *</th>
<th>Gold plating under Article 42</th>
<th>Compliance level</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>✓</td>
<td>✓</td>
<td>Y</td>
<td>Red</td>
<td>Additional requirements including full compliance with AIFMD and appointment of a local representative based in Austria</td>
</tr>
<tr>
<td>Belgium</td>
<td>✓</td>
<td>✓</td>
<td>Y</td>
<td>Green</td>
<td>Minimum AIFMD requirements as per Article 42 and additional confirmations requested as part of the application</td>
</tr>
<tr>
<td>Denmark</td>
<td>✓</td>
<td>✓</td>
<td>Y</td>
<td>Red</td>
<td>Appointment of a depositary required. Additional documentation and confirmations requested as part of the application</td>
</tr>
<tr>
<td>Finland</td>
<td>✓</td>
<td>✓</td>
<td>Y</td>
<td>Yellow</td>
<td>Appointment of a depositary required plus compliance with OECD Model Tax Agreement; Additional documentation and confirmations requested as part of the application</td>
</tr>
<tr>
<td>France</td>
<td>✓</td>
<td>✓</td>
<td>Y</td>
<td>Red</td>
<td>Appointment of a depositary and centralising agent; AIFM must comply with French rules applicable to portfolio management companies</td>
</tr>
<tr>
<td>Germany</td>
<td>✓</td>
<td>✓</td>
<td>Y</td>
<td>Red</td>
<td>Appointment of a depositary required. Additional information, documentation and confirmations requested as part of the application</td>
</tr>
<tr>
<td>Greece</td>
<td>✓</td>
<td>✗</td>
<td>N/A</td>
<td>Uncertainty</td>
<td>Although AIFMD is transposed, Article 42 is not part of the Greek implementation law; no placement possibilities exist</td>
</tr>
<tr>
<td>Ireland</td>
<td>✓</td>
<td>✓</td>
<td>N</td>
<td>N/A</td>
<td>Currently no additional requirements in addition to minimum AIFMD requirements as per Article 42</td>
</tr>
<tr>
<td>Italy</td>
<td>✓</td>
<td>✗</td>
<td>N/A</td>
<td>Uncertainty</td>
<td>Although AIFMD is transposed, Article 42 is not part of the Italian implementation law; no placement possibilities exist</td>
</tr>
</tbody>
</table>

*Marketing without an EU passport refers to the option open to EU Member States under Article 42 AIFMD to permit non-EU AIFMs to market either EU AIFs or non-EU AIFs in their jurisdiction to professional investors only, subject to certain minimum requirements including but not limited to compliance with Articles 22 (annual report), Article 23 (disclosure to investors) and Article 24 (regulatory reporting).

Whilst many member states will permit marketing without an EU passport, each member state needs to be assessed on a case-by-case basis in relation to the domicile of the AIFM & AIF / any permitted “pre-marketing” activities / whether required cooperation arrangements are in place.

The information is provided by Deloitte on a best endeavours basis using publicly available information as per October 2014; given the changing regulatory environment of AIFMD, host state regulators reserve the right to change or impose additional requirements at any time.
Alternative Investment Fund Managers Directive – Article 42
Marketing: non-EU AIFMs marketing EU and/or non-EU AIFs – selected country overview

<table>
<thead>
<tr>
<th>Country</th>
<th>AIFMD implemented?</th>
<th>Is marketing without an EU passport provided for? *</th>
<th>Gold plating under Article 42</th>
<th>Compliance level</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Luxembourg</td>
<td>✓</td>
<td>✓</td>
<td>N</td>
<td>N</td>
<td>Currently no additional requirements in addition to minimum AIFMD requirements as per Article 42</td>
</tr>
<tr>
<td>Netherlands</td>
<td>✓</td>
<td>✓</td>
<td>N</td>
<td>N</td>
<td>Minimum AIFMD requirements as per Article 42 and additional confirmations requested as part of the application</td>
</tr>
<tr>
<td>Norway</td>
<td>✓</td>
<td>Unknown</td>
<td>Unknown</td>
<td>N</td>
<td>Not EU member state but a member of EEA; partial transposition of AIFMD into Norwegian law; full implementation not possible until AIFMD implemented into EEA Agreement</td>
</tr>
<tr>
<td>Portugal</td>
<td>×</td>
<td>Unknown</td>
<td>Unknown</td>
<td>Unknown</td>
<td>AIFMD not implemented; position unclear</td>
</tr>
<tr>
<td>Spain</td>
<td>✓</td>
<td>Unknown</td>
<td>Unknown</td>
<td>Unknown</td>
<td>Position unclear</td>
</tr>
<tr>
<td>Sweden</td>
<td>✓</td>
<td>✓</td>
<td>Y</td>
<td></td>
<td>Minimum AIFMD requirements as per Article 42 and additional documentation and confirmations requested as part of the application</td>
</tr>
<tr>
<td>Switzerland</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>Not EU member state hence not obliged to transpose AIFMD. New distribution rules and investor classifications implemented in 2013 with transitional arrangements until 2015. Distribution to qualified investors permitted depending on definition of qualified investors; for distribution to certain categories of qualified investors requires appointment of a Swiss representative and a Swiss paying agent</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>✓</td>
<td>✓</td>
<td>N</td>
<td></td>
<td>Currently no additional requirements in addition to minimum AIFMD requirements as per Article 42</td>
</tr>
</tbody>
</table>

*Marketing without an EU passport refers to the option open to EU Member States under Article 42 AIFMD to permit non-EU AIFMs to market either EU AIFs or non-EU AIFs in their jurisdiction to professional investors only, subject to certain minimum requirements including but not limited to compliance with Articles 22 (annual report), Article 23 (disclosure to investors) and Article 24 (regulatory reporting).

Whilst many member states will permit marketing without an EU passport, each member state needs to be assessed on a case-by-case basis in relation to the domicile of the AIFM & AIF / any permitted “pre-marketing” activities / whether required cooperation arrangements are in place.

The information is provided by Deloitte on a best endeavours basis using publicly available information as per October 2014; given the changing regulatory environment of AIFMD, host state regulators reserve the right to change or impose additional requirements at any time.
## Alternative Investment Fund Managers Directive - disclosures

### Transparency requirements – who needs to disclose what?

<table>
<thead>
<tr>
<th></th>
<th>Non-EU AIF</th>
<th>Non-EU AIFM</th>
<th>EU marketing</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Non-EU AIF</td>
<td>Non-EU AIFM</td>
<td>No EU marketing</td>
<td>N/A</td>
</tr>
<tr>
<td>2</td>
<td>Non-EU AIF</td>
<td>Non-EU AIFM</td>
<td>EU marketing</td>
<td>Full transparency requirements apply – Annual report (Article 22), Disclosure to investors (Article 23) and Regulatory Reporting (Article 24). National private placement regime.</td>
</tr>
<tr>
<td>3</td>
<td>Non-EU AIF</td>
<td>EU AIFM</td>
<td>No EU marketing</td>
<td>The annual report requirements (Article 22) and the investor disclosure requirements (Article 23) do NOT apply. The regulatory reporting requirements (Article 24) apply.</td>
</tr>
<tr>
<td>4</td>
<td>Non-EU AIF</td>
<td>EU AIFM</td>
<td>EU marketing</td>
<td>Full transparency requirements apply – Annual report (Article 22), Disclosure to investors (Article 23) and Regulatory Reporting (Article 24).</td>
</tr>
<tr>
<td>5</td>
<td>EU AIF</td>
<td>Non-EU AIFM</td>
<td>No EU marketing</td>
<td>National discretion until 2015 at the earliest, when the non-EU marketing/management passport may take effect. Ireland is permitting a transitional period until at least 2015. QIAIFs authorised prior to 22 July 2013 and managed by a non-EU AIFM may adhere to the pre-existing non-UCITS regime during the transitional period, without any of the new transparency provisions applying. A QIAIF authorised on or after 22 July 2013 which is managed by a non-EU AIFM must appoint a fully authorised AIFM within two years of its launch date. Only limited parts of the transparency provisions relating to the annual report and investor disclosures will apply to this category of QIAIFs during the transitional period (similar to the pre-existing QIF regime). The remuneration disclosure requirements will not apply to this category of QIAIFs during the transitional period. The regulatory reporting under Article 24 of AIFMD will also not apply in an Irish context.</td>
</tr>
<tr>
<td>6</td>
<td>EU AIF</td>
<td>Non-EU AIFM</td>
<td>EU marketing</td>
<td>Full transparency requirements apply – Annual report (Article 22), Disclosure to investors (Article 23) and Regulatory Reporting (Article 24).</td>
</tr>
<tr>
<td>7</td>
<td>EU AIF</td>
<td>EU AIFM</td>
<td></td>
<td>Full transparency requirements apply – Annual report (Article 22), Disclosure to investors (Article 23) and Regulatory Reporting (Article 24).</td>
</tr>
<tr>
<td>8</td>
<td>Sub-threshold AIFMs (Irish)</td>
<td></td>
<td></td>
<td>Sub-threshold or “Registered AIFMs” are subject to minimal disclosure and reporting requirements outlined by the Directive. National regulators may impose further requirements on Registered AIFMs established on their territory or marketing via private placement in other EU member states. In an Irish context, certain of the annual report requirements apply to Registered AIFMs managing QIAIFs (general principles, content and format of the balance sheet, activities of the financial year and material changes) but not the remuneration disclosure requirements. Additional requirements may apply if the QIAIF is marketed under private placement in other EU member states.</td>
</tr>
</tbody>
</table>

QIAIFs authorised prior to 22 July 2013 and managed by a non-EU AIFM may adhere to the pre-existing non-UCITS regime during the transitional period, without any of the new transparency provisions applying. A QIAIF authorised on or after 22 July 2013 which is managed by a non-EU AIFM must appoint a fully authorised AIFM within two years of its launch date. Only limited parts of the transparency provisions relating to the annual report and investor disclosures will apply to this category of QIAIFs during the transitional period (similar to the pre-existing QIF regime). The remuneration disclosure requirements will not apply to this category of QIAIFs during the transitional period. The regulatory reporting under Article 24 of AIFMD will also not apply in an Irish context.
# Alternative Investment Fund Managers Directive - disclosures

## Annual report – Article 22

### Overview
- An AIFM must prepare an audited annual report for each EU AIF it manages and for each AIF it markets in the EU.
- The annual report must be provided to investors on request, and to the relevant EU authorities:
  - the home member state of the AIFM;
  - the home member state of the AIF;
  - for non-EU AIFMs marketing under the national private placement regimes in the EU;
  - the local EU regulator of each target market.
- The annual report must be published within six months of the financial year-end.

### Items to include in the annual report

| 1. | A balance-sheet or a statement of assets and liabilities |
| 2. | An income and expenditure account for the financial year |
| 3. | A report on the activities of the financial year |
| 4. | Any material changes to the pre-investment disclosures |
| 5. | The AIFM must disclose in its annual report the total amount of remuneration for the financial year, split into fixed and variable remuneration, paid by the AIFM to its staff, indicating the number of beneficiaries and, where relevant, carried interest paid by the AIF |
| 6. | The aggregate amount of remuneration broken down by senior management and members of staff whose actions have a material impact on the risk profile of the AIF |

* Material changes to any of the items which were required to be disclosed to investors prior to their investment must be disclosed – see overleaf. 'Material' is defined to include anything which would cause an investor to re-think their investment.

### Additional requirements where the AIF has a controlling interest in a non-listed company
- AIFMD imposes requirements on AIFMs managing AIF which acquire control of companies. The AIFM may be required to make disclosures in the annual report of an AIF about each non-listed company over which the AIF has control.
- Alternatively, the disclosures may be included in the annual report of the relevant non-listed company.

See overleaf for more information.

### Preparation and audit of accounting information
- The accounting information in the annual report must be:
  - Prepared in accordance with the AIF rules and in accordance with accounting standards in the AIF’s home member state or, for non-EU AIF, the country where the AIF has its registered office.
  - Audited by an EU auditor or, for non-EU AIF and where permitted by member states, subjected to an audit meeting international audit standards in force in the country where the AIF has its registered office (Article 22(3)). No alternatives are specified for AIF without a registered office.

### Required for QIAIFs

<table>
<thead>
<tr>
<th>QIAIF</th>
<th>Within six months of financial year-end (within four months prior to AIFMD)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Required for QIAIFs structured as unit trusts within two months of the reporting period end (no change)</td>
</tr>
</tbody>
</table>

### Required for RIAIFs

<table>
<thead>
<tr>
<th>RIAIF</th>
<th>Within six months of financial year-end (within four months prior to AIFMD)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Within two months of the reporting period end (no change)</td>
</tr>
</tbody>
</table>
## Alternative Investment Fund Managers Directive - disclosures

### Annual report – Article 22 – Remuneration disclosures

- The AIFM must disclose in its annual report the total amount of remuneration for the financial year, split into fixed and variable remuneration, paid by the AIFM to its staff, indicating the number of beneficiaries and, where relevant, carried interest paid to the AIF. Remuneration for the entire AIFM may be disclosed but there is a requirement to break information down by AIF insofar as this information exists or is readily available. The AIFM should indicate whether the remuneration disclosure relates to any of the following:
  a) Total remuneration of the identified staff of the AIFM indicating the number of beneficiaries
  b) Total remuneration of those staff of the AIFM who are fully/partly involved in the activities of the AIF indicating the number of beneficiaries
  c) The proportion of the total remuneration of the staff of the AIFM attributable to the AIF and the number of beneficiaries (pro rata allocation).

- The aggregate amount of remuneration broken down by senior management and members of staff whose actions have a material impact on the risk profile of the AIF.

### ESMA

ESMA clarified that the AIFMD regime on variable remuneration applies only to the first full performance period following authorisation.

For example, in the case of an AIFM which was authorised in 2013 and has a 31 December year-end, the disclosure on variable remuneration should apply to the 2014 accounting period.

### CBI

The CBI has included some Q&A on disclosures of remuneration.

**Q. When should disclosures on remuneration first appear in the relevant AIF financial statements?**

**A.** The starting date for the first relevant AIF annual report, which would contain remuneration disclosures, would be the first full financial year of the relevant AIF following the AIFM's AIFMD compliant remuneration pay out process policy required to have taken effect. However, as set out by ESMA in the AIFMD Q/A "for an existing AIF whose accounting period ends on 31 December which submits an application for authorisation by 22 July 2014 and obtains an authorisation after that date (including when the authorisation is obtained after 31 December 2014), the AIFMD rules on variable remuneration should apply to the calculation of payments relating to the 2015 accounting period".

Different managers have interpreted the wording from the CBI in different ways, including that the remuneration data does not need to be disclosed until the AIFM has been through a full performance period, on the basis that it does not make sense for completeness to try to disclose only the one aspect of remuneration (ie, fixed). This approach would follow the approach suggested by the FCA. It also follows the approach advocated by ESMA in relation to disclosure of the variable portion of the remuneration disclosures.

However, the CBI did not directly address the matter of non-EU managers. Their first sentence refers to the implementation of the new rules on variable remuneration (pay out process rules), so this could mean that they are in effect taking the same approach as the FCA, ie, as US/Swiss managers are not obliged to implement any new policies, they might not qualify for the year’s grace period and may have to start disclosing remuneration immediately.

### AIFMs authorised by the CBI

The FCA guidance states that no remuneration disclosures (fixed or variable) are required by the EU managers until they have a full year in which their remuneration policies have been in place. This is most likely the first full year after authorisation. For example, if authorised in 2014, the first full year is 2015, so the disclosures will apply to the accounts for 2015 which will presumably be prepared in 2016. The guidance is available at the following link: [http://www.fca.org.uk/your-fca/documents/finalised-guidance/fq14-02-02](http://www.fca.org.uk/your-fca/documents/finalised-guidance/fq14-02-02)

Certain managers have interpreted the guidance to mean that the FCA year’s grace period applies only to managers who must adopt new AIFMD polices/procedures.

As non-EU managers are not obliged to implement any new policies (eg establish a remuneration committee, defer variable remuneration or pay it in shares rather than cash), it has been interpreted they do not qualify and must include their remuneration disclosures immediately.
Alternative Investment Fund Managers Directive - disclosures
Annual report - private equity rules

Disclosures

• Not applicable to SMEs or Real Estate SPVs
• Notification thresholds to regulator of 10%, 20%, 30%, 50% and 75%
• @ 50%, the AIFM shall notify the non-listed company, its shareholders and its home member state
• @50%, AIFM shall also ensure that the board of the acquired company informs its employees
• @ 50%, AIFM must make available its intentions regarding the future of the non-listed company and the likely repercussions on employment, including any material change in the conditions of employment

“Asset Striping” restrictions

Upon obtaining control over a non-listed company, for a period of **2 years** the AIFM must:

• Not vote in favour, facilitate, support or instruct any distribution, capital reduction, share redemption and/or acquisition of own shares by the company which:

1. would reduce the net assets lower than the amount of subscribed capital plus reserves which may not be distributed under local law
2. would exceed the amount of accumulated profit in reserves

PE funds
## Alternative Investment Fund Managers Directive - disclosures

### Disclosure to investors – pre-investment – Article 23

For each EU AIF that they manage and for each AIF that they market in the EU, AIFMs must disclose certain information to investors prior to their investment in accordance with the AIF rules or instruments of incorporation.

### Investment strategy
- The investment strategy and objectives
- The types of assets in which the AIF may invest
- Information on where any master AIF is established and where underlying funds are established if the AIF is a fund of funds
- The techniques the AIF may employ and all associated risks
- Any applicable investment restrictions
- A description of the procedures by which the AIF may change its investment strategy or investment policy, or both
- The circumstances in which the AIF may use leverage
- The types and sources of leverage permitted and the associated risks
- Any restrictions on the use of leverage and any collateral and asset reuse arrangement
- The maximum level of leverage which the AIFM is entitled to employ on behalf of the AIF

### Contractual and service provider arrangements
- A description of the AIF’s liquidity risk management
- Redemption rights in normal and exceptional circumstances
- Redemption arrangements

- Changes to the main legal implications of the contractual relationship entered into for the purpose of investment, including information on jurisdiction, on the applicable law and on the existence or not of any legal instruments providing for the recognition and enforcement of judgments in the territory where the AIF is established
- The identity of the AIFM, the AIF’s depositary, auditor and any other service providers and a description of their duties and the investors’ rights
- How the AIFM is complying with the professional negligence cover requirements

### Delegated management function
- A description of delegated management functions
- Any safe-keeping function delegated by the depositary
- The identification of the delegate and any conflicts of interest that may arise from such delegations

### Valuations
- A description of the AIF’s valuation procedure
- The methodology for valuing assets, including hard-to-value assets

### Investor treatment
- All fees, charges and expenses and maximum amounts thereof, borne by investors either directly or indirectly
- A description of how the AIFM ensures a fair treatment of investors and, whenever an investor obtains preferential treatment or the right to obtain preferential treatment
- A description of that preferential treatment, the type of investors who obtain such preferential treatment and, where relevant, their legal or economic links with the AIF or AIFM
- The procedure and conditions for the issue and sale of units or shares of the AIF

The AIFM shall also describe how and when information on illiquid assets, arrangements for managing the AIF’s liquidity, risk and leverage will be disclosed.
## Alternative Investment Fund Managers Directive - disclosures
### Disclosure to investors – periodic and regular – Article 23

#### Periodic disclosures

For each EU AIF that they manage and for each AIF that they market in the EU, AIFMs shall periodically disclose to investors:

- The percentage of AIF assets that are subject to special arrangements because they are illiquid (for example, side pocket arrangements) must be disclosed – as a minimum – at the same time as the annual report is made available.

- Any new liquidity management arrangements. Immediately notify investors when gates or side-pockets are activated or redemptions are suspended. For AIFs they manage other than unleveraged closed ended AIFs, notify investors when material changes are made.

- The AIF’s current risk profile and the AIFM’s risk management systems) must be disclosed – as a minimum – at the same time as the annual report is made available.

- Material changes to any of the pre-investment disclosures

#### Regular disclosure

AIFMs managing EU AIFs employing leverage or marketing in the Union any AIFs which employ leverage shall disclose on a regular basis, for each such AIF:

- the total amount of leverage employed by the AIF. This must be calculated in accordance with the gross and commitment methods employed by the AIF and disclosed – as a minimum – at the same time as the AIFs annual report is made available.

- Information on any change to the maximum level of leverage permitted must be calculated in accordance with the gross and commitment methods and any right of re-use of collateral or any guarantee under the leveraging arrangements shall be provided without undue delay and shall include:
  - the original and revised maximum level of leverage;
  - the nature of the rights granted for the re-use of collateral;
  - the nature of guarantees granted; and
  - details of changes in any service providers relating to the above items.
Alternative Investment Fund Managers Directive - disclosures

Regulatory reporting

<table>
<thead>
<tr>
<th>AIFM level reporting</th>
<th>AIFM identification information</th>
<th>Top 5 markets</th>
<th>Top 5 instruments</th>
<th>Regulatory AuM</th>
<th>Detailed list of AIFs</th>
</tr>
</thead>
<tbody>
<tr>
<td>AIFM reporting</td>
<td>• AIF identification information</td>
<td>• Top 5 markets</td>
<td>• Top 5 instruments</td>
<td>• Regulatory AuM</td>
<td>• Detailed list of AIFs</td>
</tr>
<tr>
<td>Reporting frequency</td>
<td>Reporting due by*</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&lt; €100 million</td>
<td>Annual</td>
<td>End Jan</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>€100 million to €1 billion</td>
<td>Half-yearly</td>
<td>End Jul, Jan</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&gt; €1 billion</td>
<td>Quarterly</td>
<td>End Apr, Jul, Oct, Jan</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Each AIF &gt; €500 million</td>
<td>Quarterly</td>
<td>End Apr, Jul, Oct, Jan</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

AIF specific rules

| Unleveraged private equity AIF | Quarterly | End Jan |

Reporting is required for the AIFM and for each AIF. An AIFM with numerous AIFs may have different reporting periods between AIFs, which may differ from the AIFM’s reporting period.

Substantially leveraged AIFs

| AIFs employing leverage on a “substantial basis” are AIFs in which the exposure calculated under the ‘commitment approach’ exceed 3 x NAV. | • AIFs employing leverage on a “substantial basis” are AIFs in which the exposure calculated under the ‘commitment approach’ exceed 3 x NAV. | These AIFs must additionally report the top 5 sources of borrowed cash or securities. |

AIF level reporting (Applicable to sub-threshold and regular AIFMs)

| • AIF identification information | • Inception date | • Domicile | • Prime brokers | • Base currency | • Top 3 funding sources (by jurisdiction) | • Predominant AIF type | • Breakdown of AIF strategies (dependent on AIF type) | • Top 5 AIF instruments traded | • Geographical focus | • Top 10 exposures of the AIF | • Top 5 portfolio concentrations | • Typical deal/position size | • Principal markets in which the AIF trades | • Investor concentration |

AIF level reporting (Not applicable to sub-threshold AIFMs unless required by a member state under private placement)

| • Instruments traded and individual exposures | • Value of turnover in each asset class | • Total long and short value of exposures | • Dominant influence | • Expected investment return using various risk metrics | • Counterparty risk profile, trading and clearing mechanisms | • Value of collateral and other credit support posted | • Re-hypothecated collateral | • Top 5 counterparties | • Clearing via a central clearing counterparty (CCP) | • Investor liquidity profile | • Value of unencumbered cash | • Investor redemptions | • Special arrangements and preferential treatment | • Investor breakdown | • Financing liquidity | • Value of borrowings | • Value of borrowed securities for short positions | • Gross exposure | • Leverage (as calculated under ‘gross’ and ‘commitment’ approaches) | • Open positions | • Historical risk profile | • Results of stress tests |

*The report is due within 30 days of period end. An extra 15 days is provided for fund of funds.
## Alternative Investment Fund Managers Directive - disclosures

**Regulatory reporting (Central Bank of Ireland): dates of first reporting**

Details of first reporting periods for Authorised AIFMs, Non-EU AIFMs Under Private Placement Regime and Registered AIFMs under Article 3(3)(d) and 24(1),(2) and (4) of the AIFMD and their AIFs.

