

5 KEY ISSUES
WE PREDICT TO BE
AT THE FOREFRONT OF THE
CP86 ON-SITE INSPECTION
FOR MANCOS & SMICS
and how best to prepare.

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AQUEST

FOR THE IRISH FUNDS INDUSTRY

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#AQUEST #CP86



CONTENTS

Improving your experience with the Regulator

Today looks like

5 key issues

4 ways to prepare

1 resource to leverage

Meet Daniel Lawlor

Improving your experience with the Regulator

You can leverage this CP86 review to improve your relationship with the Regulator.

This report has been written with this intention in mind.

Other industry stakeholders will share perspectives from a legal, compliance or operational perspective.

Aquest views things from a regulator's perspective.

We arm you with the tools and the ideas you need to understand better a regulator's point of view so you can demonstrate to the regulator that you're on the same page as them. **That's what we call being Regulator Intelligent (RQ)!**

Expect the contents of this piece and the perspectives of Aquest, to present you with direction that will work hard to make you RQ.



**Are you Regulator
Intelligent?**

TODAY LOOKS LIKE...

With Central Bank CP86 onsite inspections looming on the horizon, all Fund Management Companies (ManCos) and Self Managed Investment Companies (SMICS) that received the themed inspection letter will be wondering whether they will be chosen for an onsite visit.

Most are proceeding on the basis that a visit is likely and have their staff preparing now. **Waiting until they receive a notification for an on-site visit, will not provide sufficient time to properly prepare for a very important engagement with their regulator.**

What areas will the Central Bank be most interested in?

We predict 5 key issues to be at the forefront of the Central Bank's CP86 on-site inspection.

Ensuring the best chance of achieving a good outcome while turning this process into an opportunity to build and develop a positive relationship with the Central Bank, is really the only agenda that matters in relation to CP86.



5 KEY ISSUES

WE PREDICT TO BE AT
THE FOREFRONT OF YOUR
CP86 ON-SITE INSPECTION.

1. ORGANISATIONAL
EFFECTIVENESS

2. GOVERNANCE

3. INVESTMENT MANAGEMENT

4. RISK MANAGEMENT

5. RESOURCES

ISSUE 1: THE OE ROLE

This role was created by the Central Bank during the CP86 process.

The guidance provided by the Central Bank concerning how the OE role is to be carried out, is very high level and principles based. This leaves lots of scope for ManCos to determine how best to carry out the OE role.

Since CP86 has been finalised, the Central Bank has been flagging that it will carry out a review to see how well ManCos are getting on with the OE role.

We believe that ManCos should be fully prepared for the Central Bank to ask specific questions about the OE including:

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1. How does the OE role justify the current level of resources in light of the CBI's resource requirement for new ManCos?
 2. What is the OE role doing in practice day-to-day, weekly, monthly, semi annually? Specifically, how is the OE role defined?
 3. What is the specific OE role profile and how has that changed in light of the newly authorised ManCos?
 4. Can the OE role clearly and succinctly demonstrate what is expected of them; first by the ManCo and secondly by the Central Bank?
 5. What is their time agreement with the ManCo in 2017, 2018 and how has that changed for 2019?
 6. Most importantly, describe how their role adds value to investors?

**THE CP86 REVIEW WILL HELP GIVE
THE CENTRAL BANK A BETTER
UNDERSTANDING OF:**

- > how well the OE role concept is working in practice**
- > to what degree the OE role is falling short of their expectations**
- > whether CP86 needs revising & updating industry wide**

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ISSUE 2: GOVERNANCE

Although not specifically flagged in the thematic review letter, the Central Bank will no doubt be very interested in governance issues affecting ManCos and SMICs.

The Central Bank will be on the lookout for evidence of challenge and engagement by the directors.

In our view, board minutes should not simply recount the information contained in delegate's reports to the board. The Central Bank can easily see this information by reviewing a board pack. Instead, the Central Bank will be reviewing minutes to see the extent to which the directors are engaging with the materials presented to them by delegates.

Expect questions such as:



1. How does the board approach the approval of new sub funds?

2. What is the documented process that the Board uses to approve new sub funds?



3. Is it meticulous and systematic in the way it works through the approval of;

- an investment approach



- a risk framework

- the distribution strategy

for each and every investment fund under management (just like the CP86 guidance requires it to be), or is the board's fund approval much less engaged? If so, why?



