



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

2015

Fund Management Company Boards - Feedback statement on consultation on delegate oversight guidance



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Introduction

1. On 12 June 2015 the Central Bank of Ireland (the “Central Bank”) published draft Central Bank guidance on Fund Management Companies - Delegate Oversight (the “Delegate Oversight Guidance”). The Central Bank invited all stakeholders to provide observations and comments on the draft Delegate Oversight Guidance. The closing date for comments was 24 July 2015 and two responses were received.
2. The Delegate Oversight Guidance focused on the matters covered in the report of the Committee on Collective Investment Governance but was revised as Central Bank guidance. This document sets out the Central Bank’s feedback on the consultation on the Delegate Oversight Guidance.
3. This feedback statement is accompanied by the finalised Delegate Oversight Guidance. The Central Bank published finalised guidance on the Organisational Effectiveness role and on Directors’ Time Commitments as part of the CP86 feedback statement. All three pieces of guidance have now been located in a new document titled “Fund Management Companies – Guidance”. The Central Bank intends that future fund management company guidance will also ultimately be located in this document.

Feedback on consultation on Delegate Oversight Guidance

1. The principal comments received on the draft Delegate Oversight Guidance were as follows:
 - a. The Delegate Oversight Guidance should be consistent in how it refers to the purpose of the paper as it used the terms “good practice”, “guidance” and “principles” somewhat interchangeably. It would also be beneficial for the Delegate Oversight Guidance to differentiate between principles and explanatory material, including examples of good practice. One respondent cautioned against the prescriptive nature of some of the matters set out in the draft Delegate Oversight Guidance and believed that setting out a step by step process may lead to a “check the box” approach.
 - b. To ensure consistency of guidance and rules it would be helpful if the Delegate Oversight Guidance included reference to the specific rules on which the guidance is seeking to elaborate.
 - c. Further clarity on what is expected in connection with the risk appetite statement would be beneficial.
 - d. To avoid duplicative reporting by management companies, the delegate monitoring responsibilities of externally managed investment companies should be capable of being satisfied by relaying the periodic reports received by the management company to the investment company boards for their consideration.
 - e. With respect to the distinction between the role of designated persons and directors, Irish funds should not need to appoint another Irish delegate (in addition to the administrator and depositary) in order to be able to meet the Central Bank’s requirements on managerial functions. The use of an Irish delegate to perform management roles should not be the default position.
 - f. The definition of “delegate” should be amended to clarify that it relates to third parties performing the critical regulated activity of the investment fund or fund management company.
 - g. The terms “relevant company” and “fund management company” appear to be used substantially interchangeably. One term should be used throughout.

- h. Paragraph 22 should be amended to refer to situations where “reporting” standards fall short of the required levels and require remedial action to be taken.
- i. There were several comments directed at narrowing the scope of the board and limiting the information provided by a delegate. Paragraph 23 should be amended to limit the scope of information to be provided by delegates as they will not wish to provide information which is not relevant to the delegation and is unnecessary. Paragraphs 27 should be amended to specify that investment managers should only report breaches of policies that specifically relate to the portfolio management function relevant to the fund. Similarly, paragraph 28 should be amended so that the directors are required to understand the relevant aspects of the investment manager’s business so as to allow them effectively supervise their delegate.
- j. Paragraph 24 should be amended to provide that the board should approve a proposed investment approach “based on the recommendations of the Investment Manager who has expertise in this regard”.
- k. Paragraph 26 should be amended so that only material or significant changes to the investment approach would require board approval.
- l. Paragraph 31 infers that the board should be monitoring or overseeing marketing materials. Given the large amount of marketing material that may be produced, this expectation is unreasonable. Distributors are required to comply with applicable regulatory requirements themselves such as MiFID.
- m. The Delegate Oversight Guidance states that the board has ultimate responsibility for all aspects of management. Therefore, it is not clear why paragraph 32 states that the board retains ultimate responsibility for risk management. This may imply that risk management differs from other management functions.
- n. A fund management company would typically receive a summary of the business continuity plan and not the business continuity plan programme itself. As such the board cannot be satisfied that the programme is adequate. Rather the fund management company must be satisfied that the information provided

demonstrates that the delegate has in place processes/procedures to ensure the tasks can be carried out where there is business interruption.

