



GDPR – Is your Fund ready?

Etain de Valera
21st September 2017

Countdown to GDPR

- ▣ General Data Protection Regulation - Regulation (EU) 2016/679
- ▣ Replaces existing data protection law in all member states on 25 May 2018
- ▣ Designed to result in single, uniform set of data protection rules applying across the EU (EU Regulation instead of EU Directive)
- ▣ Retains and enhances existing data protection concepts and requirements
- ▣ Increases obligations on controllers/processors
- ▣ Affords new rights to data subjects
- ▣ Now is the time to act!

Key Data Protection Terminology

- ▣ Definitions (Article 4) – Similar to existing regime
- ▣ **Personal data** – relates to identified or identifiable living individuals (not anonymised data)
- ▣ **Processing** – widely defined – includes any collection, recording, organisation, structuring, storage, adaptation or alteration, retrieval, consultation, use, disclosure, erasure or destruction of data
- ▣ **Controller** – entity which determines the purposes and means of processing of personal data –
- ▣ **Processor** – entity which processes personal data on behalf of controller – e.g. outsourced service provider

GDPR and Funds: Data Controller or Processor?

- ▣ Funds and Fund Management Companies – Data Controllers
- ▣ Relevant Data Subjects – investors in the fund, employees or persons authorised to act on behalf of legal persons who provide personal data
- ▣ Fund service provider entities such as administrators, paying agents and distributors are more likely to be data processors.
- ▣ Assessment as to whether a controller or processor must be done however on a case by case basis
- ▣ Administration/Distribution/Paying Agency Agreements - what do they say?
- ▣ To be a processor - clearly defined scope of activities so that not determining the purpose or means of processing

GDPR and Funds: Extraterritorial Effect

- ▣ Who is in scope?
- ▣ GDPR applies to processing of personal data by controllers/processors in the EU regardless of whether the actual processing takes place in the EU.
- ▣ Irish Funds, Management Companies, Service Providers
- ▣ Also applicable to processing of personal data of data subjects in the EU by a controller or processor not established in the EU where the activities relate to either:
 - (a) *offering goods or services to EU citizens (irrespective of whether payment is required) ; or*
 - (b) *monitoring of behaviour that takes place within the EU”*

GDPR and Funds: Extraterritorial Effect

- ▣ The recitals to GDPR are instructive (though not of themselves binding) as to what is meant by “offering goods or services to data subjects” for the purposes of this extra-territorial effect. Recital 23 provides:

“In order to determine order to determine whether such a controller or processor is offering goods or services to data subjects who are in the Union, it should be ascertained whether it is apparent that the controller or processor envisages offering services to data subjects in one or more Member States in the Union. Whereas the mere accessibility of the controller's, processor's or an intermediary's website in the Union, of an email address or of other contact details, or the use of a language generally used in the third country where the controller is established, is insufficient to ascertain such intention, factors such as the use of a language or a currency generally used in one or more Member States with the possibility of ordering goods and services in that other language, or the mentioning of customers or users who are in the Union, may make it apparent that the controller envisages offering goods or services to data subjects in the Union.”

GDPR and Funds: Extraterritorial Effect

- ▣ Non-EU service providers will have to consider the basis on which they are processing data i.e. is it apparent that they are doing so in connection with their own offering of goods or services
- ▣ Non- EEA Investment Managers, Paying Agents, Distributors – processing personal data in connection with the offering of goods or services by the Fund or their own offering of goods or services?
- ▣ Consequences - Where data controllers/processors outside of the EU who target data subjects within the EU come within scope of the GDPR, they will have to designate a representative within the EU in order to ensure compliance with the GDPR (there is an exemption of which they can avail but it is very limited).