ISSUE 3: INVESTMENT MANAGEMENT

In the thematic review, the Central Bank has asked questions about how the designated person for investment management carries out the role in practice.

The Central Bank has looked for copies of reports from the designated person to the board and from delegates to the designated person.

 It clearly wants to enquire whether a coherent framework was put in place. **Designated persons with investment management responsibility should be more than ready to answer questions on this matter.**

 One topic under the Investment management heading that the Central Bank will likely be interested in, is the extent to which the ManCo and/or SMIC **relies** on the information provided by the delegate investment manager.

 Does the ManCo have its own independent data feeds and does it carry out its own investment analysis?



If it is dependent on information reported by the Investment manager with reconciliations being made as best as possible with information provided by the Fund administrator, **the Central Bank will likely want to know how exactly does it mitigate risk?**

Finally it is worth noting an extract from a speech by **Ed Sibley, Deputy Governor for Financial Regulation at the Central Bank of Ireland** at the Irish Funds Conference in May 2019.

In his speech he noted that some ManCos may be ceding too much control to Investment managers, giving them too much decision making power.

With this in mind, **ManCos should arm themselves with evidence of examples where they have engaged robustly, and in a challenging fashion, with their delegate investment managers.**

ISSUE 4: RISK MANAGEMENT

Similar to Investment management, the Central Bank has asked plenty of questions and required the submission of detailed documents in relation to a ManCo's fund risk framework.



ManCos should be able to demonstrate how a risk framework was agreed at the time a new fund was established, and how the ongoing monitoring of the fund is **mapped back** to that risk framework,



Again, like investment management, if the ManCo is dependent upon reporting from the Investment manager on fund risk management and does not receive independent data feeds to carry out its own analysis, **it should be ready to provide a credible and considered analysis as why it uses this approach.**

This should include an analysis of how it manages and mitigates the risks associated with relying on information from third parties.

RISKY OR SAFE?

You do not have independent data feeds to carry out your own analysis?

Prove to us that this is a credible and safe approach.

ISSUE 5: RESOURCES

For a SMIC or Legacy ManCo (this means ManCos more than two years old and operating in a secondment model) they should expect that the primary focus will be on resources.

 In particular, these SMICs and ManCos should be able to answer in detail, questions about how they have responded and adopted to CP86,

 The Central Bank will be keen to understand how SMICs and Legacy ManCos are demonstrating compliance with all of their obligations under UCITS to the AIFMD and to learn about the additional resources put in place to ensure this compliance.

ManCos and SMICS that have adopted a 'wait-and-see' approach should be prepared for Central Bank challenge.

RESOURCES?

How does the OE role justify the current level of resources in light of the CBI's resource requirement for new ManCos?

4 WAYS

**TO PREPARE FOR
AN ON-SITE INSPECTION**

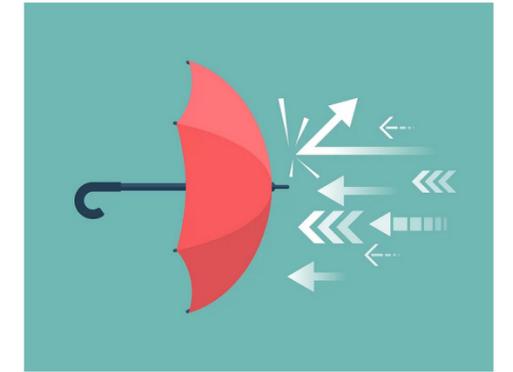
1. KNOW THYSELF

2. LEADERSHIP? HEAR THIS

3. MANAGE EXPECTATIONS

4. MOCK INTERVIEWS

Have a full assessment of your submission to the Central Bank in order to be fully prepared for what to expect when they are inspecting.



