

Funds Quarterly Legal and Regulatory Update

Period covered:
1 October, 2010 to 31 December, 2010

DILLON  EUSTACE

DUBLIN CORK BOSTON NEW YORK TOKYO



Contents

Funds Quarterly Legal and Regulatory Update

Criminal Justice (Money Laundering and Terrorist Financing) Act 2010

Page 3

UCITS, Non-UCITS & Hedge Funds

Page 3

UCITS IV

Page 16

MiFID 2

Page 20

ISE adopts New Rules on Corporate Governance

Page 21

Dodd Frank Wall Street Reform & Consumer Protection Act

Page 21

The Central Bank of Ireland

Page 22

FUNDS QUARTERLY LEGAL AND REGULATORY UPDATE

▣ Criminal Justice (Money Laundering and Terrorist Financing) Act 2010

The Third Anti-Money Laundering Directive was transposed into Irish law on 5 May, 2010 by the Criminal Justice (Money Laundering and Terrorist Financing) Act, 2010 (the “CJA Act 2010”) and has been effective as of 15 July, 2010.

The Central Bank of Ireland (the “Central Bank”) is continuing to meet with the various industry representative bodies to review the draft Core Guidance Notes. The topic of reliance on third parties particularly third parties from countries with secrecy laws remains a key issue to be resolved between the Central Bank and the various industry groups. It is now anticipated that the Core Guidance Notes will be finalised in February, 2011. Any changes made in the Core Guidance Notes will then be reflected in the Sectoral Guidance Notes and the Central Bank will engage with the various industry representative bodies to finalise same.

If you would like further information on anti-money laundering requirements Dillon Eustace regularly advises on all aspects thereof and provides training sessions on this topic. Training can be held either at Dillon Eustace’s office at 33 Sir John Rogerson’s Quay, Dublin 2 or in house training can be provided at a venue of your choosing.

▣ UCITS, Non-UCITS & Hedge Funds

(a) EC’s Draft Directive on Alternative Investment Fund Managers

At its meeting held in Luxembourg on 19 October, 2010, the ECOFIN reached agreement on the draft Alternative Investment Funds Managers Directive (“AIFMD”). On 11 November, a successful plenary vote by the European Parliament has led to the adoption of the AIFMD. Further details on the implementation of the AIFMD will be decided in 2011. The AIFMD is due to be implemented across the EU in 2013.

In November, 2010 the IFIA published an “Industry Information Note” outlining some of the main issues that apply to the fund industry in Ireland.

As previously set out, the draft AIFMD on AIFM covers Non-UCITS funds including hedge funds, private equity and commodity funds and aims to create a harmonised regulatory and supervisory framework for AIFM within Europe.

The AIFMD will require all applicable AIFM to be authorised and subject to harmonised regulatory standards on an ongoing basis. It will also increase the reporting and transparency of AIFM and the funds they manage for investors and public authorities. The aim is to improve Member States macro prudential oversight of the funds sector and take harmonised action where appropriate with regard to the proper functioning of financial markets.

It is proposed that the AIFMD will:

- ▣ Adopt an 'all encompassing' approach to ensure that no significant AIFM is outside of regulation and oversight, while providing exemptions for much smaller managers. It will only apply to AIFM managing a portfolio of €100 million plus. A higher threshold of €500 million applies to AIFM not using leverage (and having a five year lock-in period for their investors) as they are not regarded by the EC as posing systemic risks. According to analysis by the EC, a threshold of €100 million implies that about 30% of hedge fund managers, managing almost 90% of assets of EU domiciled hedge funds, would be covered by the proposed Directive;
- ▣ Aim to regulate major sources of risks in the alternative investment value chain by ensuring that AIFM are authorised and subject to ongoing regulation and that key service providers, including depositaries and administrators, are subject to robust regulatory standards, as is currently the situation in Ireland;
- ▣ Increase the transparency of AIFM and the funds they manage for supervisors, investors and other key stakeholders;
- ▣ Ensure that all regulated entities are subject to governance standards and have robust systems in place for the management of risks, liquidity and conflicts of interest;
- ▣ Permit AIFM to market funds to professional investors throughout the EU subject to compliance with regulatory standards; and
- ▣ Grant access to the European market to third country funds after a transitional period of three years. The EC have said this is to allow the EU to check whether the necessary guarantees are in place in the countries where the funds are domiciled

(with respect to among others equivalence of regulatory and supervisory standards and exchange of information on tax matters).