Obligations on Data Controllers: An Overview

- ▣ **Communication** - with data subjects in a transparent manner
- ▣ **Data Information Notice** - provision of certain information to the data subject when collating personal data
- ▣ **Lawful Processing** - ensuring that processing of data (including the processing of special categories of data) is lawful
- ▣ **Consent** – enhanced requirements
- ▣ **Purpose Limitation** - Data to be kept for specified, explicit and lawful purposes and not further processed for any incompatible purposes
- ▣ **Data Minimisation** - Data should be adequate, relevant and not excessive:
 - ▣ Keep only the minimum amount of personal data needed for the purpose for which it is being processed
 - ▣ Avoid keeping irrelevant or excessive data

Obligations on Data Controllers: An Overview (cont.)

- ▣ **Relevance** – obligation to keep data up to date
- ▣ **Storage Limitation** Personal data should only be retained for such period as is necessary rather than being kept on a “just in case” basis
- ▣ **Security Measures** - measures must be taken against accidental loss, unauthorised access to, alteration, disclosure or destruction of personal data
- ▣ **Third country transfer** - ensuring that transfer of data to third countries/international organisations is in compliance with GDPR
- ▣ Appointment of Data Protection Officer (if applicable) / Implementation of Data Protection Impact Assessments (if applicable)

Obligations on Data Processors: An Overview

- ▣ GDPR expands the nature of obligations on data processors:
 - ▣ Processors should process on instructions only
 - ▣ No appointment of delegate processors without consent of controller and subject to the same conditions as regards sub-processing agreements
 - ▣ Notification of data breach “without undue delay”
 - ▣ Record keeping of data processing activities;
 - ▣ Compliance with conditions for transfer
 - ▣ Co-operation with supervisory authorities
 - ▣ Mandatory requirements for content of processing agreements

Fund Documentation – Key considerations

- ▣ Obligation to communicate in a clear and transparent way with data subjects as regards data processing and their additional rights
- ▣ Data subject must be provided with certain information relating to the processing of their personal data
- ▣ Information must be provided **at the time** the personal data is being obtained
- ▣ For Funds this will mean that the Application Form for investment, should provide this information and should be updated accordingly.
- ▣ Also updates to Prospectus, websites and other investor communications as regards processing of data and a data subjects rights
- ▣ Relevant service provider contracts will need to be reviewed and updated as necessary.
- ▣ Application Form should include the following:

Application Form – Data Protection Notice

- ▣ Nature of data being collected
- ▣ Purposes for which data may be used
- ▣ Persons to whom data may be disclosed
- ▣ Legal basis for the processing (where applicable) i.e. consent or necessary lawful purpose
- ▣ Where relevant, the legitimate interest justifying processing of the data
- ▣ Where relevant, details on international data transfers
- ▣ Retention times (or criteria used to determine how long data retained)
- ▣ Data protection rights (including right of access, correction, erasure and data portability)
- ▣ Right to withdraw consent to data processing at any time (where applicable)
- ▣ Right to complain to DPA
- ▣ Contact details of Data Protection Officer (if applicable)
- ▣ Existence of “automated decision making” (i.e. whether the data subject will be subject to “profiling”) in the processing of such data

Application Forms – Legal Basis For Processing

- ▣ Personal data can only be processed where it is “lawful” to do so.
- ▣ Must justify that the processing of personal data is lawful on one of the following grounds:
 - ▣ consent of data subject given for one or more specific purposes; or
 - ▣ the processing of personal data is necessary for any of the following:
 - i. performance of contract to which data subject is party
 - ii. the data controller to comply with its legal obligations
 - iii. the protection of the public interest or vital interests of the data subject or any other person; or
 - iv. the “legitimate interests” of the data controller - must be justified

Application Forms - Consent Requirements

- ❑ Consent as a basis of lawful processing must be “freely given, specific, informed and unambiguous”
- ❑ Data subject must be aware that he has given consent and the extent of such consent
- ❑ Separate consent should be given for each personal data processing operation
- ❑ Positive indication of agreement to such processing is required: cannot be inferred from silence, pre-ticked boxes or inactivity.
- ❑ Consent should not be relied upon as a lawful means of processing the data where there is a clear imbalance between the data controller and the data subject: it must be “freely given”
- ❑ Controllers must be able to demonstrate that valid consent was given

Application Form Consent – Remediation?

