

YOUR CUSTODY PARTNER IN MALTA  
**WE'RE AIFMD READY**



# Sparkasse Bank Malta plc (SBM) fully ready and prepared for AIFM Directive

Recently, one of the main priorities for the EU Commission was to establish a harmonised EU regime for collective investment funds. As a result, the Alternative Investment Fund Managers Directive (AIFMD) was officially approved in November 2010 and has been enforced by all EU member states since 22nd July 2013. The Directive provides an authorisation and supervisory framework for Alternative Investment Fund Managers (AIFM) that administer Alternative Investment Funds (AIF) situated in the European Union - with the notion of being very similar to the UCITS Directive. In this way, both regulatory agencies as well as investors will be in a better position to assess the fund more effectively.

## The Directive regulates:

- EU fund managers that manage Alternative Investment Funds (essentially hedge funds and private equity funds) ("AIFs") (wherever they are based);
- fund managers (wherever they are based) that manage AIFs established in the EU; and
- fund managers (wherever they are based) that market the units or shares of an AIF in the EU.

## In a nutshell, the AIFMD mainly brings to light the following eleven points:

1. **Organisational requirements for AIFM** – Investment Managers need to abide by certain conduct of business requirements.
2. **Clear delegation of the AIFM responsibilities** – the AIFM cannot delegate the tasks of portfolio management and risk management simultaneously.
3. **High level of diligence is required from portfolio managers** – ensuring that the investment decisions are taken in the best interest of investors and complying with the objectives, investment strategy and risk limitations of the AIF.
4. **Ensuring a proper disclosure for conflicts of interest** – with a clear conflicts of interests policy and full disclosure the AIFMD describes and provides clear indications on how to discover any possible conflicts of interest.
5. **Method of calculating Assets under Management (AUM)** – the AIFMD denotes that the AUM calculation should be based on the values of all managed assets, including leverage.
6. **Elevating transparency requirements** – the Directive stipulates the frequency and the content for all documentations which are mandatory for disclosure.
7. **Standardising the methodology for calculating leverage** – leverage should be broken down and expressed as a ratio between the exposure of an AIF's leverage and its net asset value (NAV).
8. **Appointing a depository for cash-flow monitoring and assets safe-keeping.**
9. **Minimum requirements to third countries** – the AIFMD specifies the repercussions when third countries are unable to sign cooperation agreements with EU member states requirements.
10. **Implementing robust risk and liquidity management and practices** – a permanent risk manager is required to be appointed to the AIF or AIFM to report to the competent authorities. The AIFM is also requested to monitor and set liquidity limits, and conduct stress-testing.
11. **Introduction of loss of asset liability** – One of the most significant considerations for the depository will be its potential liability for the loss of financial assets, even in instances where the loss has not arisen through its own negligence.

## The impact on the custodian/depository:

1. **Depository Contract:** otherwise known as the custody agreement, includes a detailed description of the services that the depository is stipulated to provide. This contract explains all the procedures that need to be adopted for each type of asset held in custody and governs the relationship with the AIF. The AIFMD states that this contract should provide an explanation of how the oversight and safe-keeping of assets should be carried out.
2. **Depository Functions:**
  - Safe-keeping – The safe-keeping requirement in terms of the assets held in custody include: an adequate reconciliations process, due care of the financial instruments, as well as assess and implement on-going monitoring procedures in order to combat and minimise the chance of fraud, negligence, and inadequate registration.
  - Cash Flow monitoring – The directive stipulates that the custodian should implement an effective framework for the purpose of cash-flow reconciliations. Additionally, the depository is bound to ensure that consistency exists between their cash positions and those of the AIFM.
  - Oversight – The custodian has an obligation to: oversee the subscriptions/redemptions on the clients account, oversee the valuation of assets, and overlook that the settlements of transactions are done in a timely manner.
3. **Depository Liability:** According to the AIFMD, a depository is liable to return the financial instruments in custody, in situations where the loss is caused by the depository or its sub-custodian operations, such as insolvency of the sub-custodian. However, the depository is not liable for the consequences of external events such as natural disasters, acts of state or governments.

## Here is a short Q&A dealing with FAQ on the Bank's role as a depository under AIFMD:

### Can the Bank offer a standard custody agreement template as required under the AIFMD?

The Bank has adopted a 'one custody agreement per sub-fund' policy. In this manner each custody agreement can be tweaked in accordance to the investment objectives of a specific sub-fund. Sample agreements are available upon request.

### **How does SBM deal with its cash monitoring obligations under AIFMD?**

The essence of this obligation is to minimise cash 'leakages' by reducing or restricting the cash accounts of the fund to the custodian. As a prerequisite, SBM will demand to act as the banker to the fund. This would therefore involve the AIF in opening both its clients'/subscription accounts as well as its trading accounts directly with the Bank as banker and custodian. In this manner the Bank has a holistic oversight and control over ALL cash transactions.