<table>
<thead>
<tr>
<th>Reporting obligation of AIFM or AIF</th>
<th>Authorisation/Registration/Notification date</th>
<th>Period for first report</th>
<th>Dates for submission of first report*</th>
<th>Reporting thereafter</th>
</tr>
</thead>
</table>

*Fund of funds have a further 15 days*
UCITS

• Overview of recent EU developments and consultations
• UCITS V
• UCITS VI
• UCITS in Ireland:
  – Central Bank of Ireland proposed UCITS Rulebook (CP77)
  – Central Bank of Ireland Consultation on the adoption of ESMA’s revised guidelines on ETFs and other UCITS issues (CP84)
The financial crisis highlighted divergent depositary regimes across the EU and focussed regulators on remuneration and behaviour in the financial sector. UCITS V aims to harmonise 3 areas:

1. UCITS depositary regime clarifying duties and liability
2. Remuneration rules with other sectors
3. Sanctions regime for UCITS breaches

UCITS V entered into force on 18 September 2014, and must be transposed into national law by 18 March 2016.

Days after the release of the UCITS V proposal, the European Commission published a consultation document on UCITS on 26 July 2012. It covered eight wide-ranging areas and sought more information on market practices. The areas include: addressing UCITS IV eligible assets, EDM techniques, OTC Derivatives, liquidity management, depositary passport, money market funds and long term investments.

Since that consultation paper several areas have been addressed separately outside the UCITS framework.

Respondents to the consultation commented that the depositary passport would be better addressed outside the UCITS framework.

In November 2013, ESMA removed the UCITS VI proposal from their agenda. It is possible therefore that the remaining proposals within the consultation will be addressed separately.

In October 2014, Stephen Maijoor (ESMA's chairman) confirmed that ESMA's current focus is ensuring that the current rules are applied correctly.

On 23 December 2014, the European Securities and Markets Authority (ESMA) published a discussion paper on different share classes of UCITS.

The paper discusses what constitutes a share class and how to distinguish share classes from compartments of UCITS. ESMA aims to unify divergent national practices as to the types of share class that are permitted.

The Discussion Paper sets out ESMA's views on what constitutes a share class, including how to distinguish share classes within sub-funds of UCITS. The paper sets out possible approaches to the extent of differentiation between share classes that should be permitted and poses 14 questions on the topic.

This consultation closed on 27 March 2015.

On 28 November 2014, ESMA published its technical advice to the European Commission on delegated acts required by the UCITS V Directive on the content of two of the delegated acts on depositaries. Issues ESMA advises on are:

Depositary independence - ESMA identifies two types of links between the management company or investment company and the depositary (namely, common management and supervision, and cross-shareholdings between these entities), which may jeopardise their independence. It recommends measures to address the risks that may arise.

The insolvency protection of UCITS assets when delegating safekeeping - ESMA proposes measures, arrangements and tasks for the third party to which custody is delegated as well as measures to be put in place by the depositary.
UCITS V
Focus on investor protection

The financial crisis highlighted divergent depositary regimes across the EU and focussed regulators on remuneration and behaviour in the financial sector.

UCITS V aims to harmonise 3 areas:
1. UCITS depositary regime clarifying duties and liability
2. Remuneration rules with other sectors
3. Sanctions regime for UCITS breaches

UCITS V was approved by the European Parliament on 15 April 2014 and by the EU Council on 23 July 2014.

It must be transposed by member states by 18 March 2016, and existing depositaries have until 18 March 2018 to become eligible under UCITS V.

**Key elements**

**Depositary**
- The depositary framework is aligned with AIFMD, clarifying new safekeeping (including strict liability), oversight and cash monitoring duties.
- Unlike AIFMD, the depositary will not be permitted to contractually discharge liability.

**Remuneration**
- The rules on remuneration also reflect those of AIFMD.
- The rules include the establishment of a remuneration policy to promote sound and effective risk management.
- Rules on payment of 50% of bonus out of units of the fund, bonus deferral over at least 3 years and clawback and malus provisions apply.

**Sanctions**
- UCITS V proposes a minimum catalogue of administrative sanctions and a minimum list of sanctioning criteria.
- Public reprimands are a feature of the proposed regime.

**Key Features**
- ESMA will issue remuneration guidelines to specify applicability to delegates and to employees subject to different sets of remuneration requirements (AIFMD, CRD, MiFID)
- The total variable remuneration shall generally be considerably contracted in subdued or negative financial performance
- Remuneration paid to management companies is also subject to the remuneration principles
- At least 40% of variable remuneration should be deferred (EP had proposed 25%) over a period of at least 3 years
- Custody assets may only be reused (e.g. for securities lending) subject to new requirements, including title transfer of high quality, liquid collateral to the UCITS under the arrangement
- Limit of depositary eligibility entities that meet minimum conditions
**UCITS V**

**Focus on investor protection**

<table>
<thead>
<tr>
<th>Remuneration</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Staff in scope should include “any employee and any other member of staff at fund or sub-fund level who are decision takers, fund managers and persons who take real investment decisions, persons who have the power to exercise influence on such employees or members of staff, including investment advisors and analysts”</td>
</tr>
<tr>
<td>• Remuneration rules should apply to “any third party which takes investment decisions that affect the risk profile of the UCITS because of functions which have been delegated”</td>
</tr>
<tr>
<td>• At least 40% of variable remuneration should be deferred over a period which is appropriate “in view of the holding period recommended to investors” and for a period of at least 3 years</td>
</tr>
<tr>
<td>• Guaranteed variable remuneration should only be exceptional and limited to the first year</td>
</tr>
<tr>
<td>• ESMA to issue guidelines on the application of the remuneration framework, taking into account management company size, internal organisation, and the nature, scale and complexity of activities as well as aligning to the extent possible with AIFMD</td>
</tr>
<tr>
<td>• Cooperating closely with EBA, ESMA is to include in its guidance how different sectoral remuneration principles are to be applied where employees or other categories of personnel are subject to different sectoral remuneration principles (AIFMD, CRD, MiFID)</td>
</tr>
<tr>
<td>• Details of the remuneration policy should be included in the prospectus or the prospectus should provide a website reference to a summary of the remuneration policy. The KIID should also include a statement on remuneration referring to a website for further details</td>
</tr>
<tr>
<td>• The annual report disclosure on aggregate fixed and variable pay and remuneration broken down by various categories of staff should also include a description of how remuneration benefits have been calculated and the outcomes of the remuneration policy reviews</td>
</tr>
<tr>
<td>• Establish remuneration policies and practices that are consistent with, and promote, sound and effective risk management and do not encourage excessive risk-taking</td>
</tr>
<tr>
<td>• At least 50% of variable remuneration should comprise of units of the UCITS (unless the management of UCITS accounts for less than 50% of the total portfolio managed by the management company)</td>
</tr>
<tr>
<td>• An Independent internal review of the policy must be conducted at least annually</td>
</tr>
<tr>
<td>• Pension policy should be in line with business strategy, objectives, values and long-term interests</td>
</tr>
<tr>
<td>• Rules for payments related to termination of employment (should not reward failure)</td>
</tr>
</tbody>
</table>

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<thead>
<tr>
<th>ManCo remuneration</th>
</tr>
</thead>
<tbody>
<tr>
<td>• The principles regarding sound remuneration policies should also apply to payments made by the UCITS itself to management companies</td>
</tr>
<tr>
<td>• The total variable remuneration shall generally be considerably contracted where subdued or negative financial performance of the management company or of the UCITS concerned occurs, taking into account both current compensation and reductions in payouts of amounts previously earned, including through malus or clawback arrangements</td>
</tr>
<tr>
<td>• The Commission is invited to analyse which are the common costs and expenses of retail investment products in the member states and whether further harmonisation of those costs and expenses is needed and submit its findings to the European Parliament and to the Council</td>
</tr>
</tbody>
</table>
UCITS V
Focus on investor protection

Depositary rules
- Custody assets may only be reused provided that the reuse is executed for the account of the UCITS, the depositary is carrying out the instructions of the management company on behalf of the UCITS, the reuse is for the benefit of the UCITS and the interest of the unit-holders and the transaction is covered by high quality and liquid collateral received by the UCITS under a title transfer arrangement. The market value of the collateral at all times has to amount to at least the market value of the reused assets plus a premium
- The depositary should provide the management company, on a regular basis, with a comprehensive inventory of all assets of the UCITS
- Pure CSD services such as settlement will not be considered a delegation of custody but the entrusting of securities of the UCITS to CSD will be considered a sub-custody delegation arrangement
- Extension of the depositary eligibility criteria from the Commission’s draft to include any other category of depositary authorised by member states that is subject to ongoing supervision as well as minimum capital, prudential and organisational requirements. Additional high level requirements regarding infrastructure, policies and procedures, record-keeping, organisation, business continuity and senior management have been added.

- Definition of “safekeeping” distinguishing between custody duties and asset monitoring duties
- A new “strict liability” for assets held in custody – in the event of loss anywhere in the sub-custody network these assets must be returned by the depositary “without undue delay”
- The depositary can discharge its liability only if there is an “external event beyond its reasonable control, the consequences of which would have been unavoidable despite all reasonable efforts to the contrary”
- No ability for the depositary to contractually discharge liability (whereas AIFMD does include a provision on this)
- The depositary would be liable for the assets in the event of a sub-custodian failure or fraud
- Harmonisation of the depositary oversight duties between different legal structures (already the case in Ireland)
- Restriction of delegation to safekeeping duties and ensure that risks are specified where sub-custodian networks are used
- New cash monitoring duties for depositaries

Sanctions regime
Minimum administrative sanctions shall be “effective, proportionate and dissuasive”
- Administrative sanctions include a public statement which identifies the person responsible and the nature of the breach as well as temporary suspension or, permanent bans for repeated and serious breaches
- National regulators may decide on a case-by-case basis not to publish the identity of persons involved where they consider that this would be disproportionate
- All publicly disclosed sanctions should be simultaneously reported to ESMA, which should also publish an annual report on all sanctions imposed
- Member states should be able to decide not to lay down rules for administrative sanctions for breaches which are subject to national criminal law
- Secure communication channels should be established to enable anonymous reporting of breaches
- New requirements have been included relating to the recording of UCITS ManCo telephone conversations
- Maximum administrative pecuniary sanctions of at least EUR 5,000,000 or 10% of annual turnover for legal persons or EUR 5,000,000 for individuals
- Member states must notify the Commission of the measures they have taken to apply the common rules on sanctions and the Commission will conduct a review 3 years after entry into force of UCITS V
UCITS VI
Rolling back complexity?

Days after the release of the UCITS V proposal, the European Commission published a consultation document on UCITS on 26 July 2012. It covered eight wide-ranging areas and sought more information on market practices. The areas include: addressing UCITS IV eligible assets, EDM techniques, OTC Derivatives, liquidity management, depositary passport, money market funds and long term investments.

Since that consultation paper several areas have been addressed separately outside the UCITS framework.

Respondents to the consultation commented that the depositary passport would be better addressed outside the UCITS framework.

In November 2013, ESMA removed the UCITS VI proposal from their agenda. It is possible therefore that the remaining proposals within the consultation will be addressed separately. In October 2014, Stephen Maijoor confirmed that ESMA’s current focus is ensuring that the current rules are applied correctly.

However, it remains to be seen whether the European Commission proceed with their remaining proposed amendments.

Areas covered in the original “UCITS VI” consultation

- Eligible assets
- EPM techniques
- OTC derivatives
- Liquidity management
- Depositary passport
- Money market funds
- Long term investments
- Addressing UCITS IV

Key areas

- Eligible assets
  - The Commission expresses concern over the appropriateness of sophisticated investment strategies for UCITS and is considering a review of eligible assets.
  - A “look through” approach for transferable securities, investments in financial indices or closed-ended funds is proposed.
  - Distinguishing or limiting the scope of eligible derivatives based on the payoff is considered. While the term “exotic derivative” is used no definition is provided.
  - Moving away from VaR as a method of global exposure and relying solely on the commitment approach is proposed.
  - The paper considers permitting in UCITS only derivatives which are traded on multilateral trading platforms and cleared through a Central Clearing Counterparty (CCP).

Key considerations

- Rowback of eligible assets
  - The UCITS III reforms enabled UCITS to gain exposure to a range of otherwise ineligible assets through the use of derivatives structuring.
  - A look through to underlying assets or a limitation on the scope of derivatives that may be used could have a significant impact on the investment profiles of many UCITS.
  - Many UCITS employing leverage under the commitment approach would be unable to comply with the 100% global exposure limit of NAV if they used the commitment approach.
  - The reforms could lead some providers to exit UCITS in favour of setting up more flexible AIFs.
  - It is unclear whether grandfathering would be provided for existing UCITS.
## UCITS VI

### Rolling back complexity?

<table>
<thead>
<tr>
<th>Key areas</th>
<th>Key considerations</th>
</tr>
</thead>
</table>
| **Efficient portfolio management** |  • Efficient portfolio management (EPM) techniques relate to activities such as securities lending and repos and reverse repos.  
• A UCITS is not permitted to borrow or lend but the Commission is concerned that certain EPM activities are the equivalent of borrowing or lending.  
• The Commission is concerned with the transparency, counterparty risk, quality of collateral and re-investment of collateral associated with EPM techniques.  
• The consultation considers making EPM transactions recallable at any time.  
• The consultation considers putting a limit on the amount of portfolio assets that may be the object of EPM.  |
| **OTC derivatives**            |  • Securities lending can be a very significant source of revenue for many UCITS. This practice may be significantly impacted by the proposed changes.  
• Limiting a proportion of the portfolio that could be lent or otherwise engaged in EPM would constrain opportunities for revenue generation and could therefore impact competitiveness.  
• New criteria on the eligibility, liquidity, diversification and re-use of collateral could also have cost impacts. The industry has pointed out that ESMA’s new guidelines in this area should be sufficient.  
• Mandatory haircuts on collateral received could also reduce UCITS market access.  |
| **Liquidity management**       |  • It is unclear what action the Commission may take in relation to contracting with a single counterparty as it has only solicited views at this stage. Any changes may affect UCITS that engage in a single OTC transaction covering their entire portfolio.  
• Changes also need to be considered in terms of developments on EMIR, which seeks to mitigate OTC derivative counterparty risk.  |
|                                |  • The Commission is concerned initially with gathering market views and information on market practice.  
• Industry has pointed out that since UCITS IV, UCITS are subject to a liquidity management framework.  
• It is also important to recognise the need for different redemption practices (particularly time limits) in respect of different fund types and those with different investment strategies.  |
**UCITS VI**

**Rolling back complexity?**

**Key areas**

**Depositary passport**

• AIFMD and UCITS V will harmonise EU depositary rules and therefore possibly create the basis for an EU depositary passport.

• The Commission is seeking views on the advantages and drawbacks for the creation of EU passport for depositaries.

• The paper enquires as to whether the introduction of a depositary passport would require further harmonisation (e.g. NAV calculation, tasks, permitted activities, capital requirements, supervision, etc.).

• The Commission is seeking information on specific issues, burdens and costs which are associated with the supervision if the UCITS and depositary are not located in the same country.

**Addressing UCITS IV**

• The Commission is seeking to be empowered under the UCITS Directive to adopt delegated acts with respect to self-managed investment companies with a view to harmonising requirements with those applicable to UCITS management companies.

• Some 'tidy up' measures are also proposed, including application of the same information standards in all master-feeder scenarios, improvement of notification procedure between member states and increasing legal certainty around the 20 working day time limit for notification for cross-border mergers.

• Some of AIFMD’s provisions are more detailed: organisational rules, delegation, risk and liquidity management, valuation, reporting or calculation of leverage. The Commission is considering whether further alignment between UCITS and AIFMD is necessary to improve consistency.

**Key considerations**

**Depositary passport**

• Industry has given a cautious welcome to the concept of a depositary passport.

• The potential advantages include increased efficiencies and economies of scale, resulting in lower depositary fees. A depositary passport also creates the potential for centres of excellence to emerge that are equipped to serve a global operating model.

• The potential disadvantages include the loss of local expertise and a risk of applying local rules incorrectly or providing less robust oversight, as well as increased concentration in a few market players.

• There may also be local tax residency implications for contractual UCITS if the residence of the depositary were to shift.

• The industry has recommended a step-by-step approach in which ESMA should first ensure that the required level of harmonisation has been reached under UCITS V.

**Harmonisation measures**

• The application of the full UCITS management company requirements to SMICs was an area of contention during and after the implementation of UCITS IV.

• Eventually it was agreed with the Central Bank that the appointment of a permanent compliance function and permanent internal audit function could be disappplied in the case of SMICs.

• Commission harmonising measures could raise these full management company issues for UCITS SMICs, which have been able to disapply some rules based on their “nature, scale and complexity”.

• Harmonisation of UCITS management company delegation and substance requirements in line with the letter box entity rules of AIFMD is also a key industry concern.
## UCITS VI
### Rolling back complexity?

### Key areas

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ESMA’s UCITS guidelines

Collateral diversification

- ESMA’s “Guidelines on ETFs and other UCITS issues” include a new 20% issuer diversification rule with respect to collateral received for the purposes of EPM techniques and OTC derivative transactions.

- The rule was due come into effect on 18 February 2014 for all pre-existing UCITS that were able to avail of the one year transitional period.

- The 20% issuer concentration rule would have created significant challenges for some UCITS, and money market funds in particular, which would typically receive large quantities of collateral in the form of high-quality government securities.

- In response to industry requests and following consultation, ESMA issued a final report on 24 March 2014 which provides an exemption from the 20% collateral diversification rule for government backed securities. The exemption is available to all UCITS rather than just money market UCITS, as previously proposed.

- UCITS availing of the exemption should instead receive securities from at least six different issues, but securities from any single issue should not account for more than 30% of the UCITS NAV.

- New disclosure requirements also apply:
  - Prospectus disclosure where a UCITS intends to be fully collateralised in government backed securities, listing the government issuers to which they may be exposed to beyond the 20% limit
  - The prospectus disclosure should be applied at the first update following official application of the guidelines or at the latest, 12 months after application of the guidelines
  - Annual report disclosure (see separate box)

- These guidelines apply from 2 months after publication of the official translated versions by ESMA.

Annual report disclosure where a UCITS exceeds the collateral diversification limit

- The UCITS’ annual report should contain details of the following in the context of OTC financial derivative transactions and efficient portfolio management techniques:
  - where collateral received from an issuer has exceeded 20% of the NAV of the UCITS, the identity of that issuer; and
  - whether the UCITS has been fully collateralised in securities issued or guaranteed by a member state.

- These new disclosure requirements are not valid for year-end 2013 but will apply to any accounting period that ends after the date of application of the new guidelines.

EPM revenue disclosure

- ESMA’s guidelines require disclosure in the annual report of revenues arising from efficient portfolio management techniques for the entire reporting period together with the direct and indirect operational costs and fees incurred. This had led the industry to consider whether share class hedging qualifies as an EPM technique for the purposes of this disclosure. This could in turn have required managers to split out revenue from derivatives in order to identify gains on share class hedging as EPM revenue.

- However, the CBI has now confirmed that a “reasonable interpretation” would be that the disclosure is “applicable only to revenue from securities lending arrangements and repurchase/reverse repurchase agreements”. This is subject to any clarification which may be provided by ESMA. While share class hedging is usually considered as part of EPM techniques, ESMA’s intent appears to have been to capture only revenues from securities lending, repos and reverse repos and the inclusion of gains from share class hedging could have distorted that information.
ESMA’s guidelines on ETFs and other UCITS issues

Transparency and risk mitigation

ESMA’s Guidelines on ETFs and other UCITS issues' are a regulatory response to concerns over increasing complexity in UCITS in recent years.

The Guidelines impact:

- UCITS ETFs
- Index-tracking UCITS
- UCITS investing in financial indices,
- UCITS using financial derivatives
- UCITS using efficient portfolio management (EPM) techniques

The guidelines took effect on 18 February 2013 with 12 month transitional arrangements for certain requirements. ESMA issued a Q&A document to address various aspects.

ESMA issued a final report in 24 March 2014 which provides an exemption from the 20% collateral diversification rule the government backed securities (see overleaf for more details).

---

**Financial reporting disclosures**

- Disclose tracking errors and additionally in the annual report explain any divergence in comparison with anticipated errors and difference between the performance of the UCITS and the performance of the index tracked
- Disclose information on EPM techniques in the annual report, including revenues arising from EPM techniques together with the direct and indirect operational costs and fees incurred
- Disclose information in the annual report on underlying FDI exposures, the identity of counterparties and the type and amount of collateral received

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**One year transitional arrangements**

- Financial indices rules
- Collateral requirements, except re-investment of cash collateral
- Revenue sharing arrangements
- ETF identifier
- Fund documentation disclosure requirements

---

**Key actions**

- Review EPM techniques and arrange for return of EPM profits to the fund
- Review collateral practices, swap arrangements, financial indices investments
- Update policies, procedures and the RMP to meet the new requirements

---

**ETFs / index tracking UCITS**

- Disclose replication methodology
- Provide for direct redemption if the stock exchange value of the units or shares of the UCITS ETF significantly varies from its net asset value

---

**Collateral management for OTCs and EPM**

- New stricter criteria
- Maximum exposure of 20% of NAV to a single issuer
- UCITS receiving collateral for at least 30% of its assets should have an appropriate stress testing policy in place
- New criteria in relation to cash collateral and the re-investment of cash collateral

---

**EPM techniques**

- Return all net revenue from EPM to the fund
- UCITS should be able to recall securities lent or assets subject to repos at any time

---

**Total return swaps**

- Underlying exposures to FDIs should be taken into account for issuer concentration rules
- Where the counterparty has discretion over the composition or management of the UCITS’ investment portfolio, the agreement between the UCITS and the counterparty is deemed an investment management delegation arrangement.

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**Financial indices**

- Stricter criteria for investing in financial indices
- New disclosure rules on components and methodologies
- ‘Backfilling’, i.e. retrospective changes to previously published index values, is not permitted
Central Bank of Ireland – revised UCITS Regulations (CP 77)

The proposed new approach

<table>
<thead>
<tr>
<th>Replacement of UCITS Notices and Guidance Notes</th>
<th>Elimination of overlap with UCITS Regs.</th>
<th>Rules-based approach</th>
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</thead>
<tbody>
<tr>
<td>“Residual guidance” published online</td>
<td>UCITS Rulebook</td>
<td>Removal of certain requirements at CBI’s discretion</td>
</tr>
<tr>
<td>Removal of the promoter regime</td>
<td>New financial statement requirements</td>
<td>Removal of “regulated markets” guidance</td>
</tr>
</tbody>
</table>

A new approach

- CP 77, issued on 2 Jan. 2014, proposes to replace the existing UCITS Notices and Guidance Notes with a new, more concise “UCITS Rulebook”.
- The existing framework is reorganised into three sections covering product, management company and depositary requirements.
- The UCITS Rulebook eliminates duplication of texts and is written in a more directive style to provide certainty around the regulatory requirements. In future the UCITS Rulebook will need to be read in conjunction with the UCITS Regulations in order to have a complete overview of the regulatory requirements.
- Existing guidance will be recast as rules in the Rulebook, eliminated or published separately to the Rulebook on the CBI’s website. It has yet to be fully determined which guidance will remain distinct from the Rulebook, termed “residual guidance” by the CBI.
- While the conditions imposed on UCITS are not materially changing, the removal or reorganisation of guidance may have implications for the compliance approach.
- Firms could have to exercise more judgement in areas where the rules are less prescriptive or guidance is absent.
- The approach taken is consistent with the way in which the CBI implemented AIFMD through the AIF Rulebook.
- To the extent it is considered appropriate to have consistency between the UCITS and the AIF Rulebooks, the CBI will seek to incorporate amendments or additions from the UCITS Rulebook into the AIF Rulebook when it is next updated.
- Responses to CP 77 were due by 28 March 2013. The new Rulebook is expected in Q4 2014.

Removal of the UCITS promoter regime

- In recognition of the evolving regulatory landscape, the promoter regime was already removed for AIFs.
- In removing the promoter regime for UCITS, the CBI will place reliance on the UCITS management company regulatory regime.
- As an additional safeguard, the CBI elaborates on the obligations of directors when a UCITS gets into difficulty.
- The promoter capital requirement of a minimum of €635,000 in net shareholder funds acted as a significant barrier to entry for some entities and will therefore be welcomed by industry participants.

Removal of “regulated markets” review process

- Planned withdrawal of Guidance Note 1/96 with reliance on EU requirements as implemented in the UCITS Regulations and UCITS Rulebook.
- The CBI will no longer review submissions on proposed regulated markets and will no longer publish a list of permitted markets for UCITS.
- This will increase flexibility/discretion in the determination of UCITS eligible assets but may also create an additional compliance risk for novel assets.