- ▣ Obtaining valid consent is now more onerous under GDPR
- ▣ Funds and Fund Management Companies and their service providers will need to determine whether consent already received from data subjects to date meet the GDPR requirements
- ▣ If not, organisations should:
 - (i) reach out to data subjects to get their “GDPR-compliant” consent to the processing of their data; or
 - (ii) determine whether they can rely on one of the other grounds outlined above.
- ▣ Data used for direct marketing purpose: Advisable that express “opt-in” consent is obtained (as may be difficult to rely on “legitimate interests” as the grounds on which such processing is lawful and data subjects right to object where the data is processed for “legitimate interests” of the DC).

Processing Contracts: An Overview

- ▣ Written agreement between data processor and data controller
- ▣ Does not have to be a specific data processing agreement
- ▣ But there is express mandatory content
 - ▣ Subject matter and duration of processing
 - ▣ Nature and purpose of processing
 - ▣ Types of personal data and categories of data subjects
 - ▣ Obligations and rights of controllers
 - ▣ Contains obligations of confidentiality
 - ▣ Obligations as to compliance with appropriate technical and organisational security measures
 - ▣ Assistance with notification requirements
 - ▣ Return or delete data on termination of contracts
 - ▣ Provision of information and audit and inspection rights for compliance

Policies and Procedures

- ▣ Enhanced responsibility of Fund boards and Fund management company boards as regards data protection
- ▣ GDPR imposes responsibilities as regards internal governance for data protection
- ▣ Ensure appropriate data protection policy in place. Potential issues to be addressed:
 - ▣ Due diligence on data processors and sub-processors
 - ▣ Appointment if necessary of data protection officer - responsibilities
 - ▣ processes and procedures for escalation and notification of data breaches:
 - ▣ Mandatory notifications to DPC within 72 hours of becoming aware of the breach – unless breach unlikely to result in a risk to data subjects
 - ▣ Mandatory notification to affected data subjects “without undue delay” – where there is a high risk to data subjects so that the data subjects can take necessary precautions
 - ▣ Data processors required to notify data controllers of data security issue without undue delay
- ▣ Triggers for data protection impact statements required where processing is high risk to an individual’s rights (e.g. transfers of data)

Transfers Abroad

Data may only be transferred outside of EEA in the following cases:

1. Adequacy Decision

- ▣ European Commission must consider that recipient country ensures “adequate level of protection”
- ▣ Andorra, Argentina, Canada, Faroe Islands, Guernsey, Isle of Man, Israel, Jersey, New Zealand, Switzerland and Uruguay have been determined by the Commission to have adequate protection
- ▣ EU-US Privacy Shield:

[http://ec.europa.eu/justice/data-protection/international-transfers/eu-us-privacy-shield/index_en.htm]

Transfers Abroad

2. Appropriate Safeguards

If there is no “adequacy” decision granted by the Commission, a transfer of personal data outside of the EEA may still be possible if there are “appropriate safeguards” in place which include:

- ▣ Binding Corporate Rules
- ▣ Data transfer agreement adopted/approved by the Commission
- ▣ Legally binding agreement between public authorities or bodies

Transfers Abroad

3. Derogations for specific situations

- ▣ If there is no “adequacy” decision granted by the Commission or other “appropriate safeguards” in place , a transfer of personal data outside of the EEA may still be possible in certain other circumstances, including:
 - ▣ Data subject has explicitly consented to proposed transfer **after** being informed of the associated risks
 - ▣ Transfer is necessary for the performance of the contract between the data subject and data controller
 - ▣ Transfer is required for establishment, exercise or defence of legal claims
 - ▣ Transfer is necessary on public interests ground
- ▣ Fund and Fund Management Companies should discuss with their service providers the basis on which a transfer of data may take place particularly in the context of any outsourcing arrangements

