



AIFMD Outsourcing and Delegation – what you need to know

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Outsourcing and Delegation – General provisions

- Delegation must not alter the responsibility of the AIFM.
- Obligations of AIFM towards AIF/investors shall not be altered.
- AIFM shall ensure that the delegate carries the function effectively and in accordance with laws and regulatory requirements.
- AIFM should retain necessary expertise and resources to be able to supervise and manage risks associated with delegation AIFM should also check that the delegate does the same with sub-delegate.
- AIFM shall ensure the continuity and quality of delegated tasks
- A written agreement shall define clearly the rights and obligations of the AIFM and the delegate.
- If **portfolio management** delegated, it shall be in accordance with the investment policy of the AIFM AIFM must ensure that the delegate: -
 - >Disclose any development that may have a material impact on its ability to carry out the delegated functions
 - >Protect confidential information
 - >Establish a contingency plan for disaster recovery and test periodic backup facilities

Objective reasons to delegate

- **To be authorised to delegate**, the AIFM must demonstrate objective reasons that justify the delegation structure :-
 - > More efficient conduct of AIFM's management of AIF
 - >Optimising of business functions and processes
 - >Cost saving
 - >Expertise of the delegate in administration/specific market/investment
 - >Access of the delegate to global trading facilities The rule of "justification"
- **Resources, experience and good reputation**
 - AIFM has to evaluate whether the delegate has sufficient resources to perform the task and whether the persons conducting the task in the delegate entity have sufficient experience and good reputation.
 - Factors to be considered:-
 - 1) **Substance**: AIFM shall check the adequacy of the resource (sufficient personnel with skills, knowledge and experience)
 - 2) **Knowledge**: AIFM shall check whether the persons have appropriate theoretical knowledge and practical experience
 - 3) **Good reputation**: AIFM shall check the records of the persons. Negative records include relevant criminal offences, judicial proceedings and administrative sanctions.
 - N.B: factor 3) de facto satisfied if delegate is regulated in EU, unless evidence to the contrary

Conflicts of Interest

Non-exhaustive criteria to assess whether a delegation would result in a conflicts of interest situation:-

- > AIFM and delegate (or delegates and investors) are members of the same group or have any other contractual relationship.
- >Likelihood of financial gain of delegate at the expense of the AIFM or investors.
- >Likelihood of interest of the delegate in the outcome of service or activity provided to AIFM or AIF.
- >Likelihood that delegate receives inducements from third person.
- >AIFM ensures that the delegate takes all reasonable steps/has procedures in place to identify, manage and monitor potential conflicts of interest situations and disclosed to the investors
- >Functional and hierarchical independence of **risk or portfolio management function**:-
 1. Avoidance of combination of portfolio management tasks and operating tasks.
 2. Avoidance of combination of risk management tasks with operating tasks or supervision of them.
 3. Separation is ensured in the whole hierarchical structure of the delegate

Outsourcing and delegation

Delegation of portfolio or risk management

The following entities should be considered as authorised for the purpose of asset management and subject to supervision:-

- 1) Management companies authorised under the UCITS Directive.
- 2) Investment firms and credit institutions authorised under MiFID to perform portfolio management
- 3) Specific rules apply when delegation to undertakings which do not fulfil the above criteria delegation to third-country entities

Delegation of Depositary duties

- AIFMD has strict rules around doing this.
- FCA have advised (Sept 2013) they are taking a strict view of AIFMD's delegation duties.

Letter Box Entities

AIFM is deemed a letter-box entity and is no longer considered to be AIFM when:-

- 1) AIFM no longer retains necessary resource and expertise to supervise the delegation and manage the risk associated with it
- 2) AIFM no longer has the power to:-
 - (i) take decisions in key areas under the responsibility of senior management.
 - (ii) to perform senior management function (e.g. implementation of investment policy, investment strategy).
- 3) AIFM loses the right to inquire, inspect, have access or give instructions or this becomes impossible in practice
- 4) The delegated tasks substantially exceed the remaining tasks (using a qualitative and quantitative approach)

E.g. types and importance of the assets managed under delegation, geographical and sectorial spread of the investments, risk profile of the AIF, type of investment strategies, types of tasks delegated, configuration of delegates and their sub delegates.

Operational issues

Delegation to third countries

- Specific rules related to delegation to third-country undertakings where the delegation of portfolio or risk management is concerned
- Written agreement between authorities of the countries of the AIFM and of the delegate and providing the following rights to home regulating authority:-
 - Access to relevant information/documents
 - Request on-site inspection
 - Receive immediate information from third country authority in case of breach (iv) Cooperate in enforcement powers in case of breach of the AIFM directive

Effective Supervision

- Situations in which delegation deemed to prevent the effective supervision of the AIFM:-
 - AIFM, auditors or authorities do not have access to data related to the delegated functions or the business premises of the delegate
 - Delegate does not cooperate with competent authorities of the AIFM.
 - All information necessary to supervise the delegated functions are not made available.

Sub-delegation

- The AIFM shall demonstrate its approval for the sub-delegation in writing.
- A general consent in advance by the AIFM shall not be deemed consent
- Notification shall contain full details of the sub-delegate, tasks delegated and competent authority.

How can we help?

Global Perspectives have assisted multiple clients with AIFMD including:-

- Advising non-EU managers of their AIFMD requirements
- Assisting AIFM's with their applications for authorisation
- Ensuring compliance with delegation requirements
- AIFMD Reporting requirements
- Selecting suitable AIFMD software vendors
- Supporting the Depositary selection process

We would be happy to assist you with your AIFMD requirements.

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