The Directive is subject to a co-decision process which includes the ECON Committee of the European Parliament and the Council of Ministers Working Group. The ECON Committee of the European Parliament appointed a Rapporteur (MEP Jean-Paul Gauzes) who is responsible for guiding the Directive through Parliament.

In October, 2009 the IFIA reported that the European Fund and Asset Management Association (“EFAMA”) AIFM Working Group on which the industry participates reached broad agreement on the issues they had been considering:

- ▣ Agreement on a level playing field, but as of yet without clarity on impacts for closed ended, listed funds passported under the prospectus directive or securitization vehicles (discretionary managed fund versus company issues);
- ▣ Definition of management services aligned to UCITS Annex II;
- ▣ Capital requirements aligned with UCITS with a similar cap;
- ▣ Valuation to be a function as per UCITS model;
- ▣ Depository rules to follow current UCITS requirements and for there not to be full liability;
- ▣ Delegation requirements to be more flexible as current UCITS requirements, allow for delegation of portfolio / investment management to third country non AIFM entities;
- ▣ To make the leverage requirements much more flexible; and
- ▣ Third country funds, to allow private placement and reverse solicitation according to national rules to continue, but not have provision for an EU passport.

MEPs of the European Parliament's ECON had voted in favour of the Parliamentary version of the EU's AIFM and European finance ministers have agreed to give the Presidency the mandate to negotiate on behalf of the Council with Parliament.

The three-way (“trilogue”) discussions between representatives of the European Parliament's ECON (Economic and Monetary Affairs) Committee, the Presidency of the Council of the European Union and the European Commission have now begun.

On the negotiating table are the two differing versions of the draft Directive, approved in May by ECON and the Economic and Financial Affairs (“ECOFIN”) Council, part of the Council of the European Union. The ECON team is understood to include the chairwoman of ECON, Sharon Bowles, the rapporteur, Jean-Paul Gauzès, and the six shadow rapporteurs taken from the main political blocs in the European Parliament. The Council is represented by the

Belgian government as the President of the Council of the EU. The Commission officials present at the discussions are there to assist the parties agreeing on a compromise text. But they will naturally favour any wording which backs up their original version of the draft Directive, published in April, 2009.

Where there is already broad agreement between the texts, such as on registration and authorisation of EU managers, those areas will be incorporated immediately into the new compromise text, drafted by the EC. This will leave the negotiating teams free to discuss solutions to areas where there is disagreement – including the issue of third countries. The other controversial areas include: valuation; depositaries; scope; leverage; remuneration; delegation; capital requirements; and short selling.

In order to reconcile the different approaches taken, the groups may agree to adopt either the ECON or Council position on a particular issue. Alternatively, they may agree to adopt a compromise position that combines elements of both texts.

The aim will be for all the issues to be resolved, and majority backing effectively secured, before the compromise text is finally voted on. In preparation for this vote and in an ongoing attempt to reach agreement the Belgian Presidency has released several compromise texts.

The latest texts do not include any detail on either requirements for marketing or private placement of 3rd country funds/managers or on requirements relating to Private Equity. The treatment of 3rd country funds is the most significant unresolved issue in the ongoing negotiations with there still being divergent views between countries within the European Council.

It is understood that the primary differences relate to the provisions to allow private placement to continue, possibly for a limited period, subject to certain conditions and the possibility of a European marketing passport, under certain conditions, for 3rd country funds.