Data Protection Officer

- ▣ **Currently:** no specific requirement under existing legislation: optional for all controllers/processors (but must specify a compliance person when registering with the DPC)
- ▣ **Under the GDPR, an organisation must appoint a DPO where:**
 - ▣ the processing is carried out by a ***public authority or body***
 - ▣ the ***core activities*** of the ***controller or processor*** consist of processing operations which, by virtue of their ***nature, scope*** and/or ***purposes***, require ***regular and systematic monitoring*** of data subjects ***on a large scale; or***
 - ▣ the ***core activities*** of the ***controller or processor*** consist of the processing on a ***large scale*** of ***special categories of data*** and data relating to ***criminal convictions and offences***

Article 29 Working Party Guidelines:

http://gdprandyou.ie/wp-content/uploads/2017/05/wp243_rev01_enpdf.pdf

GDPR – Compliance Steps for Funds and ManCos

- i. Data Inventory –review/health check of personal data and processing activities – data protection audit/assessment
- ii. Review Prospectus, Application Forms, Websites and Service Provider contracts and update as necessary;
- iii. Review basis for processing – e.g. consent, legitimate interests, necessary for contract performance etc
- iv. Consider changes to be made to ensure procedures cover all the rights of a data subject (right of access, erasure, correction, data portability etc)
- v. DPO appointment (if applicable)
- vi. Ensure service providers review security arrangements in place to protect data and ensure that a personal data breach can be identified, reported and investigated
- vii. Review transfer of data outside of the EEA
- viii. If engaging in any new processing, consider whether a Data Protection Impact Statement should be carried out

Contact

Etain de Valera

Dillon Eustace

33 Sir John Rogerson's Quay, Dublin 2, Ireland

Telephone +353 1 66 700 22

Fax +353 1 66 700 42

E-Mail: etain.devalera@dilloneustace.ie

Website: www.dilloneustace.ie

Dublin Cayman Islands Tokyo New York



PRIIPs - Impact on QIAIFs

Aisling O'Malley

PRIIPS is Coming!

- ▣ Following what has been a protracted journey through the EU legislative process, the EU Regulation on Packaged Retail and Insurance-Based Investment Products ("PRIIPs") (EU 1286/2014) (the "PRIIPs Regulation") will finally take effect on 1 January 2018.

- ▣ **Objective**

The aim of the PRIIPs Regulation is to encourage efficient EU markets by helping retail investors to better understand and compare the key features, risks, rewards and costs of different PRIIPs, through access to a highly prescriptive and consumer-friendly Key Information Document ("KID"). The 'one-eyed KID'!

- ▣ **Flexibility to use 'UCITS' KIID?**

Article 32 of the PRIIPs Regulation provides Member States with the flexibility to allow AIFs which are subject to the PRIIPs Regulation to prepare a "UCITS" KIID instead of a PRIIPs KID until 31 December 2019.

Both the CSSF and the FCA have availed of this flexibility and will permit AIFs in their jurisdictions which are offered to retail investors to prepare a UCITS style KIID in order to comply with its obligations to prepare a KID under the PRIIPs Regulation until December 2019.

To date, the Central Bank has not put in place a mechanism for Irish PRIIPs to avail of the flexibility afforded by Article 32 of the PRIIPs Regulation.

PRIIPS is Coming!

▣ What is a PRIIP?

PRIIP stands for **Packaged Retail and Insurance-based Investment Products**.

The PRIIPs Regulation defines a “PRIIP” as *“an investment ... where, regardless of the legal form of the investment, the amount repayable to the retail investor is subject to fluctuations because of exposure to reference values or to the performance of one or more assets which are not directly purchased by the retail investors”*.

▣ Definition of ‘Retail Investor’

The definition of “*retail investor*” within the PRIIPs Regulation is a “**retail client**” as defined in MiFID II which in turn is defined as a client “**who is not a professional client**” as defined in MiFID II.

Therefore, any person who does not fall within the “professional client” definition will be a “retail client” and therefore considered to be a “retail investor”.

Scope – Who Will The PRIIPS Regulation Apply To?

