

## Chapter 3

# Requirements for alternative investment fund managers

### 3.1 Application

#### 3.1.1

**G** The application of this chapter is summarised in the following table; the detailed application is provided in each section.

Type of firm	Applicable sections
<i>Full-scope UK AIFM of a UK AIF.</i>	All of chapter 3.
<i>Full-scope UK AIFM of an EEA AIF operating from an establishment in the UK.</i>	All of chapter 3.
<i>Full-scope UK AIFM of an EEA AIF operating from a branch in another EEA state.</i>	All of chapter 3 with the exception of FUND 3.8 (Prime brokerage firms).
<i>Incoming EEA AIFM branch which manages a UK AIF.</i>	FUND 3.8 (Prime brokerage firms).
<i>Full-scope UK AIFM of a non-EEA AIF marketed in the UK.</i>	All of chapter 3 with the exception of FUND 3.12 (Marketing in the home Member State of the AIFM).
<i>Full-scope UK AIFM of a non-EEA AIF not marketed in the UK.</i>	All of chapter 3 with the exception of FUND 3.3 (Annual report of an AIF), FUND 3.11 (Depositaries) and FUND 3.12 (Marketing in the home Member State of the AIFM).
<i>UK depositary of a UK AIF or a non-EEA AIF.</i>	FUND 3.11 (Depositaries).

## 3.2 Investor information

### Application

3.2.1 **R** This section applies to a *full-scope UK AIFM* of:

- (1) a *UK AIF*;
- (2) an *EEA AIF*; and
- (3) a *non-EEA AIF*.

### Prior disclosure of information to investors

3.2.2 **R** An *AIFM* must, for each *UK AIF* and *EEA AIF* that it manages, and for each *AIF* it *markets* in the *EEA*, make available to *AIF* investors before they invest, in line with the *instrument constituting the fund*, the following information and any material changes to it:

- (1)
  - (a) a description of the investment strategy and objectives of the *AIF*;
  - (b) if the *AIF* is a *feeder AIF*, information on where the *master AIF* is established;
  - (c) if the *AIF* is a fund of funds, information on where the underlying funds are established;
  - (d) a description of the types of assets in which the *AIF* may invest;
  - (e) the investment techniques that the *AIF*, or the *AIFM* on behalf of the *AIF*, may employ and all associated risks;
  - (f) any applicable investment restrictions;
  - (g) the circumstances in which the *AIF* may use *leverage*;
  - (h) the types and sources of *leverage* permitted and the associated risks;
  - (i) any restrictions on the use of *leverage* and any *collateral* and asset reuse arrangements; and
  - (j) the maximum level of *leverage* which the *AIFM* is entitled to employ on behalf of the *AIF*;
- (2) a description of the procedures by which the *AIF* may change its investment strategy or investment policy, or both;
- (3) a description of the main legal implications of the contractual relationship entered into for the purpose of investment, including information on jurisdiction, the applicable law and the existence or

- absence of any legal instruments providing for the recognition and enforcement of judgments in the territory where the *AIF* is established;
- (4) the identity of the *AIFM*, the *AIF's depositary*, the auditor and any other service providers and a description of their duties and the investors' rights;
  - (5) a description of how the *AIFM* complies with the requirements referred to in ■ IPRU-INV 11.3.11G (Professional negligence) relating to professional liability risk;
  - (6) a description of:
    - (a) any *AIFM management function* delegated by the *AIFM*;
    - (b) any safe-keeping function delegated by the *depositary*;
    - (c) the identity of each delegate appointed in accordance with ■ FUND 3.10 (Delegation); and
    - (d) any conflicts of interest that may arise from such delegations;
  - (7) a description of the *AIF's* valuation procedure and of the pricing methodology for valuing assets, including the methods used in valuing any hard-to-value assets, in line with ■ FUND 3.9 (Valuation);
  - (8) a description of the *AIF's* liquidity risk management, including the redemption rights of investors in normal and exceptional circumstances, and the existing redemption arrangements with investors;
  - (9) a description of all fees, charges and expenses, and the maximum amounts directly or indirectly borne by investors;
  - (10) a description of how the *AIFM* ensures a fair treatment of investors;
  - (11) whenever an investor obtains preferential treatment or the right to obtain preferential treatment, a description of:
    - (a) that preferential treatment;
    - (b) the type of investors who obtain such preferential treatment; and
    - (c) where relevant, their legal or economic links with the *AIF* or *AIFM*;
  - (12) the procedure and conditions for the issue and sale of *units* or *shares*;
  - (13) the latest net asset value of the *AIF* or the latest market price of the *unit* or *share* of the *AIF*, in line with ■ FUND 3.9 (Valuation);
  - (14) the latest annual report, in line with ■ FUND 3.3 (Annual report of an AIF);
  - (15) where available, the historical performance of the *AIF*;
  - (16) (a) the identity of the *prime brokerage firm*;

- (b) a description of any material arrangements of the *AIF* with its *prime brokerage firm* and the way any conflicts of interest are managed;
  - (c) the provision in the contract with the *depository* on the possibility of transfer and reuse of *AIF* assets; and
  - (d) information about any transfer of liability to the *prime brokerage firm* that may exist; and
- (17) a description of how and when the information required under ■ FUND 3.2.5 R and ■ FUND 3.2.6 R will be disclosed.

[Note: article 23(1) of *AIFMD*]

3.2.3

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- (1) An *AIFM* must inform investors before they invest in the *AIF* of any arrangement made by the *depository* to contractually discharge itself of liability, in accordance with regulation 30 of the *AIFMD UK Regulation*.
- (2) The *AIFM* must also inform investors without delay of any changes with respect to *depository* liability.

[Note: article 23(2) of *AIFMD*]

3.2.4

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Where the *AIF* is required to publish a *prospectus* under article 3 of the *Prospectus Regulation*, only information referred to in ■ FUND 3.2.2 R and ■ 3.2.3 R that is additional to that contained in the *prospectus* needs to be disclosed, either separately or as additional information in the *prospectus*.

[Note: article 23(3) of *AIFMD*]

**Additional information to be made available on securities financing transactions and total return swaps**

3.2.4A

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- (1) The *Securities Financing Transactions Regulation* sets out the additional information which a *full-scope UK AIFM* must make available to investors before they invest.
- (2) ■ COLL 4.2.5BEU and ■ COLL 4.2.5CEU copy out the relevant provisions of that regulation.
- (3) A *full-scope UK AIFM* of an *AIF* that does not use *securities financing transactions* or *total return swaps* is not required to include the information in ■ COLL 4.2.5CEU in its pre-contractual documents.

**Preparation of key information document in accordance with the PRIIPs regulation**

3.2.4B

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- (1) The *PRIIPs Regulation* requires the manufacturer of a *PRIIP* to draw up a *key information document* in accordance with the *PRIIPs Regulation* before that *PRIIP* is made available to retail investors (as defined in the *PRIIPs Regulation*).
- (2) The requirements of the *PRIIPs Regulation* are directly applicable.

- (3) As a result, if an *AIFM* makes the *AIF* it manages available to *retail clients* in the *United Kingdom* it must comply with the *PRIPs Regulation*.
- (4) This means that, in addition to the prior disclosure of information set out at ■ FUND 3.2.2R and ■ FUND 3.2.3R, the *AIFM* must prepare:
  - (a) a *key information document*; or
  - (b) if the *AIF* is a *non-UCITS retail scheme*, a *key information document* or a *NURS-KII document*.

**Periodic disclosure**

3.2.5

**R**

An *AIFM* must, for each *UK AIF* and *EEA AIF* it manages, and each *AIF* it markets in the *EEA*, disclose to investors periodically:

- (1) the percentage of the *AIF's* assets that are subject to special arrangements arising from their illiquid nature;
- (2) any new arrangements for managing the liquidity of the *AIF*; and
- (3) the current risk profile of the *AIF* and the risk management systems employed by the *AIFM* to manage those risks.

[Note: article 23(4) of *AIFMD*]

3.2.6

**R**

An *AIFM* that manages a *UK AIF* or an *EEA AIF* or markets an *AIF* in the *EEA* must, for each such *AIF* that employs *leverage*, disclose on a regular basis:

- (1) any changes to:
  - (a) the maximum level of leverage that the *AIFM* may employ on behalf of the *AIF*; and
  - (b) any right of reuse of *collateral* or any guarantee granted under the leveraging arrangement; and
- (2) the total amount of leverage employed by that *AIF*.

[Note: article 23(5) of *AIFMD*]

**Subordinate measures**

3.2.7

**G**

Articles 108 and 109 of the *AIFMD level 2 regulation* provide detailed rules supplementing this section.

