

# Alternative Investment Fund Managers Directive

What does this mean for your business?



**EY**

Building a better  
working world

## Background to the Alternative Investment Fund Managers Directive (AIFMD)

---

The Alternative Investment Fund Managers (AIFM) Directive (the Directive) is sizing up to have profound structural impact on the alternative asset management industry, both in Europe and internationally.

While the main focus of the AIFM Directive is on fund managers, the Directive has a broad scope and impacts not only European Union (EU) and non-EU AIFM, but also EU and non-EU domiciled Alternative Investment Funds (AIFs), service providers to these funds and their investors.

The Directive lays down requirements for the AIFM covering authorisation, capital, marketing, conduct of business, delegation of functions and service providers and transparency reporting.

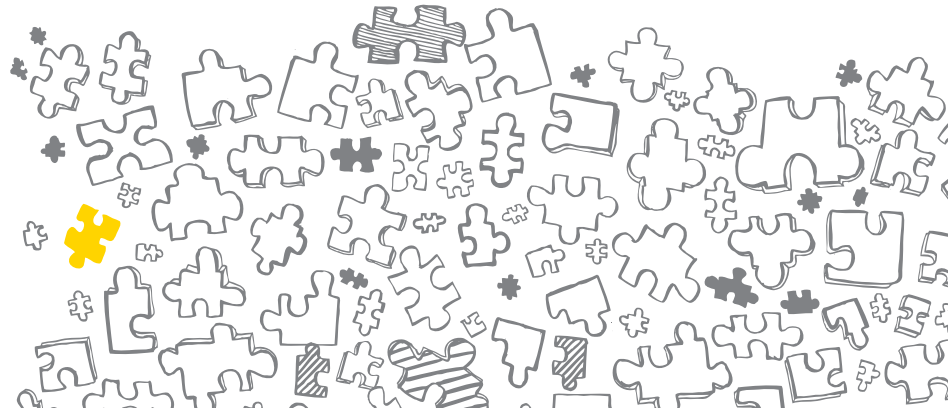
In return for more regulation of the AIFM, their service providers and fund products, the proposed Directive provides for the introduction of passports allowing AIFMs to offer their management services and market their AIF throughout the EU.

The Directive's impact is far beyond achieving basic compliance.

AIFMs are conducting strategic reviews of their fund ranges and their operating models.

Service providers, particularly those who assume depository or valuation responsibilities for AIFs, are assessing the strategic impact of the Directive on their current operating model and considering new service offerings set to meet client needs in a new regulatory environment.

Overall, the Directive will mean new opportunities and challenges for all the key stakeholders across the alternatives sector's value chain.





## How EY can help you

### **EY can provide advice, support and guidance to AIFMs and their service providers during the transition process.**

As AIFMs, EY can support you in defining your post-AIFM product ranges and operating models and assist you through the transition phase, minimising the disruption to your business.

As a provider, EY can work with you to define organisational and operational frameworks which meet the requirements of the Directive. EY have worked with many AIFMs, service providers and industry bodies, helping them to navigate the AIFM Directive in a pragmatic and solutions oriented manner.

In this brochure, we will highlight some of the main challenges of the AIFM Directive and the solutions EY have developed to help market participants meet such challenges. Should you have any questions regarding the AIFM Directive, our dedicated AIFM Directive team are available to help you.

# Organisational requirements

## Challenge

As an AIFM your competent authority (Central Bank of Ireland, FCA, etc.) will require you to demonstrate as part of your AIFMD application process that you are able to comply with each of the requirements of the Directive.

In order to do so you will need to be able to describe your business processes, governance framework and associated internal controls to demonstrate that you have a 'sound and controlled business operation' i.e., that your internal processes and procedures are effectively designed and operate appropriately under AIFMD requirements. This suite of documentation will then form part of your AIFMD license application and the basis for your overall operating structure.