Half-yearly financial statements

- The CBI is proposing to require the additional submission of half-yearly unaudited management accounts covering the second six months of the financial year.
- Since these accounts would need to be submitted within two months of the period end, the supervisory objective appears to be the earlier receipt of accounting information prior to issue of the annual report.
- The imposition of this requirement will add an additional administrative burden on management companies and their administrations and will potentially require an additional, earlier sitting of the board to sign off the half-yearly accounts.
Central Bank Consultation on the adoption of ESMA’s revised guidelines on ETFs and other UCITS issues (CP84)

Transparency and risk mitigation

ESMA’s “Guidelines on ETFs and other UCITS issues” include a 20% issuer diversification rule with respect to collateral received for the purposes of EPM techniques and OTC derivative transactions. In response to industry requests and following consultation, ESMA issued a final report on 24 March 2014 which provides an exemption from the 20% collateral diversification rule for government backed securities. The exemption is available to all UCITS rather than solely money market fund UCITS, as previously proposed.

CP84 outlines the Central Bank’s proposals to implement the exemption from the 20% collateral diversification for all UCITS as provided for under the revised ESMA guidelines. It proposes to make the derogation subject to a requirement to determine whether the collateral is of “high quality”, taking into account various criteria specified in the CP. The proposal aims to address the Central Bank’s concerns to satisfactorily address risk mitigation without diverging from the ESMA guidelines. The proposed rules to apply to collateral diversification will be included in the UCITS Rulebook. Views are sought, in particular, on whether the proposed rules constitute a proportionate regulatory regime for collateral received by UCITS on foot of an EPM transaction or on foot of an OTC derivative transaction.

<table>
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<tr>
<th>Consultation</th>
<th>Submissions deadlines</th>
<th>Feedback</th>
<th>Implementation</th>
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</thead>
</table>

CP84 suggestions:

- Provide that all UCITS may avail of the derogation from the collateral diversification requirement where the collateral consists of securities issued or guaranteed by a Member State, one or more of its local authorities, a third country or a public international body of which one or more Member States belong;

- Delete the existing rule in the UCITS Notices which requires that collateral received by UCITS must be "of high quality"; and

- Replace this with a rule to be added to the UCITS Rulebook, that UCITS may only accept ‘high quality’ collateral and that in determining whether collateral is of high quality shall conduct an assessment prior to accepting the collateral which takes into account:

Where the acceptance of the collateral would mean that the collateral issuer constituted more than 20% of the total collateral held by the UCITS, the UCITS will apply the additional resources which a prudent UCITS would apply to a more detailed assessment of the credit quality of that collateral.

Credit quality of already-accepted collateral will be monitored on an on-going basis. Additional resources will continue to be applied to the more frequent and more detailed re-assessment of collateral issuers who constitute more than 20% of the collateral of a UCITS. Where there is evidence of deteriorating credit quality of collateral held, the UCITS will put into action a plan promptly to remedy its exposure to that collateral of deteriorating quality in an orderly manner and will prioritise the reduction of its exposure to any collateral counterparty who represents more than 20% of the collateral held.

Unless the board decides otherwise, the UCITS will not accept as new or replacement collateral, or continue without a timely remediation plan to hold, collateral which has not been awarded or does not continue to hold one of the two highest available ratings by each recognised credit rating agency that has rated the instrument.
European fund products

- Packaged Retail and Insurance-based Investment Products Directive (PRIIPs)
- European Long Term Investment Fund (ELTIF)
- Money market funds
- European Venture Capital Fund (EuVECA)
- European Social Entrepreneurship Fund (EuSEF)
Packaged Retail and Insurance-based Investment Products (PRIIPs)

Packaged Retail and Insurance-based Investment Products (PRIIPs) is an initiative aimed at better protecting and informing consumers in relation to products they may be offered.

On 15 April the European Parliament formally adopted the PRIIPs Regulation, following political agreement with the Council of Ministers. The PRIIPs Regulation requires the production Key Information Documents (KID) by PRIIPs manufacturers and sellers. The KID aims to provide clear and comparable information about products to aid consumers in decision making and prevent mis-selling. UCITS already has a Key Investor Information Document (KIID) which will eventually be replaced by the new industry-wide KID after a transitional period of 5 years.

UCITS managers will be keen to avoid disproportionate costs in transitioning to the new KID after only implementing the KIID in 2011. The KID will be introduced by regulation and be directly applicable in member states to ensure harmonisation.

The PRIIPs KID regulation came into force on 29 December 2014, it applies in all Member States from 31 December 2016, and the UCITS transition period ends on 31 December 2019.

### Comprehension Alert

A “comprehension alert” must inform the retail investor of investment products that may be difficult to understand. The criteria for being difficult to understand are:

- The product invests in underlying assets that are not commonly invested in by retail investors
- The product uses a number of different mechanisms to calculate the final return
- The investment’s pay-off takes advantage of the retail investor’s behavioural biases, such as a teaser rate followed by a much higher floating conditional rate

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
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<tbody>
<tr>
<td>Jul 2012</td>
<td>Commission proposal</td>
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<td>Dec 2014</td>
<td>Approved</td>
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<tr>
<td>31 Dec 2016</td>
<td>Requirement to prepare a KID</td>
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<tr>
<td>31 Dec 2019</td>
<td>End of transition for UCITS</td>
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<tr>
<td>2019</td>
<td>Commission review</td>
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</tbody>
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- Applicable to manufacturers of PRIIPs and to persons advising or selling PRIIPs in banking, insurance, securities and funds sectors (some exemptions apply)
- Written in the official language(s) of the member state or another language accepted by the regulator of that member state
- Should be easy to understand and regularly updated
- The KID is to be provided in good time before any transaction is concluded
- The KID may be provided in electronic means but the investor should be given the option to receive it on paper free of charge
- The PRIIP manufacturer will be held liable for any misleading, inaccurate or inconsistent information within the KID and a retail investor should be able to claim damages for a loss resulting from reliance on a KID
- The retail investor should be able to hold the PRIIP manufacturer liable for an infringement in case a loss is caused though the use of the KID
- The content and review process of the KID will be developed under regulatory technical standards to be drafted by the European supervisory authorities (ESMA, EBA, EIOPA)
- Regulators will have new product intervention powers under MiFID/PRIIPs and also sanctioning powers in relation to the KID
- The European Supervisory Authorities (ESAs) have monitoring and intervention powers under MiFID and PRIIPs to temporarily prohibit or restrict the marketing, sale or distribution of a product where concerns for investors arise
- National regulators must lay down administrative sanctions for breaches of the PRIIPs rules, which include public reprimands and fines
## Packaged Retail and Insurance-based Investment Products

### KID v KIID

<table>
<thead>
<tr>
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<tbody>
<tr>
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<tr>
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<tr>
<td><strong>Synthetic risk indicator:</strong> Yes</td>
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<td><strong>Headings:</strong></td>
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<tr>
<td>1. “What is this product?” covering the type of PRIIP, a description of the consumer target and ability to bear loss, details of any insurance benefits and the term of the PRIIP</td>
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<tr>
<td>2. “What are the risks and what could I get in return?” including a synthetic risk indicator and information on the possible maximum loss of invested capital</td>
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<tr>
<td>3. “What happens if the [name of PRIP manufacturer] is unable to pay out?” including a brief description of whether the related loss is covered by a compensation or guarantee scheme and if so, the name of the guarantor and which risks are covered</td>
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<tr>
<td>4. “What are the costs?” covering both direct and indirect costs to be borne by the investor, including summary indicators of these costs.</td>
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<tr>
<td>5. “How long should I hold it and can I take money out early?” including information on any cooling off or minimum holding period, penalties for early disinvestment the potential consequences of cashing the PRIIP before the end of the term or recommended holding period</td>
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<tr>
<td>6. “How can I complain?” covering information about how and to whom an investor can make a complaint</td>
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<tr>
<td>7. “Other relevant information” including a brief indication of any other documentation to be provided to the investor (excluding any marketing material)</td>
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<table>
<thead>
<tr>
<th>KIID (UCITS only)</th>
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<tr>
<td><strong>Length:</strong> No more than 2 slides of A4 pages</td>
<td></td>
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<tr>
<td><strong>Comprehension Alert:</strong> No</td>
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<tr>
<td><strong>Synthetic risk indicator:</strong> Yes</td>
<td></td>
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<td><strong>Headings:</strong></td>
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<tr>
<td>1. “Title and explanatory statements” containing the title ‘Key Investor Information” at the top of the first page and certain prescribed explanatory statements regarding the nature of the document.</td>
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<tr>
<td>2. “Objectives and Investment Policy” covering a joint description of the objectives and policy of the UCITS in plain language. To include the essential features of the UCITS which a typical investor should know and other information if relevant</td>
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</tr>
<tr>
<td>3. “Risk and Reward Profile” including a synthetic risk indicator and narrative presentation of risks materially relevant to the fund which are not adequately captured by the indicator</td>
<td></td>
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<tr>
<td>4. “Charges for this Fund” inclusion of a table specifying the entry, exit and ongoing charges with a narrative explanation of the charges</td>
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<tr>
<td>5. “Past Performance” including a bar chart presenting the past performance of the UCITS over a 10 year period and supplementary information</td>
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<tr>
<td>6. “Practical information” including the name of the depositary, statement on the liability of the management company, tax information, information on the umbrella/share classes, where and how to find further information</td>
<td></td>
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</table>
European Long-term Investment Fund

Advent of a two-tier Europe?

The European Long-term Investment Fund (ELTIF) is a new product aimed at promoting sustainable long-term investment in the European economy. Its focus is on investment in long-term projects including infrastructure, sustainable energy, new technologies.

As ELTIFs are available to both retail and institutional investors, they potentially herald the advent of a two-tier fund scenario in Europe: AIFs which are pass-portable to professional investors under AIFMD, and ELTIFs which are also passported under AIFMD to retail investors.

ELTIFs are being introduced by regulation and therefore will be directly binding in EU member states without gold-plating.

The final text was approved on 20 April 2015. The ELTIF entered into force on 8 June 2015, and will be applicable from 9 December 2015. On 31 July 2015, ESMA published a consultation paper outlining draft technical measures for the ELTIF.

The opportunity

• The European Commission estimates infrastructure transaction volumes at between €100–€150 billion a year.
• An estimated €1,500 to €2,000 billion will be needed to finance infrastructure project needs in Europe up to 2020.
• Pension funds and insurance companies with long-term liabilities are seen as key targets, as well as retail individuals planning for future liabilities who might benefit from regular returns afforded by long-term investments.
• The ELTIF is an approved channel for EIB funding.

Investment restrictions

• At least 70% of capital must be invested in "eligible investment assets" (listed to the right);
• A maximum of 10% of its capital in: instruments by or loans to QPUs; in a single real asset; in any single ELTIFs/EuVeCa/EUSeF; 5% of capital in certain UCITS eligible assets. Max 20% of the ELTIFs capital can be invested in aggregate in ELTIFs/EuVeCa/EUSeF. Max 25% of the units of a single ELTIFs/EuVeCa/EUSeF can be held.
• Portfolio composition and diversification rules apply. The ELTIF has five years to comply with these.
• Up to 30% of capital may be borrowed to acquire eligible investment assets (must not be used to fund loans given by the ELTIF), if the ELTIFs holdings are insufficient to acquire the asset.
• Prohibited investments: exposure to commodities (including via derivatives); short selling; securities lending/borrowing, repurchase transaction (or other agreements which has an equivalent economic effect and if 10% of the ELTIF assets are affected); using derivatives (derivatives for hedging purposes are permitted).

Eligible Investments

• ELTIFs can invest in either ‘Eligible Investment Assets’ or in certain UCITS eligible assets. “Eligible Investment Assets” include:
  ➢ Equity, debt or quasi equity instruments issued by qualifying portfolio companies
  ➢ Loans granted to qualifying portfolio companies
  ➢ Units/shares of other ELTIFs, EuVECs, EuSEFs (which have not invested over 10% of their capital in ELTIFs);
  ➢ Direct holdings (or via qualifying portfolio holdings) of individual real assets worth at least EUR100 million. “Real assets” include infrastructure and other assets which enable economic or social benefit (e.g. education, counselling, R&D). Commercial/residential property are included when they are integral/ancillary to a long-term investment project which contributes to smart, sustainable and inclusive growth in Europe.

Qualifying portfolio undertakings

• A portfolio undertaking (not a CIS) which is:
  ➢ not a financial undertaking;
  ➢ not listed or traded on a regulated market or a multilateral trading facility – EXCEPT small or medium listed company (i.e., max EUR500 million market capitalisation) are QPUs;
  ➢ established in the EU or in a third country that has a cooperation arrangement.
• A PPU can be a financial undertaking if it exclusively finances QPUs or real assets.
## European Long-term Investment Fund
### Advent of a two-tier Europe?

<table>
<thead>
<tr>
<th>Draft paper</th>
<th>Commission proposal</th>
<th>Parliament &amp; Council</th>
<th>EU trilogies</th>
<th>Adopted</th>
<th>Technical measures</th>
<th>Implemented</th>
</tr>
</thead>
</table>

### Authorisation
- The ELTIF must apply to its home member state regulator for authorisation, and provide them with the fund rules or instruments of incorporation, identify the AIFM and the depository, describe the investor disclosures.
- The AIFM must apply to the ELTIF’s home regulator for approval to manage the ELTIF, providing the depositary agreement, detailing the delegation of portfolio and risk management and administration.
- Internally managed ELTIFs can apply for dual approval simultaneously, which can take 3 months.
- Approval shall be granted within two months.
- ELTIFs cannot convert to non-ELTIF funds.

### UCITS or AIF?
- AIF only. (Only EU AIFs can become ELTIFs).

### Minimum investment
- €10,000

### Marketing passport
- Yes – to retail and professional

### Authorised or Registered AIFM
- Authorised only

### Regulated?
- Yes

### Retail/Professional investors
- Retail & professional

### Open/closed ended
- Closed ended, has the option to include redemption rights.

### Diversity requirements
- Max 10% of capital in assets of a single issuer or single asset
- 70% may be invested in equity/debt/loans or infra-structure projects. This limit is disapplied during a start-up period of 5 years to build up this portfolio, and also during the end of the life of the fund when positions are being closed
- Up to 30% can be invested in diversified assets

### Eligible assets
- 70% may be invested in equity/debt/loans or infra-structure projects. This limit is disapplied during a start-up period of 5 years to build up this portfolio, and also during the end of the life of the fund when positions are being closed
- Up to 30% can be invested in diversified assets

### Permitted ELTIF investments
- non-financial unlisted entities established to invest in infrastructure, property, ships, aircraft, rolling stock
- listed small and medium enterprises
- European Social Entrepreneurship Fund
- European Venture Capital Fund

### Leverage?
- Up to 30% of the capital of the ELTIF, non-recourse and used only to acquire eligible assets

### Legal structure
- Any, excluding partnerships

### Can investors transfer interests?
- Yes, they can sell their interests in the secondary market

### Transparency requirements
- Details of how the ELTIF’s investment objectives and strategy qualify the fund as long-term in nature.
- Prospectus Directive disclosure requirements
- AIFMD disclosure requirements.
- Prominent description of eligible assets.
- Prominent warning of the illiquid nature of the fund.
- All costs attached to the fund.
- KID disclosure requirements (if marketed to retail investors)

**Additional requirements**
- Must be an EU AIF managed by an EU AIFM and will have an EU passport
- Prior publication of a Key Information Document (KID) and disclosure rules apply
- Permitted to distribute income generated by the assets
- Retail investors have a two week cooling off period
Regulation on Money Market Funds
“Shadow banking” concerns

The European Commission released its draft Regulation on Money Market Funds (MMFs) on 4 September 2013. The proposal seeks to address the risk that investor “runs” could affect market stability. The European Council published a compromise proposal in December 2014. The European Parliament approved Nina Gill’s text on 29 April 2015, the terms of which are summarised below. The regulation is now undergoing trialogue negotiations.

Several of the amendments mirror some of the new rules introduced by the SEC to the US Money Market Fund regulation in 2014, particularly the liquidity fees and gates, the cut-off point of maturity of 90 days below which amortised cost can be used and the introduction of both retail and government type MMFs.

| CNAV MMFs          | • Retail CNAV MMF, including charities, non-profit organisations, public authorities and public foundations
|                    | • Public Debt CNAV MMF which must invest 99.5% of its assets in public debt instruments and, by 2020, at least 80% of its assets in EU public debt instruments
| Investment policy  | • MMFs will only be permitted to invest in money market instruments, deposits with credit institutions, financial derivative instruments and reverse repo agreements that meet certain requirements.
|                    | • A new 5% single issuer limit is proposed.
| Risk management    | • New portfolio rules on the weighted average maturity and weighted average life of assets are proposed.
|                    | • Know Your Customer rules in terms of redemption behaviours and stress testing requirements are also proposed.
|                    | • An MMF may not “solicit or finance” a credit rating agency to rate the MMF under the proposals.
| Transparency       | • New labelling requirements are imposed and communications must make clear that investment is not guaranteed.
|                    | • Regulatory reporting on a quarterly basis will be required.

| LNAV               | • A new type of Low Volatility Net Asset Value Money Market Fund (LVNAV MMF). These MMFs may use amortised cost accounting for assets with a residual maturity of below 90 days and value using constant NAV rounded to two decimal places. LNAVs would be authorised for a period of 5 years and subject to an Commission review to be presented to Council and Parliament after 4 years. Under the review, the Commission should examine the possibility of extending the authorisation of LVNAVs indefinitely.
| Securities with 90 day maturity | • All assets with a residual maturity exceeding 90 days would be priced using mark-to-market or mark-to-model. Where the constant NAV deviates from the shadow NAV by more than 20 bps, the NAV would need to be floated.
| Collateral         | • Liquidity fees and redemption gates will apply to LVNAV, Retail CNAV and Public Debt CNAV MMFs.
European Venture Capital Fund
Investing in the SME sector

The European venture capital industry is fragmented and dispersed and has been hampered from growing by the lack of a common EU regulatory framework. With SMEs finding it difficult to access bank credit following the financial crisis, the EU has sought ways to open up non-bank lending to the SME sector.

AIFMD creates a new EU distribution passport for AIFMs marketing to professional investors. However, the smaller scale of the venture capital industry means that many of these managers would fall below the de minimis thresholds and would have to opt in to the full compliance regime to avail of an EU passport, placing greater cost on these below threshold firms.

To promote the development of a cross-border venture capital industry and boost investment in SMEs, a regulation on European Venture Capital Funds (EuVECAs) was adopted (EuVECA regulation) and took effect on 22 July 2013 to coincide with the implementation of AIFMD.

### Qualifying managers
- Use of the EuVECA label and associated EU passport is open to managers who:
  - Have total AuM of less than €500 million comprising unleveraged, closed-ended funds with a lock-up period of five years
  - Are established in the EU
  - Have registered with their local regulator under AIFMD
  - Manage portfolios of qualifying venture capital funds

### EuVECA definition
- An EuVECA is a fund that:
  - Meets the definition of an AIF
  - Intends to invest at least 70% of its aggregate capital contributions and uncalled committed capital in assets that are qualifying investments
  - Does not use more than 30% of its aggregate capital contributions and uncalled committed capital to acquire non-qualifying investments
  - Is established in the EU

### Qualifying investments
- "Qualifying investments" are equity, or quasi-equity instruments, secured or unsecured loans granted to a “qualifying portfolio undertaking”, shares of a qualifying portfolio undertaking and units or shares in other EuVECAs.
- A “qualifying portfolio undertaking includes a company that is:
  - Not admitted to trading on a regulated market
  - Employs less than 250 people
  - Has an annual turnover not exceeding €50 million or an annual balance sheet total not exceeding €43 million
  - Is not a collective investment undertaking, a credit institution, an investment firm or an insurer
  - Is established in the EU or a country with a cooperation arrangement

### Additional requirements
- In addition to compliance with the “Registered AIFM” regime, managers must adhere to certain lighter requirements based on AIFMD, including:
  - Conduct of business
  - Conflict of interests
  - Certain organisational requirements
  - Valuations
  - Annual report and annual audit
  - Investor disclosures
  - The EuVECA is open to professional investors with a minimum investment of €100,000
European Social Entrepreneurship Fund (EuSEF)

Supporting social entrepreneurs

The European Social Entrepreneurship Funds (EuSEF) Regulation applies from 22 July 2013 and introduces a marketing passport to allow fund managers to market qualifying social entrepreneurship funds to EU investors. It aims to make it easier for social enterprises to raise funds across Europe by:

• Creating a designation (that is, a brand) of “European Social Entrepreneurship Fund” or “EuSEF”, which can be used by funds that meet prescribed conditions;

• Setting out a framework for a marketing passport, which allows funds with EuSEF status to be sold to a wide range of European investors.

Qualifying managers

• Use of the EuSEF label and associated EU passport is open to managers who:
  • Have total AuM of less than €500 million comprising unleveraged, closed-ended funds with a lock-up period of five years
  • Are established in the EU
  • Have registered with their local regulator under AIFMD
  • Manage portfolios of qualifying social entrepreneurship funds

Additional requirements

• In addition to compliance with the “Registered AIFM” regime, managers must adhere to certain lighter requirements based on AIFMD, including:
  • Conduct of business
  • Conflict of interests
  • Certain organisational requirements
  • Valuations
  • Annual report and annual audit
  • Investor disclosures
  • The EuSEF is open to professional investors with a minimum investment of €100,000

Qualifying investments

• “Qualifying investments” are equity, or quasi-equity instruments, secured or unsecured loans granted to a “qualifying portfolio undertaking”, shares of a qualifying portfolio undertaking and units or shares in other EuSEFs.

• A “qualifying portfolio undertaking includes a company that is:
  • Not admitted to trading on a regulated market
  • Is managed in an accountable and transparent way, in particular by involving workers, customers and stakeholders affected by its business activities
  • Is established in the EU or a country with a cooperation arrangement
  • Has the achievement of measurable, positive social impacts as its primary objective where the undertaking:
    ➢ provides services or goods to vulnerable or marginalised, disadvantaged or excluded persons;
    ➢ employs a method of production of goods or services that embodies its social objective; or
    ➢ provides financial support exclusively to social undertakings as defined in the two bullet points above.

EuSEF definition

• An EuSEF is a fund that:
  • Meets the definition of an AIF
  • Intends to invest at least 70% of its aggregate capital contributions and uncalled committed capital in assets that are qualifying investments
  • Does not use more than 30% of its aggregate capital contributions and uncalled committed capital to acquire non-qualifying investments
  • Is established in the EU
Banking, capital markets developments

- Capital markets union
- 2015 enforcement priorities – Central Bank of Ireland
- Anti Money Laundering
- Probability Risk and Impact System (PRISM) inspections – Central Bank of Ireland
- MiFID II
- Wholesale conduct
- EMIR
- Market Abuse Directive II (MAD II)
- Client Assets
Capital markets union (CMU)

What is the Capital Markets Union (CMU)?
The CMU is the European Commission’s ‘landmark project’ which aims to create a single market for capital, unlock funding for Europe’s businesses and boost growth in the EU’s 28 Member States. It aims to achieve this by making the investment chain as efficient as possible through improving the access to finance across the EU, increasing and diversifying the sources of funding available and ensuring the effective allocation of capital through markets. Its objectives also include:
- helping SMEs raise finance as easily as large companies
- creating a single market for capital by removing barriers to cross-border investments, and
- diversifying the funding of the economy and reducing the cost of raising capital

The CMU is part of the Commission’s “Investment Plan for Europe” which it launched in November 2014. Its measures include:
- the implementation of European Long-term Investment Funds (ELTIF) regulation,
- ‘high-quality’ securitisation,
- standardised credit information on SMEs,
- private placement and
- the review of the Prospectus Directive.

Who does it affect?
It affects businesses across the EU, including regulated entities such as fund managers, fund service providers and investment funds.

The European Commission’s ‘Green Paper’?
The purpose of the Green Paper was to foster debate across the EU on possible measures needed to create a true single market for capital. The Commission is seeking feedback from the European Parliament and the Council, other EU institutions, national parliaments, businesses, the financial sector and all those interested. The deadline closed on 13 May 2015. The Green Paper suggested the following principles should underpin a CMU:
- how to reduce the costs of setting up and marketing investment funds across the EU;
- how to further develop venture capital and private equity;
- whether targeted measures in the areas of company, insolvency and securities laws as well as taxation could materially contribute to CMU; and
- the treatment of covered bonds, with a specific consultation in 2015 on a possible EU framework.