### 3.3 Annual report of an AIF

#### Application

3.3.1 **R** This section applies to a *full-scope UK AIFM* of:

- (1) a *UK AIF*;
- (2) an *EEA AIF*; and
- (3) a *non-EEA AIF marketed in the UK*.

#### Provision of an annual report

3.3.2 **R** An *AIFM* must, for each *UK AIF* and *EEA AIF* it manages and for each *AIF* it markets in the *UK*:

- (1) make an annual report available to investors for each financial year;
- (2) provide the annual report to investors on request; and
- (3) make the annual report available to the *FCA* and, in the case of an *EEA AIF*, to the *competent authority* of that *AIF*.

[**Note:** article 22(1) first paragraph and article 24(3)(a) of *AIFMD*]

3.3.3 **R** Subject to **■ FUND 3.3.4R** (2) and **■ FUND 3.3.4AR**, an *AIFM* must make the annual report available, in line with **■ FUND 3.3.2R** (1), no later than six months after the end of the financial year.

[**Note:** article 22(1) first paragraph of *AIFMD*]

3.3.4 **R**

- (1) Where the *AIF* is required to make an annual financial report public under **■ DTR 4.1.3 R** (Publication of annual financial reports) or an equivalent provision implementing article 4.1 of the Transparency Directive in the *Home State* of the *AIF*, only information referred to in **■ FUND 3.3.5 R** that is additional to the annual financial report needs to be provided to investors on request, either separately or as an additional part of the annual financial report.
- (2) Where additional information in (1) is provided as an addition to the annual financial report, that report must be made public no later than four months following the end of the financial year, under **■ DTR 4.1.3 R** (Publication of annual financial reports) or an equivalent

provision implementing article 4.1 of the Transparency Directive in the *Home State* of the *AIF*.

[Note: second paragraph, article 22(1) of *AIFMD*]

**3.3.4A** **R** ■ FUND 3.3.3R does not apply to a *full-scope UK AIFM* of a *non-UCITS retail scheme*.

**3.3.4B** **G** A *full-scope UK AIFM* of a *non-UCITS retail scheme* is required to make available and publish its annual report within four *months* after the end of each *annual accounting period* (see ■ COLL 4.5.14R (Publication and availability of annual and half-yearly long report)).

### Contents of the annual report

**3.3.5** **R** The annual report must contain:

- (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 in the information required to be made available to investors under ■ FUND 3.2.2 R (Prior disclosure of information to investors) during the financial year covered by the report;
- (5) (a) the total amount of *remuneration* paid by the *AIFM* to its staff for the financial year, split into fixed and variable remuneration, including, where relevant, any *carried interest* paid by the *AIF*; and  
 (b) the number of beneficiaries; and
- (6) the aggregate amount of *remuneration* broken down by senior management and members of staff of the *AIFM* whose actions have a material impact on the risk profile of the *AIF*.

[Note: article 22(2) of *AIFMD*]

**3.3.5A** **G** The *FCA* has provided additional *guidance* on the disclosure requirements relating to *remuneration* paid by an *AIFM* to its staff. The *guidance* can be found at: [ <http://www.fca.org.uk/your-fca/documents/finalised-guidance/fg14-02> ]

### Accounting information in the annual report

**3.3.6** **R** The accounting information given in the annual report must be:

- (1) prepared in accordance with the accounting standards of the *Home State* of the *AIF* (or, for a *non-EEA AIF*, the accounting standards of the third country where it is *established*) and with the accounting rules set out in the *AIF's instrument constituting the fund*; and
- (2) audited by one or more persons empowered by law to audit accounts under the Audit Directive (or for a *non-EEA AIF*, under international auditing standards in force in the country where the *non-EEA AIF* is established).

[Note: article 22(3) of *AIFMD*]



**3.3.7** **R** The auditor's report, including any qualifications, must be reproduced in full in the annual report.

[Note: second paragraph article 22(3) of AIFMD]

**Timing of first annual report**

**3.3.7A** **R** An AIFM must comply with the provisions in this section in relation to the first financial year end date of the AIF following the AIFM's authorisation as an AIFM.

**Information to be included in annual reports on securities financing transactions and total return swaps**

**3.3.7B** **G** (1) The *Securities Financing Transactions Regulation* sets out the additional information which a *full-scope UK AIFM* of an AIF must include in the AIF's annual report.

(2) ■ COLL 4.5.8ABEU and ■ COLL 4.5.8ACEU copy out the relevant provisions of that regulation.

(3) A *full-scope UK AIFM* of an AIF that has not used *securities financing transactions* or *total return swaps* during the relevant period is not required to include the information in ■ COLL 4.5.8ACEU in the AIF's annual report.

**Subordinate measures**

**3.3.8** **G** Articles 103 to 107 of the *AIFMD level 2 regulation* provide detailed rules supplementing this section.

## 3.4 Reporting obligations to the FCA

### Application

3.4.1 **R** This section applies to a *full-scope UK AIFM* of:

- (1) a *UK AIF*;
- (2) an *EEA AIF*; and
- (3) a *non-EEA AIF*.

### Reporting obligations

3.4.2 **R** An *AIFM* must regularly report to the *FCA* on behalf of each *AIF* it manages:

- (1) the main instruments in which it is trading;
- (2) the principal markets of which it is a member or where it actively trades; and
- (3) the principal exposures and most important concentrations of each *AIF* it manages.

[Note: article 24(1) of *AIFMD*]

### Content of reporting information

3.4.3 **R** An *AIFM* must, for each *UK AIF* and *EEA AIF* it manages, and for each *AIF* it markets in the *EEA*, provide the following to the *FCA*:

- (1) the percentage of the *AIF*'s assets that are subject to special arrangements arising from their illiquid nature;
- (2) any new arrangements for managing the liquidity of the *AIF*;
- (3) the current risk profile of the *AIF* and the risk management systems employed by the *AIFM* to manage the *market risk*, *liquidity risk*, *counterparty risk* and other risks, including *operational risk*;
- (4) information on the main categories of assets in which the *AIF* is invested; and

- (5) the results of the stress tests performed in accordance with
  - FUND 3.6.3R (2) (Liquidity systems and procedures) and
  - FUND 3.7.5R (2)(b) (Risk management systems).

[Note: article 24(2) of AIFMD]

**3.4.4** **R** An AIFM must, at the FCA's request, provide at the end of each quarter a detailed list of all AIFs which it manages.

[Note: article 24(3)(b) of AIFMD]

**AIFs that employ leverage on a substantial basis**

**3.4.5** **R** An AIFM managing an AIF that employs *leverage* on a substantial basis must make the following information available to the FCA about that AIF:

- (1) the overall level of leverage employed by the AIF;
- (2) a breakdown of *leverage* arising from borrowing of cash or *securities* and *leverage* embedded in financial *derivatives*;
- (3) the extent to which the AIF's assets have been reused under leveraging arrangements; and
- (4) the identity of the five largest sources of borrowed cash or *securities* for the AIF, and the amounts of *leverage* received from each of those sources.

[Note: article 24(4) of AIFMD]

**Meaning of employing leverage on a substantial basis**

**3.4.6** **EU** Use of leverage on a 'substantial basis'

- 1. Leverage shall be considered to be employed on a substantial basis for the purposes of Article 24(4) of Directive 2011/61/EU when the exposure of an AIF as calculated according to the commitment method under Article 8 of this Regulation exceeds three times its net asset value.

[Note: article 111(1) of the AIFMD level 2 regulation]

**Additional information**

**3.4.6A** **R** In addition to the information in ■ FUND 3.4.2 R, an AIFM must regularly report the following information to the FCA:

- (1) on behalf of each AIF it manages:
  - (a) the geographical focus of investments expressed as a percentage of the total value of assets under management;
  - (b) an indication of whether a short position is used to hedge a position with a similar economic exposure;
  - (c) the Value at Risk (VaR), if this is calculated for the AIF for any other purpose; and

- (d) the portfolio's sensitivity to a change in foreign exchange rates and commodity prices, if this is calculated for the *AIF* for any other purpose; and
- (2) the information in ■ FUND 3.4.3 R for each *non-EEA AIF* it manages that is not *marketed* in the *EEA*, if:
  - (a) the *AIFM* is subject to quarterly reporting under article 110 of the *AIFMD level 2 regulation* (see ■ SUP 16.18.4EU); and
  - (b) that *AIF* is the *master AIF* of a *feeder AIF* which the *AIFM* also manages and that *feeder AIF* is:
    - (i) an *EEA AIF*; or
    - (ii) a *non-EEA AIF* that is marketed in the *EEA*.

