

Article 36 Consultation
MARKETS Policy Division
Central Bank of Ireland
Block D
Iveagh Court
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**RESPONSE TO Consultation Paper P 78 - DEPOSITARY DUTIES
ARTICLE 36 OF THE ALTERNATIVE INVESTMENT FUND MANAGERS DIRECTIVE ("AIFMD")
Centaur Fund Services Limited and Centaur Financial Limited**

1. Cash monitoring and Oversight services under Articles 21 (7) and 21 (9) of AIFMD

CP 78 Proposals

We have considered the Central Bank of Ireland's ("CBI") proposal for fund administration firms wishing to provide both Article 21(7) cash monitoring and Article 21(9) oversight services.

Centaur Fund Services Limited ("CFS") does not intend to provide either of these services to its clients. Instead, as the CBI is aware, a completely separate entity, Centaur Financial Limited ("CFL"), which is not a subsidiary of CFS, has been set up to provide depository services. We therefore welcome the confirmation that the CBI will not require authorization for these activities.

CFS and CFL Observations

Whilst the proposal outlined in CP78 has no direct impact upon CFS or CFL, we would be concerned that the CBI's reporting line proposal (i.e. the proposal that the depository function should be housed in a subsidiary of the fund administration firm and should report to the administration firm) could potentially cause issues for European AIFMs when deciding upon depository appointments.

In our experience - based on in depth discussions with a variety of industry participants, - it has been very evident that the notion of a depository firm (responsible for providing, in particular, the oversight services under Article 21 (9)) having a reporting line at any level into the fund's administration firm whose records it will, in part, oversee, is unlikely to be acceptable to AIFMs or supported by their regulatory bodies or professional advisors.

2. Record keeping and verification duties in relation to other assets under AIFMD Article 21 (8) (b)

CBI Position

The CBI confirmed in CP 78 and Q ID 1021 of the AIFMD Q & A that where an Irish entity proposes to provide the safe-keeping duties set out in Article 21(8) (a) and (b) of AIFMD, it must have authorisation to provide "custodial operations involving the safe-keeping and administration of investment instruments" ("Activity (h)"), under the Investment Intermediaries Act 1995 ("the Act").

AIFMD and AIFMR

It should be noted, in relation to Article 21(8) (a) and (b) of AIFMD and the AIFMD Level 2 Regulations ("AIFMR"), that care has been taken to distinguish between the two categories of assets which are in scope. "Custody" Assets are clearly distinguished from "Other Assets".

The provisions of Article 21 (8) (a) of AIFMD relating to “Custody Assets” clearly stipulate that they need to be entrusted to a depositary for safekeeping. In practice, hedge funds will seek to appoint their prime brokers to carry out this function.

Article 21(8)(b) of AIFMD states:

“(b) for other assets:

*(i) the depositary shall **verify the ownership** of the AIF or the AIFM acting on behalf of the AIF of such assets and shall **maintain a record** of those assets for which it is satisfied that the AIF or the AIFM acting on behalf of the AIF holds the ownership of such assets;*

(ii) the assessment whether the AIF or the AIFM acting on behalf of the AIF holds the ownership shall be based on information or documents provided by the AIF or the AIFM and, where available, on external evidence;

(iii) the depositary shall keep its record up-to-date.”

The duties in relation to “Other Assets”, which are set out further in Article 90 (2) of AIFMR are limited to **ownership verification** and **record keeping**. It is crucial to note that there is no actual “safekeeping” taking place or required in relation to “Other Assets” as described in Article 21 (8) (b).

CFS and CFL Observations

1. Existing Fund Administration activities

As we discussed during our meeting with the CBI on 11 April 2014, we are of the view that the record keeping and verification duties relating to “Other Assets” described in AIFMD and AIFMR are **substantially the same as those duties which fund administrators currently already perform** in relation to fund assets, which form a necessary and integral part of the reconciliation process and calculation of the net asset value of a fund.

Indeed, it is arguable that ownership verification and record keeping of “Other Assets” is already being regulated, in practice, by the CBI under Section 10 of the Act under which fund administrators are presently authorised as outlined below (“activity (g)”):

“(g) the administration of collective investment schemes, including the performance of valuation services or fund accounting services or acting as transfer agents or registration agents for such funds”

It is our view that in order to provide valuation and fund administration services, an administrator must carry our ownership verification and record keeping services of all fund assets, including “Other Assets”. It is not possible to produce a NAV for a fund without performing this activity.

