

# CP86 – Synopsis of CBI Rules, Guidance and Transitional Arrangements

The Central Bank of Ireland (CBI) published a feedback statement on its third and final consultation on fund management company effectiveness (CP86) since its first CP86 consultation was issued in September 2014, as well as a document entitled “Fund Management Companies – Guidance” which includes all guidance issued by the CBI as a result of the CP86 consultation process.

We set out below a synopsis of the new rules and guidance issued by the CBI as a result of the CP86 consultation process and the effective dates of such rules and guidance relevant for:

- UCITS management companies;
- Self-managed UCITS investment companies/ICAVs;
- Authorised AIFMs; and
- Internally managed AIF investment companies/ICAVs

(each referred to as a **Fund ManCo** and collectively **Fund ManCos**).

We have prepared an overview of the requirements applicable to externally managed investment companies/ICAVs. Please contact us if you would like a copy. In brief, most of CP86 does not apply to such entities other than certain oversight of delegate requirements.

## NEW RULES FOR FUND MANCOS

### Rule 1: Streamlined Managerial Functions

The managerial functions for all Fund ManCos (required to be detailed in the business plan (BP)/ programme of activity (PoA)) are consolidated into the following 6 managerial functions:

- Investment Management;
- Fund Risk Management;
- Operational Risk Management;
- Regulatory Compliance;
- Distribution; and
- Capital and Financial Management (together the **Managerial Functions**).

A Fund ManCo which delegates activities will continue to be required to identify a designated director or other designated person (DP) who will have responsibility for each Managerial Function. While the same person may perform more than one Managerial Function, including both of the risk management functions, the same person must not perform both Managerial Functions relating to risk management and investment management. The final guidance in relation to the performance of the Managerial Functions is summarised below.

### Rule 2: New Organisational Effectiveness Role

Each Fund ManCo will be required to designate an independent director (who could be the chairperson of the board) to undertake the organisational effectiveness role and who should not perform any of the 6 Managerial Functions. The purpose of this role is to keep the effectiveness of the organisational arrangements of the Fund ManCo under review and it will also include monitoring conflicts of interest and internal audit, unless monitoring of internal audit is allocated to a DP.

### Rule 3: Effective Supervision/Location of Directors and Designated Persons (DPs)

In its third CP86 consultation, the CBI proposed to introduce requirements regarding the location of directors and DPs based on the CBI’s Probability Risk and Impact System (PRISM) rating of a Fund ManCo, but which would also allow for the flexibility to have DPs based outside of Ireland. As a result of responses to the consultation in relation to the need to facilitate organisational models which draw appropriately on the expertise of the promoter/ investment manager, the CBI has adjusted its initial proposal to permit more involvement by persons located outside of the EEA (EU member states and Iceland, Norway and Liechtenstein). The final requirements are as follows:

a Fund ManCo which has a PRISM impact rating of **Low** will be required to have at least:

- two Irish resident directors;
- half of its directors resident in the EEA or other countries which CBI designate; and
- half of Managerial Functions performed by at least two DPs resident in the EEA or other countries which CBI designate; and

a Fund ManCo which has a PRISM impact rating of **Medium Low or above** will be required to have at least

- three Irish resident directors or two Irish directors and one DP based in Ireland;
- half of its directors in the EEA or other countries which CBI designate; and
- half of Managerial Functions performed by at least two DPs resident in the EEA or other countries which CBI designate.

All Fund ManCos which are self-managed UCITS or internally managed AIFs have a PRISM rating of Low. Addressing Brexit, the CBI has indicated that, while it would not be possible to predict the outcome of Brexit negotiations, the CBI would consider the UK as having equivalent requirements to an EEA jurisdiction and hence be considered as within the EEA for these purposes.

### Rule 4: Rationale for Board Composition

Each Fund ManCo will need to include the rationale for its board composition in its BP/PoA to document how the board as a whole provides it with sufficient expertise to conduct the tasks expected of the directors and, where relevant, the DPs for a Managerial Function.

### Rule 5: Retrievability of Records

A Fund ManCo must maintain all of its records in a way that makes them immediately retrievable from Ireland. The final guidance on Operational Issues summarised below clarifies that in this context “immediately” means that documents requested by the CBI before 1pm (Irish time) should be provided to the CBI on the same day and documents requested after 1pm should be provided to the CBI before 12 noon on the following day.

## FINAL GUIDANCE FOR FUND MANCOS

While the CBI has noted that divergence from its guidance will not be a regulatory breach, the CBI’s supervisors will have reference to

its guidance when forming a view as to whether a Fund ManCo has complied with its regulatory obligations. Accordingly, a Fund ManCo would want a very good reason not to comply with a particular requirement and it should document such reason and keep it under review.