[Note: article 24(5) of *AIFMD*]

**3.4.6B** G Further details in relation to the additional reporting requirements in ■ FUND 3.4.6A R can be found in *ESMA's opinion on the "Collection of information for the effective monitoring of systemic risk under article 24(5), first sub-paragraph, of the AIFMD"* (*ESMA 2013/1340*)  
  
([https://www.esma.europa.eu/sites/default/files/library/2015/11/2013-esma-1340\\_opinion\\_on\\_collection\\_of\\_information\\_under\\_aifmd\\_for\\_publication.pdf](https://www.esma.europa.eu/sites/default/files/library/2015/11/2013-esma-1340_opinion_on_collection_of_information_under_aifmd_for_publication.pdf)) dated 1 October 2013.

**3.4.6C** R In addition to the information in ■ FUND 3.4.2R, an *AIFM* must regularly report to the *FCA* the information in ■ FUND 3.4.3R for each *non-EEA AIF* it manages that is not *marketed* in the *EEA* if the *AIFM* is subject to quarterly reporting under article 110 of the *AIFMD level 2 regulation* (see ■ SUP 16.18.4EU) for that *AIF*.  
  
[Note: article 24(5) of *AIFMD*]

**Subordinate measures**

**3.4.7** G Articles 110 and 111 of the *AIFMD level 2 regulation* provide detailed rules supplementing this section.

**Guidelines**

**3.4.8** G *ESMA's guidelines on reporting obligations under articles 3(3)(d) and 24(1), (2) and (4) of the AIFMD* (*ESMA 2013/1339*)  
  
([https://www.esma.europa.eu/sites/default/files/library/2015/11/2013-1339\\_final\\_report\\_on\\_esma\\_guidelines\\_on\\_aifmd\\_reporting\\_for\\_publication\\_revised.pdf](https://www.esma.europa.eu/sites/default/files/library/2015/11/2013-1339_final_report_on_esma_guidelines_on_aifmd_reporting_for_publication_revised.pdf))  
  
provide further details in relation to the requirements in this section.

**Further information**

**3.4.9** G Further information in relation to *AIFMD* reporting can be found in ■ SUP 16.18 (*AIFMD* reporting), including information in relation to the frequency of reporting.



**3.5 Investment in securitisation positions**

3.5.1 **G** [deleted]

3.5.2 **G** [deleted]

3.5.3 **G** [deleted]

**Application**

3.5.4 **R** This section applies to a *full-scope UK AIFM* of:

- a *UK AIF*;
- an *EEA AIF*; and
- a *non-EEA AIF*.

**Corrective action**

3.5.5 **R** Where an *AIFM* is exposed to a securitisation that does not meet the requirements provided for in the *Securitisation Regulation*, it must, in the best interests of the investors in the relevant *AIFs*, act and take corrective action, if appropriate.

[**Note:** article 17 of *AIFMD*]

3.5.6 **G** Article 41 of the *Securitisation Regulation* replaces the original article 17 of *AIFMD* with an amended provision. ■ **FUND 3.5.4R** and ■ **3.5.5R** transpose article 17 of *AIFMD*, as amended.

3.5.7 **G** A more general consequence of the replacement of article 17 of *AIFMD* is that from 1 January 2019, Section 5 (Investment in Securitisation Positions) of the *AIFMD level 2 regulation* no longer applies, subject to transitional provisions. Where the transitional provisions are inapplicable, article 5 (Due-diligence requirements for institutional investors) of the *Securitisation Regulation* (in combination with ■ **FUND 3.5.4R** and ■ **3.5.5R**), completely replaces Section 5 (articles 50 to 56 inclusive) of the *AIFMD level 2 regulation*.

## 3.5.8

**G** The relevant transitional provisions apply to certain securitisations issued during periods before 1 January 2019. They are set out in articles 43(5) and 43(6) of the *Securitisation Regulation*. Where the transitional provisions apply, they have the effect that article 51 of the *AIFMD level 2 regulation*, concerning requirements for retained interest, and the due-diligence requirements provided for in Section 5 of that regulation, may continue to apply to eligible securitisations, instead of article 5 of the *Securitisation Regulation*.



## 3.6 Liquidity

### Application

3.6.1 **R** This section applies to a *full-scope UK AIFM* of:

- (1) a *UK AIF*;
- (2) an *EEA AIF*; and
- (3) a *non-EEA AIF*.

### Alignment of investment strategy, liquidity profile and redemption policy

3.6.2 **R** An *AIFM* must ensure that the investment strategy, liquidity profile and redemption policy of each *AIF* it manages are consistent.

[Note: article 16(2) of *AIFMD*]

### Liquidity systems and procedures

3.6.3 **R** An *AIFM* must, for each *AIF* it manages that is not an unleveraged closed-ended *AIF*:

- (1) employ an appropriate liquidity management system and adopt procedures which:
  - (a) enable it to monitor the liquidity risk of the *AIF*; and
  - (b) ensure that the liquidity profile of the investments of the *AIF* complies with the *AIF*'s underlying obligations; and
- (2) regularly conduct stress tests, under normal and exceptional liquidity conditions, which enable it to assess the liquidity risk of the *AIF* and monitor that risk.

[Note: article 16(1) of *AIFMD*]

### Subordinate measures

3.6.4 **G** Articles 46 to 49 of the *AIFMD level 2 regulation* provide detailed rules supplementing this section.

## 3.7 Risk management

### Application

3.7.1 **R** This section applies to a *full-scope UK AIFM* of:

- (1) a *UK AIF*;
- (2) an *EEA AIF*; and
- (3) a *non-EEA AIF*.

### Functional and hierarchical separation

3.7.2 **R**

- (1) An *AIFM* must functionally and hierarchically separate the functions of risk management from the operating units, including from the functions of portfolio management.
- (2) An *AIFM* must, in any event, be able to demonstrate that:
  - (a) specific safeguards against conflicts of interest allow for the independent performance of risk management activities; and
  - (b) the risk management process satisfies the requirements of this section and is consistently effective.

[Note: article 15(1) of *AIFMD*]

3.7.3 **EU**

Functional and hierarchical separation of the risk management function

1. The risk management function shall be considered as functionally and hierarchically separated from the operating units, including the portfolio management function, only where all the following conditions are satisfied:
  - (a) persons engaged in the performance of the risk management function are not supervised by those responsible for the performance of the operating units, including the portfolio management function, of the *AIFM*;
  - (b) persons engaged in the performance of the risk management function are not engaged in the performance of activities within the operating units, including the portfolio management function;
  - (c) persons engaged in the performance of the risk management function are compensated in accordance with the achievement of the objectives linked to that function, independently of the performance of the operating units, including the portfolio management function;



2. The functional and hierarchical separation of the risk management function in accordance with paragraph 1 shall be ensured throughout the whole hierarchical structure of the AIFM, up to its governing body. It shall be reviewed by the governing body and, where it exists, the supervisory function of the AIFM.

[Note: article 42(1) and (2) of the *AIFMD level 2 regulation*]

**3.7.4**

**EU**

**Safeguards against conflicts of interest**

1. The safeguards against conflicts of interest referred to in Article 15(1) of Directive 2011/61/EU shall ensure, at least, that:
  - (a) decisions taken by the risk management function are based on reliable data, which are subject to an appropriate degree of control by the risk management function;
  - (b) the remuneration of those engaged in the performance of the risk management function reflects the achievement of the objectives linked to the risk management function, independently of the performance of the business areas in which they are engaged;
  - (c) the risk management function is subject to an appropriate independent review to ensure that decisions are being arrived at independently;
  - (d) the risk management function is represented in the governing body or the supervisory function, where it has been established, at least with the same authority as the portfolio management function;
  - (e) any conflicting duties are properly segregated.
2. Where proportionate, taking into account the nature, scale and complexity of the AIFM, the safeguards referred to in paragraph 1 shall also ensure that:
  - (a) the performance of the risk management function is reviewed regularly by the internal audit function, or, if the latter has not been established, by an external party appointed by the governing body;
  - (b) where a risk committee has been established, it is appropriately resourced and its non-independent members do not have undue influence over the performance of the risk management function.
3. The governing body of the AIFM and, where it exists, the supervisory function shall establish the safeguards against conflicts of interest laid down in paragraphs 1 and 2, regularly review their effectiveness and take timely remedial action to address any deficiencies.

[Note: article 43 of the *AIFMD level 2 regulation*]

**Risk management systems**

**3.7.5**

**R**

- (1) (a) An *AIFM* must implement adequate risk management systems to identify, measure, manage and monitor all risks relevant to each *AIF* investment strategy and to which each *AIF* is, or may be, exposed.
- (b) In particular, an *AIFM* must not solely or mechanically rely on credit ratings issued by credit rating agencies, as defined in article 3(1)(b) of Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit

rating agencies, for assessing the creditworthiness of the *AIF*'s assets.