The Commission will use the feedback from the Green Paper to identify the actions that are necessary to achieve its objectives, and will adopt an Action Plan in the summer of 2015 setting out its roadmap and timeline for putting in place the building blocks of a CMU by 2019.

Timeline
The CMU is a long-term project expected to last many years. However, the Commission is hoping to make early progress in some areas in the coming months. Principally, it is seeking input from interested parties into an ‘Action Plan’ it is preparing via a ‘Green Paper’. The closing date for responses to this Green Paper was 13 May 2015, and the Action Plan is expected to be published later this year.

Early Initiatives
- Pan-European Private Placements
- High-quality Securitisation
- Review of the Prospectus Regime
- Improving SME Credit Information
- Encouraging the uptake of ELTIFs

Medium-term Initiatives
- Covered Bonds, Corporate Bonds, Green Bonds, Mini Bonds
- FinTech (including crowdfunding)
- Venture Capital (including EuVECA)
- Private Equity
- Leverage Loans
- Securities Law

Early Initiatives
- Insolvency Law
- Company Law
- Tax
- Pensions (products and provision)
- Accounting standards
Capital markets union (CMU)
The Commission’s Green Paper: Overview

Principles
The Green Paper (GP) set out the principles underlying the CMU:
1. Maximizing economic growth;
2. Increasing financial stability;
3. Apply to all 28 Member States and remove barriers to entry;
4. Ensure effective consumer protection; and,
5. Attract global investment and enhance competition.

Objectives of the CMU:
- Improve access to finance across the EU;
- Increase and diversify the sources of funding available;
- Ensure effective allocation of capital through markets.

Approach
- The Commission will take a pragmatic “bottom–up” approach, identifying and tackling each barrier in turn based on its impact and feasibility of each action;
- Legislative and regulatory change will be undertaken only where necessary;
- Greater emphasis will be placed on “market driven solutions”;
- There will not be a large legislative agenda to deliver the CMU;
- The Commission will revisit previous decisions to ensure the right balance between stability and growth; and,
- There will be increased emphasis on impact assessments.

Policy Shift
The CMU incorporates three notable policy shifts of the Juncker Commission:
1. A focus on jobs and economic growth as well as financial stability;
2. A greater emphasis on legislative review and calibration rather than new initiatives; and,
3. A willingness to use alternative techniques to legislation to achieve its aims, e.g. market driven solutions.

A Single Market in Capital
The main driver behind the CMU is economic growth, but the aim of the CMU is to build a framework to enhance the free movement of capital enshrined in the treaties. Objectives of the CMU:
- Improve access to finance across the EU;
- Increase and diversify the sources of funding available;
- Ensure effective allocation of capital through markets.

Barriers
Some barriers to the CMU have already been identified, such as a historical bias towards certain types of finance and heterogeneous equity cultures.

The GP has put emphasis on identifying and understanding unknown barriers before proceeding with an action plan.
The Commission released a consultation paper (CP) on STS alongside the CMU GP. The CP builds on the ECB/ Bank of England and BCBS/ IOSCO consultations.

The focus of the consultations has been developing criteria to identify STSS that would qualify as STS would then benefit from differentiated capital treatment. The divergent treatment of non-qualifying and qualifying STS could therefore lead to a split in the securitisation market.

**Qualifying Simple, Comparable and Standard Securitisation (STSS)**

**Simple:** Homogeneous underlying assets and exposures, simple characteristics and transaction structure.

**Transparent:** Transparency and disclosure requirements to provide investors with sufficient information on the underlying assets and structure to appropriately assess the underlying risks.

**Standard/ Comparable:** Requiring a ‘true sale’ of the underlying assets to the SPV rather than a synthetic structure. Standard terms and, potentially, rights and subordination rules.

**Additional Risk Features:** the criteria would be dependent on the risks of the underlying assets.

**Capital Treatment**

**BCBS Revised Framework:** The CP proposes that the revised framework could be used to provide a new “baseline” in a review of the capital treatment of securitisations under EU regulations.

**Qualifying STS:** Further proposals reflect the potential to have beneficial capital treatment for qualifying STSS “to take account of lower risk” that is expected to attach to these instruments.

**Additional Proposals in the CP**

**Harmonized Structure:** The creation of an optional standard structure for securitization covering the legal form of the SPV, mode of transfer of assets, and the rights and subordination of note holders.

**Identification of STS criteria for short-term securitisations:** The STS criteria in the CP do not cover asset backed commercial paper, due to a number of factors that differ to longer-term securitisations, e.g. the maturity of the underlying assets.

**Risk Retention:** Including exempting investors in qualifying STS from verifying compliance, and a mechanism to monitor and verify eligibility with qualifying STSS criteria.

**Potential Characteristics of STSS**

- Ongoing disclosure and transparency requirements including loan level data;
- Homogeneous pool of underlying assets;
- ‘True sale’ of underlying assets rather than synthetic structures;
- Use of derivatives limited to hedging purposes only;
- Securities admitted to trading on a trading venue;
- Standard securitisation structures;
- No re-securitisations;
- Reduced reliance on credit ratings (including national caps).
# CMU: Early Initiatives

## Review of the Prospectus Regime

Despite a number of recent and ongoing revisions to the prospectus regime, the Commission launched a consultation to review the prospectus regime as part of the CMU. The focus of the review is to recalibrate the scope, streamline the process and content of prospectuses, and update the regime for market and regulatory developments, with a view to reducing the administrative burden.

### Scope and Exemptions

- Reviewing existing quantitative exemption thresholds (size of issue and number of persons issue addressed to);
- Creating a new exemption for secondary issuances;
- Extending the regime to cover issuance on an MTF, but under the proportionate disclosure regime;

### Contents and Procedure

- Recalibrating the proportionate disclosure regime;
- Extending the scope of incorporation by reference;
- Extending the base prospectus regime;
- Imposing a limit on the length of prospectuses;
- Streamlining the approval process of prospectuses by NCAs.

### Updating for Developments

- Tailoring the regime to recent market developments;
- Updating the regime in light of revised regulations such as the Transparency Directive;
- Creating a bespoke regime for companies admitted to trading on an SME growth market (under MiFID II);
- Creating a third country equivalence prospectus regime.

### Impact

- Recalibrating existing exemptions and creating new exemptions would allow the regime to be more flexible and reduce the situations when a prospectus would be required;
- Revising the regime for regulatory developments, such as the transparency directive, will avoid duplicative requirement and has the potential to make use of disclosure requirements under difference regimes;
CMU: Questions Remain
The GP answers some questions on the CMU and leaves others unanswered

Supervision
A critical question for the markets is the impact of CMU on supervision, specifically whether it will lead to a single supervisor.

The GP sidestepped this question saying that “there may be a further role for the ESAs to play in increasing convergence”.

Signals from the Commission and Member States is there is no appetite for a single supervisor for capital markets.

End Users
The CMU agenda will put in place a framework for a single market in capital to develop.

Growing EU capital markets will require innovative techniques from all concerned, but the framework needs to be aligned to the needs of end users if is to be used.

Questions remain over how the Commission seeks to overcome these challenges.

Institutional Change
The impact of the new internal structure in the College of Commissioners has yet to be seen, especially the role Timmermans (better regulation and subsidiarity).

Political Will
The CMU has received warm reception from some Member States, but it is unclear whether there is sufficient will:

- To tackle the more difficult and politically sensitive topics such as insolvency and tax;
- For the Commission to stay the course with its approach to put emphasis on market driven solutions.

Existing Workstreams
Little information has been provided on how existing regulatory initiatives will be tied into the CMU, e.g. MiFID II/ MiFIR level 2 work, or which decisions made in the crisis will be revisited to “balance growth and stability”.

Cultural Barriers
The Commission has already highlighted cultural barriers to the CMU, such as the heterogeneous equity cultures. The Commission has yet to indicate how such barriers could be tackled.

End Users
The CMU agenda will put in place a framework for a single market in capital to develop.

Growing EU capital markets will require innovative techniques from all concerned, but the framework needs to be aligned to the needs of end users if is to be used.

Questions remain over how the Commission seeks to overcome these challenges.
2015 enforcement priorities
Central Bank of Ireland

Central Bank of Ireland’s 2015 Enforcement Priorities

On 9 February 2015 the Central Bank of Ireland (CBI) published its statement of enforcement priorities for 2015. The CBI publishes its enforcement priorities annually to reflect its commitment to transparency in the work that it does and to focus regulated firms’ attention on expected behaviours and standards to encourage them to review their business practices and maintenance of the highest levels of compliance.

The CBI’s enforcement strategy aims to deter breaches of requirements and secure compliance with its expected behaviours and standards to protect consumers and safeguard the stability of the wider financial system and the economy.

In addition to the identified priorities, the CBI will address any other challenges resulting from regulatory developments or identified through either its supervisor arm or other sources (e.g. whistle-blowers).

In 2014, the CBI engaged in 11 enforcement settlements with regulated financial service providers and imposed overall fines of over €5 million.

1. Cross-sector enforcement priority areas

• **Prudential requirements** – adherence is key for all sectors, particularly: credit unions; credit institutions and markets and retail intermediaries.

• **Systems and controls** – the CBI considers that the existence and proper functioning of a firm’s systems and controls is fundamental to ensuring compliance with its regulatory requirements.

• **Provision of timely, complete and accurate information to the Central Bank** – several enforcement cases in 2014 concerned the provision of incomplete/inaccurate regulatory information to the Central Bank. This remains remain a cross sector focus area for 2015.

• **Appropriate governance and oversight of outsourced activities** – two significant enforcement cases in 2014 featured governance failures relating in particular to outsourcing. As the firms involved were from different industry sectors, this highlights that outsourcing governance arrangements affect all regulated sectors. The CBI reminds firms that outsourcing is no defence to regulatory failings – it expects appropriate oversight and supervision by firms of the outsourced activity.

• **Anti-Money Laundering /Counter Terrorism Financing compliance** – the CBI has taken enforcement cases due to breaches of the anti-money laundering requirements. It expects compliance by all credit and financial firms with the regulatory requirements to ensure that effective procedures are in place to counter the threats of money laundering and financing of terrorism.

• **Fitness and probity obligations.**

2. Sector-specific enforcement priority areas

• **Markets**
  - MiFID conduct of business rules
  - Client Asset Requirements

• **Credit Unions**
  - Governance

• **Consumer Protection**
  - Code of Conduct on Mortgage Arrears
  - Suitability of sales
  - Fair treatment of customers

• **Low impact firms**
The CBI is taking a strict approach towards firms with a low-impact PRISM rating and has allocated resources for enforcement actions against them. As they interact less with the CBI than other regulated firms, the CBI states that it will use its enforcement powers if any breaches are discovered as a reminder that compliance is obligatory for all firms. This approach promotes compliance through deterrence and complements the PRISM framework.
Fourth Anti-Money Laundering Directive
Just when you thought the Third Directive was implemented!

Key Changes in Directive

- It clarifies the interaction between money laundering and data protection requirements
- It includes an explicit reference to tax crimes as a predicate offence for money laundering
- It require all companies and trusts to hold information on their beneficial owners
- It clarifies the application of AML Rules to cross-border subsidiaries between home and host supervisors
- Rules on simplified due diligence will change and specific product and client exemptions will be replaced with a requirement to demonstrate lower risk based on factors including those in Annex II
- Strengthen the powers of Financial Intelligence Units (receivers of suspicious transactions reports)
- Extends provisions applying to foreign Politically Exposed Persons (PEPs) to domestic PEPs on a risk-sensitive basis
- Equivalence of third country regimes: removes the "white list" process
- Responsibility for compliance rests with senior management which extends beyond the Board
- Group entities must implement group-wide policies and procedures, including data protection policies and procedures for sharing information within the group for AML purposes.
- Annex I contains factors that must be considered in a firm’s risk based approach
- It requires Member States to carry out national risk assessments and take measures to mitigate risks
- It extends existing provisions for casinos to all gambling
- It reduces the transaction threshold at which traders in high value goods are required to identify customers from €15,000 to €7,500
- It sets out a framework for minimum administrative sanctions to apply across member states

Key stages

<table>
<thead>
<tr>
<th>FATF Recommendation February 2012</th>
<th>Commission March 2013</th>
<th>COREPER agreed a general approach</th>
<th>Implementation 2015/2016</th>
</tr>
</thead>
</table>

On 17 December 2014, the Presidency of the Council of the EU announced that it had reached political agreement with the European Parliament on the proposed Fourth Money Laundering Directive and the revised Wire Transfer Regulation. The European Parliament also announced that it had agreed with the Council on central registers for beneficial owners of companies. The Fourth Anti Money Laundering Directive and Wire Transfer Regulation need to be endorsed by COREPER and ECON and on Civil Liberties, Justice and Home Affairs, before being put to a vote by the Parliament in plenary in 2015.

Key points of discussion

Customer Due Diligence

- Proposed changes to simplified due diligence will have a significant impact on administrators who place a heavy reliance on this exemption to reduce the identification burden. While in practice it is likely that most clients and products that qualify for simplified treatment will continue to do so under the proposed risk based test additional resources and processes will be required to demonstrate this.
- Firms, trusts and other clients will be required to retain and produce documentation so that funds can meet their AML obligations. This should reduce the burden on administrators when obtaining necessary documentation. Clarity will be required in terms of the level of documentation that must be retained by clients in this regard as this will depend on the risk weighting assigned to them by the administrator.
- Domestic Irish PEPs must be identified, this is unlikely to cause issues for Irish domiciled funds but may be an issue for non-Irish funds.

Risk Based Approach

- Each country must conduct a risk assessment, firms will be expected to incorporate these risk assessments when selling cross-border into those markets. Firms with large distribution networks will need to consider how it approaches this requirement and whether multiple policies or high water mark approach is best. More onerous obligations may have a sales impact.
- The factors detailed in Annex I relating to a firms risk based approach may also present challenges. For those that have previously adopted the FATF guidelines in this regard the impact will be less significant.
# AML

## Recent activity

AML continues to be an area of focus for the Central Bank of Ireland with particular attention on the retail banks in the last number of months. They have emphasised the importance of the risk based approach and governance in place in the firms under review.

### AML Developments

The Central Bank of Ireland scheduled inspections for two administrators and one wholesale bank during 2014, with a focus on governance and thematic review of risk areas.

<table>
<thead>
<tr>
<th>CJA 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>• The Criminal Justice Act, 2013 (“CJA, 2013”) amends the Criminal Justice (“Money Laundering and Terrorist Financing) Act 2010 (“the 2010 Act”) and was signed into law on 12 June 2013</td>
</tr>
<tr>
<td>• The Act removes the requirement to have all documentation maintained in the State, provided such records are capable of being reproduced in the State as soon as practicable. Maintenance of documentation in the State was a key issue for the international funds industry and the removal of this requirement has been welcomed</td>
</tr>
<tr>
<td>• Designated persons will be required to monitor customers to check whether they become a PEP during the course of a business relationship. Enhanced monitoring obligations are also proposed for PEPs</td>
</tr>
<tr>
<td>• New procedures for simplified and enhanced customer due diligence are also included</td>
</tr>
<tr>
<td>• Guidance Notes will not be updated with new requirements</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Recent sanctions reasons (50K, 65K)</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Failing to demonstrate it had instructed any of its staff on the law in relation to money laundering and terrorist financing</td>
</tr>
<tr>
<td>• Failing to provide this instruction to the Directors of the firm</td>
</tr>
<tr>
<td>• Failing to demonstrate that it had met the requirements for placing reliance on third parties</td>
</tr>
<tr>
<td>• Failing to adopt adequate written policies and procedures in relation to the identification and reporting of suspicious transactions</td>
</tr>
<tr>
<td>• Failure to establish that third parties it relied on to meet AML obligations met the definition of Relevant Third Party</td>
</tr>
<tr>
<td>• Failure to identify PEPs</td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Recent inspections (see framework)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Focus in recent inspections:</td>
</tr>
<tr>
<td>• Governance</td>
</tr>
<tr>
<td>• Risk based approach</td>
</tr>
<tr>
<td>• Suspicious Transaction Reporting</td>
</tr>
<tr>
<td>• Management Information</td>
</tr>
<tr>
<td>• People and Training</td>
</tr>
<tr>
<td>• AML Controls</td>
</tr>
<tr>
<td>• CDD &amp; Ongoing Monitoring</td>
</tr>
<tr>
<td>• Outsourcing</td>
</tr>
<tr>
<td>• IT systems</td>
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</tbody>
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<table>
<thead>
<tr>
<th>Next steps</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Confirm CJA 2013 implemented</td>
</tr>
<tr>
<td>• Request review of risk areas identified by sanctions and inspections findings</td>
</tr>
<tr>
<td>• Assess compliance in light of Central Bank AML framework</td>
</tr>
<tr>
<td>• The CBI published a letter to the Banking industry on AML in Feb, with a letter to the funds industry expected in Q2 2015.</td>
</tr>
</tbody>
</table>
AML

Central Bank review framework

Background

The Criminal Justice (Money Laundering and Terrorist Financing) Act 2010 ("CJA2010") imposed detailed obligations on firms in relation to the development of policies, processes and procedures for ensuring compliance with AML/CFT obligations. The guidelines published by the Department of Finance provide further detail in relation to how these obligations should be fulfilled and compliance evidenced.

The Central Bank as part of its previous communications has used the following AML/CFT model framework to demonstrate the mapping of the legislative obligations and guidance to the standard business practices operated by firms. Items shaded “blue” applies to all firms, items shaded “green” apply to firms with higher level of sophistication and scale.

1. Establish AML Governance
   1.1 Adopt formal policies
   1.2 Define governance structure
   1.3 Define roles & responsibilities
   1.4 Define clear approval/escalation process
   1.5 Define training & awareness strategy

2. Adopt Risk-based Approach
   2.1 Identify risk faced by firm
   2.2 Establish risk rating methodology
   2.3 Complete customer due diligence (CDD)
   2.4 Conduct on-going customer monitoring
   2.5 Conduct transaction monitoring
   2.6 Conduct risk based periodic customer review
   2.7 Create AML intelligence

3. Investigate / Escalate Suspicious Activity and Sanction Hits
   3.1 Report suspicious activity
   3.2 Report sanctions hits

4. Report Management Information
   4.1 Report AML MI
   4.2 Produce annual MLRO report
   4.3 Keep records

5. Manage people and training
   Implement training & awareness strategy

6. Monitor and Improve Effectiveness of AML Controls
   6.1 Conduct on-going monitoring of processes
   6.2 Analyse internal process trends
   6.3 Review new regulation & guidance
   6.4 Support internal / external audits
PRISM overview
Approach to risk-based supervision

- Probability Risk and Impact SysteM (PRISM) is the Central Bank of Ireland’s (CBI) approach to supervising financial services firms on a risk basis. Under PRISM, the CBI places higher emphasis, and therefore a higher proportion of its supervisory resources, on supervising those firms that have the greatest ability to adversely impact their statutory objectives of promoting financial stability and ensuring consumer protection.

- The PRISM framework recognises that not all financial services firms pose the same degree of risk to achieving these objectives, and in doing so enables the CBI to focus its efforts on regulating higher risk firms through structured engagement plans that provide for early intervention to mitigate emerging risks. Firms that are of lesser risk to the economy and the consumer are still subject to financial regulation by the CBI, but this is undertaken on a reactive basis combined with a series of themed inspections that are conducted annually.

- PRISM provides a systematic and structured approach to determining the potential risk posed by financial services firms, by assessing the impact and probability of individual firm failure on a common scale. Firms are divided into four categories: high impact (including ultra-high impact), medium-high impact, medium-low impact, and low impact. The impact rating of the firm will determine the number of supervisory resources allocated to its supervision by the CBI.

- In the case of funds, which are considered low risk, the probability element of the assessment is less important than impact and PRISM allows for mitigants to be used to reduce the probability aspect. Firms’ individual PRISM ratings can change over time and should be considered when managing regulatory risk. An important element of PRISM is the focus on the board and a number of PRISM visits have occurred with fund directors to date.
<table>
<thead>
<tr>
<th>Impact</th>
<th>Probability (excludes low)</th>
<th>Mitigants</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
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<td>Internal mitigation</td>
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<tr>
<td>Metrics</td>
<td>Supervisors</td>
<td>Engagement</td>
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<tr>
<td>Financial</td>
<td>Prudential supervisors</td>
<td>Business Model Analysis</td>
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<tr>
<td>Capital</td>
<td>Consumer supervisors</td>
<td>Governance</td>
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<tr>
<td>Solvency</td>
<td>Markets supervisors (funds)</td>
<td>Financial Risk Review</td>
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<td>Customers</td>
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<td>Stress testing</td>
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<tr>
<td>AUM</td>
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<td>SREP / ORSA</td>
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<td>Full Risk Assessment</td>
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<td>Meetings with senior staff</td>
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</table>

**Impact Score (non-negotiable)**

**Risk Rating - Mitigants**

**Central Bank Quality Assurance**
## Areas of focus

<table>
<thead>
<tr>
<th>Impact</th>
<th>Review</th>
<th>Approach</th>
</tr>
</thead>
<tbody>
<tr>
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</tr>
<tr>
<td></td>
<td>Meetings with senior staff</td>
<td></td>
</tr>
<tr>
<td>Impact Score (non-negotiable)</td>
<td>How a firm makes money and the risks it takes to do so</td>
<td>Detailed, appropriate and integrated risk appetite statement</td>
</tr>
<tr>
<td></td>
<td>Governance structure, individuals and structures</td>
<td>Corporate governance code, board effectiveness, Fitness and Probity</td>
</tr>
<tr>
<td></td>
<td>Risks encountered by the firm when carrying on its business</td>
<td>Strong risk identification, management, change control, mitigation and transfer</td>
</tr>
<tr>
<td></td>
<td>Understand what changes would destabilise the business</td>
<td>Accurate, realistic and appropriate testing parameters</td>
</tr>
<tr>
<td></td>
<td>Capital amount is adequate</td>
<td>Additional capital or restructuring of capital</td>
</tr>
<tr>
<td></td>
<td>Full review including desk top review and interviews. Focus is governance, strategy and key risks</td>
<td>Inspection procedures and mock interviews</td>
</tr>
<tr>
<td></td>
<td>Interviews with senior staff in respect of strategy, strengths and weaknesses, governance and risk profile</td>
<td>Focus is on competence therefore training plan, fitness and probity files and mock interviews are important</td>
</tr>
</tbody>
</table>
Purpose of PRISM visits

• A PRISM visit does not equate to a supervisory inspection. The CBI’s primary objective in conducting a PRISM visit is to understand the firm’s business and associated risks. This is so that it can, in its supervisory role, establish:
  ✓ Have risks associated with the firm’s business plan on a forward-looking basis been identified and clearly understood?
  ✓ Has appropriate ownership for managing risks been assigned at senior management and board levels?
  ✓ Are there sufficient controls embedded within the firm’s business model to manage risks?
  ✓ What is the effectiveness of the controls and how frequently are they monitored?
  ✓ What risks, if any, are unacceptable and need to be mitigated?
  ✓ What risks, if any, are less well defined and warrant further review / inspection?

Frequency of visits

• The purpose of regular visits is to ensure that directors and senior management understand emerging risks arising from changes to the firm’s strategy
• High impact firms receive multiple visits per year with each visit having a different focus across a range of topics including governance, risk appetite, and individual risk type policies and procedures
• Medium-high impact firms receive full risk assessments every two to four years
• Low impact firms are supervised on a reactive basis with thematic reviews across sectors and/or occasional summary inspections
Key themes and hot topics

- Clarity of organisation and governance – delineation and concentrations
- Delegation of responsibility and ultimate accountability
- Outsourced functions and retained responsibility / Board oversight
- Alignment of business plan with clearly articulated risk appetite
- Completeness of material risk assessment
- Capital adequacy and stress testing
- Oversight of reward and remuneration
- Reporting of management information to the Board
- Adequacy of resourcing and appropriate skill levels in control functions
- Compliance framework effectiveness
- Business continuity planning
- Oversight of investment policy / strategy
- Board committee ‘review and challenge’ of senior management
- Monitoring of actual risk profile / limits
- Financial crime and AML
- Progress on any outstanding RMP actions
Risk process

- Identify
- Quantitative
- Qualitative
- Manage
- Avoidance
- Reduction - probability
- Mitigation - impact
- Transference
- Acceptance

- Monitor
- Mitigation - impact
- Transference
- Acceptance

- Reporting
- Mitigation - impact
- Transference
- Acceptance

- Strategy and Change
- Appetite Statement
- RAG

- Understand
- Quantitative
- Qualitative
- Measure

- Risk process

- Identify
- Quantitative
- Qualitative
- Manage
- Avoidance
- Reduction - probability
- Mitigation - impact
- Transference
- Acceptance

- Monitor
- Mitigation - impact
- Transference
- Acceptance

- Reporting
- Mitigation - impact
- Transference
- Acceptance

- Strategy and Change
- Appetite Statement
- RAG
Introduction to MiFID
Drivers for Policy Change and Key Changes

On 14 January 2014, the political agreement was reached on revisions to the existing MiFID and the creation of MiFIR, a new piece of regulation. More recently, the European plenary released draft texts of the revisions to MiFID and a draft of MiFIR. Together, these are referred to as ‘MiFID II’. Some of the changes which MiFID II brings are likely to have a substantial effect on private banking businesses across the EU.