- ▣ The PRIIPs Regulation applies to persons who:
 - **manufacture PRIIPs for sale to retail investors in the EU**, for example, fund managers, life insurance companies, credit institutions and investment firms.
 - **advise on or sell PRIIPs to retail investors in the EU**, for example, stockbrokers, distributors, advisers and other firms that provide advice to retail clients on funds, structured products and derivatives.

- ▣ The following products fall within the scope of the PRIIPs Regulation:
 - (i) life assurance based investment products;
 - (ii) **investment funds**;
 - (iii) structured term deposits; and
 - (iv) derivatives.

- ▣ Although a product may fall within the definition of a PRIIP, that product must also be sold to **retail investors within the EU** to fall within the scope of the PRIIPs Regulation.

In The Context Of A QIAIF, Who Is The 'Product Manufacturer'?

- ▣ The PRIIPs Regulation, when referring to 'PRIIP manufacturers' refers to "fund managers, insurance undertakings, credit institutions or investment firms.....'they are in the best position to know the product'

- ▣ AIFM or Investment Manager or possibly a collaborative arrangement?

Is Your QIAIF Required to Produce a PRIIPS KID?

QIAIF's

- ▣ At first glance, QIAIFs may be considered out of scope given that they are typically marketed to non-retail investors.
- ▣ **However**, one surprising consequence for QIAIFs is that the definition of “Qualifying Investor” under the Central Bank’s AIF Rulebook may in certain circumstances bring a QIAIF within the definition of a PRIIP where such QIAIFs do not limit investor eligibility to professional clients under MiFID.

Is Your QIAIF Required to Produce a PRIIPS KID?

- ▣ Per the Central Bank's AIF Rulebook:
- ▣ The Qualifying Investor AIF shall only accept subscriptions from an investor who:
 - a) **is a professional client within the meaning of Annex II of MiFID;** or
 - b) receives an appraisal from an EU credit institution, a MiFID firm or a UCITS management company that the investor has the appropriate expertise, experience and knowledge to adequately understand the investment in the Qualifying Investor AIF; or
 - c) certifies that they are an informed investor by providing the following:
 - Confirmation (in writing) that the investor has such knowledge of and experience in financial and business matters as would enable the investor to properly evaluate the merits and risks of the prospective investment; or
 - Confirmation (in writing) that the investor's business involves, whether for its own account or the account of others, the management, acquisition or disposal of property of the same kind as the property of the Qualifying Investor AIF.

Is Your QIAIF Required to Produce a PRIIPS KID?

- ▣ Accordingly, if you look at the definition of Qualifying Investor (as quoted above), Category (a) will not be a retail investor for the purposes of the PRIIPs Regulation. However, Category (b) and Category (c) – on the basis that they do not themselves fall within Category (a) – will not be professional clients and will therefore be “retail investors” for the purpose of the PRIIPs Regulation.
- ▣ In the event that an Irish QIAIF is offered to a prospective investor falling within Category (b) or Category (c), that could bring the QIAIF within the remit of the PRIIPs Regulation and require a PRIIPs KID.

Knowledgeable Employees

- ▣ If a QIAIF is offered or sold to “knowledgeable employees” (i.e. benefitting from an exemption from the Qualifying Investor criteria and minimum investment requirement on the basis of their involvement in the management of the QIAIF) as permitted by the AIF Rulebook, care would need to be taken to ensure that knowledgeable employees fall within the definition of “professional client” to avoid PRIIPs.

Is Your QIAIF Required to Produce a PRIIPS KID?