### Guidance Part I – Delegate Oversight

This guidance focuses on the role of boards where significant tasks are delegated externally and sets out a framework for good practice in relation to the monitoring and oversight of delegates, delegated tasks and tasks to be retained. Specific guidelines on the supervision of delegates in relation to investment management, distribution, risk management and investment operations and administration are included. We have prepared an overview of this guidance. Please contact us if you would like a copy.

### Guidance Part II – Organisational Effectiveness

This guidance focuses on the Organisational Effectiveness role to be undertaken by an independent director. It clarifies that the types of matters to be covered under this role include (but are not limited to) reviewing (at least annually) the organisational structure and arrangements of the Fund ManCo, including in relation to the Managerial Functions and suggesting improvements for consideration by the board; keeping board composition under review and reporting to the board; organising periodic board effectiveness evaluations and overseeing how well the decisions taken by the Fund ManCo and the arrangements for the supervision of delegates are working in the interests of investors; considering the conflicts of interest affecting the Fund ManCo and its funds under management and initiating action, such as escalation to the board, where these are having, or are likely in the near future to have, an adverse impact.

### Guidance Part III – Directors' Time Commitments

This guidance recommends that:

- directors and boards should agree a minimum time allocation for board meeting attendance, which should be documented in each director's letter of appointment, as well as additional time for ad hoc issues;
- additional time should be allocated where a director carries out a chairperson role;
- a DP role for Managerial Functions should be considered separately to the role of director and a separate time commitment should be allocated;
- a separate letter of appointment should be issued in respect of DP roles for Managerial Functions, which should be subject to annual review;
- directors should consider any conflicts of interests and the types and complexity of funds/sub-funds;
- membership of board committees should be considered as a separate role.

This guidance does not set a hard limit on the number of board appointments which a director may hold. However, the CBI currently intends to treat in excess of 20 directorships (of Irish authorised investment funds or Fund ManCos) combined with a high aggregate level of annual professional time commitment in excess of 2000 hours as a risk indicator, which may entail additional supervisory attention under the CBI's risk-based approach.

If it would be proposed to appoint a director who exceeds the risk indicator thresholds, the CBI could withdraw from any corporate QIAIF the option of the 24 hour authorisation time-frame. The recommendations in the guidance may also be used by the CBI for future reviews of board effectiveness, director time commitments and quality of board operations.

### Guidance Part IV – Managerial Functions

This guidance focuses on who can be a DP as well as the role and capacity of a DP.

This guidance provides that a DP can be a director or employee of the Fund ManCo, or can be seconded to the Fund ManCo, on a full or part-time basis, from another firm, such as the investment manager or a firm which specialises in the provision of DPs. A Fund ManCo could therefore appoint DPs based outside of Ireland, provided that the Fund ManCo complies with Rule 3 above (the location rule).

The CBI's feedback statement on its third CP86 consultation also clarified that the guidance does not prohibit the appointment of the same individual as director and DP. While a director can also be a DP, this guidance distinguishes between the role of a director being part of the governing body which is not involved in managing the Fund ManCo on a day-to day basis and that of a DP which is described as the Fund ManCo's line of management between the board of directors and its delegates.

In brief, this guidance provides that DPs should:

- monitor and oversee compliance by a Fund ManCo with its obligations and ensure that the strategies, policies and directions issued by the board are acted upon and complied with;
- report to the board on a regular basis and escalate issues where pre-defined parameters agreed with the board are exceeded or where the DP judges that immediate escalation is warranted;
- monitor and oversee Fund ManCo employees or delegates who carry out the tasks which fall within the scope of their responsibility and review their work on an ongoing basis in a manner agreed with the Fund ManCo;
- have experience and expertise in the Managerial Function and enough knowledge of the area to constructively challenge both information received and the people providing it;
- be sufficiently senior in their role vis-a-vis delegates and engagement with the CBI; and
- have enough time available to them to carry out their roles thoroughly and to a high standard.

This guidance also covers:

- the manner in which DPs should ensure oversight of regulatory obligations;
- the format of DP interaction with delegates, including reporting, meetings/ calls, on-site visits, the appropriate level of challenge and engagement and records of engagement;
- the role of the DP in advising on, implementing and reviewing required policies/ procedures, structures and limits and the board's involvement;
- the frequency of monitoring and oversight by DPs.