Once the text has been approved by Parliament, it will pass to the next meeting of ECOFIN, which would be expected to adopt it.

In the unlikely event of a simple majority of MEPs voting against the eventual text, there would follow a second reading, a process limited to three months, during which a further compromise version of the Directive would need to be drafted and agreed upon. However, all parties to the trilogues have stated a preference for a First Reading passage.

Once Parliament and Council have voted in favour of the Directive, it will pass to the next stage, which is its implementation into national law. This process is expected to last until 2012, when the Directive would come into force.

For detailed information on the Directive including how it may impact your business, please contact Donnacha O'Connor in Dillon Eustace.

(b) New European Systemic Risk Board

A new European Systemic Risk Board ("ESRB") was established on Thursday 16 December, 2010.

It is aimed at contributing to the prevention or reduction of systemic risks to financial stability in the EU that arise from developments within the financial system.

The European Central Bank has commented that the ESRB will also contribute to the smooth functioning of the internal market and is aimed to ensure a sustainable contribution of the financial sector to economic growth.

However, the European Commission has stated that the ESRB will not have any binding powers to impose measures on Member States or national authorities. It has been conceived as a "reputational" body with a high level composition that should influence the actions of policy makers and supervisors by means of its moral authority.

The seat of the ESRB will be in Frankfurt, Germany. The Chair of the ESRB is the President of the European Central Bank, Jean-Claude Trichet, while Mervyn King, Governor of the Bank of England, was elected as first Vice-Chair of the ESRB by the members of the General Council of the European Central Bank.

The General Board of the ESRB will have its inaugural meeting on 20 January, 2011.

(c) CESR's Definition of European Money Market

CESR has published its guidelines on a common definition of European money market funds. The guidelines aim to improve investor protection by setting out criteria to be applied by any fund that wishes to market itself as a money market fund. The criteria reflect the fact that investors in money market funds expect the capital value of their investment to be maintained while retaining the ability to withdraw their capital on a daily basis. A common definition will also help provide a more detailed understanding of the distinction between

funds which operate in a very restricted fashion and those which follow a more 'enhanced' approach.

CESR's guidelines set out two categories of money market fund: Short-Term Money Market Funds and Money Market Funds. This approach recognises the distinction between short-term money market funds, which operate a very short weighted average maturity and weighted average life; and money market funds which operate with a longer weighted average maturity and weighted average life. For both categories of fund, CESR expects that there should be specific disclosure to explain clearly the implications of investing in the type of money market fund involved. For Money Market Funds, for example, this means taking account of the longer weighted average maturity and weighted average life of such funds. For both types of money market fund, this should reflect any investment in new asset classes, financial instruments or investment strategies with unusual risk and reward profiles.

The guidelines will enter into force in line with the transposition deadline for the revised UCITS Directive (1 July, 2011). However, money market funds that existed before that date will be granted an additional six months to comply with the guidelines as a whole.

(d) EC's Proposal for Regulating Short Selling

Following CESR's consultation paper on short selling in June, 2010 the EC has now published its draft proposal for regulating short selling and certain aspects of credit default swaps.

The Alternative Investment Management Association ("AIMA") has set out the key points to note from the EC's proposal and they include:

- ▣ scope –covers:
 - ▣ financial instruments admitted to trading on an EU regulated market or MTF (even when such instruments are traded outside that trading venue);
 - ▣ derivatives which relate to such a financial instrument or an issuer of such a financial instrument (even when such derivatives are traded outside a trading venue);
 - ▣ debt instruments issued by a Member State or the European Union and derivatives relating to such debt instruments or an obligation of a Member State or the Union;

- ▣ a disclosure regime is proposed in respect of significant net short positions whereby:

- ▣ **for shares** - private disclosure to the regulator at 0.2% and further increments of 0.1% of issued share capital; public disclosure at 0.5% with 0.1% increments;
- ▣ **for sovereign debt and CDS** – private disclosure only, thresholds to be determined;