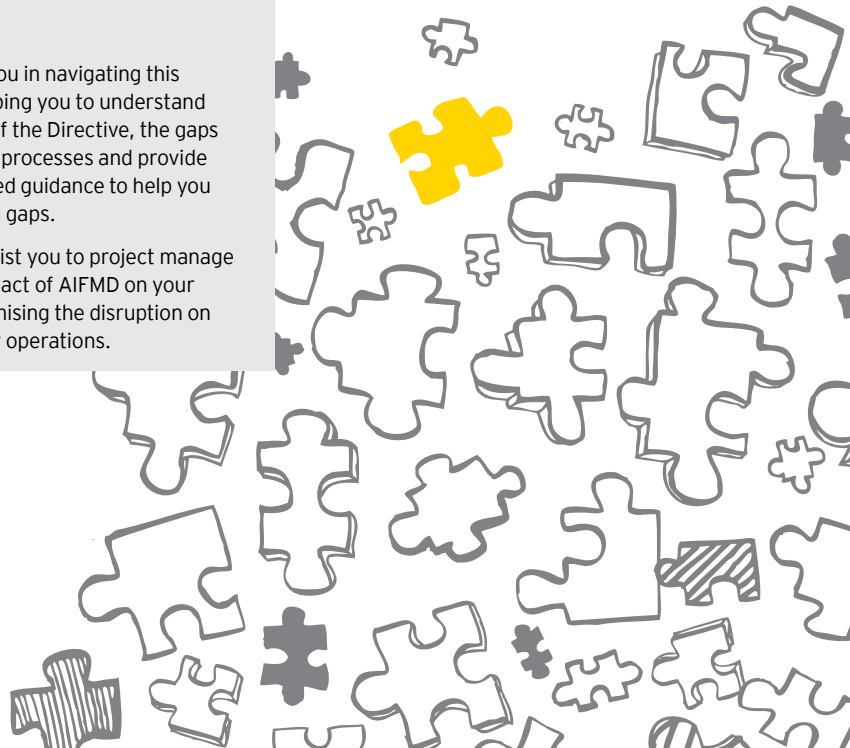
The Level II guidance provides detailed information on the organisational requirements of an AIFM. At one level, these requirements are general in nature and relate to establishing, implementing, maintaining and evaluating the adequacy and effectiveness of the systems, internal control mechanisms and arrangements. From a structural point of view the AIFM will now need to have, amongst other things, a permanent compliance and risk management function as well as specific

procedures around managing conflicts of interest, delegations, recording of portfolio transactions and policies and procedures for the valuation of assets.

## Solution

EY can assist you in navigating this regulation, helping you to understand requirements of the Directive, the gaps in your current processes and provide you with detailed guidance to help you remediate such gaps.

EY can also assist you to project manage the change impact of AIFMD on your business, minimising the disruption on your day to day operations.



# Tax optimisation of AIFM corporate structure

## Challenge

Tax is not a primary consideration of the AIFM Directive. However, many of the strategic and operational issues that fund managers need to consider in responding to it will have significant tax implications. Likewise any jurisdictional choices that face an AIF or AIFM will, most likely, have taxation consequences. An AIFMD authorised by a Member State is permitted to delegate certain functions. These delegation functions should also be considered to ensure that the principles of tax residency are preserved as intended and no unwanted permanent establishments for tax purposes are created. Transfer pricing documentation needs to be considered to ensure it reflects the facts. The payment of fees between AIF, AIFM and delegates may have significant VAT implications.

Each AIFM needs to determine which entity in its corporate group structure in which Member State should apply for authorisation and whether or not it needs to maintain its corporate structure in the other Member States.

Besides commercial reasons, tax consequences will be a key driver for the AIFM group's decision of which entity, and which

Member State, should they seek to apply for authorisation.

This decision may result in AIFM group restructuring and consolidation of legal entities within the group.

Investment management services provided to an AIF should be able to benefit from the VAT exemption for collective/special investment funds based on EU VAT principles.