The guidance provides that the frequency of monitoring and oversight by DPs, including the frequency of receipt of information from delegates, should be determined based on the activities of the Fund ManCo and its funds under management. This includes, but is not limited to:

- the complexity of the investment strategy;
- the markets in which the investment fund operates;
- the types of investment instruments utilised;
- the underlying investment activities (as positions are bought and sold);
- the frequency of investor subscriptions/redemptions;
- the utilisation, valuation and security of margin and/or collateral;

- the number of and functions provided by fund service providers; and
- the use of efficient portfolio management techniques

While DPs should monitor the tasks for which they are responsible on a day-to-day basis, this does not necessarily mean that monitoring and oversight has to take place daily. By way of example, the guidance provides that a proposal whereby the DP for monitoring Investment Management received monthly reporting in relation to an investment fund that deals and trades in complex securities on a daily basis might not be viewed favourably whereas a proposal to receive reporting on a monthly basis for an investment fund that pursues a long-term buy and hold strategy may be acceptable.

In addition to regularly scheduled monitoring and oversight, the guidance provides that more frequent review should occur on an ad hoc basis where circumstances demand this, for example where breaches are occurring or where market volatility has increased.

#### Guidance Part V – Operational Issues (Record Retention & Retrievability and Email Address)

This guidance outlines the CBI's minimum expectations with regard to the retention, maintenance, security, privacy, preservation and accessibility of the documentation and records pertaining to a Fund ManCo and its funds under management (Relevant Documents).

In brief, the guidance provides that a Fund ManCo should have immediate and unfettered access from Ireland to all Relevant Documents, which should be available on request to the CBI in accordance with the timelines outlined under Rule 5 above. Relevant Documents would include agreements, reports, documents filed with the CBI, board minutes, policies and procedures, financial statements, minutes of meetings etc.

This guidance also provides that a Fund ManCo must have a record management policy and procedures appropriate to its nature, scale and complexity as well as a clearly defined records retention schedule. Relevant Documents can be maintained in hard or electronic format.

Each Fund ManCo should also maintain a designated and monitored email address for correspondence with, and responding to, information requests issued by the CBI. Guidance is included in relation to the operation and monitoring of the email address, which must be capable of being checked daily. A single address can be maintained for all funds under management or for each fund under management. The CBI may periodically test the effectiveness and efficacy of the designated email address. We have prepared a summary of the requirements in relation to the dedicated email address. Please contact us if you would like a copy.

#### Guidance Part VI – Procedural Matters

This guidance reflects the CBI's existing procedures relevant to Fund ManCo authorisation and passport applications.

### TRANSITIONAL ARRANGEMENTS AND NEXT STEPS

Rules and Guidance	Fund ManCo Authorised before 1/11/2015	Fund ManCo Authorised between 1/11/2015 and 30/06 2017 (inclusive)	Fund ManCo Authorised after 30/06/2017
6 Managerial Functions	1/07/18	Applicable from date of authorisation	
Performance of the organisation effectiveness role	1/07/18	Applicable from date of authorisation	
Effective supervision requirement/ location rule	1/07/18	1/07/18	The CBI will only authorise entities that are organised in a way that complies with these provisions.
Retrievability of records			
Guidance: Part I Delegate Oversight	4/11/15	Applicable from date of authorisation	
Guidance: Part II Organisational Effectiveness	Applicable from the date that a Fund ManCo has appointed a person to the Organisational Effectiveness role, or 1/07/18 at the latest.		
Guidance: Part III Directors' Time Commitments	4/11/15	Applicable from date of authorisation	
Guidance: Part IV Managerial Functions	1/07/18	1/07/18	Applicable from date of authorisation
Guidance: Part V Operational Issues	Retrievability of records: 1/07/18 Dedicated email address: 30/06/17, but CBI requesting email address be communicated to it before 28 April 2017.	Retrievability of records: 1/07/18 Dedicated email address: 30/06/17, but CBI requesting email address be communicated to it before 28 April 2017.	Retrievability of records: Applicable from date of authorisation. Dedicated email address: Applicable from date of authorisation.
Guidance: Part VI Procedural matters	This guidance is a reflection of the existing Fund ManCo guidance. Therefore no transitional arrangements apply.		

Key points to be addressed:

Existing entities can make changes to their organisational structure during the transitional period but only changes which bring them closer to compliance with the final CP86 rules and guidance

Fund ManCos will need to consider the final Rules and Guidance and update their BP/ PoA accordingly within the prescribed timelines. We understand that it may not be necessary to submit revised BPs/ PoAs to the CBI for review but any such updates could be subject to spot checks carried out by the CBI.

We will be working closely with our clients in relation to the impact of these changes. In the meantime, if you have any queries, please contact your usual contact at A&L Goodbody.

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