Key Drivers

G20 Commitments
- Enhancements to transparency in both cash and OTC derivatives.
- This was communicated in Pittsburgh 2009 and Washington 2011.

Review of MiFID
- A review of MiFID I (2003) was expected to occur.
- There was an industry perception that MiFID I left gaps and did not address some key issues & challenges.

Modernisation
- Desire to address the changing financial landscape, in relation to how firms do business, how markets work and the rate at which financial services are impacted by technology.

Key Areas of Change for Private Banking

- Governance
- Investor Protection
- Pre/Post Trade Transparency
- Market Structure
- Conflicts of Interest
- Transaction Reporting
- Third Country Access Regime
- Commodities

MiFID

MiFID II
### Introduction

**Drivers for Policy Change and Key Changes**

The conduct focus of MiFID (2003) has been expanded in MiFID II to strengthen investor protection. This area is likely to have a greatest relevance for private banking firms, with changes to the suitability & appropriateness requirements. The proposed rules broadly reflect requirements found in under the UK’s Retail Distribution Review. Conversely, private banking firms that have already faced the challenges of implementing the RDR are likely to be in a better position to absorb changes arising from MiFID II in comparison to EU counterparts.

<table>
<thead>
<tr>
<th>Area</th>
<th>Requirement</th>
</tr>
</thead>
</table>
| **Suitability & Appropriateness** | - **Knowledge & Competence of Portfolio Managers** - must be able to ensure and demonstrate to the competent authorities, upon request, that the natural persons giving advice possess the necessary knowledge and competence to fulfil their obligations.  
- **Suitability of Packed Products** – suitability must be considered for on an overall basis.  
- **Appropriateness vs PRIPs** - appropriateness regime will continue under MiFID II and should be considered alongside EU’s initiative on Packaged Retail Investment Products (PRIPs).  
- **Appropriateness of UCITS** - Firms will need to apply the appropriateness test when selling structured UCITS. |
| **Remuneration** | - **Ban on third-party remuneration for independent investment advice** - whereas adviser charging under the RDR applies to all retail investment advice.  
- **Ban on third-party remuneration for portfolio management** - Where portfolio management is typically remunerated through client fees, a ban on commission is unlikely to raise too many eyebrows. |
| **Best Execution** | - **Continued Focus on Best Execution.** Given that a wider range of execution venues are now available in the Union, it is appropriate to enhance the best execution framework for retail investors. |
| **Reporting** | - **Enhanced Client Reporting.** Private Banks will be required to disclose total costs of investments. Costs and fees must include hidden costs and fees in one figure. Costs must include all advice, platform, product and investment costs that affect the investment return and itemised statements must be issues at least once a year. |
| **Governance** | - **Product Approval Process.** Firms must have a product approval process that identifies a target market of end clients and has an appropriate distribution strategy. |
Governance
Key Changes and Impact

Key Changes

- MiFID II requires firms to comply with the governance requirements set out in the Capital Requirements Directive IV (CRD IV).
- MiFID II limits the number of directorships a management body may hold at the same time in different entities.
- ESMA will specify in more detail the standards and criteria for the requirements in relation to governance.

Impact for Private Banking Firms

- MiFID II formalises the expectations of regulators and industry best practices that some firms have been adopting with regard to governance.
- Management bodies should re-assess their governance structures well in advance of MiFID II. It is likely there will be a greater focus by regulators on individuals within senior management in performing their roles, greater use of attestations etc.

Management bodies need to understand fully its firm’s business activities.
- Management bodies need to define the firm’s risk profile and appetite.
- Must ensure that the management body is sufficiently diverse regarding age, gender, geographic provenance and educational and professional background.
- Combining too high a number of directorships would preclude the management body from spending adequate time on the performance of that oversight role.

The management body:
- Is accountable for defining and overseeing the:
  - Implementation of governance standards including monitoring and assessment of firms business activities against strategic objectives.
  - Organisation of the firm and segregation of duties; including the skills, knowledge and expertise required by personnel and the resources, procedures and arrangements for the provision of services and activities.
  - Effective identification and management of conflicts of interest. With a particular focus on the role management bodies play.

The management body is responsible for ensuring remuneration policy is designed to encourage:
- Responsible business conduct.
- Fair treatment of clients.
This must be implemented in line with CRD IV requirements.
Conflicts of Interest
Key Changes and Impact

There has recently been an increasing industry focus on conflicts of interests. In the UK, the FCA has conducted thematic reviews and required attestations from firms with regard to their conflict of interest control frameworks. MiFID II seeks to turn up the heat on conflicts of interest by increasing the expectations placed upon firms in how they ensure conflicts are identified and managed appropriately.

---

Extension of Conflict of Interest Regime

Investment Research
Dealing Commission
Gifts & Entertainment
Personal Account Dealing
Error Correction /Handling
Cross Fund Sales

---

Disclosure Requirements

- MiFID II conflict of interest disclosure requirements will require firms to disclose the steps that were taken to mitigate an identified conflict of interest.

- MiFID II will require firms to make disclosures in sufficient detail; taking into account the nature of the client in order to enable the client to make an informed decision with regard to the identified conflict.

- **The act of disclosure alone will no longer be acceptable!**

---

Impact on Private Banking Firms

- Focus on management body to have appropriate oversight of conflicts i.e. to be in receipt of conflict specific MI.

- Greater focus on wealth managers to identify key conflicts and ensure adequate management arrangements in place. Reliance can no longer be placed on generic disclosures.
The creation of MiFID II was partially driven by the desire to create further transparency and stability in common financial markets. As such, MiFID II seeks to change the market landscape by adjusting requirements and scope of market infrastructure firms. The changes to this area are likely to have a limited impact on private banking firms, depending upon the extent to which the relevant derivatives are traded.

**MiFID I Key Changes**

- Creation of a new multilateral trading venue (OTF) for eligible derivatives.
- Requirement to trade certain derivatives on a MiFID trading venue. The scope of this will be determined at level 2.
- Trading generally faces more regulations

**Impact for Private Banking Firms**

- For private banks that have outsourced their order execution capabilities, the introduction of OTFs will be of limited relevance.
Joining the Dots
Related Regulation

- MiFID II can be thought of as a regulatory nexus, sitting between a number of other European regulation, and even non-European regulation.
- Firms should consider the synergies during implementation.

**MiFID II**
- EMIR and MiFID will together more wholly implement the G20 commitments made in Pittsburgh with regard to the requirement for greater transparency in OTC and derivatives markets. EMIR will require OTC derivatives to be cleared through CCPs.
- MiFID II and MAD were proposed together and therefore provide more consistency to the regulations. MAD will be extended to cover the MiFID II OTFs.
- MiFID II requires investment firms to be compliant with CRD IV in relation to governance requirements. There is also likely to be links between the two regulations in terms of remuneration.

**Dodd-Frank**
- Dodd-Frank overlaps with MiFID II in a number of areas:
  - Transparency
  - Position limits & monitoring
  - Clearing obligations

**PRIPs**
- PRIPs aims to improve transparency in the investment market for retail investors by providing a Key Information Document (KID). The objectives of PRIP will have very significant parallels with suitability, appropriateness, conflicts of interest and inducements under MiFID.

**CRD IV**
- Those investment management firms captured by AIFMD should be considering how its compliance under this links to MiFID II. Specific consideration should be given to investor protection and remuneration requirements.
MiFID II requirements are not likely to ‘bite’ until Q1 of 2017. However, during Q2 of 2014, ESMA will publish a discussion paper regarding its approach to MiFID II Level 2 measures and will invite participants to submit comments. Following this, in Q4 of 2014, ESMA will take the feedback from this discussion paper and publish several consultation papers containing the draft technical standards and invite participants to submit comments.

- Publication in Official Journal
- European Parliament plenary vote
- ESMA Discussion paper on technical standards
- ESMA consultation on advice
- Entry into force

• Political agreement reached on MiFID II
• FCA internal MiFID II project begins

ESMA consultation on technical standards
ESMA delivers draft regulatory/implementing technical standards
Implementing measures finalised
National Transposition deadline
End of Q4 2016/Q1 2017 new rules take effect

Dates are estimates only
The MiFID II Discussion and Consultation papers have recently been published and provide insight into the areas where industry input is encouraged and can help shape the regulation. Outlined below are some of the areas identified by the discussion papers for industry input.

<table>
<thead>
<tr>
<th>Discussion Paper</th>
<th>Consultation Paper</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Investor Protection</strong></td>
<td><strong>Investor Protection</strong></td>
</tr>
<tr>
<td>• Authorisation</td>
<td>• Investment advice and the use of distribution channels</td>
</tr>
<tr>
<td>• Branch Establishment</td>
<td>• Product governance</td>
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<tr>
<td>• Publication of Best Execution data</td>
<td>• Conflicts of interest</td>
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<td></td>
<td>• Remuneration</td>
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<td></td>
<td>• Legitimacy of 3rd person inducements</td>
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<td></td>
<td>• Investment advice on an independent basis</td>
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<tr>
<td><strong>Transparency</strong></td>
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<tr>
<td>• Equity Pre and Post trade Transparency</td>
<td>• Suitability</td>
</tr>
<tr>
<td>• Scope of Non-Equity Financial Instruments</td>
<td>• Appropriateness</td>
</tr>
<tr>
<td>• Non-Equity Pre and Post Trade Requirements</td>
<td>• Reporting to Clients</td>
</tr>
<tr>
<td>• Trading Obligation for Derivatives</td>
<td>• Best Execution</td>
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<td></td>
<td>• Product Intervention</td>
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</tbody>
</table>
## MiFID II / MiFIR

### Setting the scene

<table>
<thead>
<tr>
<th>How did MiFID I change markets?</th>
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</thead>
<tbody>
<tr>
<td>• MiFID I <strong>increased competition in equity markets</strong> by introducing a new category of trading venue – a Multilateral Trading Facility (MTF). As a result, trading activity shifted away from the traditional exchanges to MTFs and the proportion of equity trading taking place OTC significantly reduced.</td>
</tr>
<tr>
<td>• However, competition brought <strong>unintended consequences</strong>, such as the fragmentation of trading information for price formation purposes.</td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>What changes does MiFID II / MiFIR introduce?</th>
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</thead>
<tbody>
<tr>
<td>• MiFID II / MiFIR Introduces a new category of trading venue for non-equities, the ‘<strong>organised trading facility</strong>’ (OTF), with the aim of bringing more OTC activity onto regulated and transparent venues.</td>
</tr>
<tr>
<td>• <strong>Mandatory trading</strong> on regulated venues for derivatives that are both clearing eligible and sufficiently liquid, as well as <strong>trading obligation for most equities</strong>.</td>
</tr>
<tr>
<td>• Increased competition in clearing, with obligation for <strong>CCPs</strong> and <strong>trading venues</strong> to provide <strong>non-discriminatory and transparent access</strong> to one another across all instruments.</td>
</tr>
<tr>
<td>• Expanded pre- and post-trade <strong>transparency regime</strong>.</td>
</tr>
<tr>
<td>• Enhanced <strong>investor protection</strong>.</td>
</tr>
<tr>
<td>• Changes in <strong>governance requirements</strong> and additional obligations in the area of the <strong>organisation</strong> of investment firms.</td>
</tr>
<tr>
<td>• Rules to curb <strong>high-frequency and algorithmic trading</strong>.</td>
</tr>
<tr>
<td>• Provisions on <strong>position management</strong> and <strong>limits</strong> for commodity derivatives.</td>
</tr>
<tr>
<td>• Improved access to the EU for provision of investment services by third country firms to professional clients, subject to positive <strong>equivalence assessment</strong> and registration with ESMA.</td>
</tr>
</tbody>
</table>
EU capital markets
Implications for market participants across the trade life cycle

1. Pre-trade
   - Operators of trading venues will need to publish the required pre-trade information for in-scope instruments.
   - Changes to existing waivers for equities to ensure greater proportion of trading ‘lit’.

2. Execution
   - Operators of trading venues and other platforms will need to re-design their platforms and comply with requirements, whilst taking into account expected increase in trading volume and competition on platforms.
   - Trading venues and market participants required to implement enhanced controls on algorithmic trading and HFT.
   - Investment firms should review potential conflicts of interest, particularly in the light of enhanced “best execution” rules.

3. Clearing
   - Trading venues and CCPs will face both opportunities and challenges from increased competition.

4. Reporting
   - Expanded scope of instruments to be publicly reported on a real-time basis.
   - Introduction of a ‘consolidated tape’ for equities.
   - Trading venues to apply commodity position limits.
Investor protection
Implications of new rules to strengthen investor protection

Direct and indirect scope changes
- Firms will need to apply the full MiFID II / MiFIR regime when selling or advising on structured deposits.
- Applicability of suitability and appropriateness rules on distribution of “own” financial instruments is clarified.
- MiFID II modifies the Insurance Mediation Directive (IMD) to the extent that the general loyalty duty, rules on conflicts of interest and general information conduct obligations will also apply to insurance-based investment products. Member States will also be able to prohibit inducements in relation to this type of insurance product.

Changes in relation to investment advice
- Introduction of the notion “independent” advice and related information requirement;
- Requirement to inform the client whether a periodic assessment of suitability will be provided;
- Requirement to provide written advice before the transaction is made.

Ban on third party inducements for independent investment advice and portfolio management (with Member State discretion for insurance investment products) and strengthened conflicts of interest rules
- Inducement rules will significantly affect investment advice business models in EU countries that have not already banned commission, with potential inconsistency in regimes across EU.
- Firms should assess their use of third party inducements and incentive structures for all investment services, regardless of client type, to ensure there are no conflicts of interest.
- New explicit obligations are included to avoid CoI in the area of remuneration or performance assessment of staff involved in the provision of services to clients.
**Investor protection**

**Implications of new rules to strengthen investor protection**

**Safeguarding of client assets**

- When retail client assets are involved, the possibility for firms to conclude title transfer financial collateral arrangements for the purpose of securing or otherwise covering their obligations is **limited**.

**Strengthened best execution rules**

- Firms should ensure that best execution for retail clients includes the **total cost**, that they are **not receiving any benefit for routing orders to a particular venue** that would be a conflict of interest and that they meet disclosure requirements.

**Introduction of product governance rules** e.g. firms must have a product approval process

- Product governance provisions are **extensive**. Firms should assess their product governance process for all products, **regardless of sophistication of target client**. Product governance and product knowledge are also made part of the general loyalty duty.

**Disclosure rules when an investment service is offered together with another service or product as a package**

- Firms should assess their use of packages e.g. offering advice alongside another service or product. Where packages compare unfavourably, this will be **more transparent to consumers**.

**Appropriate test when selling structured UCITS or certain other complex instruments e.g. shares or bonds that embed derivatives**

- Firms will need to consider whether they are selling financial instruments that are now classed as complex and, if so, apply the appropriateness test. This could **drive distributors towards less complex products**.

**ESMA, EBA and competent authorities provided with temporary product intervention powers**

- Product intervention rules may make firms more risk averse and **dampen innovation**.
# Third country regime

**More harmonised provision of investment services to EU**

## Objective

- The provision of investment services by third country firms into the EU is subject to national regimes and requirements as it was not harmonised under MiFID I.
- MiFID II / MiFIR seeks to introduce a more harmonised regime for third country firm access to the EU.

## Key third country proposals

- **Retail or ‘elective’ professional* clients:** MS will be able to decide whether to require third-country firms to establish a branch to provide investment services to retail and ‘elective’ professional clients in their MS. The branch would need to meet certain MiFID II / MiFIR requirements and be subject to authorisation and supervision in the MS.
- **Eligible counterparties or ‘per se’ professional clients:** subject to the third country receiving a positive equivalence assessment and registration with ESMA, third country firms will be able to provide investment services to eligible counterparties and ‘per se’ professional clients in the EU without a branch. Where a positive equivalence assessment has not been taken, the provision of investment services would remain subject to national regimes.

## Opportunities

- **Improved access:** Following a positive equivalence assessment and registration with ESMA, third country firms would have improved access to the EU for investment services to eligible counterparties and ‘per se’ professional clients.

## Risks/uncertainties

- **Uncertainty of equivalence assessments:** the third country firm cannot be certain that the third country will receive a positive equivalence assessment.
- **Uncertainty of national regimes:** national regimes vary across MS and MS may choose to change their national regime.
- **Exchange of information:** the third country would need to agree with MS on exchange of information related to tax matters prior to authorisation of third country firm branches. This may have implications regarding banking secrecy laws. It is currently unclear how the regime will apply to existing branches and therefore whether this is likely to affect both retail and professional clients.

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*’elective’ professional clients are retail clients that have waived protections in order to be treated as professional.*
**MiFID II / MiFIR**

Significant implications for EU capital markets

- **Increased competition** between trading venues and CCPs, driving down transaction costs
- **Inducements rules** will bring significant changes to distribution in many EU countries, with potential inconsistencies in regimes
- **Curbs on HFT and new requirements on trading venues** to promote financial stability
- **Increased volume of trading** on trading venues, particularly for derivatives
- **Unknown impact on liquidity** from transparency, HFT and commodity rules
- **Extended transparency requirements** to promote price formation and a narrowing of bid offer spreads
- **Third country firms** will have improved access to EU for professional clients (subject to equivalence assessment)

**MiFID II / MiFIR timeline**

<table>
<thead>
<tr>
<th>Key milestone</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1 14</td>
<td></td>
<td></td>
<td></td>
<td>3 Jan 17</td>
</tr>
<tr>
<td>Q2 14</td>
<td></td>
<td></td>
<td></td>
<td>Implementation date</td>
</tr>
<tr>
<td>Q3 14</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Q4 14</td>
<td></td>
<td>Dec 14: ESMA technical advice</td>
<td></td>
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<tr>
<td></td>
<td>Q3 14: Entry into force. MS will have 24 months to transpose the directive</td>
<td>June 2015 - ESMA to submit to the Commission final regulatory technical standards</td>
<td>June 2016 is the date by which the delegated acts under Level 2 must be transposed by member states (24 months after MiFID II enters into force).</td>
<td>3 July 2016: Member states to adopt and publish measures transposing the MiFID II Directive into national law.</td>
</tr>
<tr>
<td></td>
<td>Q2 14: Expected ESMA consultation on technical standards</td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td>April: European Parliament vote</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>14 Jan: Political agreement reached</td>
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</tbody>
</table>
FCA changing the approach on wholesale conduct
Trends that might translate to other EU countries

“We will take a more assertive and interventionist approach to risks caused by wholesale activities, not just when retail markets are directly affected but also in order to enhance trust and confidence in the integrity of markets” Clive Adamson, March 2013

- Following recent scandals in the UK, such as the manipulation of LIBOR and the mis-selling of interest rate hedging products to small and medium-sized enterprises, the FCA has a renewed focus on wholesale conduct.
- UK Firms should be prepared for more vigilance and earlier intervention from supervisors as wholesale conduct issues emerge.
- Competition and behavioural economics will play a greater role in future.

FCA areas of focus

1. Imbalances of knowledge, skills & market power
   - Some wholesale participants may need protection, given imbalances of knowledge, skills or market power.
   - The FCA has moved away from ‘caveat emptor’. It will act to protect a wider range of client relationships than before.

2. Consumer protection & market integrity
   - The FCA will no longer accept intervention is unnecessary just because counterparties are equally sophisticated.
   - Even if wholesale participants are evenly matched, their (mis)conduct can harm market integrity.

3. Retailisation
   - The FCA will look at wholesale products which end up being sold in retail markets – ‘retailisation’.
   - In many cases of mis-selling, products designed for a specific market were sold widely outside it.
UK supervisory wholesale conduct themes for 2014
Trends that might translate to other EU countries

<table>
<thead>
<tr>
<th>Product governance</th>
<th>• Continued focus by the FCA on firms promoting <strong>good customer outcomes and market integrity</strong> at each stage of the product lifecycle, with approach drawing on the <strong>treatment of retail business</strong>.</th>
</tr>
</thead>
</table>
| Transparency & competition | • **FCA strategic review of wholesale markets** – the FCA has signalled interest in asset management for institutional clients and equity underwriting by investment banks.  
  • Increased focus on **charging structures**, particularly in the asset management sector. |
| Asymmetrical information | • FCA concern where **one party knows significantly more than another** in transactions, for example, due to differences in expertise, complexity or poor disclosure. FCA yet to take specific action. |
| Conflicts of interest & incentives | • FCA focus on ensuring incentives are **aligned to good customer outcomes**.  
  • Conflicts of interest in **asset management** and **insurance broking** are under review.  
  • Increased focus on the **agency role of firms**.  
  • Review of the **use of dealing commissions** and of **best execution**. |
| Behavioural biases | • A **key part** of the FCA’s strategy. The FCA will be alert to **exploitation of behavioural biases**.  
  • Work to date has focussed on retail markets, but some of the considerations are relevant to wholesale markets also. |
| Benchmark manipulation | • Litigation and enforcement in relation to the **LIBOR scandal** is set to continue and regulators across the globe are investigating potential **misconduct in FX markets**. |
| Client assets | • The FCA is considering **fundamental changes to the client assets regime**. |
| Technology | • Focus on risks posed by evolving technology e.g. **algorithmic and high-frequency trading**. |
European Market Infrastructure Regulation (EMIR)

Overview

- In September 2009 G-20 Leaders agreed that 'All standardised OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties by end-2012 at the latest. OTC derivative contracts should be reported to trade repositories. Non-centrally cleared contracts should be subject to higher capital requirements'. EMIR provides the framework for implementing the bulk of these requirements in the EU and will be complemented by changes to the Markets in Financial Instruments Directive (MiFID II) and changes to the Capital Requirements Directive (CRD IV)

- EMIR introduces sweeping requirements aimed at reducing counterparty risk, improving transparency and mitigating systemic risk. The requirements will, in some shape or form, affect all participants in OTC derivative markets

- The scope is far reaching and covers the five main asset classes: interest rate, credit, foreign exchange (FX), commodity and equity derivatives

- Some relief from the clearing and margining requirements has been granted to non-financial firms, pension funds and intra-group transactions, although strict conditions apply

The four main pillars of EMIR

- All standardised OTC derivatives will be cleared through central counterparties (CCPs)

- Harmonised framework for the provision of clearing services within Europe

- Non-cleared derivatives will be subject to strengthened risk management requirements, including the need to collateralise positions

- All OTC and exchange traded derivatives will be reported to trade repositories (TRs)

- The legislative process to date has been long but the end goal is within sight and compliance dates are looming. Whilst the detail on the shape and form that margins for non-cleared trades will take is still unclear, firms now have sufficient clarity on the rest of the requirements to be actively stepping up their implementation plans, leveraging efforts with other regulatory change programmes where possible
EMIR - Regulatory response to the financial crisis
Addressing interconnectedness in OTC derivative markets

EMIR is a regulatory response to the risks arising from the interconnectedness in the OTC derivative markets

Problem

In the **bilateral model** each market participant has a legal relationship with, and separate (gross) exposure to each of the other participants, creating a tangled web of exposures

Solution

In the **CCP model**, each market participant has a legal relationship with and (gross) exposure to the CCP only, regardless of the identity of their counterparty in the underlying trade

#### Weaknesses exhibited during the crisis

<table>
<thead>
<tr>
<th>Counterparty credit risk</th>
<th>Lack of transparency</th>
<th>Weak risk management</th>
</tr>
</thead>
<tbody>
<tr>
<td>Possible systemic implications that a default or fear of a default can have due to the interconnected web of market participants</td>
<td>Regulators did not have sufficient oversight of global positions to detect the accumulation of pockets of risk within the financial system</td>
<td>Especially for bespoke transactions, led to realised losses in times of market stress</td>
</tr>
</tbody>
</table>

#### Regulatory response

- All standardised derivatives should be centrally cleared
- Non centrally cleared derivatives should be bilaterally collateralised and subject to higher capital requirements
- All OTC derivatives should be reported to a TR
- All standardised and sufficiently liquid OTC derivatives should be traded on an exchange or electronic trading platform
EMIR Timeline

**Clearing**
- 15 Mar – 15 Sep: CCPs apply for authorisation
- Q3: ESMA starts process to determine products to be cleared & timeframes
- Q2 2014: Firms clear derivatives business, 3 year phase in for non-financial firms

**Trade Reporting**
- 15 Mar 2013: TR registration begins
- July to September 2013: Reporting start date for credit and interest rates (if TR has registered before 1 April 2013)*
- 1 Jan 2014: Reporting start date for all other contracts (if TR has registered for product type before 1 October 2013)**
- Q3: ESMA starts process to determine products to be cleared & timeframes
- Q2 2014: Firms clear derivatives business, 3 year phase in for non-financial firms

**Risk mitigation for non-cleared trades**
- 15 Mar 2013: Requirements for confirmations enter into force
- 15 Sep 2013: Requirements for portfolio reconciliation, portfolio compression and dispute resolution enter into force

**Bilateral margin requirements**
- End Sep 2013: Finalisation of BCBS/IOSCO rules
- Jan 2015: Firms to exchange variation margins. From 2015 and phased in to 2019 firms to exchange initial margins

**Historical contracts:**
- Contracts outstanding on 16/08/12 and still outstanding on the reporting start date:
- Contracts outstanding on 16/08/12 that are closed on reporting start date:
- Contracts entered into on or after 16/08/12 that are closed on reporting start date:

*Where a TR registers after 1 April 2013 (credit and interest rates) or 1 October 2013 (other contracts) firms must start reporting within 90 days of the date of registration. If there is no TR registered by 1 July 2015 reports must be sent to ESMA
**Information on collateral must be reported 180 days later
EMIR: Indirect Clearing
Offering protection to indirect clients

The availability of indirect clearing is vital to ensure all market participants have access to CCPs. In many cases an indirect clearing arrangement will be the only way for firms to access central clearing. EMIR requires that such arrangements offer indirect clients an equivalent level of protection as clients in a default scenario.