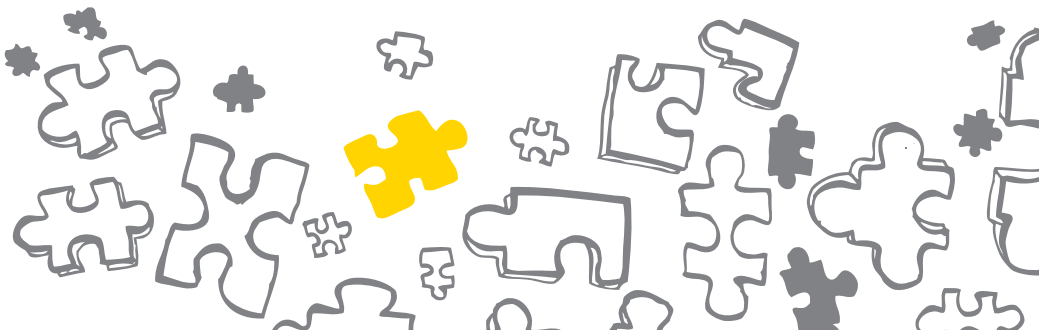
## Solution

### Tax optimisation at AIFM level

EY can help mitigate any adverse tax consequences. Moreover, EY can assist exploring tax optimisation opportunities and help determine whether the choices made under the AIFMD could adversely affect the tax structure of the AIF it manages

### VAT treatment of AIFM services

EY can help you with a review of the VAT treatment of the services including additional services provided by an AIFM and can assist the AIFM when approaching the tax authorities.



# Depository

## Challenge

Effectively taking a 'policeman' role under the AIFM Directive, the responsibilities of a depository under the Directive are such that depositories will need to review their current state operating models and remediate any identified gaps to enable them to carry out their enhanced regulatory and client responsibilities under the Directive.

## Depository Lite offering

EU managers marketing non-EU AIFs into Europe will be required to appoint a service provider who can carry out depository functions consistent with the Directive, albeit with liability for loss of assets outside their responsibility.

## Solution

EY can work with you to define the appropriate target operating model for your business. Our tailored solution and professionals will work through key considerations impacting your business, including:

- ▶ Client onboarding and risk assessment
- ▶ Asset safekeeping
- ▶ Cash flow monitoring
- ▶ Oversight duties

In addition, EY can provide assurance services on the following areas related to the depository requirements of the Directive:

- ▶ Provide assurance on the Depository's cash flow monitoring processes and procedures including investor trading and operational cash flows
- ▶ Assisting Depositories to define third party information based on the applicable auditing standards (e.g., ISAE3402)
- ▶ Auditing compliance of third party sub-custodians within defined requirements

- ▶ Design and implement ownership verification manual per asset class and jurisdiction
- ▶ Review statements of recognised external certifications by qualified external auditors and other experts
- ▶ Assurance on AIFMs effective implementation of quantitative and qualitative risk limits
- ▶ Investor payment reconciliations
- ▶ Review of effective implementation of valuation policies and procedures (IPEV, INREV) and NAV calculations policies

## Administrator

---

### Challenge

As a fund administrator, your clients will look to you for tailored solutions to help them to achieve compliance with the Directive. This may require you to reassess your current processes and redesign systems in order to provide these solutions as well as require ongoing support and expertise in the delivery of these service solutions.

### Solution

EY can work with you to define and scope your client service offerings in a post AIFM Directive environment. Key considerations on your business include:

- ▶ Reliance by third party depositories on your NAV close process and associated due diligence requirements of such depositories on your processes and controls.
- ▶ Developing and defining an appropriate asset valuation offering for your clients, together with defining the scope of each valuation process, the associated valuation models, inputs and putting an appropriate controls process in place.

EY can help through providing assurance services on processes and models in place, work with you to develop the appropriate framework and policies necessary to enable development of such offerings.

## Valuations

### Challenge

As an AIFM you are now required to have detailed valuation policies and procedures in place for each asset class you trade. Furthermore, to comply it is expected that you will impose a valuation governance model for your fund products.

Aside from the written policies and procedures, the Level II guidance requires a consistent application and periodic review of valuation policies and procedures. Transparent and proper methodologies need to be applied to the valuation of assets and models, where applied, must be validated. While the ultimate responsibility for valuation rests on the AIFM, due to the complexity of valuation of certain asset classes, external valuers may be used.

### Solution

EY can support with the valuation of assets. We have dedicated staff with the required skillset to independently value all types of asset classes. We can also assist in the design and implementation of valuation policies and models.