Marketing

- ❑ In order for a QIAIF to be able to be marketed by its AIFM on a cross-border basis within the EEA, it can only be marketed to “professional clients” within the meaning of MiFID unless the specific rules of the relevant member state permit the marketing of foreign EU AIFs to investors who do not constitute “professional clients”.
- ❑ In other words, there is no cross-border marketing passport provided by AIFMD for marketing to Categories (b) or (c) of the definition of “Qualifying Investor”. Accordingly, the capacity to market to Categories (b) and (c) is a matter of Irish regulation and that of any other member state permitting such an offering.
- ❑ Therefore in most cases, where the AIFM wants to market the QIAIF on a cross-border basis within the EEA, it will want to restrict the offering of its shares to “professional clients” only so that the marketing passport can be availed of.
- ❑ Certain Member States do permit the marketing of foreign EU AIFs to non-professional investors, for example, Italy permits the marketing of Irish QIAIFs to retail investors in Italy who meet a minimum initial subscription requirement of 500,000 Euro.
- ❑ Accordingly, it appears that PRIIPs seems in practice to be more of an issue for sales in the domestic Irish market and the Italian market.

Is Your QIAIF Required to Produce a PRIIPS KID?

Top Ups from existing 'Retail' Investors in a QIAIF

- ▣ If an existing investor who is not a “professional client” within the meaning of MiFID subscribes for additional shares after 1 January 2018, it would appear that the obligation to prepare a PRIIPs KID will be triggered by virtue of the offering of the QIAIF to a ‘retail’ investor.
- ▣ Rules relating to additional top-ups are not specifically dealt with in the PRIIPs Regulation itself. However it is reasonable to apply the same rules relating to top-up subscriptions as those applicable to UCITS KIID which are outlined in the ESMA Q&A on UCITS.
- ▣ In this regard, the ESMA Q&A on UCITS confirms that a KIID will be required for any top-up subscription except where shareholders in a UCITS invest via a regular savings plan, in which case a *“KIID is not required in relation to the periodic subscriptions, unless a change is made to the subscription arrangements, for example, increases or decreases in the subscription amount, which would require a new subscription form”*.
- ▣ In its Q&A on AIFMD, the CSSF has confirmed that it is applying the above approach, i.e. that a KID should be provided to an existing retail investor who subscribes for additional shares in the AIF unless it is investing via a regular savings plan.

Is Your QIAIF Required to Produce a PRIIPS KID?

Some other issues to consider:

▣ Data Exchange Model

The PRIIPS Regulation will necessitate data exchange between different stakeholders of a PRIIP.

For example, insurers may need data from fund managers as they will be required to provide PRIIP KIDs for their insurance products that have an investment component managed by an independent asset manager. An appropriate data exchange model should be implemented among stakeholders.

EFAMA has published information exchange templates which provide a description of the set of data which must be provided by the manager to the insurer. It has published two types of template, the first containing the minimum data necessary which a manager would provide free of charge to insurers for them to produce a KID and the second being a more detailed information exchange which may require an agreement to be put in place between the parties.

▣ Review of Distribution Process

The distribution process and relevant agreements governing the distribution process should be reviewed to ensure compliance with the PRIIPs Regulation and clarify the respective obligations (e.g. to provide the KID in good time to investors prior to concluding a contract) and liabilities of the manufacturer and adviser/seller in relation to the PRIIPs KID.

If the QIAIF will only be marketed within the EEA to “professional clients”, it would be prudent to include a clause obliging the distributor to only offer the shares of the QIAIF within the EEA to “professional clients” within the meaning of MiFID.

PRIIPs KID Requirements

Pre-Contractual: To be provided to investors in 'good time'.

PRIIPs KID contents

- ▣ The Delegated Regulations provide for a mandatory template for the PRIIPs KID, covering the texts and layout to be used:
 - PRIIPs KID contents
 - Header
 - What is this product?
 - What are the risks & what could I get in return?
 - What happens if the PRIIP manufacturer is unable to pay out?
 - What are the costs?
 - How long should I hold it and can I take my money out early?
 - How can I complain?
 - Other relevant information
 - Comprehension alert

PRIIPs KID Requirements

Comparison of UCITS KIID & PRIIPs KID

UCITS KIID	PRIIPs KID
Two pages	Three pages
Risk indicator based on market risk	Risk indicator based on market risk and credit risk
No inclusion of transaction costs	Inclusion of transaction costs
Past performance indicator	Forward-looking performance scenarios (no past performance) detailing expected returns for products over one, three and five years during unfavourable, moderate and favourable market conditions and separately for a stress scenario at intermediate periods.