- (2) An *AIFM* must, at least:
- (a) implement an appropriate, documented and regularly updated due diligence process when investing on behalf of the *AIF*, according to the investment strategy, objectives and risk profile of the *AIF*;
  - (b) ensure that the risks associated with each investment position of the *AIF* and their overall effect on the *AIF*'s portfolio can be properly identified, measured, managed and monitored on an ongoing basis, including through the use of appropriate stress testing procedures; and
  - (c) ensure that the risk profile of the *AIF* corresponds to the size, portfolio structure and investment strategies and objectives of the *AIF* as set out in the *instrument constituting the fund*, *prospectus* and offering documents.

[Note: article 15(2) first paragraph and article 15(3) of *AIFMD*]

- 3.7.5A** G An *AIFM* should use the form in ■ SUP 15 Annex 6C R to notify the *FCA* of any material changes to the risk management policy and of the arrangements, processes and techniques referred to in article 45 of the *AIFMD level 2 regulation*, as required by article 41(4) of the *AIFMD level 2 regulation*.

### Review of risk management systems

- 3.7.6** R An *AIFM* must:
- (1) review the risk management systems with appropriate frequency and, in any event, at least once a year; and
  - (2) adapt them whenever necessary.

[Note: article 15(2) second paragraph of *AIFMD*]

### Maximum leverage levels

- 3.7.7** R
- (1) An *AIFM* must:
    - (a) set a maximum level of *leveraging* which it may employ on behalf of each *AIF* it manages; and
    - (b) where the *leverage* arrangement allows the right to reuse *collateral* or the granting of a guarantee, set out the extent of that right or guarantee.
  - (2) An *AIFM*, in complying with (1), must take into account relevant matters including:
    - (a) the type of *AIF*;
    - (b) the investment strategy of the *AIF*;
    - (c) the sources of *leverage* of the *AIF*;

- (d) any other link or relevant relationship with other financial services institutions which could pose systemic risk;
- (e) the need to limit the exposure to any single counterparty;
- (f) the extent to which the *leverage* is collateralised;
- (g) the asset-liability ratio; and
- (h) the scale, nature and extent of the activity of the *AIFM* on the markets concerned.

[Note: article 15(4) of *AIFMD*]

**3.7.8** **R** An *AIFM* must demonstrate that the *leverage* limits it sets under ■ FUND 3.7.7R (1)(a) are reasonable and that it complies with those limits at all times.

[Note: article 25(3) first sentence of *AIFMD*]

**3.7.9** **G** To comply with ■ FUND 3.7.8 R, an *AIFM* should report to the FCA any changes to the *leverage* limits it sets.

**Subordinate measures**

**3.7.10** **G** Articles 6 to 11 of the *AIFMD level 2 regulation* provide detailed rules on the calculation of levels of *leverage*, articles 38 to 47 of the *AIFMD level 2 regulation* provide detailed rules on risk management and article 112 of the *AIFMD level 2 regulation* provides detailed rules on circumstances when *competent authorities* may impose *leverage* limits or other restrictions on the management of AIFs.

## 3.8 Prime brokerage firms

### Application

3.8.1

R

This section applies to:

- (1) a *full-scope UK AIFM* of:
  - (a) a *UK AIF*;
  - (b) an *EEA AIF* managed or *marketed* from an establishment in the *UK*; and
  - (c) a *non-EEA AIF*; and
- (2) an *incoming EEA AIFM branch* which manages or *markets* a *UK AIF*.

### Selection of a prime brokerage firm

3.8.2

R

An *AIFM* must exercise due skill, care and diligence in the selection and appointment of a *prime brokerage firm*.

[Note: article 14(3) second paragraph of the *AIFMD*]

### Prime brokerage firm contract

3.8.3

R

Where the *AIFM*, on behalf of an *AIF*, uses the services of a *prime brokerage firm*, the terms must be in a written contract. In particular, any possibility of transfer and reuse of *AIF* assets must be provided for in that contract and must comply with the *AIF's instrument constituting the fund*. The contract must provide for the *depository* to be informed of the contract.

[Note: article 14(3) first paragraph of the *AIFMD*]



## 3.9 Valuation

### Application

- 3.9.1 **R** This section applies to a *full-scope UK AIFM* of:
- (1) a *UK AIF*;
  - (2) an *EEA AIF*; and
  - (3) a *non-EEA AIF*.

### Responsibility of the AIFM

- 3.9.2 **R** An *AIFM* is responsible for the proper valuation of *AIF* assets, the calculation of the net asset value and the publication of that net asset value.
- [Note: article 19(10) first sentence first paragraph of *AIFMD*]

### Standard of care of the valuation

- 3.9.3 **R** An *AIFM* must ensure that any valuation of an *AIF*'s assets is performed impartially and with all due skill, care and diligence.
- [Note: article 19(8) of *AIFMD*]

### Establishment of procedures for valuation of assets

- 3.9.4 **R** An *AIFM* must ensure that, for each *AIF* it manages, appropriate and consistent procedures are established so that under the rules laid down in the applicable national law of the country where the *AIF* is established and the *instrument constituting the fund*:
- (1) a proper and independent valuation of the assets of the *AIF* can be performed; and
  - (2) the net asset value per unit or share of the *AIF* is calculated and disclosed to investors.

[Note: article 19(1), (2) and (3) first paragraph of *AIFMD*]

**Frequency of valuation of assets and calculation of net asset value**

3.9.5

**R**

- (1) An *AIFM* must ensure that the valuation procedure in ■ FUND 3.9.4 R provides for the assets of any *AIF* under the *AIFM*'s management to be valued and the net asset value per *unit* or *share* to be calculated at least once a year.
- (2) Where an *AIF* is open-ended, such valuations and calculations must also be carried out at a frequency that is appropriate both to the assets held by the *AIF* and its issuance and redemption frequency.
- (3) Where an *AIF* is closed-ended, such valuations and calculations must also be carried out in case of an increase or decrease of the capital by the relevant *AIF*.

[Note: article 19(3) second, third and fourth paragraphs of *AIFMD*]

**Informing investors of valuations of assets and calculations of net asset value**

3.9.6

**R**

An *AIFM* must ensure that investors in the *AIFs* under its management are informed of the valuations and calculations in the manner set out in the relevant *instrument constituting the fund*.

[Note: article 19(3) fifth paragraph of *AIFMD*]

**Performance of the valuation function**

3.9.7

**R**

- (1) An *AIFM* may perform the valuation itself, provided that:
  - (a) the valuation task is functionally independent from the portfolio management; and
  - (b) the remuneration policy and other measures ensure that conflicts of interest are mitigated and that undue influence upon the employees involved is prevented.
- (2) An *AIFM* that does not perform the valuation function itself must ensure that the function is performed by an *external valuer*.
- (3) An *external valuer* appointed under (2) must be a *person* independent from:
  - (a) the *AIF* in respect of which the valuation function is performed;
  - (b) the *AIFM*; and
  - (c) any other *persons* with *close links* to the *AIF* or the *AIFM*.

[Note: article 19(4) first paragraph of *AIFMD*]

**Appointment of the depositary as an external valuer**

3.9.8

**R**

The *depositary* appointed for an *AIF* may not be appointed as an *external valuer* of that *AIF* unless:

- (1) it has functionally and hierarchically separated the performance of its depositary functions from its tasks as an *external valuer*; and

- (2) the potential conflicts of interests are properly identified, managed, monitored and disclosed to the investors of the *AIF*.

[Note: article 19(4) second paragraph of *AIFMD*]

**Appointment of an external valuer**

3.9.9

**R**

Where an *external valuer* performs the valuation function, the *AIFM* must be able to demonstrate that:

- (1) the *external valuer* is subject to mandatory professional registration recognised by law or legal or regulatory provisions or rules of professional conduct;
- (2) the *external valuer* can provide sufficient professional guarantees to be able to perform the relevant valuation function effectively under this section; and
- (3) the appointment of the *external valuer* complies with the requirements of **FUND 3.10.2 R** (General delegation arrangements) and the *AIFMD level 2 regulation*.

[Note: article 19(5) of *AIFMD*]

**Delegation by an external valuer**

3.9.10

**G**

*AIFMs* should be aware that regulation 24(2) of the *AIFMD UK Regulation* prohibits an *external valuer* from delegating valuation to a third party.

**Notification of appointment of an external valuer**

3.9.11

**R**

- (1) An *AIFM* must notify the appointment of an *external valuer* to the *FCA*.
- (2) An *AIFM* must notify the *FCA* under (1) using the material change form in **SUP 15 Annex 6C R**.