# Risk and liquidity management

---

## Challenge

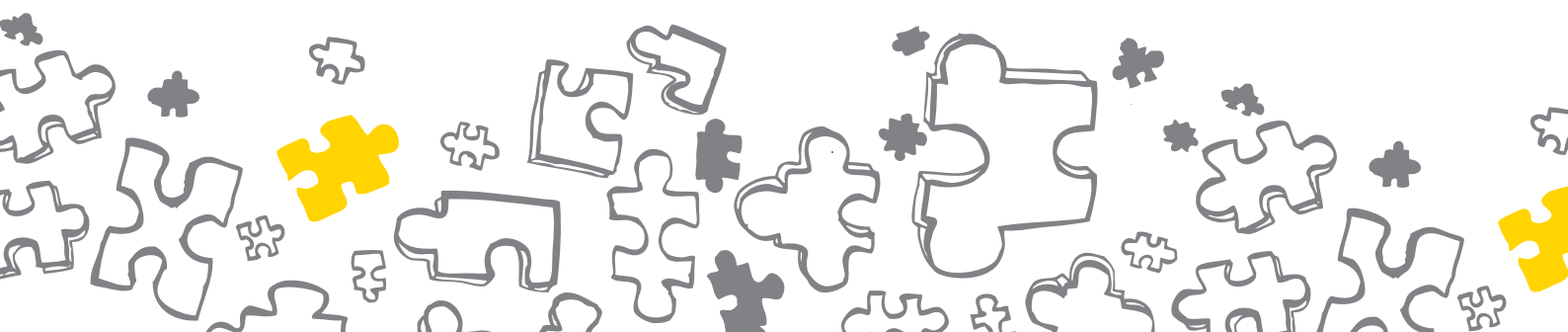
Risk and liquidity management are two key elements in the AIFM Directive Level II guidance and are focal points for regulatory and supervisory authorities. As part of the license application, AIFMs need to document the risk management processes and demonstrate that identified risks are being managed accordingly.

As part of the transparency requirements of the Directive, an AIFM needs to disclose the risk profile of its organisation. Risk must be measured and monitored on an ongoing basis. Undertaking processes such as backtesting, stress testing and environmental analysis can be required to align risk profiles for different risk categories such as market, credit and liquidity management.

## Solution

EY can support in overcoming the many risk and liquidity management challenges. We have extensive experience in planning, reviewing and providing risk and liquidity management policies. We then support the embedding of these policies by working with clients to develop management and monitoring processes to align risk management with overall organisational frameworks.

EY can further support the alignment of risk policy by helping with the undertaking, documentation and distribution of back tests, stress tests and scenario analysis.





## Assurance on policies and procedures

---

### Challenge

The provisions of the Directive include the requirement to implement certain policies and procedures that an AIFM will need to have in place and maintain in order to be compliant. Examples of such policies and procedures include:

- ▶ Conflicts of interest policy
- ▶ Risk management function
- ▶ Portfolio execution
- ▶ Liquidity management/reporting
- ▶ Valuation policies, processes and governance
- ▶ Delegation policies

### Solution

The AIFM will be required to periodically assess these procedures. We can assist to review the design and implementation of these procedures and perform the period assessments, providing assurance to the AIFM on their compliance requirements under the Directive. These required policies and procedures may be embedded in existing control frameworks for which we can provide assurance and other attestation services as well (e.g., an 'AIFM Directive compliant' ISAE3402 type 2 report).