PRIIPs KID Requirements

Updates and Filing Requirements

- ❑ PRIIP manufacturers must review the KID regularly and revise it where the review indicates that changes need to be made.
- ❑ The periodic review should take place at least every 12 months and it should also be reviewed where there is a change that significantly affects or is likely to significantly affect the information contained in it.
- ❑ There is currently no Central Bank guidance in respect of the filing requirements for PRIIP KIDs but we would expect them to be in line with the filing requirements for the UCITS KIID regime (i.e. email filing to a designated Central Bank email address).

Liability & Sanctions

Liability

- ▣ In essence product manufacturers will be held liable where a retail client suffers loss as a result of (1) the KID being inconsistent with binding pre-contractual or contractual documentation, (2) where the KID is misleading or inaccurate or (3) where the KID does not comply with the required form and content requirements as set out in the PRIIPs Regulation.
- ▣ Civil liability of a manufacturer in relation to the KID will remain a matter of national law.
- ▣ The issue of liability could become muddled where there is more than one PRIIPs manufacturer and further whether they are located in different jurisdictions.
- ▣ Consider the categorisation of the PRIIP Manufacturer being dealt with contractually (for example in the relevant management agreement/IMA, as the case may be).

Sanctions

- ▣ Chapter V of the PRIIPS Regulation deals with administrative penalties.
- ▣ Generally, sanctions for breaching the PRIIPS Regulation will remain at national level.
- ▣ No guidance from the Central Bank as yet as to how it will formulate the sanctions regime for the PRIIPs Regulation

Action Required

Manufacturers of QIAIFs need to consider the following:

Is the current offering in the QIAIF open to potential investors in the EU who are not MiFID professional clients?

- ▣ If the answer is yes, you will need to produce a KID and generally comply with the Regulation from 1 January 2018 unless you decide to limit your offering to investors who are MiFID professional clients or unless the QIAIF is only made available to non-EU investors.
- ▣ A practical approach to limiting your offering to investors who are MiFID professional clients is to ensure that your subscription form/application form only provides for investment by such MiFID professional clients, i.e. it does NOT include the additional form of 'qualifying investor' permitted by the Central Bank's AIF Rulebook. You may also wish to consider reflecting this within your offering document.

Does the QIAIF currently have any shareholders/unitholders who are not MiFID professional clients?

- ▣ If the answer is yes, you may wish to consider prohibiting any further investments by such investors if you decide that you want to limit your future offerings to investors who are MiFID professional clients only.
- ▣ Alternatively, and on the basis that existing investors who are not professional clients may continue to subscribe, this would require the production of a PRIIPs KID.



Introduction to MiFID II Product Governance Requirements

21 September 2017

Shane Geraghty

Legislative Provisions

- ▣ Directive 2014/65/EU on markets in financial instruments (“**MiFID II**”)
- ▣ European Communities (Markets in Financial Instruments) Regulations, S.I. 375 of 2017 (“**Irish MiFID II Regulations**”)
- ▣ Commission Delegated Directive (EU) 2017/593 (“**Delegated Directive**”)
- ▣ Commission Delegated Regulation (EU) 2017/565 (“**Delegated Regulation**”)
- ▣ Regulation No. 600/2014 on markets in financial instruments (“**MiFIR**”)
- ▣ ESMA Guidelines on MiFID II product governance requirements (“**ESMA Guidelines**”)
- ▣ ESMA Opinions, Q&As and Regulation Technical Standards
- ▣ MiFID II and all relevant supporting regulations and standards come into force from 3 January, 2018

Product Governance

- ▣ MiFID II product governance rules apply to firms who:
 - (i) manufacture; and/or
 - (ii) distribute financial instruments (as defined); or
 - (iii) who sell or advise on structured deposits.