- o. The depositary is not a delegate of the investment fund or fund management company and paragraphs 45 and 58 should be amended to reflect this.

Central Bank:

- a. The Delegate Oversight Guidance sets out guidance and it has been amended to use this term consistently throughout. The Central Bank believes that the Delegate Oversight Guidance achieves the correct level of prescription and did not agree with an approach which would revise the guidance to be more general in nature.
- b. The Delegate Oversight Guidance already contained a general reference to boards having ultimate responsibility under “applicable law”. A specific reference to the Companies Act 2014 and the Irish Collective Asset-management Vehicles Act 2015 has now been inserted. The Delegate Oversight Guidance also already contained a reference to limits on delegation under Regulation 23(2) of the EC (UCITS) Regulations 2011 and Regulation 21(4) of the EU (AIFM) Regulations 2013.
- c. Guidance on the content of risk appetite statements goes beyond the scope of this work on delegate oversight.
- d. The Delegate Oversight Guidance has been amended to provide that a fund management company may include reports received from its delegates in its reports to the board of an externally-managed investment company. However, reports from the fund management company should not consist solely of reports received from its delegate but should also include commentary from the fund management company describing how it has performed its role.
- e. The Central Bank does not require Irish funds to appoint another Irish delegate to carry out the management roles. Matters concerning designated persons will be dealt with in a future Central Bank consultation.
- f. The definition of “delegate” has been amended to specify the delegates to whom it refers.
- g. The terms “relevant company” and “fund management company” have different meanings. The term “relevant company” includes fund management companies, AIF management companies and externally-managed investment companies. Both terms are used in different contexts in the Delegate Oversight Guidance and have been retained.
- h. The suggested amendment would significantly alter the proposed good practice in a way that would limit its scope. This would not accord with the Central Bank’s intended good practice. Accordingly, this change has not been incorporated.
- i. There may be significant developments in a delegates’ business which could have an important impact on the performance of the delegated activities in relation to an investment fund but which do not specifically and directly relate to the investment fund in question (for example, if the delegate is merging with another entity). Further, there may be breaches of policies which do not directly affect the investment funds under management but which the board would be concerned to know about (for example, breaches of internal employee dealing rules or conflicts of interest policies). Accordingly, the proposed good practices are broader than requesting information on matters which relate solely and directly to the investment funds in question.

- j. The approval of the investment approach by the board is a key feature of the Delegate Oversight Guidance. That guidance as currently drafted provides that the board will receive a presentation from the investment manager before approving the investment approach. However, the proposed good practice places responsibility on the board for approving the investment approach. Incorporating the proposed amendment could dilute this good practice by implying that the board could base its decision to approve the investment approach solely on the recommendations of the investment manager. That is not the intention of the proposed good practice. Accordingly, this amendment has not been incorporated.
- k. The board is responsible for controlling the fund management company. As part of this control, it is important that the board approves the investment approach and any changes to it. Allowing changes to be made to the investment approach by another party would diminish this control to an unacceptable extent. Accordingly, this proposed change has not been made. However, the Central Bank has accepted a suggested amendment to include a reference to a representative being present to answer questions when amendments to the investment approach are proposed.
- l. The Delegate Oversight Guidance does not provide that boards must review all marketing materials. However, the board should know how the investment fund is being distributed and should be satisfied that marketing materials will not conflict with the prospectus. If they are not satisfied, they should enquire further and this enquiry may include examining marketing materials.
- m. Paragraph 32 has been amended to remove the reference to the board having ultimate responsibility for risk management. The Central Bank agrees that this point is covered by the general statement that the board retains ultimate responsibility for all aspects of management in paragraph 2. This amendment in no way dilutes the responsibility of the board for risk management.
- n. The board is not necessarily reviewing a delegate's business continuity plan ("BCP") to assess whether it is adequate for the business of the delegate. It is reviewing the BCP to satisfy itself that the BCP is sufficient to discharge the fund management company's own BCP obligations. The Delegate Oversight Guidance is drafted on this basis.
- o. Given that the depositary may not have been appointed directly by the fund management company, paragraph 45 was drafted to contain flexibility for the board of a fund management company to decide whether it wished to receive a depositary report. Paragraph 58 references delegates and the depositary separately so it is clear that the depositary is not a delegate. However, an externally managed investment company will always appoint a depositary directly and should always receive direct reports from the depositary.

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