In addition to this set up, SBM thoroughly monitors each and every incoming/outgoing payment from both clients' and trading account for every Sub-fund. The Bank employs effective procedures to ensure that all outgoing payments whether for trading purposes, redemptions or third party fees, abide by the Offering Memorandum and Offering Supplement.

### **Does the Bank perform an oversight function as required under AIFMD?**

SBM does indeed perform this function to the full. The Bank carries out frequent reconciliations over ALL Assets belonging to the fund, the frequency of which is determined by the fund's activity and NAV calculation date.

The Bank performs several reconciliations and oversight checks to enable it to fulfil its oversight function as summarised below:

- Reconciliations of holdings – Strict procedures are in place so that the Bank's positions are reconciled with those booked by the fund's administrator as well as with the Bank's sub-custodians and depositories – this procedure helps eliminate any possible loss of assets or discrepancies in the amount of units or shares held by the fund.
- Reconciliations of pricing – Procedures are also in place to identify any significant discrepancies that may be considered to be inconsistent with the Offering Supplement and Offering Memorandum. On-going monitoring is designed to highlight and identify discrepancies of any nature be it Forex, short deliveries and settlements, pricing, accrued interest, etc.
- Reconciliations of exposures – Reconciliations are also conducted with a view to monitor the exposure limits of the portfolio as set out in the Offering Documents. For this purpose, the Bank checks for breaches or any overexposures the portfolio manager may have exposed the fund to.
- Reconciliations of shareholder register – In order to comply with AIFMD, SBM is expected to reconcile the subscriptions orders with the subscription proceeds, as well as the number of units or shares issued as a result of the subscription proceeds received. The same applies to redemption orders. This is done to check the consistency between the total number of units or shares in the AIF's accounts and the total number of units or shares in the AIF's shareholder register.
- NAV verifications – the Bank carries out a verification of NAV calculation periodically
- Look through functions and other regulatory and compliance issues – the Bank promotes and embraces good governance and prudential management – and applies this in all it does for and on behalf of the AIF – the Bank will therefore apply further controls and implement checks and balances to make sure that this spirit is being reflected in full throughout the AIF and within the AIFM's internal operations.

### **How does the Bank deal with assets that cannot be held in custody in its traditional sense, and is the Bank capable of presenting a consolidated statement of holdings?**

From inception, the Bank recognised the importance of being able to deliver an all encompassing statement of holdings to the fund's service providers. A statement designed to capture all

assets, including assets for which the custodian is performing a verification of ownership and record keeping function.

The Bank's statements therefore capture positions held with prime brokers, shares in SPVs or any other assets as well as bank accounts held with other banks. These are recorded to the AIF's account, brought forward, reported and reconciled seamlessly in one statement.

### **What action is SBM taking in terms of the AIFMD's reporting obligations for accounts held with prime brokers?**

The Bank can offer two main entry points to prime brokers.

The first route is that of the Bank appointing the prime broker as its sub-custodian. The second is via a tri-party pledge agreement between fund, custodian and prime broker. (Further details upon request)

### **What are the safekeeping duties undertaken by SBM with regards to assets held in custody and how is the Bank protecting against loss of assets?**

The Bank's custody infrastructure is large, robust and far reaching. To mitigate risk and possible loss of assets, the Bank encourages AIFs to operate exclusively within this footprint. Custody accounts are held as clients' accounts and well segregated from the Bank's assets in accordance with the Control of Assets Regulations.

SBM ensures that records and segregated accounts are continuously reconciled efficiently as to guarantee high level of accuracy of the AIF's holdings. Furthermore, on-going due diligence and stress testing on the robustness of the infrastructure is carried out frequently including on-site visit as and when necessary.

### **Can SBM automate end of day reports in various formats?**

The Bank is able to send various reports once the End of Day procedures are completed via email. These may also be sent in various formats. All official advices will be sent in pdf format while the statement of holdings may be sent in pdf format as well as excel format, csv and may be delivered via FTP. A client may either receive advices via email to multiple authorised recipients or traditional post.

### **About Sparkasse Bank Malta plc**

Sparkasse Bank Malta plc is licensed and regulated in Malta by the Malta Financial Services Authority (MFSA) to provide Banking, Investment and Custody services. The MFSA is the single regulator for financial services in Malta - regulating Private Pensions, Trustee Services, Investment Business, Insurance Business and Banking.

Established in 2002 the MFSA has taken over the supervisory functions previously carried out by the Central Bank of Malta, the Malta Stock Exchange and the Malta Financial Services Centre. The Authority is a fully autonomous public institution and reports to Parliament on an annual basis

### **Contact:**

paul.mifsud@sparkasse-bank-malta.com  
anna.mironova@sparkasse-bank-malta.com



Sparkasse Bank Malta plc  
101 Townsquare,  
Ix-Xatt Ta' Qui-Si-Sana,  
Sliema, SLM 3112 – Malta

Tel: +356 2133 5705  
Fax: +356 2133 5710  
[info@sparkasse-bank-malta.com](mailto:info@sparkasse-bank-malta.com)  
[www.sparkasse-bank-malta.com](http://www.sparkasse-bank-malta.com)