- ▣ MiFID II Firms

- ▣ Credit institutions when providing MiFID II investment services and activities

- ▣ AIFMs and UCITS Management Companies with licence extensions for portfolio management and potentially non-core services

- ▣ MiFID II product governance rules apply to those financial instruments manufactured before 3 January, 2018 and which are distributed afterwards

Key Concepts

- ▣ A “**Manufacturer**” is a firm that manufactures an investment product, where manufacturing includes the creation, development, issuance or design of that product, including when advising corporate issuers on the launch of a new product
- ▣ A “**Distributor**” refers to a firm that offers, recommends or sells an investment product and service to a client

Manufacturers

- ▣ Manufacturers are required to comply with the requirements in a way that is appropriate and proportionate, taking account the nature of the product, the investment service and the target market
- ▣ Product Approval Process
- ▣ Identify the Potential Target Market
- ▣ Consider Conflicts of Interest
- ▣ Threat to Financial Markets
- ▣ Retention of Board Control
- ▣ Expertise of staff

Manufacturers

- ▣ Review and Monitoring of Compliance Function
- ▣ Assessment of Risks of Poor Outcomes
- ▣ Proposed Charging Structure
- ▣ Provision of information to Distributors
- ▣ Regulator Product Reviews

Distributors

- ▣ Distributors required to comply with product governance requirements in a way that is appropriate and proportionate, taking into account the nature of the product, the investment service and the target market
- ▣ Knowledge and Understanding of Products
- ▣ Governance Obligations with respect to Products
- ▣ Appropriate information from Manufacturers
- ▣ Procedures to comply with relevant MiFID II obligations

Distributors

- ▣ Regular and Periodic Reviews
- ▣ Retention of Board Control
- ▣ Review and monitoring by Compliance Function
- ▣ Working with Collaborators

Target Market Assessment

- ▣ Not necessarily the same for Manufacturers and Distributors
- ▣ ESMA Guidelines set of specific requirements/guidelines for both manufacturers and distributors with respect to target market assessment as well as guidelines which apply to both
- ▣ Process of identifying target market should be based on quantitative and qualitative analysis and considerations

Categories for target market identification (Cumulative)

- ▣ Type type of client to whom the product is targeted (using MiFID II client categorisation)
- ▣ Knowledge and experience that the target market should have about the elements such as relevant product type, features and/or knowledge in thematically related areas
- ▣ Financial situation of the target market with a focus on the ability to bear loss
- ▣ Risk tolerance and compatibility of the risk/reward profile of the product with the target market
- ▣ Client's objections and needs (this may vary from specific to generic)

Target Market Identification – Distributors

- ▣ Distributors must ensure that the intended distribution strategy is consistent with the identified target market
- ▣ Distributors should use same categories as Manufacturers for target market identification but define the target market in a more definitive manner
- ▣ Must obtain adequate and reliable information from Manufacturers
- ▣ Distributors likely to look to UCITS/AIFMs in respect of funds being distributed
- ▣ Extensive obligations on distributors which need to be understood
- ▣ Distributors required to perform due diligence on non-MiFID II Manufacturers

What Next for AIFMs and UCITS Management Companies?

- ▣ Where using third party MiFID Firms for distribution purposes, review the requirements applicable to manufacturers under MiFID II so to ensure that Distributors can receive necessary information in order to comply with MiFID II requirements
- ▣ Review existing arrangements and processes with respect to distribution policies
- ▣ Consider adding the 5 categories used for target market identification into existing target market identification processes required under the Central Bank's Fund Management Company Guidance

Further Reading

- ▣ Dillon Eustace Client Briefing: “MiFID II Product Governance “
- ▣ Irish Funds Q&A: “MiFID II – Implications for the Irish Funds Industry”

Contact

33 Sir John Rogerson's Quay, Dublin 2, Ireland

Telephone +353 1 66 700 22

Fax +353 1 66 700 42

E-Mail: enquiries@dilloneustace.ie

Website: www.dilloneustace.com

Dublin Cayman Islands New York Tokyo