

ASSET MANAGEMENT AND INVESTMENT FUNDS

Central Bank – Funds Industry Seminar

March 2020

The Central Bank recently convened a meeting with Irish fund industry representatives to discuss both its authorisation and supervision framework for Irish UCITS funds and to explain some recent changes in the authorisation process.

The Central Bank indicated that it hoped that two similar seminars would be held during the course of the year for UCITS funds and that it would also aim to host a seminar on qualifying investor alternative investment funds (QIAIFs) during the year.

GATEKEEPER PRINCIPLES

Several senior representatives of the Central Bank's funds authorisation and supervision teams spoke about the role of the Central Bank in protecting the interests of investors and how the gatekeeper principles it has adopted seek to achieve this. This "gatekeeper" role is set against a backdrop of the ever increasing size, scale and complexity of the Irish UCITS funds industry which in and of itself gives rise to the need for heightened scrutiny by the Central Bank under its supervisory and market stability mandates and similarly scrutiny by ESMA at a European level. It was noted that the Central Bank had streamlined some of its processes, for example, relying on self-certifications of compliance in respect of the use of indices and for various fund documents, with occasional spot checks. This streamlining of certain processes is necessary to allow the Central Bank to take a more risk-based approach in its authorisation process and supervisory role in order to focus its attention on more complex UCITS submissions.

AREAS OF ENHANCED FOCUS

Obligations of fund boards

The role of a fund board in considering and approving the establishment of a fund was discussed at the seminar. The Central Bank indicated that it may now request evidence of the review process that has been undertaken by a board in establishing a new fund. The Central Bank may ask to review board minutes which should demonstrate the board's consideration of the key elements relating to the establishment of a fund. It is therefore important that a fund board can demonstrate the analysis that it has undertaken in establishing a new fund and that accurate and comprehensive board minutes reflect the level of board discussion that took place.

In our view a fund board should consider the investment objective and policy of a fund, the nature of its underlying investments and the risk profile of a fund in advance of any submission being made to the Central Bank for the fund's approval. The investment approach memorandum (which is required pursuant to the Central Bank's Fund Management Guidance or "CP86") should be provided to the board in respect of any new fund in an existing umbrella as it identifies the key characteristics of the fund. This document includes a summary of the types of investments the fund may make, its dealing frequency, liquidity

profile and its distribution strategy. The investment approach memorandum should identify the proposed portfolio of the fund by reference to such things as asset type, issuer type, market capitalisation, credit rating, geographic or sector focus. The investment approach memorandum should be accompanied by the draft investment objective and policy and fee details. These commercial details may change over the course of the Central Bank review process and so prior to any submission for approval the final form of the fund documents, including the final form of investment approach memorandum, should be presented to the board for consideration, with any material changes highlighted, in order for the board to approve the establishment of the fund.

For entirely new UCITS vehicles, directors who are proposed for board positions should, in our view, seek the kind of information referred to above in advance of their appointment and prior to the first board meeting so that they understand the nature of the fund for which they are to assume the role of director.

Central Bank's updated UCITS Q&A ID 1094

The Central Bank explained the rationale for its recent update of the UCITS Q&A (ID 1094). This updated Q&A allows the Central Bank to carry out additional

scrutiny and request additional information for funds that invest in CFDs, CLOs, CoCo's or binary options. The additional information may include model portfolio information, the due diligence carried out by the investment manager on the underlying portfolio and evidence that the portfolio is suitable for retail investors.

The Central Bank accepted that these particular types of investment may not be suitable investments for sale to retail investors directly but they may be suitable investments for a UCITS portfolio. However, a board needs to demonstrate to the Central Bank how it will monitor and measure the market, liquidity, counterparty and other risks for UCITS that invest in these types of assets. Our briefing on the update of the Central Bank's UCITS Q&A is [here](#) and refers to

these new requirements in detail.

Investment Advisers

Specific mention was made by the Central Bank of it identifying a number of instances where investment advisers in a fund appear to have taken on a discretionary investment management role which is a breach of the UCITS Regulations. Investment advisers are not regulated and are not permitted to carry out discretionary investment management activity for an Irish fund. The Central Bank identified some examples of this, such as where the investment adviser receives fees in excess of those of the investment manager (including performance fees) for its advisory role and where an investment adviser is appointed to an index replicating ETF

where the relevance of an advisory role is questionable. The Central Bank confirmed that it is the responsibility of the board to ensure that appropriate due diligence is undertaken on the role that each service provider in the fund structure assumes.

CONCLUSION

The seminar emphasised the Central Bank's role in the authorisation and supervision of UCITS funds – it sees the two roles as being the two sides of the same coin. The seminar also highlighted the need for fund boards to exercise and be able to demonstrate their effective decision-making in relation to the establishment and ongoing operation of UCITS funds.

KEY CONTACTS



Kevin Murphy
Partner
+353 1 920 1177
kevin.murphy@arthurcox.com



Tara O'Reilly
Partner
+353 1 920 1787
tara.oreilly@arthurcox.com



Sarah Cunniff
Partner
+353 1 920 1171
sarah.cunniff@arthurcox.com



Dara Harrington
Partner
+353 1 920 1206
dara.harrington@arthurcox.com



Cormac Commins
Partner
+353 1 920 1786
cormac.commins@arthurcox.com



Ian Dillon
Partner
+353 1 920 1788
ian.dillon@arthurcox.com



Siobhán McBean
Partner
+353 1 920 1052
siobhan.mcbean@arthurcox.com