[Note: article 19(7) first part of first paragraph of *AIFMD*]

3.9.12

**G**

Under regulation 24(3) of the *AIFMD UK regulation*, the *FCA* may require an *AIFM* to appoint another *external valuer* where it considers that the appointment does not comply with **FUND 3.9.9 R**.

**Subordinate measures**

3.9.13

**G**

Articles 67 to 74 of the *AIFMD level 2 regulation* provide detailed rules supplementing this section.

## 3.10 Delegation

### Application

**3.10.1** **R** This section applies to a *full-scope UK AIFM* of:

- (1) a *UK AIF*;
- (2) an *EEA AIF*; and
- (3) a *non-EEA AIF*

in relation to the delegation of those *AIFM management functions* for which it is responsible, other than supporting tasks such as administrative or technical functions.

[Note: recital 31 of *AIFMD*]

### General delegation requirements

**3.10.2** **R** An *AIFM* must ensure the following conditions are met when a delegate carries out any function on its behalf:

- (1) the *AIFM* has notified the *FCA* of the delegation before the delegation arrangements become effective; and
- (2)
  - (a) the *AIFM* is able to justify its entire delegation structure with objective reasons;
  - (b) the delegate has sufficient resources to perform the respective activity and the persons who effectively conduct the business of the delegate are of sufficiently good repute and experience;
  - (c) (subject to **FUND 3.10.7 G**) the delegation of *AIFM investment management functions* is conferred only on a delegate that is authorised or registered for the purpose of asset management and subject to supervision;
  - (d) in addition to (c), where the delegation of *AIFM investment management functions* is conferred on a third-country delegate, cooperation between the *FCA* and the supervisory authority of the delegate is ensured;
  - (e) the delegation does not prevent the *FCA* from supervising the *AIFM* effectively and, in particular, does not prevent the *AIFM* from acting, or the *AIF* from being managed, in the best interests of its investors; and
  - (f) the *AIFM* is able to demonstrate that:



- (i) the delegate is qualified and capable of undertaking the functions in question;
- (ii) it was selected with all due care; and
- (iii) the *AIFM* can monitor the delegated activity effectively at any time, give further instructions to the delegate at any time and withdraw the delegation with immediate effect when this is in the interest of investors.

[Note: article 20(1) of *AIFMD*]

**3.10.2A** **R** An *AIFM* must notify the *FCA* of delegation arrangements under **■ FUND 3.10.2R (1)** using the form in **■ FUND 3 Annex 2 R**.

**3.10.3** **G** For the purposes of **■ FUND 3.10.2R (2)(d)** cooperation is ensured between the *FCA* and the supervisory authorities of a third-country delegate where a cooperation arrangement is in place between the two authorities in accordance with *AIFMD* and article 78(3) of the *AIFMD level 2 regulation*.

**Sub-delegation**

**3.10.4** **R** An *AIFM* must ensure the following conditions are met when any of its delegates carries out a sub-delegation:

- (1) the *AIFM* has consented to the sub-delegation before the sub-delegation arrangements become effective;
- (2) the *AIFM* has notified the *FCA* of the sub-delegation before the sub-delegation arrangements become effective; and
- (3) the conditions in **■ FUND 3.10.2R (2)** (General delegation requirements) are satisfied in relation to the sub-delegation, with references to 'delegate' and 'delegation' replaced by references to 'sub-delegate' and 'sub-delegation'.

[Note: article 20(4) of *AIFMD*]

**3.10.4A** **R** An *AIFM* must notify the *FCA* of sub-delegation arrangements under **■ FUND 3.10.4R (2)** using the form in **■ FUND 3 Annex 2 R**.

**3.10.5** **R** An *AIFM* must comply with the *rules* in this section which are applicable to a sub-delegation in relation to any further sub-delegation of its functions by a sub-delegate.

[Note: article 20(6) of *AIFMD*]

**Delegation of AIFM investment management functions**

**3.10.6** **R** An *AIFM* must not delegate or consent to the sub-delegation of *AIFM investment management functions* to:

- (1) the *depository* or a delegate of the *depository*; or

- (2) any other entity whose interests may conflict with those of the *AIFM* or the investors of the *AIF*, unless:
  - (a) that entity has functionally and hierarchically separated the performance of its *AIFM investment management function* from its other potentially conflicting tasks; and
  - (b) the potential conflicts of interest are properly identified, managed, monitored and disclosed to the investors of the *AIF*.

[Note: article 20(2) and (5) of *AIFMD*]

**3.10.7** G The *FCA* may consent to the delegation by a *Full-scope UK AIFM* of its *AIFM investment management functions* to an entity which is not authorised or registered for the purpose of asset management and subject to supervision in accordance with regulation 26 of the *AIFMD UK regulation*.

**3.10.7A** D An *AIFM* that wishes to apply for the approval of its delegation arrangements in accordance with regulation 26 of the *AIFMD UK regulation* must do so using the form in ■ **FUND 3 Annex 2 R**.

**Letterbox entity**  
.....

**3.10.8** R An *AIFM* must not delegate its functions to the extent that, in essence, it can no longer be considered to be the *AIFM* of the *AIF* and to the extent that it becomes a letter-box entity.

[Note: article 20(3) of *AIFMD*]

**3.10.9** EU Letter-box entity and AIFM no longer considered to be managing an AIF

1. An AIFM shall be deemed a letter-box entity and shall no longer be considered to be the manager of the AIF at least in any of the following situations:
  - (a) the AIFM no longer retains the necessary expertise and resources to supervise the delegated tasks effectively and manage the risks associated with the delegation;
  - (b) the AIFM no longer has the power to take decisions in key areas which fall under the responsibility of the senior management or no longer has the power to perform senior management functions in particular in relation to the implementation of the general investment policy and investment strategies;
  - (c) the AIFM loses its contractual rights to inquire, inspect, have access or give instructions to its delegates or the exercise of such rights becomes impossible in practice;
  - (d) the AIFM delegates the performance of investment management functions to an extent that exceeds by a substantial margin the investment management functions performed by the AIFM itself. When assessing the extent of delegation, competent authorities shall assess the entire delegation structure taking into account not only the assets managed under delegation but also the following qualitative criteria:
    - (i) the types of assets the AIF or the AIFM acting on behalf of the AIF is invested in, and the importance of the assets managed under delegation for the risk and return profile of the AIF;

- (ii) the importance of the assets under delegation for the achievement of the investment goals of the AIF;
- (iii) the geographical and sectoral spread of the AIF's investments;
- (iv) the risk profile of the AIF;
- (v) the type of investment strategies pursued by the AIF or the AIFM acting on behalf of the AIF;
- (vi) the types of tasks delegated in relation to those retained; and
- (vii) the configuration of delegates and their sub-delegates, their geographical sphere of operation and their corporate structure, including whether the delegation is conferred on an entity belonging to the same corporate group as the AIFM.

[Note: Article 82(1) of the *AIFMD level 2 regulation*]

**Liability for delegated functions**.....

**3.10.10** **G** An *AIFM's* liability towards the *AIF* and its investors is not affected by the *AIFM* delegating functions to a third party, or by any further sub-delegation (see regulation 28(1) of the *AIFMD UK Regulation*).

**Review of delegation and sub-delegation**.....

**3.10.11** **R** An *AIFM* must review on an ongoing basis the services provided by each:

- (1) delegate appointed under **FUND 3.10.2 R**; and
- (2) sub-delegate appointed under **FUND 3.10.4 R**.

[Note: article 20(1) and 20(4) of *AIFMD*]

**3.10.12** **G** An *AIFM* should make each of its delegates aware of the requirement to review the services provided by each of its sub-delegates on an ongoing basis (see regulation 28(2) of the *AIFMD UK Regulation*).