1. On-site Lay of the Land workshop
2. Document Submission Review
3. x6 Mock Interviews 1-on-1 with the Leadership Team
4. Full day workshopping the CP86 Inspection Preparation timeline
5. Clarity on the firm's core areas of weakness
6. Clarity on specific questions you will want to pay particular attention to
7. Group preparation under supervision of Daniel Lawlor to ensure the best possible outcome for the firm
8. Support during an on-site inspection

Aquest.ie/CP86Programme

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1. KNOW THYSELF

The Central Bank inspection team will be very well prepared for each onsite inspection that they undertake.

They will have reviewed the pack of documents submitted in great detail and will have cast a very critical eye over everything they read. They will not be coming onsite to verify what they have read; they will be coming onsite to find out **more** than they already know.

 ManCos will be in a better position to engage constructively and effectively with the Central Bank where they have already taken the time to review their own materials from a similar, critical perspective.

 This means reviewing the materials as if you were the regulator, identifying strengths and weaknesses and coming up with a list of the types of questions you would ask if you yourself were the regulator.



2. LEADERSHIP? HEAR THIS...

Prepare the leadership team.

A ManCo should expect that a number of the senior leadership team will be interviewed individually by the Central Bank inspectors.

In my experience, leadership teams that don't prepare as a group are certain to provide inconsistent answers to the Central Bank around matters of fact that should be easy to get right. Eg. number of sub funds under management.



From a regulator's perspective, this kind of inconsistency raises a flag: do the leadership team really know what they are doing? Are they on top of their game?



Group briefings of the senior leadership team are **essential** to ensure everyone is on the same page and providing consistent answers to questions of fact.

Getting the basics right is the foundation for getting a successful outcome to an onsite inspection.



3. MANAGE EXPECTATIONS

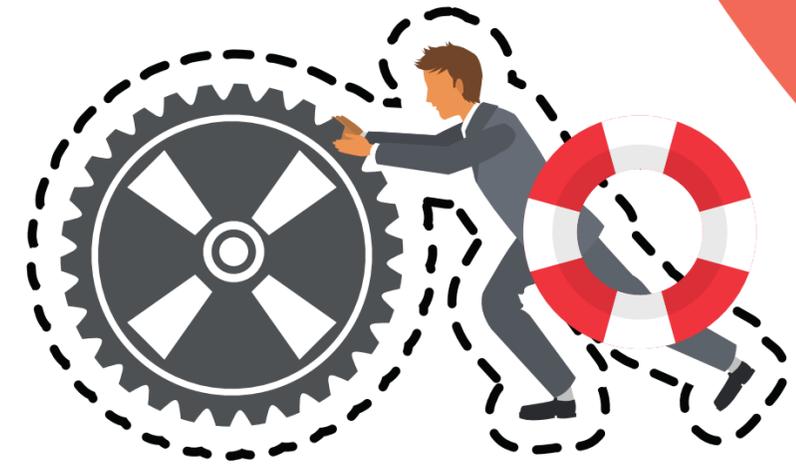
Part of the CP86 inspection preparation process is to manage internal expectations of what the possible outcome might be. Knowing what a good outcome looks like is very important in terms of managing what happens afterwards.

Every ManCo that's subject to an onsite inspection, should, at a minimum expect to receive a risk mitigations programme (RMP) from the Central Bank.

In it, the Central Bank will identify risks that it has noticed as part of the review process, include a list of actions to be taken to mitigate these risks and provide a specified time frame within which this action should be made complete.

Where you decide to challenge some of the actions required in the RMP, it is important to do so in a measured fashion. Pushing back on all risks identified is simply not credible and is more likely to irritate the regulator.

It is much better to identify one or two key areas where there is a concern, and suggest an alternative approach to the regulator. The alternative should achieve the same outcome but in a manner of which is more appropriate for the ManCo in question.



4. MOCK INTERVIEWS

Finally, the Central Bank inspection team will be very well prepared for interviews that they conduct. They will come in the door already knowing where your potential areas of weaknesses are and have a good idea of where to probe.