- CMs that offer indirect clearing arrangements must do so on reasonable commercial and publicly disclosed terms.
- CM must be able to facilitate:
  - Omnibus segregation: separate records and accounts enabling each client to distinguish its assets and positions from those of its indirect clients; or
  - Individual segregation: separate records and accounts enabling each client to distinguish the assets and positions held for an indirect client from those held for other indirect clients.

Procedures for handling the default of a client providing indirect clearing
- A CM must establish a credible mechanism for transferring the positions and assets to an alternative client or CM. A client or CM is not obliged to take these positions unless there is a prior agreement to do so.
- A CM must have procedures which allow for the prompt liquidation of the assets and positions of indirect clients and to pay all monies due to the indirect clients.

Obligations on Clearing Members (CM)

• Contractual terms: A client must consult a CM on the terms of an indirect clearing arrangement which may affect their operations. The contract must include requirements on the client to honour all obligations of the indirect client towards the CM.
• Segregation: Clients providing indirect clearing services must keep separate records and accounts that enable them to distinguish between their own assets and positions and those held for the account of their indirect clients. They must offer indirect clients a choice between omnibus or individually segregated accounts, ensuring that indirect clients are fully informed of the risks associated with each option.
• Provision of information: A client must provide the CM with sufficient information to identify, monitor and manage any risks arising from facilitating indirect clearing. In the event of default of the client, all information held on its indirect clients must be made immediately available to the CM.

Obligations on clients
EMIR mandatory clearing requirements

Process for determining products that must be cleared

There will be a two-pronged approach for deciding which OTC derivative contracts will be centrally cleared on a mandatory basis

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**“Bottom Up”**

1. National competent authority authorises a CCP to clear a particular OTC derivative product class

2. National competent authority notifies ESMA

3. ESMA launches a public consultation and consults with the ESRB and where appropriate supervisors in third countries on whether product(s) should be subject to clearing obligations and the date from which it will take effect. ESMA has 6 months to make a decision

4. ESMA to develop technical standards and submit to the European Commission for endorsement

5. Details of clearing obligation published on ESMA’s public register including CCPs that can be used; product class; and the start date for clearing

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**“Top Down”**

1. ESMA has power on its own initiative to consider whether clearing obligations should apply when no CCP offers a product class for clearing

2. ESMA conducts a public hearing, consults with the ESRB and where appropriate supervisors in third countries

3. ESMA develops technical standards and submits to European Commission for endorsement

4. ESMA publishes call for development of proposal to clear that product class of derivative

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**Public Register**

ESMA will establish an on-line public register to identify the OTC derivative products subject to the clearing obligation. The register will also include details on authorised/recognised CCPs and the dates from which the clearing obligation takes effect as well as information on notifications to clear (before ESMA’s assessment) so that the market is kept informed of any possible clearing obligations
EMIR – Margin requirements
Non-cleared derivatives

Not all OTC derivatives will be suitable for central clearing. These positions will need to be collateralised to reduce risks within the financial system. EMIR provides a high-level framework and further detail is expected next year.

EMIR framework for margins for non-cleared derivatives

- Financial and non-financial counterparties (above the clearing threshold) must have **timely, accurate and appropriately segregated exchange of collateral**. This collateral should not be re-used
- The standards are still being drafted but collateral may be in the form of **initial margin (IM)**, **variation margin (VM)** or both
- The standards will also outline which types of assets will be **eligible for collateral**
- Valuation of collateral is expected to be done **daily**, with **haircuts** applied if necessary
- Financial counterparties will need to hold capital to manage the risk not covered by appropriate exchange of collateral

Draft international standards on margins for non-cleared derivatives are expected to be reflected in EMIR

**Margining rules: IM and VM must be exchanged** by all financial firms and systemically-important non-financial entities

**Initial Margin**
- IM should be exchanged by both parties on a gross basis. Margin must be immediately available and fully protected. Collateral collected as IM should not be re-hypothecated or re-used
- Can use a quantitative portfolio margin model (supervisor approved) or a standardised schedule to calculate IM
- To manage the liquidity impact of the proposed margining requirements a variety of IM thresholds are being considered, below which counterparties would have the option not to collect initial margin

**Variation Margin** - VM must be calculated and collected frequently (e.g. daily) for all non-cleared derivatives. The ‘full net current exposure’ must be used to calculate VM. Intragroup transactions to be subject to VM

**Eligible collateral** - Cash; high quality government and central bank securities; high quality corporate and covered bonds; equities included in major stock indices; and gold. The Basel Committee and IOSCO (International Organisation of Securities Commissions) has proposed a schedule for proposed standardised haircuts

**Exemptions**
- **Product**: Considering exempting foreign exchange swaps and forwards
- **Counterparties**: Non-financial entities that are not systemically-important, sovereigns and central banks
EMIR – MiFIR Reporting Requirements
Increasing transparency for trade and post trade derivatives

Counterparties and CCPs shall ensure that the details of any derivative contract (OTC and ETD) they have concluded and any modifications or termination of the contract are reported to the TR no later than the working day following the conclusion, modification or termination of the contract.

(Art. 9 EMIR Law)

1. Reporting requirements start as from February 2014 (all OTC and listed derivatives)
2. By the end of the day following the execution, the contract and all its characteristics are reported
3. Where no contracts are concluded, modified or terminated, no reports are expected, apart from the updates to valuations or collateral (as from august 2014)
4. Data to report:
   • Information on collateral can be reported on a portfolio or single transaction basis
   • Fields on the contract valuation, as maintained and valued by the CCP
   • Changes in market-to-market or market-to-model valuations on reported bilateral transactions
5. Counterparty ID is provided by a Legal Entity Identifier (LEI). Without LEI (apart for Natural persons), the reporting is not meeting ESMA requirements
6. Record keeping following termination of the contract:
   • at least 5 years for counterparties
   • at least 10 years for TRs

- All derivatives instruments have to reported to Trade Repository…
- ...By T+1...
- ...On a daily basis...
- ...Using new standardised identifiers...
- ..With record keeping for several years.
## EMIR Reporting Requirements

Large volume of information from multiple sources and open issues

<table>
<thead>
<tr>
<th>Counterparty data :</th>
<th>Common data :</th>
</tr>
</thead>
<tbody>
<tr>
<td>Where: back office static data</td>
<td>Where: static data / front and middle office and risk management data</td>
</tr>
<tr>
<td>Issues: LEI not yet available</td>
<td>Issues: UTI not standardised – Organisation between counterparties</td>
</tr>
</tbody>
</table>

### Counterparty data:
- Information related to the counterparties to the contract
- Reported separately by each counterparty or their appointed 3rd party
- 26 data fields
- The counterparties and the other entities (such as broking entity, CCP, clearing member, reporting entity) are identified based on a unique code (i.e. LEI)

### Common data:
- Contract Type
- Details on the transaction
- Risk mitigation / Reporting
- Clearing
- Modifications to the report

### Common data specific to each type of products
- Foreign Exchange
- Interest Rates
- Options
- Commodities

- Information pertaining to the derivative transactions executed between the two counterparties
- Common data reported must be agreed between both parties
- 59 data fields split into 5 sections
- The details of the transaction are reported by Unique Trade ID (UTI)
- The derivative products are identified by a unique product ID (UPI), which reflect the class and type of derivative
- Reporting log for the modification of data
- Specific information and fields are different from the class of derivatives being reported
- Not required to be reported if the UPI is reported in the Common data and contains all the information to be reported for the specific product
EMIR Reporting Requirements

Roles & Responsibilities for the Reporting framework

Options

1. Reporting by both counterparties
   - Counterparty A and B report separately to TR
   - It is possible for each party to report to a different TR
   - The TRs will reconcile the reported transactions via a Unique Trade ID (UTI)
   - Both parties have to ensure that common data are consistent across both reports for the same trade

2. Reporting by one counterparty on the behalf of the other
   - Counterparty B reports the Counterparty data of each party and only one copy of the Common data
   - The full set of details should still be provided by counterparty A to B, as long as the information is available

3. Reporting by a (single / different) 3rd Party on behalf of 1 or both counterparties
   - Conduct due diligence process of the reporting 3rd party
   - Data Liabilities remain on the counterparty
   - Voluntary delegation agreement, however the national authority can revoke the utilisation of a third party
   - Written agreement between the parties
The European Market Infrastructure Regulation (EMIR) will introduce mandatory clearing and reporting requirements for OTC derivatives contracts as well as additional requirements for central counterparties (CCPs) and trade repositories. The impact on EU entities is critical because 60% of Europe’s OTC derivative trading takes place in London.

Transactions involving non-EU counterparties raise a number of extraterritorial issues in the context of EMIR. On 3 September 2013 ESMA published reports with technical advice on equivalence standards with the US, Japan, Australia, Hong Kong, Singapore and Switzerland and further technical advice is expected. ESMA is due to make its decision on the registration of the first Trade Repositories by early November 2013. It is expected that no reporting will have to take place before February 2014.

### Key provisions for investment managers

<table>
<thead>
<tr>
<th>Reporting</th>
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<tbody>
<tr>
<td>All OTC derivatives contracts must be reported to trade repositories within one day of conclusion (includes contracts that are outstanding when EMIR enters into force). Trade repositories need to be authorised by ESMA or established in a third country and EU recognised.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Mandatory clearing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Standardised derivatives contracts (CCPs and ESMA will establish a list) must be cleared by a CCP. Investment managers will need to submit the details of the contract to a chosen clearing member and post additional margins.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Risk mitigation techniques</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bilaterally cleared OTC derivatives (not eligible for clearing) will be subject to formal requirements (in particular: higher capital charges, timely confirmation). Technical standards (e.g. confirmation time, criteria for using marking-to-model) expected.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Scope</th>
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<tbody>
<tr>
<td>The reporting requirement will apply to all counterparties. Mandatory clearing will apply to financial counterparties (MiFID firms, banks, insurances, AIFM, institutions for occupational retirement provision) and non-financial counterparties.</td>
</tr>
</tbody>
</table>

### Challenges

- **Performance**
  
  Increased costs could affect performance
  
  Cost-benefit analysis of using such products

- **Choice of clearing partners**
  
  Number, selection criteria, pricing models, systems modifications and new outsourcing agreements.

- **Risk Management**
  
  Concerns about CCPs’ ability to handle increased volumes /credit risk: Diversification vs. higher liquidity buffers?

- **Legal documents**
  
  Contracts and agreements to be negotiated and amended to be aligned with EMIR

- **Valuation**
  
  Approach to valuation of OTC derivatives to be determined
  
  Valuation process and controls over complex instruments

- **Collateral management and margins**
  
  Investment managers likely to face higher margins /collateral requirements (stricter rules for CCPs), eligible collateral /haircuts are an issue.
The European Market Infrastructure Regulation (EMIR) requires reporting of all derivative contracts to a trade repository (TR), clearing of certain OTC derivatives via a central counterparty (CCP) and risk mitigation techniques for non-cleared OTC derivatives. It also imposes requirements on CCPs and TRs.

On 8 October 2014, the Central Bank was appointed the sole NCA for EMIR by the Minister for Finance in Statutory Instrument S.I. 443 of 2014. The Central Bank of Ireland has issued Q&A which should be read in conjunction with the Q&A issued by each of the European Commission and ESMA.

For financial counterparties, supervision of EMIR compliance will be incorporated into the Central Bank’s risk-based approach for supervision (PRISM) where relevant. The role of supervising EMIR compliance by non-financial counterparties (NFCs) is new and a specialist EMIR unit has been established for this purpose. The EMIR unit will also process the various notifications and applications required by EMIR (e.g. applications for intragroup exemptions).

The Central Bank understands that larger NFCs will be required, under the forthcoming S.I., to submit a regulatory return on EMIR compliance sometime during 2015 and this is likely to commence after Q1, 2015. The Central Bank’s intention is that it will subsequently follow-up on any exceptions noted on a prioritised basis. It is likely that priority will be given to cases of large scale non-reporting or high-value exceptions.

The Central Bank does not have an approved or preferred TR. All ESMA registered TRs are equally acceptable in discharging reporting obligations. The requirement is for trades to be reported to a TR; therefore, a single entity could report different trades to different TRs. The important thing is that all trades are reported, not that they are reported to the same TR. The list of registered TRs is available on the ESMA website Registered-Trade-Repositories.

The Central Bank shall accept intragroup exemption requests in respect of the clearing obligation only after the initial RTS on clearing has entered into force (which is currently anticipated as being Q1 2015 for Interest Rate Swaps).

The Central Bank’s current planning is based on the following targets:-

- Q3-Q4 2014: Finalisation of supervisory approach, including details of the regulatory return, with industry consultation as appropriate.
- Q1 2015: Putting in place necessary administrative arrangements for online submission of documents to Central Bank with associated training or seminars. Incorporation of EMIR compliance into PRISM supervision of Financial Counterparties.
- Q2 2015: First submission of regulatory returns from larger NFCs.
- Q3 2015: Themed review of smaller NFCs on a sample basis to check that suitable arrangements are in place to report to Trade Repositories as required (taking account of any amendments to MiFID level 2 guidance). Reports from larger NFCs will continue (taking into account any updated guidance as per question 4).
- Q1 2016: Themed review of smaller NFCs on a sample basis to check accuracy of TR reports for Q4 2015. All large NFCs to have submitted reports to Central Bank.

Following the recent establishment of the Global LEI Foundation, Legal Entity Identifier Codes, are now available. All pre-LEI codes which have been obtained so far including CICI codes are now deemed LEI codes.

All counterparties should ensure that they have a LEI code and use it to report to TRs. For those counterparties who cannot obtain a LEI code, the assumption is that the individual (the client) will be dealing with Financial Counterparties and that the internal client code of that Financial Counterparty can still be used to identify the client for reporting purposes.

LEI codes can be obtained from any approved pre-LOU provider. The full updated list is available on the Regulatory Oversight Committee website LEI. The Irish Stock Exchange is an approved pre-LOU provider (see direct).

The Central Bank has no preference as to which pre-LOU the LEI Code is obtained from, however the LEI must be from an approved provider in the ROC list. Please note that the same reporting code must be used for all EMIR reporting submissions.
EMIR milestones

2012
- **August**
  - EMIR entered into force

2013
- **15 Mar**
  - Timely confirmation
    - Daily mark-to-market
- **15 Sep**
  - Portfolio reconciliation and compression

2014
- **12 Feb**
  - Reporting start date for OTC transactions
- **Late 2014/2015**
  - Technical standards
  - First clearing obligations likely, subject to phasing in

2015
- **1 July**
  - Deadline for reporting to ESMA of derivatives for which a TR is not available
- **1 Dec**
  - Anticipated date for variation margin requirements for uncleared derivative trades
Market Abuse Directive II

MAD solidified the framework for tackling market abuse and harmonised the rules on market abuse across the EU. In October 2011, the European Commission released a draft for revision of the MAD to address existing shortcomings, including regulatory gaps, such as coverage of products traded on unregulated markets, OTC instruments, commodities and inconsistent sanctions. The new proposals include a Regulation and Directive at level 1. The use of a Regulation represents a major change in the level of direct European regulation for EU firms.

Key provisions

• **Scope**: MAD applied to financial instruments which are admitted to trading on a regulated market. MAD II will cover instruments traded on MTFs and OTFs, as well as to any related OTC instruments which can have an effect on them (a noteworthy target being CDS). Also, emission allowances will be covered by the rules against insider trading, with specific disclosure requirements and exemption thresholds.

• **Attempted market manipulation**: Sanctions may be imposed even if the perpetrator does not succeed in actually trading. There is no onus on regulators to prove that the market was actually manipulated when investigating such behaviour.

• **Sanctions**: The Regulation introduces minimum rules for administrative measures, sanctions and fines (this does not prevent Member States from fixing higher standards). The proposals also introduce criminal offences of insider dealing and market manipulation.

• **SME exemptions**: The proposals include exemptions for SMEs not to maintain insider lists in certain circumstances. These complement pan-European initiatives to assist SMEs with obtaining financing.

Impact

MAD II is likely to raise the same questions as MAD in respect of who should and should not be on insider lists within the fund and its providers be they the administrator, portfolio manager, legal firms and/or auditors. With a wider number of instruments impacted one would expect these lists to grow. Defining what attempted market manipulation is and implementing procedures to prevent it will also pose a challenge.
Client Assets and Investor monies
A new regime for fund service providers

On the 30th March 2015, the new Investor Money Regulations were brought into effect by Statutory Instrument 105 of 2015, with corresponding Guidance Notes published by the Central Bank of Ireland.

These new rules apply to fund service providers, including administration firms who operate bank accounts for the collection and payment of money from and to investors in respect of subscriptions and redemptions in funds.

The new rules must be implemented by 1st April 2016 and will have a significant impact on the daily processes and controls for some firms. The high level of oversight afforded to client assets generally, coupled with the fact that these are brand new requirements, make it extremely important for firms to understand the requirements and how they can comply by the deadline.

There are many different banking models in operation across the fund servicing industry, so it will be necessary to unravel the new requirements from a contractual and technical perspective within each firm.

An alternative ‘Fund Asset Regime’ may be an option for some firms but this has yet to be defined and will undoubtedly require a significant control and oversight framework that is compliant with both the AIFMD and UCITS regulations.

### Core Principles

The Investor Money Regulations introduce six Core Principals – Segregation, Designation, Reconciliation, Daily calculation, Risk management, and Investor Money examination

### Segregation and Designation

- Investor money held separately to non-investor money
- Account designated ‘Collection Account’
- Obtain ‘Investor Money Facilities Letter’ from bank

### Reconciliation and Daily Calculation

- Daily reconciliation
- Segregation of duties
- Funding deficit in investor money resource

### Key stages

- **S.I. 105 of 2015 published 30 March 2015**
- **Central Bank Guidance published 30 March 2015**
- **12 months – industry engagement**
- **Effective Date 01 April 2016**

### Risk Management

- Produce an Investor Money Management Plan (IMMP)
- Appoint a Head of Investor Money Oversight (HIMO - PCF)
- Board to approve the IMMP

### Auditor Obligations

- Annual assurance report on compliance with obligations
- Due to Central Bank within 4 months of the financial year end of the fund service provider

### Key actions

#### Impact Assessment

- Assess if the investor money rules apply
- Assess if other options are available – such as the proposed ‘fund asset regime’
- Assess business and other implications of approach e.g. AML
- Understand market position through industry engagement

#### Implementation

- Appoint project team to develop an IMMP
- Develop processes and procedures and obtain board approval on the IMMP
- Appoint HIMO
Investor money regulations
What has changed?

**Client Asset Regulations**
Previously, the client asset requirements (CAR) in Ireland applied to all investment business firms. On the face of it, the CAR therefore applied to transfer agency activities in respect of subscriptions and redemptions, involving the transfer of monies to and from the fund through collection accounts. However, the “one size fits all” approach of the CAR posed many practical challenges in applying client asset rules to third party fund service providers, in effect making it unworkable.

As of 30th March 2015, there are now two regulations, the Client Asset Regulations for Investment Business Firms (replacing the regulations of 1 November 2007) and the new Investor Money Regulations which are specifically for fund service providers who own and operate collection accounts. The intention of the Central Bank of Ireland is to ensure that all Irish investment business firms are required to comply with a client asset regime in the interests of ensuring that any money due to clients or investors in funds is remote from the insolvency of the Irish firm. It should be noted that Irish authorised collective investment schemes are not in the scope of these regulations as fund assets continue to be subject to fund rules e.g. AIFMD and UCITS Notices. This may include collection accounts that are appropriately structured as fund assets.

**Treatment of collection accounts**
The treatment of collection accounts has been an area of ongoing concern for the Central Bank of Ireland for some time. In a review published in March 2012, reviewers appointed by the Central Bank articulated their view that monies passing through collection accounts are client assets within scope but acknowledged that for practical reasons the CAR are not applied to the operation of these accounts. The report stated: “We regard this lacuna as unsatisfactory. It is undesirable that no appropriate requirements to safeguard client assets are imposed at this stage of the process. This should be resolved.”

The Investor Money Regulations are the Central Bank of Ireland’s solution to these concerns. They bring fund service providers, and in particular, collection accounts, squarely into a client asset regime. There has been extensive industry engagement with the Central Bank of Ireland on this topic and the final regulations are the result of lengthy discussion and input from industry regarding the role and responsibilities of fund service providers in handling investor money. Nonetheless, it is likely that many fund service providers will need to examine their policies, procedures, systems and contractual arrangements in some detail, in order to ascertain what steps they will need to take to achieve compliance with the new regulations in the 12 month lead-in time.
The Central Bank of Ireland (CBI) published a consultation paper on corporate governance requirements for investment firms (CP94) on 5 May 2015. This proposed new regime of corporate governance will apply to investment firms, including all MiFID firms and non-retail investment intermediaries licensed or authorised by the CBI and designated as high, medium high or medium low impact under the CBI’s Probability Risk Impact System (PRISM). Additional requirements are proposed for firms designated as high and medium high impact. The requirements will not apply to firms designated as ‘low impact’ or to foreign incorporate subsidiaries of Irish firms. However, the former are encouraged to adopt the proposed regime while the latter are encouraged to adopt an equivalent regime.

CP94 proposes that firms will be required to comply with requirements for:

• Minimum board size;
• Board composition;
• The role of the Chairman;
• The role of the CEO;
• The frequency of board meetings; and
• The role and composition of both the risk committee and the audit committee.

The CBI proposes to introduce the new requirements on a statutory basis, subject to the transposition and imposition of MiFID II. The CBI will monitor adherence to the proposed regime through its ongoing supervision of firms. Any deviations must be reported to the CBI within 5 business days, as well as the proposed remedial action. Each firm must submit an annual compliance statement specifying whether the firm has complied with the requirements.