- ▣ short sell orders are to be marked as such and weekly or more regular summaries of the volume of short selling are to be made available;
- ▣ buy-in procedures for settlement failures at T+4 are to be required and fines would apply to those who fail to deliver on the due date;
- ▣ an exemption would be available to market makers when acting in this capacity;
- ▣ restrictions will be imposed in respect of uncovered short sales, requiring the seller to have already borrowed or entered into an agreement to borrow the shares or debt instrument, or to have arranged with a third party that the share or debt instrument has been located and reserved for lending – the details of these provisions remain to be worked out;
- ▣ emergency powers are to be given to competent authorities in respect of imposing bans, restrictions or temporary suspension of short sales, with similar powers (along with a facilitation and coordination role) being provided to ESMA.

It is expected that a new Regulation will be implemented across Europe and this will apply from 1 July, 2012.

(e) Introduction of New QIF Criteria & Competitive Issues

The IFIA recently met with the Central Bank to discuss the introduction of new QIF criteria and competitive issues. Below is a summary of items the Central Bank has agreed to amend / consider amending through revised draft notices / guidance notes.

Regulated markets:

It was proposed that the Central Bank should remove the requirement that the articles of association of an investment company list the regulated markets on which the transferable securities and money market instruments acquired by the investment company must be listed or traded and allow this information to be included in the prospectus instead.

Qualifying investor criteria:

It was requested that the Central Bank revise the criteria for QIF investors to take into account MiFID “professional clients”, the proposals under the AIFMD and the investor requirements for the equivalent structure in Luxembourg.

The Central Bank has agreed to reduce the minimum subscription to €100,000 and have agreed to change the qualifying investor criteria to include professional investors.

Frequency of calculation of net asset value:

It was proposed that the Central Bank review its requirement for the NAV to be calculated on a twice yearly basis (it is acknowledged that a NAV would still have to be calculated in respect of any day on which securities are to be issued or redeemed by the QIF).

The Central Bank agreed to a minimum of one valuation per year for QIFs subject to dealing frequency.

(f) Reduction in Minimum Subscription for Professional Investor Funds

As outlined above, the Central Bank has reduced the minimum subscription amount for a QIF from €250,000 to €100,000. This meant that while the minimum subscription amount for a QIF was €100,000, the minimum subscription amount for a Professional Investor Fund (PIF) was €125,000. The Central Bank recently confirmed that the minimum subscription amount for a PIF will be reduced from €125,000 to €100,000 and amendments to NU12 of the NU Series of Notices to reflect this change will be made in due course.

(g) Re-domiciliation of Collective Investment Schemes to Ireland

The Companies (Miscellaneous Provisions) Act 2009 amended the Companies Act 1990 and the European Communities (Undertakings for Collective Investments in Transferable Securities) Regulations 2003, to provide an efficient legislative mechanism for corporate investment funds to re-domicile into Ireland. The Companies Act 1990 (Relevant Jurisdictions under Section 256F) Regulations 2010, identified the following as relevant jurisdictions from which corporate CIS could re-domicile into Ireland: Bermuda, BVI, Cayman Islands, Guernsey, Isle of Man and Jersey.

Since the introduction of this legislation a number of funds have re-domiciled and more are in the process of re-domiciling. While the legislation provided an efficient legal mechanism

for funds to re-domicile to Ireland, the Central Bank has now provided further guidance regarding the regulatory process and procedure for re-domiciling funds into Ireland e.g. the documentation that must be submitted to the Central Bank, confirmations required, etc. In addition, although there are no legislative provisions which specifically address the re-domiciliation of unit trusts to Ireland, the Central Bank has determined that a re-domiciliation process similar to that in place for corporate CIS should apply in respect of unit trusts.

Please contact a member of the Regulatory and Compliance Department in Dillon Eustace should you need further information on the regulatory process and procedure for re-domiciling investment funds into Ireland.