**Subordinate measures**.....

**3.10.13** **G** Articles 75 to 82 of the *AIFMD level 2 regulation* provide detailed rules supplementing this section.

## 3.11 Depositories

### Application

**3.11.1** **R** This section applies in accordance with the table in **FUND 3.11.2 R** and **FUND 3.11.3 R**.

**3.11.2** **R** This table belongs to **FUND 3.11.1 R**.

<i>Rule</i>	<i>Full-scope UK AIFM of a UK AIF or an EEA AIF (other than a non-EEA feeder AIF which is marketed in the UK)</i>	<i>Full-scope UK AIFM of a non-EEA AIF or a non-EEA feeder AIF which is marketed in the UK</i>	<i>UK depositary of a UK AIF (other than a non-EEA feeder AIF which is marketed in the UK) managed by a full-scope UK AIFM or an EEA AIFM</i>	<i>UK depositary of a non-EEA AIF or a non-EEA feeder AIF which is marketed in the UK</i>
3.11.4R	x			
3.11.5R	x		x	
3.11.7R	x			
3.11.9R			x	
3.11.10R	x			
3.11.12R	x			
3.11.14R	x			
3.11.16R			x	
3.11.18R	x			
3.11.19R	x		x	
3.11.20R			x	x
3.11.21R			x	x
3.11.23R			x	x
3.11.24R			x	
3.11.25R			x	x
3.11.26R			x	
3.11.28R			x	
3.11.29R			x	
3.11.30R			x	
3.11.33R		x		

**Note:** "x" means "applies".

- 3.11.3** **R** A UK depository of a non-EEA AIF or a non-EEA feeder AIF which is marketed in the UK that does not perform all of the functions of cash monitoring, safekeeping and oversight for the AIF need only comply with the following *rules* that are applicable to the functions it performs:
- (1) ■ FUND 3.11.20 R if it performs only the cash monitoring function;
  - (2) ■ FUND 3.11.21 R and ■ FUND 3.11.23 R if it performs only the safekeeping function;
  - (3) ■ FUND 3.11.25 R if it performs only the oversight function;
  - (4) ■ FUND 3.11.20 R, ■ FUND 3.11.21 R and ■ FUND 3.11.23 R if it performs only the cash monitoring and safekeeping functions;
  - (5) ■ FUND 3.11.20 R and ■ FUND 3.11.25 R if it performs only the cash monitoring and oversight functions; and
  - (6) ■ FUND 3.11.21 R, ■ FUND 3.11.23 R and ■ FUND 3.11.25 R if it performs only the safekeeping and oversight functions.

**Appointment of a single depository**

- 3.11.4** **R** An AIFM must, for each AIF it manages, ensure that:
- (1) a single *depository* is appointed; and
  - (2) the assets of the AIF are entrusted to the *depository* for safekeeping in accordance with
    - (a) for a UK AIF, ■ FUND 3.11.21 R and ■ FUND 3.11.23 R; or
    - (b) for an EEA AIF, the national laws and regulations in the *Home State* of the AIF implementing article 21(8) of AIFMD.

[Note: article 21(1) and (8) of AIFMD]

**General obligations**

- 3.11.5** **R** An AIFM and a *depository* must, in the context of their respective roles, act honestly, fairly, professionally, independently and in the interest of the AIF and its investors.

[Note: article 21(10) first paragraph of AIFMD]

- 3.11.6** **G** The Act specifies that the *trustee* of an AUT and the *depository* of an ACS must be independent of its *authorised fund manager*, and the OEIC Regulations specify that the *depository* of an ICVC must be independent of the ICVC and its *directors*. However, these requirements do not apply to AIFs which are not *authorised funds*, and, therefore, an AIFM and a *depository* of an *unauthorised AIF* may be from within the same *group*, but only if conflicts of interest are avoided and there is sufficient organisational separation between the two entities.

**Conflicts of interest: AIFM**

**3.11.7** **R** To avoid conflicts of interest between the *depository*, the *AIFM*, the *AIF* and its investors, an *AIFM* must ensure that:

- (1) it does not act as a *depository* or a delegate of a *depository*; and
- (2) a *prime brokerage firm* acting as counterparty to an *AIF* does not act as the *depository* for that *AIF*, unless:
  - (a) the *prime brokerage firm* has functionally and hierarchically separated the performance of its depository functions from its tasks as a *prime brokerage firm*; and
  - (b) potential conflicts of interest are properly identified, managed, monitored and disclosed to the investors of the *AIF* by the *AIFM*.

[Note: article 21(4) of *AIFMD*]

**3.11.8** **G** A *depository* may delegate custody tasks to one or more *prime brokerage firms* provided the *depository* complies with **FUND 3.11.26 R** to **FUND 3.11.30 R**. In addition to the delegated custody tasks, *prime brokerage firms* are allowed to provide *prime brokerage services* to the *AIF*. Those *prime brokerage services* do not form part of the delegation arrangement.

[Note: recital 43 of *AIFMD*]

**Conflicts of interest: depositories**

**3.11.9** **R** A *depository* must not carry out activities with regard to the *AIF*, or the *AIFM* on behalf of the *AIF*, that may create conflicts of interest between the *AIF*, the investors in the *AIF*, the *AIFM* and itself, unless:

- (1) the *depository* has properly identified any such potential conflicts of interest;
- (2) the *depository* has functionally and hierarchically separated the performance of its *depository* tasks from its other potentially conflicting tasks; and
- (3) the potential conflicts of interest are properly managed, monitored and disclosed to the investors of the *AIF*.

[Note: article 21(10) second paragraph of *AIFMD*]

**Eligible depositories for UK AIFs**

**3.11.10** **R** Subject to **FUND 3.11.12 R**, an *AIFM* must, for each *UK AIF* it manages, ensure the appointment of a *depository* which is a *firm established* in the *UK* and which is one of the following:

- (1) a *credit institution*; or
- (2) a *MiFID investment firm* which:
  - (a) has *own funds* of not less than €730,000; and

(b) provides the *ancillary service* of safe-keeping and administration of *financial instruments* for the account of clients; or

(3) another category of institution that is subject to prudential regulation and ongoing supervision and which, on 21 July 2011, fell within the categories of institution eligible to be a *trustee* of an *AUT* or a *depository* of an *ICVC*.

[Note: article 21(3)(a) to (c) and (5)(a) of *AIFMD*]

**3.11.11** **G** For a *depository* to be *established* in the *UK* it must have its registered office or *branch* in the *UK*. A *MiFID investment firm* that has its registered office in the *UK* must be a *full-scope IFPRU investment firm* to meet the requirements of ■ FUND 3.11.10R (2). A *MiFID investment firm* that has a *branch* in the *UK* must meet the capital requirements under the *EU CRR* for a *CRD full-scope firm* as implemented in its *Home State* to meet the requirements of ■ FUND 3.11.10R (2).

**3.11.12** **R** An *AIFM* that manages a *UK AIF* which:

- (1) has no redemption rights exercisable during the period of five years from the date of the initial investments; and
- (2) in accordance with its core investment policy:
  - (a) does not generally invest in *AIF custodial assets*; or
  - (b) generally invests in issuers or non-listed companies in order to potentially acquire *control* over such companies in accordance with regulation 35 of the *AIFMD UK regulation*

may appoint, as its *depository*, a firm which is established in the *UK* and which complies with ■ FUND 3.11.14 R.

**3.11.13** **G** For the purposes of ■ FUND 3.11.12R (2)(a), an *AIF* does not generally invest in *AIF custodial assets* if it invests in such assets on a temporary basis or if those assets do not constitute a significant proportion of its overall assets. However, in line with ■ FUND 3.11.12R (2)(b), an *AIF* may invest in *AIF custodial assets* if it invests in issuers to acquire control of such companies in accordance with regulation 35 of the *AIFMD UK regulation* or if it is in the process of divesting its investment in an issuer which it controls or previously controlled.

**3.11.14** **R** An *AIFM* must ensure that a *depository* appointed in line with ■ FUND 3.11.12 R is a *firm*:

- (1) which has the *Part 4A permission* of acting as trustee or *depository* of an *AIF*; and
- (2) which has *own funds* of at least €125,000.

[Note: article 21(3) second paragraph after (c) and (5)(a) of *AIFMD*]

**3.11.15** **G** For certain types of closed-ended *AIFs* (such as private equity, venture capital and real estate funds) a wider range of entities than those specified in **■ FUND 3.11.10 R** may perform the relevant *depository* functions. The *FCA* requires such entities to obtain authorisation as a *depository* to demonstrate that they can meet the commitments inherent in those functions, but imposes a lower level of capital requirements in recognition of the different degree of risk implied by the characteristics of the *AIF*. The capital requirements of such *firms* are contained in **■ IPRU-INV 5** (particularly **■ IPRU-INV 5.4.3R** (Own funds requirement)) but if the *firm* also undertakes *MiFID business*, its capital requirements will be contained in *IFPRU* and the *EU CRR* or in *GENPRU* and *BIPRU* depending on the scope of that *MiFID business*.

[Note: recital 34 of *AIFMD*]

### Additional requirements for depositories of authorised AIFs

**3.11.16** **R** A *MiFID investment firm* (other than a *PRA-authorised person*) which is appointed as a *depository* for an *authorised AIF* in accordance with **■ FUND 3.11.10R (2)** must maintain own funds of at least £4 million.