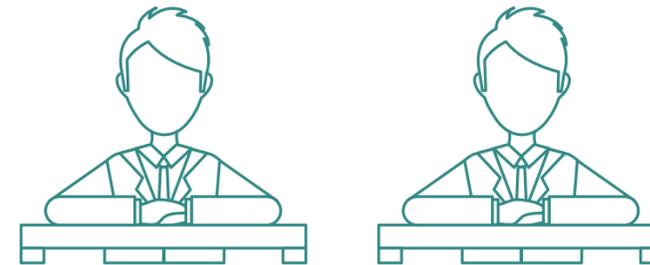
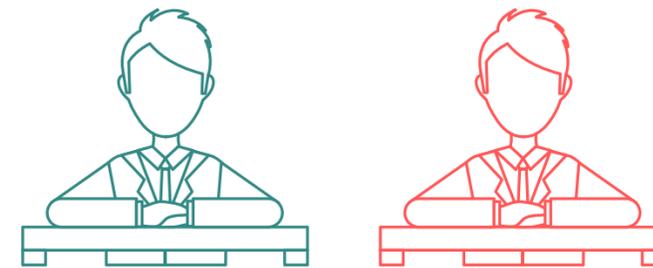
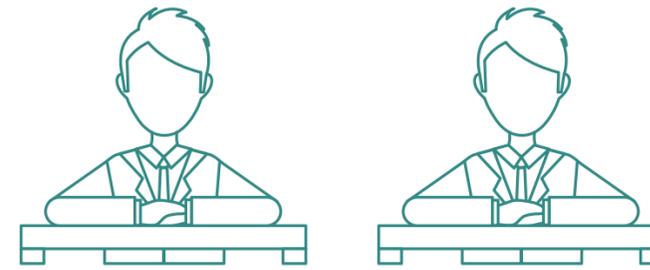
ManCos that prepare well will be effective in their interview with the regulator,

Further, well prepared ManCos will be able to use this opportunity to improve and develop their relationship with the Central Bank.

ManCos that do not prepare should expect the experience to be more stressful, time consuming and difficult.

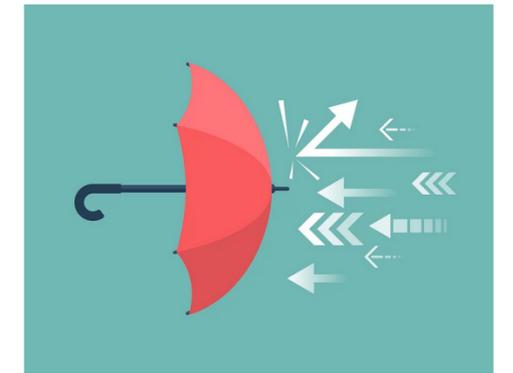
ManCos using a wait-and-see approach will almost certainly not have sufficient time to prepare for their on-site inspections.

The old adage applies: **fail to prepare, prepare to fail.**



Have Daniel Lawlor facilitate your mock interviews as part of Aquest's CP86 Preparation Advisory Programme

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**1 RESOURCE
TO LEVERAGE**



Daniel Lawlor
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MEET DANIEL LAWLOR

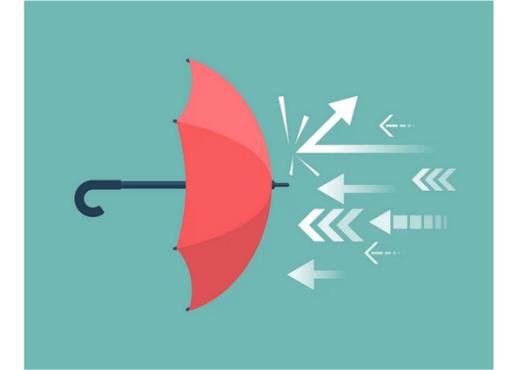
As the former head of the Central Bank of Ireland's Funds Policy Team and the Central Bank's Project Lead on CP86, Daniel was involved in designing, drafting & implementing regulatory initiatives affecting the funds industry from 2010 to 2017.

With an intimate knowledge of CP86 coupled with the perspective of an ex-regulator, Daniel is in a unique position to help firms improve their relationship with the financial regulator by becoming Regulator Intelligent.

Before joining the Central Bank, Daniel worked as an Investment funds lawyer for 9 years at William Fry, one of Ireland's leading law firms.

Today, Daniel Lawlor is MD of Aquest; a boutique firm dedicated to improving your experience with the financial regulator.

A 5-PHASE COMPREHENSIVE CP86 ADVISORY PROGRAMME FOR MANCOS & SMICS:



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