CP86 – The effectiveness of fund management companies

Investor protection is of paramount importance to the credibility and reputation of the funds industry. Assuring investors that they are front and centre for firms, as they strive to navigate the increasing technology and regulatory risks they face.

CP86 as published by the Central Bank of Ireland (the Central Bank) aims to enhance investor protection by outlining rules and guidelines that address the governance and effectiveness of delegate oversight of Irish Fund Management Companies (FMCs). On its third and last consultation issued in 2016, the Central Bank included rules and guidelines on managerial functions, operational issues and procedural matters. The final guidance consolidates the earlier guidance on delegate oversight, organisational effectiveness and directors' time commitments along with this more recent guidance.

This collective guidance forms part of the amended Central Bank Undertakings for the Collective Investment of Transferable Securities (UCITS) Regulations and Central Bank AIF Regulations effective from 1 July 2018.

The guidance highlights three key areas of focus for FMC's, namely:

Governance
How directors of FMCs should perform their roles and duties and how they should direct the company.

Compliance
How designated persons conduct their managerial functions in a manner that ensures the FMC is compliant with its regulatory obligations.

Super-visability
The ability of an FMC to engage with the Central Bank engagement model without undue constraint and the ability to react in a crisis.

Governance

Improving the effectiveness of a FMC must start with FMC directors, as they are responsible for the governance, control of the company and the oversight of its delegates. With this in mind, the guidance outlines two new rules, namely:

1. The number of designated person roles is to reduce from **fifteen to six** for Alternative Investment Fund Managers (AIFMs) and from **nine to six** for UCITS management companies. The six roles will be regulatory compliance, fund risk management, operational risk management, investment management, capital and financial management and distribution.
2. FMCs are required to have one director who carries out an organisational effectiveness role to ensure that the FMC is arranged and resourced in the most appropriate manner on an on-going basis. This director essentially oversees the totality of the delegate arrangement the FMC has in place to provide assurance that they all work well together.

Compliance

FMCs face regulatory obligations under the UCITS and AIF Regulations, Markets in Financial Instruments Directives (MIFID) I & II, the Companies Act 2014, Market Abuse Law and European Market Infrastructure Regulation (EMIR) to name but a few. Designated persons must be aware of the tasks and responsibilities of their managerial function and the regulations relevant to such. Designated persons have a critical role to play in enabling the FMC to demonstrate compliance with these regulations.

Super-visability

The introduction of CP86 as part of the amended UCITS and AIF regulations highlight the importance of access to company records, directors and designated persons by the regulator. It prescribes that access to each of these is unhindered and effective with strong communication channels in situ. In support of this supervisory objective it outlines the following requirements:

1. The location rule

An FMC with a **PRISM** impact rating of **medium low or above** will be required to have, at least:

- three Irish resident directors **or** at least two Irish resident directors and one designated person based in Ireland;
- 50% of its directors in the EEA; and
- two designated persons in the EEA.

Similarly an FMC which has a **PRISM** impact rating of **low** will be required to have, at least:

- two Irish resident directors;
- 50% of its directors in the EEA; and
- two designated persons in the EEA.

2. Retrievability of records rule

Records such as board minutes, policies and procedure documents, letters of engagement contracts with delegates and/or reports to designated persons must be able to be provided timely, upon request by the regulator. FMCs are expected to keep all records in a well-defined, understandable manner with a schedule outlining document location, creation date, contents and any other pertinent details. These documents will serve as evidence of all regulatory compliance.

The guidance suggests that FMCs should maintain an email address solely for compliance with these rules, be it an email address for all investment funds or for each fund as desired. This email should be monitored daily for any correspondence received from the Central Bank.

How Grant Thornton can help

Existing FMCs will have to assess the impact these new requirements (as part of the amended Central Bank UCITS Regulations and Central Bank AIF regulations) will have on their business. They should review their governance arrangements in Ireland and where relevant within a wider group context by 1 July 2018.

In the context of new FMCs, the Central Bank will only approve applications from new FMCs, submitted on or after **1 July 2017,** where the FMC is compliant with the new requirements. New FMCs will need to incorporate these requirements into their business structure, business plans and activities if they want to demonstrate 'substance' in Ireland. 'Substance' will be key for the Central Bank in assessing applications for authorisation.

Contact

At Grant Thornton we can help FMCs to understand the impact of these new requirements on their business. We can provide assistance in assessing the impact of the new requirements and with implementing new compliance and governance frameworks to support the FMC in demonstrating compliance. Please contact a member of our team below for further information and discussion.

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