The consultation period for CP94 will close on 5 August 2015.
Tax developments
**Common Contractual Fund (CCF)**

**What is a CCF**

**Legal aspects**

- Different Unit Classes Possible
- Established by a Management Company
- UCITS and Non-UCITS
- Investors are ‘Co-Owners’ of Underlying Assets
- Not a Separate Legal Entity
- Regulated by Irish Central Bank
- Irish domiciled fund structure
- Single or Umbrella Structure
- Common Contractual Fund
- Contractual Deed
- Unincorporated Body
- ‘Units’ Issued

Initially designed for pension pooling but widened to general asset pooling

**Tax aspects**

- Irish tax transparent regulated fund product
- Transparency confirmed in Irish legislation
- Must be authorised by Central Bank of Ireland
- Must not be constituted under unit trust law or statute law (established under a contractual deed)
- Must not have unit holders who are individuals – institutional product only
- Designed so that taxes apply to the underlying investor and not the investment vehicle
- The relevant double tax treaty is the one between the investor and investment country

**Finance Act 2003**
- Introduction of CCF legislation
- UCITS only
- Only pension fund investors permitted

**Finance Act 2005**
- Enhanced CCF legislation
- Non UCITS included
- Institutional investors as well as pension funds
Common Contractual Fund (CCF)

Taxation of CCFs

- Tax Transparent
- No Irish Tax for Fund
- No Subscription Tax
- VAT Generally Not Applicable
- No WHT on Distributions Made
- No DIRT on Deposits Held
- No Net Asset Value Tax

Advantages of CCFs

- Economies of Scale
- Improved Tax Efficiency & Returns for Investors
- UCITS or non-UCITS
- Access to more Investment Managers
- Risk Management / Enhanced Corporate Governance
- Investment Diversification
- International Recognition

Investors
- Co-owners of underlying assets held pro-rata to their investment
- Investors need to consider tax treatment in home country
- Applicable Double Tax Treaty is that between the investor and investment country

Investments
- Consider local rules re returns from investment
- Applicable Double Tax Treaty is that between the investor and investment country
Common Contractual Fund (CCF)

**Transparency and Double Tax Treaties**

- One of the key considerations in designing the CCF was to ensure that an investor must not be at any tax disadvantage as a result of investing in a CCF.
- The investor should be in the same position as a result of investing in a CCF as if it had invested directly in the underlying assets.

- The tax transparent status of a CCF means that double-tax-treaty reliefs between the investor home jurisdiction and the jurisdiction in which the underlying investments are based should be available.
- Irish tax legislation confirms that a CCF is "transparent" for Irish tax purposes.
- The wording used in the Irish tax legislation replicates the language used in the US tax regulations governing transparent structures.
- Many new treaties confirm transparency of CCF in treaty partner location.

**Indicative Current Structure**

- Possible WHT on returns from investments / Investment Fund
- Higher administration costs in having multiple fund products/investments

**Possible Future Structure**

- Savings on WHT on returns from investment direct to tax exempt investors
- Economies of Scale
- Experience would show a saving of 10-20 basis points
- Enhanced Governance/Oversight
The Irish Real Estate Investment Trust (REIT) was introduced in the Finance Act 2013 as part of a government initiative to attract capital to the Irish property market by providing an attractive structure for income and capital appreciation.

A number of Irish REITs have been launched. Irish REITs are listed on the main market of a recognised stock exchange in an EU member state and attract fresh capital into the Irish property market thus improving the stability of the property market. It also allows smaller scale investors the opportunity to access quality commercial property returns in a regulated environment.

**Constitution and ownership**
- Must be Irish incorporated and tax resident
- Its shares must be listed on a recognised stock exchange in an EU member state
- Cannot be a closely controlled company (unless owned by certain “qualifying investors” such as pension funds, a QIAIF and NAMA)
- Ordinary shares can be of only one class. There can be fixed rate non voting preference shareholders

**Tax exemption**
- Tax exemption within the REIT in respect of the income and chargeable gains of a property rental business
- A Disposal of REIT shares does not attract Irish CGT for non-Irish resident investors
- The provisions allow a REIT to have 100% subsidiaries that also qualify for the tax exemption

**Tax charges**
- Property income dividends paid by the REIT are subject to Irish Dividend Withholding Tax (current rate 20%). Treaties may reduce the tax withheld.
- A tax charge will arise if the REIT pays a dividend to shareholders with 10% or more of the share capital, distribution or voting rights in the REIT (other than “qualifying investors” i.e. pension funds and others as defined)
- A corporation tax charge will arise where a property asset is developed at a cost exceeding 30% of its market value and sold within a three year period

**Costs of converting or transferring assets**
- Stamp duty, which is currently at 2%, will apply to properties acquired. A transfer of shares in a REIT will also be liable to stamp duty at a rate of 1%.
- Where a company converts to a REIT, whilst there is no conversion charge, there will be a deemed sale and reacquisition of its assets at market value on that date. This may not in some cases trigger capital gains given the market is recovering.
EU Financial Transactions Tax
Time to compromise?

On 9 October 2012 the EC announced that 11 member states support using the Enhanced Co-Operation Procedure (“ECP”) to implement a harmonised FTT in the EU. The 11 member states include Germany, France, Austria, Belgium, Portugal, Slovenia, Spain, Italy, Slovakia, Estonia and Greece (“FTT Zone”).

To date a unilateral French FTT has been introduced and became effective on 1 August 2012 and a unilateral Italian FTT became effective from 1 March 2013.

Ireland’s position remains unchanged, whereby Ireland could only support an FTT which is introduced on either a global or EU wide basis. Ireland, the UK and a number of other Member States will not participate in the introduction of an FTT via enhanced co-operation.

The UK challenged the legality of the Council decision to authorise enhanced cooperation on a common framework of FTT and the scope and objectives of the initial commission proposal, however the challenge was subsequently rejected by the Court of Justice of the European Union on procedural grounds.

On 6 May 2014, the members of the FTT zone (excluding Slovenia) released a brief statement announcing the following:

• Participating member states will work towards a “progressive implementation” (i.e. step by step) of the EU FTT
• The EU FTT will apply initially to equities and “some derivatives”
• The EU FTT will be introduced, at the latest, by 1 January 2016
• Member states which currently tax the transfer of other financial instruments will be permitted to continue to maintain existing taxes

It is anticipated, as a first step, an FTT will likely come into force under the ECP which applies tax on an issuance basis only to equity and equity derivative (however, as of May 2015 differences of opinion remain between the FTT zone countries as to what is out of scope). Nonetheless, in January 2015, members of the FTT zone re-affirmed their commitment to the FTT and are working towards a 1 January 2016 start date but a more realistic start date is 2017. Austria is chairing the FTT agenda and this is seen as a step change in trying to bring the FTT into effect.

Key impacts
• Costs - the increased costs are likely to be passed to customers
• Accounting and tax complexity – new policies, procedures and personnel with additional skill sets needed
• Business relocation – those businesses affected by a new tax or levy could consider relocating the affected parts of their operations.

Which geographical scope?
• Residence principle: A financial transaction is taxable in the EU if one party is a financial institution and at least one party is located in the EU
• Issuer principle: where the underlying financial instrument is “issued” in the FTT zone

Which financial institutions?
• UCITS, alternative investment funds and their managers
• Investment firms, banks, pension funds, holding companies, etc.
• Whether acting as party to a financial transaction (for own account or for the account of other persons), or acting in the name of a party to the transaction

Which transactions?
• Purchase and sale
• Securities lending / borrowing and repos
• Conclusion / Modification and trading of contracts
• Transfers of financial instruments between group entities
• Whether concluded on an organised market or OTC.
• Primary market transactions for shares and bonds exempted (subscription and redemption of fund units/shares not exempted)

Which financial instruments?
• All MiFID financial instruments as well as structured products (e.g. transferable securities, money-market instruments, units and shares in UCITS and AIF, forwards, futures, swaps, financial CFD).
• For derivatives: both the conclusion of the agreement and the delivery of financial instruments would be taxable

Operation of the FTT (under the original proposals)

• If passed, a tax of 0.1%, calculated on gross transactions before netting and settlement would be applied on a wide scope of financial transactions (except for transactions in derivatives, taxed at 0.01% of notional amount).
• Where two EU financial institutions enter a transaction, the FTT is paid by both parties (effectively doubling the rate). The FTT is also paid when an instrument moves within a group.
• The tax would be due the moment an electronic transaction is carried out or within three working days in all other cases.
The Foreign Account Tax Compliance Act (FATCA) is the US government’s initiative to ensure transparency in relation to offshore accounts held by US persons. FATCA imposes a 30% withholding tax on US source passive income, such as interest, dividends, rent and royalties, and also on gross proceeds from the disposition of assets which give rise to such passive income. This withholding will apply from 1 July 2014 unless foreign financial institutions (FFI), including non-US funds, enter into an agreement with the IRS and agree to annually report details of all US investors to the IRS and withhold tax on any “passthru” payments made to investors.

A series of intergovernmental agreements (IGAs) have been signed between various jurisdictions, including Ireland, and the US Treasury/IRS. These agreements enable FFIs to report locally and register for FATCA rather than having to sign an individual agreement with the IRS. Irish FIs have to report to the Irish Revenue under FATCA by 30 June 2015.

Key FATCA risks

**Reputational**
- The IRS published a list of all FATCA compliant global Financial Institutions on 2 June 2014.

**Commercial**
- Many FIs have announced that they will only conduct business with FATCA compliant counterparties, which could create serious commercial issues for non-compliant FIs.

**Legal**
- In Model 1 IGA jurisdictions, compliance with FATCA will be mandatory under local law.
- Irish FI’s must comply with Irish tax legislation
- Penalties will be applicable where a Reporting Financial Institution fails to provide/ provides inaccurate information.

**Future proofing**
- New FATCA equivalents are expected to increase the exchange of information going forward so it is important to act now to develop an approach that can be adapted.

Determining FATCA obligations

1. **Identify Financial Institutions**
2. **Identify Financial Accounts**
3. **Classify holders of Pre-existing Financial Accounts**
4. **Update on-boarding of new Financial Accounts**
5. **Identify reporting and withholding requirements**
6. **Report information on relevant accounts to relevant authority**

Key FATCA milestones

- **By 25 April 2014** FATCA registration
- **1 July 2014** Income withholding commences
- **By 22 December 2014** FATCA registration (Model 1 IGA)
- **30 June 2015** Enhanced review pre-existing high value a/cs
- **30 Sept. 2015** Exchange of reportable info for 2014
- **30 June 2016** Review of pre-existing entity and lower value a/cs
- **30 Sept. 2016** Exchange of reportable info for 2015

Entity Classification
- Classify entities in the reporting financial institution’s group. Note a non-complying entity will not prevent compliance by others

Withholding
- Under the Irish IGA Irish FIs will not be subject to withholding tax on US source income. However Non-Participating FIs in non-partner countries may still be subject to withholding at source on US sourced withholdable payments

Reporting

Pre-existing accounts classification
- Identifying relevant in scope Financial Accounts. Search pre-existing individual and entity accounts to classify them for FATCA purposes and identify US Reportable Accounts

Agreements
- Register with IRS to report as required. Registration for Irish FIs must have occurred by 31 December 2014.

Compliance
- Compliance enforced by various measures under IGA, including classification as Non-Participating where significant non-compliance and anti-avoidance measures

New Account requirements
- Ensure on-boarding processes capture ‘self certification’ data and that the reasonableness of such data can then be confirmed based on FI’s internal information
# EMEA: IGAs in negotiations and IGAs signed to date *

## Europe

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## Europe (cont.)

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*Treasury updates as of 6/1/2015*
# Americas: IGAs in negotiations and IGAs signed to date *

## Americas

### North America
- **Canada**  
  Model 1 (02/05/14)
- **Mexico**  
  Model 1 (11/19/12)

### Caribbean
- **Anguilla**  
  (UK’s Overseas Territories)  
  Model 1 (06/30/14)
- **Antigua and Barbuda**  
  Model 1 (06/03/14)
- **Bahamas**  
  Model 1 (11/03/14)
- **Barbados**  
  Model 1 (11/17/14)
- **Bermuda**  
  (UK’s Overseas Territories)  
  Model 2 (12/19/13)
- **British Virgin Islands**  
  (UK’s Overseas Territories)  
  Model 1 (06/30/14)
- **Cayman Islands**  
  (UK’s Overseas Territories)  
  Model 1 (11/29/13)
- **Cuba**  
  TBD
- **Curacao**  
  Model 1 (12/16/14)
- **Dominica**  
  Model 1 (06/19/14)
- **Dominican Republic**  
  Model 1 (06/30/14)
- **Grenada**  
  Model 1 (06/16/14)
- **Haiti**  
  Model 1 (06/30/14)
- **Jamaica**  
  Model 1 (05/01/14)
- **Montserrat**  
  Model 1 (11/30/14)
- **Saint Kitts and Nevis**  
  Model 1 (06/04/14)
- **Saint Lucia**  
  Model 1 (06/12/14)
- **Saint Maarten**  
  TBD
- **Saint Vincent and the Grenadines**  
  Model 1 (06/02/14)
- **Trinidad and Tobago**  
  Model 1 (11/30/14)
- **Turks and Caicos Island**  
  (UK’s Overseas Territories)  
  Model 1 (12/01/14)

### Central America
- **Belize**  
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- **Costa Rica**  
  Model 1 (11/26/13)
- **El Salvador**  
  TBD
- **Guatemala**  
  TBD
- **Honduras**  
  Model 1 (03/31/14)
- **Nicaragua**  
  Model 2 (06/30/14)
- **Panama**  
  Model 1 (05/01/14)

### South America
- **Argentina**  
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- **Bolivia**  
  TBD
- **Brazil**  
  Model 1 (09/23/14)
- **Chile**  
  Model 2 (03/05/14)
- **Colombia**  
  Model 1 (05/20/15)
- **Ecuador**  
  TBD
- **Guyana**  
  Model 1 (06/24/14)
- **Paraguay**  
  Model 2 (06/06/14)
- **Peru**  
  Model 1 (05/01/14)
- **Suriname**  
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- **Uruguay**  
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- **Venezuela**  
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*Treasury updates as of 6/11/2015*
## APAC: IGAs in negotiations and IGAs signed to date *

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### Australia-Oceania

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* Treasury updates as of 6/11/2015

- Model 1 IGAs signed
- Model 2 IGAs signed
- Agreed to in Substance

There are 15 action items as part of BEPS – 7 of which were addressed in the September 2014 papers issued (see items in bold below).

- **Digital economy**
- **Hybrid mismatches**
  - **Treaty abuse**
  - **Transfer pricing documentation**
  - **Transfer pricing of intangibles (1)**
- **Preferential tax regimes**
- **CFC rules**
  - Permanent establishments
- **Transfer pricing of intangibles (2), risks and capital, other**
- **Disclosure of aggressive tax planning**
  - Dispute resolution
  - Data collection and analysis measuring BEPS
- **Interest deductions**
- **Harmful tax practices**
- **Multilateral instrument to address BEPS**

### Timeline

- **November 2012**: G20 leaders met in Cairns, Australia.
- **February 2013**: OECD released "Addressing Base Erosion and Profit Shifting".
- **May 2013**: Forum of Tax Administration meeting.
- **June 2013**: OECD’s Committee on Fiscal Affairs to agree action plan.
- **July 2013**: OECD’s Action Plan delivered to G20 Finance Ministers.

- **September 2014**: The OECD published its Action Plan on Base Erosion and Profit Shifting ("BEPS") in July of 2013.
  - 7 of which were addressed in the September 2014 papers issued (see items in bold below).

- **September 2015**

- **December 2015**
  - **Interest deductions**
  - **Harmful tax practices**

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Seven papers issued 16 September 2014
Quick review of critical matters

**Action 1: Digital Economy**
- No separate digital economy
- Other work streams to provide solutions?

**Action 2: Hybrids**
- Paper stresses that double non-taxation is unacceptable in principle
- Detailed guidance to enact laws scheduled by September 2015
- 25% control threshold
- Requires (1) a hybrid and (2) either DNI or DD

**Action 5: Harmful tax practices**
- Exchange of information between tax authorities – rulings & TP
- Need for substantial activities for “preferential” regimes – Nexus gaining ground

**Action 6: Treaty abuse**
- No Consensus in principle, not in detail (LOB v Purpose)
- Further consultation during 2015
- Recognises OECD 2010 report and the specific issues for funds

**Action 8: Transfer pricing intangibles**
- Very similar in context to July 2013 paper
- Section B held – adoption of guidance delayed until 2015
- Could cause a significant change in TP outcomes
- Emphasis on functions performed, assets used and risks incurred

**Action 13: TP documentation /CbC reporting**
- C by C limited items / No agreement on practicalities – further delay
- Masterfile / local file
- Risk of increased burden

**Action 15: Multilateral instrument**
- Paper outlining how to achieve multilateral agreement
WIP until September 2015

Key Themes

- Transparent structures need further consideration and BEPS could be an opportunity
- Offshore fund regimes may need updating
- Recognition of the challenges for Funds re Treaty access
- Rules for on-market repos/stock lending to be further refined
### What we would like to see in September 2015 papers

| Action 6 – Treaties | • Ideally carve out for funds in any LOB wording in a treaty  
| | • If not a complete carve out, then suitable derivative benefits provision to facilitate funds accessing treaties  
| | • GAAR/PPT rule should provide certainty for funds given 2010 OECD report |
| Action 2 – Hybrids | • Ensuring funds are not disadvantaged by EPM - repo/stock lending  
| | • Greater recognition within OECD/G20 for tax transparent fund structures |
| Action 15 – Multilateral Agreement | • Suitable incorporation of funds into the multilateral agreement |
Withholding tax
Reclaim Opportunities

Global portfolio investors may be eligible to claim repayment of withholding tax on investments in European equities and bonds imposed by an EU Member State, which is not already recoverable under a double tax treaty or domestic exemption, and has not been offset against a domestic tax.

There may be opportunities to file a protective claim for the repayment of such withholding tax based on an analysis of EU Non-Discrimination Articles and both domestic and European case law. This opportunity is of particular relevance to funds. Claims can generally be quantified through liaison with custodians. Case law was developed significantly in 2012 to strengthen the claim basis and depending on fact patterns; withholding tax claims may be available in up to 15 EU markets.

A number of cases are currently in the pipeline in various EU territories court systems, from which many claimants may benefit.

- There are strict limitation periods enforced by each EU Member State for filing withholding tax reclaims. As time passes, older claims will lapse as limitation periods expire.
- Funds and custodian firms are already in the process of requesting data to quantify and support claims.
- Claims can be made in a number of EU markets for open limitation periods, typically between 3-5 years.
- Tax regimes in EU territories are however already looking to enact policy changes to make recovery claims more challenging.
- Generally, one year’s worth of claim entitlement will expire at the end of each year so now is the time to act to potentially receive benefit and to take full advantage of any potential claims.

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Indicates territories that have made payments

Withholding tax basis in EU law:
Tax exempt example - UCITS

- Member state 1
  - Tax exempt portfolio investor (UCIT)
  - Dividend payment 0% WHT

- Member state 2
  - Tax exempt non-resident portfolio investor (UCIT)
  - Dividend payment e.g. 15% WHT

- Member state 1
  - Company

- The lower return for a non-resident investor acts as a disincentive to invest compared to a resident investor.
- A number of EU territories have WHT rules that charge WHT on payments to non-residents but no such WHT is levied on payments to residents. Further, the non-residents are unable to use the WHT credits against a domestic tax liability.
- Therefore the non-resident may be less inclined to invest in the EU internal market.
- Rules that disincentivise the harmonisation of the EU internal market is regarded as contrary to EU law.
- The European Commission has commenced infringement procedures, which are supportive of the claim principles above, against a number of member states.
- There is strong EU jurisprudence which confirms the claim principles: Denvakit (C-170/05), Amurta (C-379/07), Aberdeen (C-303/07), Italy v Commission (C-540/07), Commission v Germany (C-284/09), Commission v Portugal (C-493/09), Santander (C-338/11 to C-347/11), et al.
**EU WHT Claims**

Example of claim territories and limitation periods

<table>
<thead>
<tr>
<th>Country*</th>
<th>Limitation Period</th>
<th>If claimed in 2014, open periods</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>5 years</td>
<td>1 January 2009</td>
</tr>
<tr>
<td>Belgium</td>
<td>5 years**</td>
<td>1 January 2010 (alternative 10 year)</td>
</tr>
<tr>
<td>Denmark (rolling limitation)</td>
<td>3 years</td>
<td>1 October 2011 (if filed by 30 September 2014)</td>
</tr>
<tr>
<td>Finland</td>
<td>5 years**</td>
<td>1 January 2009 (alternative 6 year)</td>
</tr>
<tr>
<td>France</td>
<td>3 years from 2012**</td>
<td>1 January 2009 (alternative 2 year)</td>
</tr>
<tr>
<td>Germany</td>
<td>4 years</td>
<td>1 January 2010 (alternative 1 year)</td>
</tr>
<tr>
<td>Italy (rolling limitation)</td>
<td>4 years</td>
<td>1 October 2010 (if filed by 30 September 2014)</td>
</tr>
<tr>
<td>Netherlands</td>
<td>3 years**</td>
<td>1 January 2011 (alternative 5 year)</td>
</tr>
<tr>
<td>Poland</td>
<td>5 years**</td>
<td>1 January 2009 (alternative 5 year rolling as Italy)</td>
</tr>
<tr>
<td>Portugal</td>
<td>2 years</td>
<td>1 January 2012</td>
</tr>
<tr>
<td>Spain (quarterly filings)</td>
<td>4 years</td>
<td>1 July 2010 (if filed by 20 October 2014)</td>
</tr>
<tr>
<td>Sweden</td>
<td>5 years</td>
<td>1 January 2009</td>
</tr>
</tbody>
</table>

*This list is not exhaustive and certain investor types may not have reclaim opportunities in some territories e.g. where full tax relief is already available through DTC or a Domestic investor in the territory also suffers tax (e.g. US pensions or Charities may get relief under DTC already in certain territories).

** Certain alternative limitation period arguments can apply in some territories, however it is advisable for cost/benefit purposes to use the above limitation periods.
Accounting developments
Accounting developments

Impact of EU audit reform proposals

Status of EU audit legislation

- Following more than two years of debate, a preliminary agreement was reached on 17 December 2013 by participants in the EU legislative process:
  - European Parliament negotiators
  - Lithuanian Council Presidency (representing 28 member states)
  - European Commission
- Two forms of legislation:
  - Directive – amends the current Statutory Audit Directive, applying to "all" statutory audits and would need to be transposed into national law by each member state
  - Regulation – requirements will govern statutory audits of Public Interest Entities and would apply throughout the EU upon effective date
- The new legislation came into force on 16 June 2014. Key measures include strengthening the independence of statutory auditors, making the audit report more informative and improving audit supervision throughout the union. Stricter requirements will apply to public-interest entities.
- There is a two year transition period which means that the legislation will become applicable (and is mandatory) in all 28 Member States of the EU as from 17 June 2016, consequently all stakeholders need to begin to plan now for the new rules.
- The Directive will require domestic legislation to be transposed into National Law and this will be achieved primarily by a statutory instrument.