**3.11.17** **G** Where the *firm* referred to in **■ FUND 3.11.16 R** is a *full-scope IFPRU investment firm* which is a *depository* for an *authorised AIF* appointed in line with **■ FUND 3.11.10R (2)**, it is subject to the capital requirements of *IFPRU* and the *EU CRR*. However, these requirements are not in addition to **■ FUND 3.11.16 R** and, therefore, a *firm* subject to this *rule* may use the *own funds* required under *IFPRU* and the *EU CRR* to meet the £4 million requirement.

### Eligible depositories for EEA AIFs

**3.11.18** **R** An *AIFM* must, for each *EEA AIF* it manages, ensure the appointment of a *depository* which is established in the *Home State* of the *AIF* and which is eligible to be a *depository* in that *Home State* in accordance with article 21(3) of *AIFMD*.

[Note: article 21(3) and (5)(a) of *AIFMD*]

### Written contract

**3.11.19** **R** An *AIFM* and a *depository* must ensure that the appointment of the *depository* is evidenced by a written contract. The contract must regulate the flow of information deemed necessary to allow the *depository* to perform its functions for the *AIF* for which it has been appointed as *depository*.

[Note: article 21(2) of *AIFMD*]

### Depository functions: cash monitoring

**3.11.20** **R** A *depository* must ensure that the *AIF's* cash flows are properly monitored and that:

- (1) all payments made by, or on behalf of, investors upon the subscription of *units* or *shares* of an *AIF* have been received;
- (2) all cash of the *AIF* has been booked in cash accounts opened:



- (a) in the name of:
  - (i) the *AIF*; or
  - (ii) the *AIFM* acting on behalf of the *AIF*; or
  - (iii) the *depository* acting on behalf of the *AIF*; and
- (b) at:
  - (i) a central bank; or
  - (ii) a *CRD credit institution*; or
  - (iii) a bank authorised in a third country; or
  - (iv) another entity of the same nature, in the relevant market where cash accounts are required, provided such an entity is subject to effective prudential regulation and supervision which have the same effect as *EU* law and are effectively enforced and in accordance with the principles set out in article 2 (safeguarding of client financial instruments and funds) of the *MiFID Delegated Directive*; and
- (3) where cash accounts are opened in the name of the *depository* acting on behalf of the *AIF* in accordance with (2)(a)(iii), the *depository* must ensure that no cash of the entity referred to in (2)(b), and none of the *depository's* own cash, is booked on such accounts.

[Note: article 21(7) of *AIFMD*]

### Depository functions: safekeeping of financial instruments

3.11.21

**R**

- (1) A *depository* must hold in custody all *AIF custodial assets*.
- (2) The *depository* must ensure that all *AIF custodial assets* that can be registered in a *financial instruments* account are registered in the *depository's* books within segregated accounts opened in the name of the *AIF*, or the *AIFM* acting on behalf of the *AIF*, so that they can be clearly identified as belonging to the *AIF* at all times in accordance with the applicable law and **■ CASS 6.1.16IA R** (Depositories of AIFs).

[Note: article 21(8)(a) of *AIFMD*]

3.11.22

**EU**

#### Financial instruments to be held in custody

1. Financial instruments belonging to the *AIF* or to the *AIFM* acting on behalf of the *AIF* which are not able to be physically delivered to the *depository* shall be included in the scope of the custody duties of the *depository* where all of the following requirements are met:
  - (a) they are transferable securities including those which embed derivatives as referred to in the last subparagraph of Article 51(3) of Directive 2009/65/EC and Article 10 of Commission Directive 2007/16/EC, money market instruments or units of collective investment undertakings;
  - (b) they are capable of being registered or held in an account directly or indirectly in the name of the *depository*.
2. Financial instruments which, in accordance with applicable national law, are only directly registered in the name of the *AIF* with the issuer itself or its agent, such as a registrar or a transfer agent, shall not be held in custody.

3. Financial instruments belonging to the AIF or the AIFM acting on behalf of the AIF which are able to be physically delivered to the depository shall always be included in the scope of the custody duties of the depository.

[Note: Article 88 of the *AIFMD level 2 regulation*]

**Depository functions: safekeeping of other assets**

**3.11.23** **R** For assets of the *AIF* that are not *AIF custodial assets*, a *depository* must:

- (1) verify that the *AIF*, or the *AIFM* acting on behalf of the *AIF*, is the owner of the assets based on information or documents provided by the *AIF* or the *AIFM* and, where available, on external evidence; and
- (2) maintain, and keep up to date a record of those assets for which it is satisfied that the *AIF*, or the *AIFM* acting on behalf of the *AIF*, is the owner.

[Note: article 21(8)(b) of *AIFMD*]

**Reuse of assets**

**3.11.24** **R** A *depository* must not reuse the assets of the *AIF* without the prior consent of the *AIF* or the *AIFM* acting on behalf of the *AIF*.

[Note: article 21(10) third paragraph of *AIFMD*]

**Depository functions: oversight**

**3.11.25** **R** A *depository* must:

- (1) ensure that the sale, issue, repurchase, redemption and cancellation of *units* or *shares* of the *AIF* are carried out in accordance with the applicable national law and the *instrument constituting the fund*;
- (2) ensure that the value of the *units* or *shares* of the *AIF* is calculated in accordance with the applicable national law, the *instrument constituting the fund* and ■ **FUND 3.9** (Valuation);
- (3) carry out the instructions of the *AIFM*, unless they conflict with the applicable national law or the *instrument constituting the fund*;
- (4) ensure that in transactions involving the *AIF's* assets, any consideration is remitted to the *AIF* within the usual time limits; and
- (5) ensure that an *AIF's* income is applied in accordance with the applicable national law and the *instrument constituting the fund*.

[Note: article 21(9) of *AIFMD*]

**Delegation: general prohibition**

**3.11.26** **R** (1) A *depository* must not delegate its functions to third parties, except as permitted by ■ **FUND 3.11.28R**.

- (2) The prohibition in (1) does not apply to the delegation by the *depository* of supporting administrative or technical tasks that are linked to its depository functions.

[Note: recital 42 and article 21(11) first paragraph of *AIFMD*]

- 3.11.27** G The use of services provided by securities settlement systems, as specified in the *Settlement Finality Directive*, or similar services provided by third-country securities settlement systems, does not constitute a delegation by the *depository* of its functions.

[Note: article 21(11) fifth paragraph of *AIFMD*]

- 3.11.27A** G
- (1) (a) If a *depository* performs part of its functions through a *branch* in another *EEA State* this is not a delegation by the *depository* of its functions to a third party.
- (b) This is because ‘third party’ in ■ **FUND 3.11.26R** means any party that is not part of the same legal entity as the *depository*.
- (2) Paragraph (1) also applies where the *depository* is the *UK branch* of an *EEA firm* and it performs part of its functions:
- (a) through a *branch* in another *EEA State*; or
- (b) from the *EEA State* where it has its registered office.
- (a) A *depository* that performs part of its functions through a *branch* or registered office in another *EEA State* should ensure that those arrangements do not impede the *depository’s* ability to meet the *threshold conditions*.
- (b) (i) In particular, the arrangements should not impede the *FCA’s* ability to supervise the *depository* effectively.
- (ii) For example, the *FCA’s* ability to supervise the *depository* might be impeded if the *depository* performed tasks other than administrative and supporting tasks from its *branch* or registered office in another *EEA State*.

**Delegation: safekeeping**

- 3.11.28** R A *depository* may delegate the functions in ■ **FUND 3.11.21 R** and ■ **FUND 3.11.23 R** to third parties, subject to the following conditions:

- (1) the tasks are not delegated with the intention of avoiding the requirements of *AIFMD*;
- (2) the *depository* can demonstrate that there is an objective reason for the delegation;
- (3) the *depository*:
- (a) has exercised all due skill, care and diligence in the selection and appointment of any third party to whom it wants to delegate parts of its tasks; and

- (b) continues to exercise all due skill, care and diligence in the periodic review and ongoing monitoring:
  - (i) of any third party to whom it has delegated parts of its tasks; and
  - (ii) of the arrangements of that third party in respect of the matters delegated to it;
- (4) the *depository* ensures that the third party delegate meets the following conditions at all times:
  - (a) the third party has structures and expertise that are adequate and proportionate to the nature and complexity of the assets of the *AIF*, or the *AIFM* acting on behalf of the *AIF*, that have been entrusted to it;
  - (b) (subject to ■ FUND 3.11.29 R) for custody tasks in relation to *AIF custodial assets*, the third party is subject to:
    - (i) effective prudential regulation, including minimum capital requirements, and supervision in the jurisdiction concerned; and
    - (ii) an external periodic audit to ensure that the *financial instruments* remain in its custody;
  - (c) the third party segregates the assets of the *depository's* clients from its own assets and from the assets of the *depository* in such a way that they can, at any time, be clearly identified as belonging to clients of a particular *depository*;
  - (d) the third party does not make use of the assets unless it has:
    - (i) obtained the prior consent of the *AIF*, or the *AIFM* acting on behalf of the *AIF*; and
    - (ii) given prior notification to the *depository*; and
  - (e) the third party complies with the general obligations and prohibitions relating to the *depository* in ■ FUND 3.11.5 R, ■ FUND 3.11.5 G, ■ FUND 3.11.9 R, ■ FUND 3.11.21 R, ■ FUND 3.11.23 R and ■ FUND 3.11.24 R.