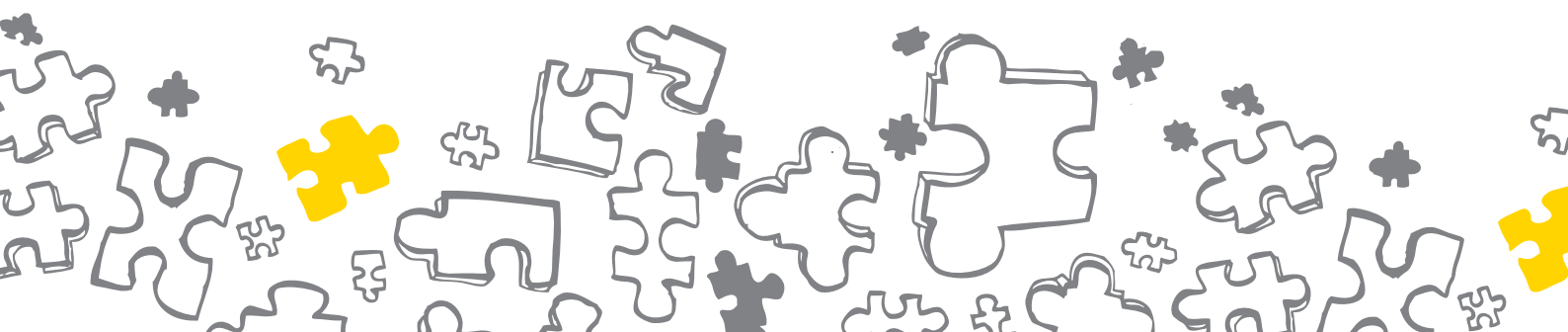
### Challenge

The Directive includes several other areas where additional assurance may be needed, for example:

- ▶ Review calculation of assets under management
- ▶ Review calculation of an AIF's leverage
- ▶ Review and design of Regulatory Reporting Framework

### Solution

We can provide assurance and attestation services for reviews that may be needed in connection with these challenges.



# Reporting

## Challenge

The AIFM Directive requires periodic regulatory reporting akin to the SEC requirements of PF reporting. In order to achieve compliance an AIFM or its service provider will look to set up a reporting framework to ensure they can perform regulatory reporting as required under the directive.

## Solution

EY can provide support in various ways on the reporting requirements under AIFMD:

- ▶ We can provide support in the design and implementation of the required reporting framework under AIFMD
- ▶ On a recurring basis, we can perform controls testing or compliance procedures on the reporting process at the AIFM and/or AIF
- ▶ On a periodic basis, we can also perform an audit or provide (additional) assurance on the investor, depositary and regulatory reportings of the AIF(s) and AIFM(s)



# Our team



**Fergus McNally**

**Partner**

Tel: +353 1 221 2599

Email: [fergus.mcnally@ie.ey.com](mailto:fergus.mcnally@ie.ey.com)



**Billy McMahon**

**Executive Director**

Tel: +353 1 221 2738

Email: [billy.mcmahon@ie.ey.com](mailto:billy.mcmahon@ie.ey.com)



**Sheldon D'Souza**

**Senior Manager**

Tel: +353 1 221 2951

Email: [sheldon.d'souza@ie.ey.com](mailto:sheldon.d'souza@ie.ey.com)



**Donal O'Sullivan**

**Partner**

Tel: +353 1 2212 455

Email: [donal.osullivan@ie.ey.com](mailto:donal.osullivan@ie.ey.com)



**Andrew Lomax**

**Manager**

Tel: +353 1 221 1700

Email: [andrew.lomax@ie.ey.com](mailto:andrew.lomax@ie.ey.com)



**Sinéad Colreavy**

**Senior Manager**

Tel: +353 1 221 2930

Email: [sinead.colreavy@ie.ey.com](mailto:sinead.colreavy@ie.ey.com)

**About EY**

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organisation and may refer to one or more of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organisation, please visit [ey.com](http://ey.com).

© 2013 Ernst & Young. Published in Ireland. All Rights Reserved.

2664.indd 07/13. Artwork by the BSC (Ireland)

Images sourced from Shutterstock.com

The Irish firm Ernst & Young is a member practice of Ernst & Young Global Limited. It is authorised by the Institute of Chartered Accountants in Ireland to carry on investment business in the Republic of Ireland.

Ernst & Young, Harcourt Centre, Harcourt Street, Dublin 2, Ireland.

Information in this publication is intended to provide only a general outline of the subjects covered. It should neither be regarded as comprehensive nor sufficient for making decisions, nor should it be used in place of professional advice. Ernst & Young accepts no responsibility for any loss arising from any action taken or not taken by anyone using this material.

[ey.com](http://ey.com)