Expected date of application: Regulation and Directive

- March 2014
- 27 May 2014
- 16 June 2014
- June 2016

Definition of public interest entity (PIE)

- The PIE definition:
  - Companies listed on EU regulated market and governed by the law of an EU member state
  - Credit institutions authorised by EU member state authorities
  - Insurance undertakings authorized by EU member state authorities
  - Other entities a member state may choose to designate as a PIE
- Extraterritorial implications:
  - Non-EU companies that are listed on regulated markets in the EU do not appear to qualify as PIEs
  - EU branch offices of non-EU credit institutions and non-EU insurance undertakings appear to qualify as PIEs
  - EU subsidiaries of non-EU parents appear to qualify as PIEs if the subsidiaries themselves fit the criteria

* Except where mandatory firm rotation transitional measures apply

Adoption or Regulation and Directive
Publication in official journal
Entry into force
Regulation comes into effect* - Directive should be transposed in national law

<+20 Days → <+2 Years→
Impact of EU audit reform proposals

### Mandatory audit firm rotation
- Audit firm appointments for statutory audits of PIEs to last for at least one-year term which is renewable
- Maximum duration of audit engagement not to exceed 10 years,* unless a member state decides to extend rotation period to:
  - Maximum 20 years in case of tendering, or
  - Maximum 24 years in case of joint audit
- Competent member state authority (for instance audit oversight authority and/or securities regulator) may extend auditor appointment on an exceptional basis for a further two-year term
- Four year cooling off period after the end of the statutory audit services before audit firm can undertake the audit of the entity again
- PIE to perform a transparent audit tendering process with close involvement of audit committee when a tender does occur

*Member state option to set a maximum duration of less than 10 years

### Non-audit services (NAS)
- Audit firms and network members prohibited from providing certain NAS
  - Such NAS not to be directly or indirectly provided by the audit firm or network members to the audited PIE, its parent undertaking or its controlled undertakings in the EU, during a period covered by audited financial statements and until issuing of the audit report (next slide)
- Other NAS permitted to be provided to the audited PIE subject to audit committee approval
- Member states may prohibit additional non-audit services and establish stricter rules for NAS which are not prohibited
- Member states may adopt legislation allowing valuation services and certain tax services, providing that these services have no direct effect, or have an immaterial effect, on the audited financial statements
- Fees for permissible NAS provided by the audit firm not to exceed 70% of the average fees paid in the last three consecutive financial years for statutory audits of the PIE and, where applicable, its parent or controlled undertakings, and of the group consolidated financial statements
- Cooling-in period for the design and implementation of internal control or risk management procedures related to the preparation and/or control of financial information or financial information technology systems applies during the fiscal year prior to the period covered by the audited financial statements
- No cooling-off period

### Timeline for transitional measures - mandatory audit firm rotation – (subject to further interpretation as the Regulation is finalised)

<table>
<thead>
<tr>
<th>Adoption of Regulation</th>
<th>February 2014</th>
<th>Publication in Official Journal</th>
<th>March 2014</th>
<th>Entry into force</th>
<th>Effective Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>20 Days</td>
<td>27 May 2014</td>
<td>16 June 2014</td>
<td>June 2016</td>
<td>6 Years</td>
<td>June 2016</td>
</tr>
<tr>
<td>2 Years</td>
<td></td>
<td></td>
<td></td>
<td>9 Years</td>
<td>June 2020</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>10 Years</td>
<td>June 2023</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>June 2024 (or 2026*)</td>
</tr>
</tbody>
</table>

*If 10-year period starts at effective date rather than entry into force – clarification being sought.
^Or less if member state opts to reduce 10-year maximum.
**Current status and timetable**

**Classification & Measurement**
- Most recent version of standard published Oct 2010
- ED proposing limited amendments published Nov 2012
- Amended standard in July 2014

**Impairment**
- Most recent ED published March 2013
- Final standard issued in July 2014

**General Hedge Accounting**
- Published as final in November 2013

**Classification of financial assets**

- **Are the cash flows considered to be solely principal and interest?**
  - Yes: Hold to collect contractual cash flows
  - No: Amortised cost

- **What is the business model?**
  - Hold to collect contractual cash flows AND to sell
    - FVTPL Option
  - All other strategies
    - FVOCI
    - FVTPL Option
    - FVTPL

- **What is the measurement category?**
  - Amortised cost
    - FVOCI option for equity investments with dividends in P&L
  - FVOCI
  - FVTPL

- **Are alternative options available?**
  - Yes
  - No

**Mandatory effective date removed from IFRS 9(2014). New mandatory effective date expected to be set as 1 Jan 2018 on completion of final phases. Restated comparatives are not expected to be required**

**Reclassifications are required if change in business model**
**Impairment - Expected credit losses**

**General approach**

- **Reporting date**
  - 12-month expected losses
  - Significant increase in credit risk
    - **Exception:** low credit risk ('investment grade')
  - Purchased/originated credit-impaired and short term trade receivables
  - Policy choice: trade/lease receivables
  - Lifetime expected losses

**Hedge Accounting**

**Objectives**

- Reflect in financial statements the effect of an entity’s risk management activities
- Introduce a more principle-based approach
- Align hedge accounting more closely with risk management

**IFRS 9**

No longer “low credit risk”
IFRS 15 - Revenue from Contracts with Customers

The IASB and FASB initiated a joint project to clarify the principles for recognising revenue and to develop a common revenue standard for IFRSs and US GAAP – IFRS 15

The standard is to be applied on an individual contract basis. However, a portfolio approach is permitted provided it is reasonably expected that the impact on the financial statements will not be materially different from applying the Standard on an individual contract basis.

IFRS 15 is effective for reporting periods on or beginning after 1 January 2017, with earlier application permitted.

Within the scope of IFRS 15:

- All contracts with customers except those that are within the scope of other IFRSs, such as leases, insurance contracts, and financial instruments [IFRS 15:5]

Not within the scope of IFRS 15:

- The recognition of interest and dividend income are not in scope of the new Standard

- Transfers of assets that are not related to the entity’s ordinary activities (such as the sale of property, plant and equipment, real estate or intangible assets) will also be required to follow some of the recognition and measurement requirements of the new model.

- The new standard does not apply to non-monetary exchanges between entities in the same line of business where this is done to facilitate sales to customers, or potential customers.
IFRS 15 - Revenue from Contracts with Customers

Accounting requirements for revenue – The five-step model framework

- **Step 1** Identify the contract with a customer
- **Step 2** Identify the performance obligations in the contract
- **Step 3** Determine the transaction price
- **Step 4** Allocate the transaction price to the performance obligations in the contract
- **Step 5** Recognise revenue when (or as) the entity satisfies a performance obligation

Identify distinct performance obligations ("unbundling")

Implications for the Investment management sector

- **When should variable or uncertain revenues be recognised?**
  - Contracts in the IM sector will often include significant variable elements, such as performance fees.
  - New requirements – variable consideration is only included in the transaction price if it is highly probable that the amount of revenue recognised would not be subject to significant future reversals as a result of subsequent re-estimation. This may impact how managers record performance fees.
  - In certain scenarios, a significant degree of judgement will be required to estimate the amount of consideration that should be taken into account.

- **When should ‘upfront’ fees be recognised?**
  - An ‘upfront’ fee should be regarded as an advance payment for future goods and services, and should be recognised as revenue when those goods and services are provided (unless control of distinct goods and services is transferred to the customer at the outset).

- **Should contract costs be capitalised?**
  - IFRS 15 distinguishes between costs in obtaining a contract and costs of fulfilling a contract
  - Issue for IM sector as significant costs are incurred that are directly attributable to obtaining contracts with customers, for example, through ‘success fees’ (e.g. commissions only payable if contract is obtained).
  - New standard requires entities to capitalise success fees, which will have an impact on operating profits.
  - Also, the new standard requires capitalised contract costs to be amortised on a systematic basis that is consistent with the pattern of transfer of the goods or services.

Contract approval, each party’s rights identified, payment terms identified, commercial substance, consideration is probable
Choosing your GAAP
<table>
<thead>
<tr>
<th>Theme</th>
<th>IFRS</th>
<th>FRS 102</th>
<th>Existing Irish GAAP</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Overall effort expected to complete transition</strong></td>
<td>Low</td>
<td>Moderate</td>
<td>N/A</td>
</tr>
<tr>
<td>Irish GAAP and IFRS have been undergoing a convergence and therefore only minor differences currently exist between Irish GAAP and IFRS. The key difference is the requirement to include a Cash Flow Statement.</td>
<td>Judgment will be required to determine the necessary changes to your existing accounting policies and disclosure requirements. Any changes required are likely to be simplification rather than requiring enhancement which may be of some on-going benefit to the Fund.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Investor Considerations</strong></td>
<td>Internationally Recognised</td>
<td>Less Recognised</td>
<td>N/A</td>
</tr>
<tr>
<td>It is necessary to consider whether investors will have any preference for IFRS over FRS 102. In our experience investors have not previously challenged Irish or UK GAAP and so there is no reason to believe that they would raise any concerns over moving to FRS 102.</td>
<td></td>
<td>Existing Irish GAAP is no longer available for use.</td>
<td></td>
</tr>
<tr>
<td><strong>Financial Instrument Disclosures</strong></td>
<td>Limited Change Required</td>
<td>Reduced Disclosures</td>
<td>Almost Identical to IFRS</td>
</tr>
<tr>
<td>No changes to the existing recognition and measurement policies or to the disclosures would be required. Key difference between Irish GAAP and IFRS is that Irish GAAP did not require ‘Off-setting’ disclosures required under IFRS and US GAAP. This will be relevant to the Fund as there are some offsetting arrangements in place (For example Repos).</td>
<td>FRS 102 introduces simplified disclosure requirements for Financial Instruments. A divergence between the ‘Leveling’ of investments may exist between FRS 102 and IFRS whereby certain investments which are valued based on a modelled price may fall into ‘Level 3’ under FRS 102 rather than ‘Level 2’ under IFRS. This could be relevant to the Fund if any investments held in the future are based on modelled prices.</td>
<td></td>
<td>Key difference between Irish GAAP and IFRS is that Irish GAAP did not require ‘Off-setting’ Disclosures required under IFRS and US GAAP.</td>
</tr>
<tr>
<td>Theme</td>
<td>IFRS</td>
<td>FRS 102</td>
<td>Existing Irish GAAP</td>
</tr>
<tr>
<td>----------------------------</td>
<td>-------------------------------------</td>
<td>----------------------------------------</td>
<td>---------------------</td>
</tr>
<tr>
<td>Valuation of Investments</td>
<td><strong>Fair Value Pricing</strong></td>
<td><strong>Fair Value Pricing</strong></td>
<td><strong>Fair Value Pricing</strong></td>
</tr>
<tr>
<td></td>
<td>Bid / Ask pricing is not strictly required under IFRS 13 although fair value methodology needs to represent exit price. Mid-price may be used as a practical expedient.</td>
<td>Section 12 of FRS 102 requires Bid / Ask pricing. However, there is an option under FRS 102 to choose to adopt the recognition and measurement principles of IFRS which among other things would eliminate the strict requirement to apply Bid / Ask pricing.</td>
<td>Under FRS 26 Bid / Ask pricing is required.</td>
</tr>
<tr>
<td>Ongoing Frequency of Updates</td>
<td><strong>Frequent Updates Possible</strong></td>
<td><strong>Limited Updates</strong></td>
<td>N/A</td>
</tr>
<tr>
<td></td>
<td>FRS 102 will only be updated every 3 years and at this point changes under IFRS that occurred during the interim period may then be introduced to FRS 102.</td>
<td></td>
<td>Existing Irish GAAP was generally updated in line with IFRS.</td>
</tr>
<tr>
<td>Complexity of Standards</td>
<td><strong>Complex Standards</strong></td>
<td><strong>Reduced Complexity</strong></td>
<td>Almost Identical to IFRS</td>
</tr>
<tr>
<td></td>
<td>FRS 102 comprises only 226 pages.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Requirement to include a Cash flow Statement</td>
<td><strong>Always Required</strong></td>
<td><strong>May Not `Be Required</strong></td>
<td>May Not Be Required</td>
</tr>
<tr>
<td></td>
<td>IFRS requires a cash flow statement to be provided in all cases</td>
<td>Exemption exists for open ended investment funds with liquid investments from providing a cash flow statement.</td>
<td>Exemption exists for open ended investment funds with liquid investments from providing a cash flow statement.</td>
</tr>
<tr>
<td>Consolidation Exemption</td>
<td><strong>Exemption for “Investment Entities”</strong></td>
<td><strong>Exemption where held for “Subsequent Resale”</strong></td>
<td><strong>Subsidiaries are required to be consolidated</strong></td>
</tr>
<tr>
<td></td>
<td>IFRS 10 includes a specific consolidation exemption for subsidiaries where an entity meets the definition of an “Investment Entity”</td>
<td>Exemption exists from consolidating subsidiaries where they are held for subsequent resale. The exemption doesn’t go quite as far as IFRS when you consider Master / Feeder Funds etc.</td>
<td></td>
</tr>
</tbody>
</table>
US GAAP
## US GAAP

### Liquidation basis of accounting

<table>
<thead>
<tr>
<th>Background</th>
</tr>
</thead>
<tbody>
<tr>
<td>On April 22, 2013 the FASB issued ASU 2013-07, Liquidation Basis of Accounting</td>
</tr>
<tr>
<td>Provides guidance on when and how to apply the liquidation basis of accounting and required disclosures</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Scope</th>
</tr>
</thead>
<tbody>
<tr>
<td>Applies to all entities (public and non-public), except investment companies regulated under the Investment Company Act of 1940</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Effective date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Entity already reporting on liquidation basis upon effective date under another standard, does not apply this guidance</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Recognition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adopt the liquidation basis of accounting when liquidation is imminent unless liquidation follows a plan specified in entity’s governing documents</td>
</tr>
<tr>
<td>Liquidation is imminent when:</td>
</tr>
<tr>
<td>A plan of liquidation is approved by those with the power to do so and remote likelihood it will be blocked</td>
</tr>
<tr>
<td>Liquidation is imposed by other forces and remote likelihood entity will return from liquidation (e.g. involuntary bankruptcy)</td>
</tr>
</tbody>
</table>

### Initial Recognition/Measurement - Assets & Liabilities

#### Assets
- Recognize assets expected to be sold in liquidation, not previously recognized (e.g., trademarks)
- Measure to reflect actual amount of cash the entity expects to collect during liquidation
- Fair value measurement may be acceptable

#### Liabilities
- Recognize and measure in accordance with respective existing U.S. GAAP
- Adjust inputs used to measure liabilities to reflect liquidation
- Do not adjust amount for anticipated legal release

Remeasure liabilities (if required by relevant U.S. GAAP), assets, and other items expected to be sold in liquidation to actual or estimated carrying amount at each subsequent reporting period

### Initial Recognition/Measurement - Costs

#### Estimated costs to dispose
- Accrue estimated costs to dispose of assets, including other items expects to sell
- Present total estimated costs to dispose in aggregate separately from measurement of assets

#### Ongoing income & expense
- Accrue other costs and income expected to be incurred during liquidation period if and when reasonable basis for estimation exists

Remeasure disposal cost accruals or other ongoing income and expenses at each subsequent reporting period to reflect actual or estimated change in carrying value
**US GAAP**

**Going concern**

### Background
- On August 27, 2014 the FASB issued 2014-15, Disclosure of Uncertainties About an Entity’s Ability to Continue as a Going Concern
- Provides guidance on determining when and how to disclose going-concern uncertainties in the financial statements.
- The new standard requires management to perform interim and annual assessments of an entity’s ability to continue as a going concern within one year of the date the financial statements are issued.
- An entity must provide certain disclosures if “conditions or events raise substantial doubt about the entity’s ability to continue as a going concern.”

### Effective date
- The ASU applies to all entities and is effective for annual periods ending after December 15, 2016, and interim periods thereafter, with early adoption permitted.

### New ASU issued – three key provisions

<table>
<thead>
<tr>
<th>Disclosure Thresholds</th>
<th>Disclosure Content</th>
<th>Time Horizons</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Are the criteria met for the liquidation basis of accounting?</strong> (Subtopic 205-30)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Are there conditions or events, considered in the aggregate, that raise substantial doubt about an entity’s ability to continue as a going concern within one year after the date the financial statements are issued (or available to be issued)?</strong> (paragraphs 205-40-50-01 through 50-5)</td>
<td>Yes</td>
<td></td>
</tr>
<tr>
<td><strong>Consider management’s plans intended to mitigate the adverse conditions or events.</strong> (paragraphs 205-40-50-6 through 50-11)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Is it probable that management’s plans will be effectively implemented?</strong> (paragraphs 250-40-50-7 through 50-8)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Is it probable that management’s plans will mitigate the relevant conditions or events that raise substantial doubt?</strong> (paragraph 205-40-50-10)</td>
<td>Yes</td>
<td></td>
</tr>
<tr>
<td><strong>Are the criteria met for the liquidation basis of accounting?</strong> (Subtopic 205-30)</td>
<td>No</td>
<td></td>
</tr>
<tr>
<td><strong>No disclosures required specific to going concern</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

An entity shall disclose information to help users understand the following when substantial doubt is alleviated by management’s plans:
1. Principal conditions or events that raise substantial doubt, before consideration of management’s plans
2. Management’s evaluation of the significance of those conditions or events
3. Management’s plans that alleviated substantial doubt.

The entity also should include in the footnotes a statement indicating that there is substantial doubt about the entity’s ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued).

(Paragraph 205-40-50-13)
US GAAP

Repurchase Agreements

**Repo to maturity**
- The ASU requires repos-to-maturity to be accounted for as secured borrowings
- A repo-to-maturity of a held-to-maturity ("HTM") security would not taint an entity’s HTM portfolio.

**Repurchase Financings**
- Under current guidance in ASC 860, repurchase agreements entered into as part of a repurchase financing may be required to be accounted for on a "linked" basis.
- The new ASU eliminates this requirement and would require such repurchase agreements to be accounted for separately.

**Dollar roll transactions**
- The FASB decided to retain the existing "substantially-the-same" guidance in ASC 860 and abandon the notion that a dollar-roll transaction that does not include a trade stipulation would not be expected to result in the return of a substantially-the-same financial asset.

**Repo Disclosures**
- Transfers of assets accounted for as sales in which there is a continuing exposure to the transferred asset.
- Asset quality information for repurchase and security lending transactions that are accounted for as secured borrowings.

**Transition and Effective Date**

**Transition**
- Entities (1) are required to record a cumulative-effect adjustment to beginning retained earnings for transactions outstanding as of the period of adoption and (2) are not required to disclose transition information other than that already required by ASC 250.

**Effective date**
- For public entities the final standard is effective for annual periods (and interim periods within those annual periods) beginning after December 15, 2014. Early adoption is not permitted.
- For nonpublic entities the final standard is effective for annual periods beginning after December 15, 2014, and interim periods beginning after December 15, 2015. A nonpublic may elect to early adopt the requirements for interim periods beginning after December 15, 2014.
Insight and thought leadership
Insight and thought leadership

Deloitte produces a range of thought leadership examining significant regulatory topics and key business impacts to help keep you informed. We provide knowledge sharing through a variety of channels including events briefings, newsletters, teleconferencing and our Link’n Learn series of webcasts.

Below is some of our latest thinking which you can access on our website: [www.deloitte.com/ie/im](http://www.deloitte.com/ie/im)
ICAV – 3 months later
The results are out!

Since the Irish Collective Asset-management Vehicles (ICAV) Act 2015 (the Act) became effective on 12 March 2015, the ICAV has proven to be a popular option for fund managers. We consider how many ICAVs are now in existence and compare the ICAV's features with other Irish fund vehicles.

Go to article

Funds Bulletin
August 2015

The Deloitte Funds Bulletin delivers you our latest updates and insights on industry developments.

Go to Bulletin

5 key features of CMU

Earlier this year, the European Commission issued a Green Paper on CMU to foster debate across the EU on possible measures needed to create a true single market for capital and to seek feedback from the European Parliament and the Council, other EU institutions, national parliaments, businesses, the financial sector and all those interested. The deadline closed on 13 May 2015.

The Green Paper suggested principles which should underpin a CMU: read more

Go to article
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Go to webinar page

Loan Funds
Europe’s alternative source of business funding

The financial crisis caused liquidity problems for banks globally, with a knock-on reduction in access to capital for businesses. To address this challenge, regulators in Europe are introducing alternative sources of financing, and in particular, are implementing measures to allow investment funds to issue loans to businesses.

At a European level, the ‘European Long-Term Investment Fund’ (ELTIF) is being established, while Ireland has recently launched its own ‘Loan Originating Qualified Investor Alternative Investment Fund’ (referred to below as Irish Loan Fund (ILF)). Both measures offer a regulated fund that originates loans to business, and in this article we compare the key features of each.

Go to article

Market Abuse Directive/Regulation

On 15 July 2014, the European Securities and Markets Authority (ESMA) issued a consultation on the new Market Abuse Regulation (MAR) which entered into force on 2 July 2014. In its press release, ESMA explained that to assist in developing the implementation of the new MAR framework which will become applicable in July 2016, it is issuing two consultation papers seeking stakeholders’ views on the draft regulatory and implementing technical standards (RTS/ITS) and Technical Advice (TA).

Go to article
Funds industry faces client asset reform
Consultation Paper 71

The changes proposed in the Central Bank of Ireland’s consultation on client assets are likely to impact the funds industry. CP 71 proposes to develop a new regime for collection accounts operated by fund service providers as early as Q1 2014. Given the possible effect on daily processes and the high level of oversight afforded to client assets generally, it is important that firms understand the requirements now so that they can analyse the impact and take appropriate action.

Unravelling the new requirements from a contractual and technical perspective will take time. Alternatively, fund service providers may seek to adopt structures to remain out of scope. This carries both regulatory risk and the risk that many of these arrangements have yet to be tested by an insolvency situation.

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- Legislation changes and clarifications impacting investment funds - A French update
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- Fair Value Pricing Survey, Twelfth Edition - Positioning for the future
- 2015 Alternative Investment Outlook - Complex grounds, new frontiers
- Do you really know where your assets are, and if they are safe?
- Plans to reform the German Investment Tax Act - Overview and impact

View the current edition
The Fourth EU Anti Money Laundering Directive

The 4th AML Directive takes into account the latest recommendations of the Financial Action Task Force (“FATF”) from 2012. Once the Directive has been finalised and adopted at a European level, there will be a two year period within which it will be required to be transposed into national legislation. The new Directive outlines a number of modifications to the Third EU AML Directive, and has been welcomed overall by the industry.

Go to document

ELTIFs and CMU
Funnelling investment into SMEs and funds

Recent developments within the European Institutions herald good news for businesses across Europe - several measures are underway to increase funding and growth in the real economy including Capital Markets Union (CMU), the European Long Term Investment Fund (ELTIF) and the ‘Investment Plan for Europe’.

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AIFMD II

The Alternative Investment Fund Managers Directive (AIFMD), which entered into force on 22 July 2013, introduced an EU marketing passport for EU domiciled Alternative Investment Fund Managers (AIFM) managing and marketing EU domiciled Alternative Investment Funds (AIF), whereas non-EU domiciled AIFMs remained subject to the national placement regimes (NPPRs) of each Member State where the AIF is marketed.

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Exchange Traded Funds
Updated Revenue Guidance Note

Exchange Traded Funds (ETFs) are fund structures whose units are traded on regulated markets and investment exchanges. They are typically open-ended and redeemable on a daily basis. Most European ETFs are structured as UCITS funds.

The Irish Revenue recently published a Guidance Note on the Revenue website regarding the tax treatment of investments in Exchange Traded Funds. We summarise these developments, and provide an of ETFs and their evolution.

Go to article
Companies Act
Key impacts for investment companies and fund managers

The Companies Act 2014 ("the Act") came into effect on 1 June 2015. It consolidates the existing Companies Acts, simplifies Company Law and introduces some welcome reforms. The Act affects all Irish companies, including fund service providers such as administrators and depositaries, managers of both UCITS and AIFs, as well as investment companies.

All existing private companies will have to decide whether to become a company limited by shares (LTD), a designated activity company (DAC) or another type of company. Companies regulated by the Central Bank of Ireland ("CBI") however, will likely be required to re-register as a DAC.

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Blockchain
Disrupting the Financial Services Industry

In an attempt to try and harness its potential disruptive power, hundreds of millions are being invested in Blockchain technology by companies from all industries across the globe. With this level of focus and hype, we want to help de-mystify what Blockchain is and how organisations can leverage its key features (security, transparency, full life-cycle transaction history, real-time, immutability and cost efficiency).

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Loan originating Funds
10 key features

From 1 October 2014, the Central Bank of Ireland has permitted certain Qualifying Investor Alternative Investment Funds (QIAIFs) to originate loans (LOQIAIFs). The launch of the LOQIAIF follows a consultation process by the CBI over the past year. When issuing the new AIF Rulebook, the CBI also issued a Feedback Statement on this consultation which provides interesting insights on the rationale for the current structure of the LOQIAIF.

Go to article
Regulatory timeline
A snapshot of the changes in 2014

- Political agreement on MiFID II
- MiFID II & MiFIR text published 12 June 2014
- EMIR reporting commences 12 Feb 2014
- FATCA registration by April 2014
- Submission of AIFM application by 22 July 2014
- Issue of draft detailed MiFID II / MiFIR and MAD II / MAR measures
- PRIPS text agreed 10 Nov
- UCITS V delegated acts on independence and sub-custodian insolvency published 28 Nov 2014
- Conclusion on BEPS
- Adoption of UCITS V and PRIIPs April 2014
- Loan origination QIAIFs from 1 October 2014
- UCITS V 24 October Consultation on Delegated Acts closed
- Adoption of ELTIFs Q4 2014
- CP86 Consultation closes Dec 8th 2014
- End of transition for ESMA UCITS guidelines 18 Feb. 2014
- FATCA income withholding commences
- UCITS V 2014
- Expected publication of Central Bank’s new client asset requirements*
- PRIPS KID Regulation enters into force
- UCITS Rulebook expected from the Central Bank
- Expected in Q4 2014: Feedback on CP84 and on ESMA’s Revised Guidelines on ETFs and other UCITS issues

* Estimated timeframes subject to change
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