



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

Notice of intention to make provision for entities to act as depositaries to AIFs as set out under Regulation 22(3)(b) of the AIFM Regulations

19 November 2018

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In accordance with AIFMD¹, Regulation 22(3) of the AIFM Regulations² sets out the categories of entities who may be appointed as depositaries of AIFs. These include credit institutions, investment firms and certain IIA authorised entities. Regulation 22(3)(b) of the AIFM Regulations provides that the Central Bank may allow another type of depositary, in the case of certain closed ended Alternative Investment Funds (AIFs), which generally do not invest in assets that must be held in custody.³ At this time, the Central Bank's AIF Rulebook does not provide for this category of depositary.

The Central Bank is minded to make provision for entities to act as a depositary in the manner set out under Regulation 22(3)(b) of the AIFM Regulations, (hereafter, 'the Real Asset Depositaries'). The Central Bank considers that the depositaries will be appointed to AIFs which primarily invest in assets which are not capable of being registered or held in an account directly or indirectly in the name of the depositary. Such 'other assets' take the form of title deeds or other types of physical assets which are not exchange traded and therefore do not fall with the categorisation of a financial instrument capable of being held in custody.

Regulation 22(3)(b) provides that in order to be acceptable, the entity must be subject to mandatory professional registration recognised by law, or to legal or regulatory provisions or rules of professional conduct and must also be in a position to provide sufficient financial and professional guarantees to enable it to perform effectively the relevant depositary functions.

While the AIFM Regulations allow for a more flexible regime in terms of the category of entities, there is no waiver of the detailed safe-keeping and oversight requirements applicable to all depositaries nor of the attendant liability. Accordingly, in order to be acceptable, entities must be in a position to demonstrate to the Central Bank, their capacity and ability to meet safekeeping and oversight obligations as provide for under the AIFM Regulations. It will be of particular importance that the entity applying for authorisation can clearly demonstrate to the Central Bank it has effective policies and procedures to ensure the depositary oversight role is carried out. In this regard, it should clearly explain to the Central Bank how it has the necessary systems access to effectively oversee the AIFM and any of its delegates, particularly those which are appointed to carry out fund administration or portfolio management.

¹ 'Alternative Investment Fund Managers Directive' – Directive 2011/61/EU of the European parliament and of the council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010

² The AIFM Regulations transpose the Alternative Investment Fund Managers Directive into Irish law.

³ AIFM Regulation 22(3)(b) –

In addition to what is provided for in subparagraph (a), the Bank may allow that in relation to an AIF which has no redemption rights exercisable during the period of 5 years from the date of the initial investments and which, in accordance with its core investment policy, generally does not invest in assets that must be held in custody in accordance with paragraph (8)(a) or generally invest in issuers or non-listed companies in order to potentially acquire control over such companies in accordance with Regulation 27, the depositary may be an entity which carries out depositary functions as part of its professional or business activities in respect of which such entity is subject to mandatory professional registration recognised by law or to legal or regulatory provisions or rules of professional conduct and which can provide sufficient financial and professional guarantees to enable it to perform effectively the relevant depositary functions and meet the commitments inherent in those functions.

In addition to the safe-keeping and oversight obligations which apply to depositaries pursuant to the AIFM Regulations, it is proposed to apply the following regulatory requirements to Real Asset Depositaries:

- Require applicants to seek authorisation under the Investment Intermediaries Act 1995;
- Require compliance with the majority of conditions set out in Chapter 5 of the AIF Rulebook (Depositary Requirements). Application of this chapter means the applicant will need to satisfy the Central Bank that it has and maintains the following:
 - a. appropriate expertise and experience to carry out the depositary tasks
 - b. sufficient resources and adequate governance / internal organisation
 - c. ability to meet the capital requirement of €125,000 or one quarter of total expenditure, whichever is higher
 - d. two Irish resident directors

A Real Asset Depositary will also be subject to the following obligations set out in Chapter 5 of the AIF Rulebook:

- e. Reporting
 - f. Business Continuity Planning
 - g. To report annually to investors in the AIF on the management by the AIFM
 - h. To report breaches to the Central Bank.
- A Real Asset Depositary will be permitted to safe-keep documents of title which fall to be considered as “other assets” under Regulation 22(8)(b) of the AIFM Regulations. It may arise that an AIF to which it is appointed invests in financial instruments which can be held in custody, in accordance with Regulation 22(8)(a) of the AIFM Regulations. In the event that the Real Asset Depositary does not propose to delegate safe-keeping of these financial instruments and to enter into agreements with its sub-custodian in order to discharge the related liability, the Central Bank is minded to impose a condition of authorisation requiring that the Real Asset Depositary holds sufficient financial resources to cover the value of the financial instruments.

The Central Bank is also minded:

- To prohibit a Real Asset Depositary from providing for the safe-keeping of assets other than documents of title unless and until such time as satisfactory evidence of capacity to do so is provided to accepted by the Central Bank. Example of other types of assets are precious metals / wine / art.
- To limit the holding of financial instruments to those which the relevant AIF will acquire in limited circumstances (such as for cash

management, due to an IPO strategy or private equity acquisitions of publicly held companies);

- To require disclosure to investors on the status of the Real Asset Depositary and the limited nature of the activities and related liability which applies;
- To require applicants to possess professional indemnity insurance for loss or damage caused through the negligent performance of activities.⁴ It is likely that a pre-determined amount of cover would be required depending on the value of portfolios of the AIFs to which the Real Asset Depositary is appointed;
- To prohibit Real Asset Depositaries from acting for retail AIFs.

The Central Bank invites comment from stakeholders on this proposal. Comments should be submitted by email to fundspolicy@centralbank.ie no later than 19 January 2018. Meanwhile any applications to act as a Real Asset Depositary will be considered in line with the intentions outlined in this notice.

Depending on the outcome of the Central Bank's review, requirements to apply to Real Asset Depositaries will be included in the Central Bank's AIF Rulebook and subject to consultation in that context.

⁴ Professional liability risks may include, without being limited to, risks of:

- (a) loss of documents evidencing title of assets of the AIF;
- (b) misrepresentations or misleading statements made to the AIF or its investors; and
- (c) acts, errors or omissions resulting in a breach of:
 - (i) legal and regulatory obligations,
 - (ii) duty of skill and care towards the AIF and its investors,
 - (iii) fiduciary duties and
 - (iv) obligations of confidentiality etc.

T: +353 (0)1 224 6000
E: fundspolicy@centralbank.ie
www.centralbank.ie



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