2. Comparison to cash monitoring under Article 21 (7)

The activities specified in Article 21(8)(b) are analogous to the activity of cash monitoring under Article 21 (7). These activities are already performed as part of fund administration and the CBI, whether or not in acknowledgement of this fact, is not seeking to authorize cash monitoring activities separately.

Examples of “Other Assets” are:

- OTC securities held in the name of the AIF

- Master fund shares held by in book form by a feeder AIF
- Shares in money market funds held by the AIF, issuer or transfer agent
- Cash

Cash, as an asset, falls within the “Other Asset” category, as described in AIFMD and AIFMR. We are interested to understand the rationale for why the CBI is not seeking to authorise firms that wish to provide cash monitoring services under Article 21 (7) (which as a minimum requires verification of ownership and record keeping of cash, cash accounts and cashflows, among other things) but is seeking to authorise firms wishing to provide verification of ownership and record keeping services in relation to cash assets, under Article 21 (8) (b).

In practice, the responsibilities and activities in relation to cash and cashflows are common. Indeed the Article 21 (8) (b) responsibilities would appear, if anything, to be less onerous than those outlined in Article 21 (7), yet the CBI is seeking to authorize only the former.

3. Competitive Disadvantage

The CBI’s policy on requiring an Activity (h) authorisation to be in place for Article 21(8)(b) services to be provided undoubtedly places independent fund administration firms and groups at a competitive disadvantage to licensed custodian banking groups.

As an independent fund administration group, Centaur (through its affiliate CFL) is arguably better placed than any other party to provide independent record keeping and verification services to AIFs, particularly to those AIFs where CFS is the fund administrator. The CBI’s licensing policy on the activity has made it impossible for either CFS or CFL to offer this service.

Independent fund administration firms perform a valuable and essential role for the hedge fund industry. Independent fund administrators have established operations in Ireland since the 1990’s. The CBI’s interpretation of Article 21(8)(b) is without doubt damaging the independent fund administration business in Ireland.

4. Service Gap

In the absence of independent fund administration groups being permitted to provide services under 21(8)(b) a serious and damaging service gap has been created. In essence if the fund administration group cannot provide these services, who can?

A significant number of custodian banks / prime brokers have indicated that they are not willing and/or that they are not in a position to offer Article 21 (8) (b) services to AIFMs and AIFs. Some have agreed to provide only Article 21 (8) (a) services and others have indicated that they could provide Article 21 (8) (b) services in relation to some but not all “Other Asset” types – typically they will agree to verify those assets that they already maintain a record of, as the appointed prime broker to the funds- but they will, understandably, not provide 21(8)(b) services in respect of assets for which they currently do not maintain records. It is our view that fund administration companies or their affiliates are best placed to provide these services.

We have clear evidence that that the CBI’s position on this activity, as well as the uncertainty which has prevailed on the regulatory policy surrounding depo-lite services generally, has forced AIFMs to look elsewhere in the market to non Irish providers of independent AIFMD depo lite services.

This has also forced Centaur to consider the merits of moving parts of our business outside of Ireland to other EU jurisdictions where the regulatory position with regard to depo-lite services is more certain.

5. Availability of authorisation

The CBI has informed us that they are not minded to grant independent fund administration groups an Activity (h) custody authorisation. It is our view that administration companies and their affiliates are best placed to provide these activities. Consequently, if the view of the CBI is that a specific authorisation is required to perform these activities then it is not equitable or commercially sensible to prohibit fund administration companies or their affiliates from obtaining such authorization.

Conclusion

The decision by the CBI to require an Activity (h) custody authorisation to be in place for record keeping and verification of "Other Assets" services to be provided under Article 21 (8) (b) of AIFMD would appear to us, to be both unnecessary and questionable for the reasons outlined above.

Fund administration companies already carry out these activities in the ordinary course of their business and are best placed to do so, either through their fund administration companies or through affiliated depositary entities.

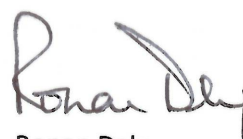
However, should the CBI retain their position, requiring these activities to be regulated, we would like to suggest that this regulatory requirement is limited to the activities as set out in 21 (8) (b), and not form part of a full Custody license (which is not available to independent administrators such as CFS) and that the CBI permit independent fund administration companies to obtain such authorisation in a timely manner.

We hope you find our views – based on real and extensive industry concerns – useful and we would be happy to discuss this matter again with you.

Yours faithfully



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