[Note: article 21(11) second paragraph of *AIFMD*]

**Delegation: third countries**

**3.11.29**

**R**

A *depository* may delegate custody tasks in relation to *AIF custodial assets* to an entity in a third country that does not satisfy the conditions in ■ FUND 3.11.28R (4)(b), provided that:

- (1) the law of that third country requires those *AIF custodial assets* to be held in custody by a local entity;
- (2) no local entity satisfies the conditions in ■ FUND 3.11.28R (4)(b);
- (3) the *depository* delegates its functions to such a local entity only to the extent required by the law of that third country and only for as long as there is no local entity that satisfies the delegation conditions in ■ FUND 3.11.28R (4)(b);

- (4) the investors of the relevant *AIF* are informed before their investment that such delegation is required due to legal constraints in the third country and of the reasons as to why the delegation is necessary; and
- (5) the *AIF*, or the *AIFM* on behalf of the *AIF*, has consented to the delegation arrangements before they become effective.

[Note: article 21(11) third paragraph of *AIFMD*]

**Delegation: sub-delegation**

**3.11.30** R A *depository* must ensure that a third party to whom the *depository* has delegated functions does not, in turn, sub-delegate those functions unless the delegate complies with the same requirements that apply to the *depository*, with any necessary changes, in relation to the delegation by the *depository* of its functions in ■ FUND 3.11.26 R to ■ FUND 3.11.29 R.

[Note: article 21(11) fourth paragraph of *AIFMD*]

**Delegation: omnibus account**

**3.11.31** G A *depository* may delegate the safe-keeping of assets to a third party that maintains a common account for multiple *AIFs*, a so-called 'omnibus account', provided it is a segregated common account that is segregated from the third party's own assets.

[Note: recital 40 of *AIFMD*]

**Provision of information**

**3.11.32** G The requirements of ■ SUP 2 (Information gathering by the FCA or PRA on its own initiative) apply to the *depository*, under which it must enable the FCA to obtain, on request, all information that the *depository* has obtained while discharging its duties and that the FCA considers necessary.

[Note: article 21(16) of *AIFMD*]

**AIFM of a non-EEA AIF**

**3.11.33** R An *AIFM* of a *non-EEA AIF* or a *non-EEA feeder AIF* which is *marketed* in the UK must:

- (1) ensure that the duties referred to in ■ FUND 3.11.20 R, ■ FUND 3.11.21 R, ■ FUND 3.11.23 R and ■ FUND 3.11.25 R are carried out in relation to that *AIF* by one or more:
  - (a) *firms* that:
    - (i) are *established* in the UK; and
    - (ii) which have the *Part 4A permission of acting as trustee or depository of an AIF*; and
    - (iii) which have *own funds* of at least €125,000, where the duties are carried out in the UK; or

- (b) entities that are not *established* in the *UK*, where the duties are not carried out in the *UK*; or
- (c) *firms* that are *established* in the *UK* and which are carrying out the duties from a non-*UK branch*;

(2) not perform the duties referred to in (1) itself; and

(3) provide the *FCA* with information about the identity of those entities responsible for carrying out the duties referred to in (1).

[Note: article 36(1)(a) of *AIFMD*]

#### **Subordinate measures**

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3.11.34

G

Articles 83 to 102 of the *AIFMD level 2 regulation* provide detailed rules supplementing this section.



## 3.12 Marketing in the home Member State of the AIFM

### Application

- 3.12.1 **G** This section applies to:
- (1) a *full-scope UK AIFM* of:
    - (a) a *UK AIF*; and
    - (b) an *EEA AIF*; and
  - (2) a *full-scope EEA AIFM* of:
    - (a) a *UK AIF*; and
    - (b) an *EEA AIF*.

### Marketing application

- 3.12.2 **D** Under regulation 54 (FCA approval for marketing) of the *AIFMD UK regulation*, a *full-scope UK AIFM* and a *full-scope EEA AIFM* may apply to *market* a *UK AIF* or *EEA AIF* it manages in the *UK* by submitting a notice to the *FCA* in the form set out in ■ FUND 3 Annex 1 D.
- 3.12.3 **G** If the *UK AIF* or *EEA AIF* is a *feeder AIF*, the *master AIF* needs to be an *AIF* that is not managed by a *non-EEA AIFM* or is not a *non-EEA AIF* for it to be *marketed* in accordance with regulation 54 of the *AIFMD UK Regulation*. If the *master AIF* is managed by a *non-EEA AIFM* or is a *non-EEA AIF*, the *AIF* may be *marketed* in the *UK* in accordance with regulation 57 (Marketing under article 36 of the directive) of the *AIFMD UK regulation* (see FUND 10.5.3G (Marketing under article 36 of AIFMD)).
- 3.12.4 **G**
- (1) A *full-scope UK AIFM* may use the form set out in ■ FUND 3 Annex 1 D to apply to *market* a *UK AIF* or *EEA AIF* (that is not a *feeder AIF*, the *master AIF* of which is managed by a *non-EEA AIFM* or is a *non-EEA AIF*) to *professional clients* and/or *retail clients*.
  - (2) A *full-scope UK AIFM* may inform the *FCA* of its intention to *market* such an *AIF* in the *UK* in its application to become authorised as a *Full-scope UK AIFM*, in which case the *firm* does not also have to submit the form in ■ FUND 3 Annex 1 D in respect of that *marketing*.
  - (3) A *full-scope UK AIFM* may also use the form in ■ FUND 3 Annex 1 D to apply to the *FCA* to *market* an *AIF* in other *EEA States* using the

AIFMD marketing passport and to notify the FCA of material changes to domestic and cross-border *marketing*.

3.12.5

G

- (1) A *full-scope EEA AIFM* that wishes to *market* a *UK AIF* or *EEA AIF* (that is not a *feeder AIF*, the *master AIF* of which is managed by a *non-EEA AIFM* or is a *non-EEA AIF*) to *professional clients* should do so using the *marketing* passport provided for under AIFMD and should, therefore, apply to its *Home State* regulator for permission to do so.
- (2) In accordance with regulation 49 (Marketing by *full-scope EEA AIFMs* of certain AIFs) of the *AIFMD UK Regulation*, a *full-scope EEA AIFM* may *market* such an AIF to *retail clients* in the UK if the FCA has received a regulator's notice in relation to the *marketing* in accordance with Schedule 3 to the Act (EEA Passport rights) or if the AIFM has applied to the FCA for permission to *market* the AIF using the form in ■ FUND 3 Annex 1 D and the FCA has approved such *marketing*.
- (3) As such, a *full-scope EEA AIFM* may use the form in FUND 3 Annex 1D to apply to *market* such an AIF in the UK to *retail clients*, but should not use this form to apply to *market* such an AIF to *professional clients* in the UK.

3.12.6

G

A *full-scope UK AIFM* or a *full-scope EEA AIFM* that intends to *market* to *retail clients* should consider the application of the *financial promotions* regime and ensure it is compliant with the relevant requirements (see ■ PERG 8.37.14 G (Application of the financial promotion and scheme promotion restrictions)).

### Marketing an ELTIF

3.12.7

G

To *market* an *ELTIF* in the *United Kingdom* a *full-scope UK AIFM* should submit a notice to the FCA using the forms in:

- (1) ■ FUND 3 Annex 1D (Notification of intention to *market* an AIF in the United Kingdom); and
- (2) ■ FUND 4 Annex 1R (Additional documentation and information to *market* an ELTIF).



## **Notification of intention to market at AIF in the United Kingdom**

This annex consists only of one or more forms. Forms are to be found through the following address:

Notification of intention to provide or amend cross border services in another EEA state with respect to marketing an AIF (Article 32); and/or Notification of intention to market an AIF in the United Kingdom (Article 31) - FUND 3 Annex 1 D



## **Notice of AIFM delegation**

This annex consists of one or more forms. Forms can be completed online now by visiting <https://www.handbook.fca.org.uk/form>

The forms are also to be found through the following address:

FUND 3 Annex 2 R - Notice of AIFM delegation

