

AIFMD: Spotlight on depositaries

Requirement to appoint depositaries generating debate, questions among AIFMs



What is the AIFMD?

In the aftermath of the global financial crisis, the European Commission drafted one of the most ambitious and complex regulatory reform agendas ever introduced into the asset management industry in the form of the Alternative Investment Fund Managers Directive (AIFMD). The Directive will have profound, wide-reaching and long-term implications for in-scope alternative investment fund managers (AIFMs), who are required to comply by 22 July 2013.

The appointment of a depositary for each alternative investment fund (AIF) is one of the most important strategic decisions AIFMs are being asked to make under the new regulatory regime. It is also the subject of significant discussion and debate among managers looking to prepare for the impending Directive.

AIFMs required to appoint depositaries

Under the AIFMD rules, AIFMs will be required to appoint a depositary – an independent third-party provider responsible for safekeeping of assets – for each AIF. The AIFM itself is not permitted to act in the capacity as a depositary for

its own funds. While some managers have publicly voiced their displeasure with this new requirement, suggesting it represents an added expense with questionable benefit to investors. The motivation for the depositary rule centers around the need for increased transparency and accountability in the wake of the financial crisis, the Madoff scandal and other similar events.

Primary functions

According to the AIFMD, the depositary has three primary functions when appointed by an AIF:

- 1. Cash flow monitoring:** The depositary is responsible for properly monitoring the AIF's cash flows and ensuring payments from investors and all AIF cash are booked in cash accounts opened in the name of the AIF, the AIFM or the depositary on the AIF's behalf.
- 2. Safekeeping and recordkeeping:** The depositary is required to ensure that the assets are held in segregated accounts to clearly identify all assets belonging to the AIF at all times.

3. Oversight of certain operational functions:

The depositary is also required to perform a range of oversight functions to help ensure the AIF acts in accordance with applicable national law and AIF rules.

Exceptions to the depositary requirement

AIFMs managing non-EU AIFs that are not marketed in the EU are not subject to the depositary requirements spelled out in the Directive.

Similarly, non-EU AIFMs managing non-EU AIFs marketed to professional investors in the EU via the national private placement regimes will not be required to comply with the full depositary provisions. However, these AIFMs will need to ensure that one or more entities are appointed to perform the cash monitoring, safekeeping and oversight duties, which cannot be performed by the AIFM itself.

A sense of urgency

In a 2012 survey of AIFMs titled "Last Boarding Call," 63 percent of AIFMs said they had yet to appoint a depositary. While this number is likely to have changed over

the past several months, it is important for AIFMs to realize that they will be required to have a depositary in place *before* they can have an authorization under the Directive. As such, clients that have not already done so to expedite the process of identifying and securing the services of a depositary for its funds.

Given the last minute 'rush to the gates' with AIFMs moving to secure the services of depositaries for their funds, some may be disappointed with the lack of choice of providers. The list of depositaries that are ready, willing and able to deliver these services and to satisfy the stringent liability requirements is not a long one. And as the compliance deadline approaches, some depositaries may actually stop accepting new clients to help mitigate their overall risk as they transition into this new regulatory regime.

Implications for depositaries

To date, much of the focus around the lead-up to the AIFMD has focused on the impacts to AIFMs. However, the new requirements will also have wide-reaching implications for the depositaries themselves, in terms of added costs and changes to their service offerings to name a few. The Directive also requires depositaries to essentially extend their responsibility over the funds they are servicing, making them liable for any losses experienced by the fund(s), one of the more contentious elements of the new rules. Even in cases where the depositary may not have a specific contract with an AIFM, to the extent that they are operating in a jurisdiction that has transposed the AIFMD, those depositaries will be considered to be operating in a strict liability regime.

The extent to which the individual depositaries will be impacted by the new rules will depend upon the jurisdiction in which they are operating, along with the state of existing regulation in those markets.

In instances in which there is a significant gap between the existing regime and the new requirements under AIFMD, those depositaries will need to enhance or modify their services offerings accordingly.

How KPMG can help ?

KPMG professionals have extensive knowledge helping some of the world's largest and most prominent AIFMs, fund administrators, depositaries and other service providers prepare for complex regulatory regime change. They help clients understand their specific requirements under the new rules and can provide expert guidance, advice and implementation support in the areas of gap analysis, implementation planning, data protection and migration, report design and much more. KPMG firms also have the capabilities and knowledge to provide ongoing assurance services once clients' systems and infrastructure are up and running.

KPMG's dedicated global team of AIFMD professionals has the credentials, the knowledge and the track record that comes from helping our clients identify and implement their requirements under the AIFMD and position themselves to achieve not only compliance, but long-term profitability under these new rules.

Common AIFMD-related acronyms

AIF	Alternative Investment Fund
AIFM	Alternative Investment Fund Manager
AIFMD	Alternative Investment Fund Managers Directive
ESMA	European Securities and Markets Authority
EU	European Union
FATF	Financial Action Task Force
MiFID	Markets in Financial Instruments Directive
MS	Member State of the European Union
MSR	Member State of Reference for a non-EU AIFM
UCITS	Undertakings for Collective Investment in Transferable Securities

For more information, please contact:

Stephanie Haot

Partner

KPMG in Luxembourg

T: +352 22 51 51 -7270

E: stephanie.haot@kpmg.lu

Anne-Sophie Minaldo

Director

KPMG in Luxembourg

T: +352 22 51 51 -7909

E: anne-sophie.minaldo@kpmg.lu

kpmg.com/socialmedia



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