(h) Amended Guidance Notes

The following guidance notes were updated to reflect recent discussions between the Central Bank and the IFIA:

Guidance Note 1/96

Notices UCITS 9 and NU 13 require that the stock exchanges and markets on which a UCITS or non-UCITS may invest must be set out in the trust deed, deed of constitution or in an investment company's articles of association. Guidance Note 1/96 provides that this requirement will now be met if a reference to the relevant section of the fund's prospectus is contained in such documents. Please note that the Central Bank will not be updating the notices to reflect this change.

Guidance note 2/96: Promoters of Collective Investment Schemes

The requirement to maintain shareholder funds shall now only apply as long as a promoter acts as promoter to Irish collective investment schemes.

Guidance note 2/99: Money Market Funds: European Central Bank Reporting Requirements

There were some minor amendments to Guidance Note 2/99 relating to the European Central Bank reporting requirements. These changes do not alter the reporting requirements for ECB money market funds rather update the references to ECB legislation.

Guidance Note 1/00: Valuation of Assets of Collective Investment Schemes

The minimum dealing frequency for UCITS is now twice per month. Such dealing day should be at regulator intervals to ensure that dealing days occur on a regular and frequent basis.

Guidance Note 1/07: Authorisation of Qualifying Investor Schemes – Application process

Notifications to the Central Bank of extensions to initial offer periods can now be made on an annual basis.

Please contact Andrew Bates or Brian Kelliher of Dillon Eustace should you wish to discuss the proposed revisions in more detail.

(i) Standardisation and Exchange Trading of OTC Derivatives / Transaction Reporting

In a consultation paper issued in July, CESR explored the need for taking regulatory actions in relation to further standardisation for credit, equity, interest rate, commodity and foreign exchange derivatives to ensure efficient and safe derivatives markets in response to the financial market turmoil.

Following this consultation, the European Commission tabled a proposal on 15 September, with a view of bringing greater transparency, safety and efficiency to the OTC derivatives market.

The proposed directive on regulating the OTC, central counterparty and trade repository markets requires that information on OTC derivative contracts should be reported to trade repositories and be accessible to supervisory authorities, with additional information also being made available to market participants to increase transparency in the markets. It is proposed that the new ESMA will be responsible for the surveillance of trade repositories and for granting their registration. These trade repositories will have to publish aggregate positions by class of derivatives to give all market participants a clearer view of the OTC derivatives market.

The Commission also proposes that standard OTC derivative contracts be cleared through central counterparties (“CCPs”), to reduce counterparty credit risk, i.e. the risk that one party to the contract defaults. CCPs may interpose themselves between two counterparties to a transaction and thus become the ‘buyer to every seller’, as well as the ‘seller to every buyer’.

This will prevent the situation where a collapse of one market participant causes the collapse of other market participants, thereby putting the entire financial system at risk.

(j) Corporate Governance Code for Irish Domiciled CIS

In late September, the IFIA published the voluntary Corporate Governance Code for Irish Domiciled Collective Investment Schemes (the “Code”).

The Code may be adopted by Irish domiciled collective investment schemes on a voluntary basis but the Code does reflect existing practices imposed under the Companies Acts 1963 to 2009 and the Central Bank’s UCITS & Non-UCITS Notices along with Guidance Notes.

Adoption of the Code should enable Irish domiciled collective investment schemes with shares admitted to trading on a regulated market to refer to this Code in a specific section in the Directors’ Report of that collective investment scheme’s Annual Report and in doing so comply with the provisions of the S.I. No. 450 of 2009.

The Code covers general requirements applicable to a board of directors including its composition, meetings, its role and committees. It further deals with the audit, compliance and risk management function.

Please contact your usual contact in Dillon Eustace for further details on the Code or if you would like a copy thereof.

(k) National Recovery Plan

The Government’s four year ‘National Recovery Plan’ has highlighted the importance of the Irish funds industry to the country’s wider economy. The plan, which includes a guarantee that the corporation tax rate will remain at 12.5%, indicates that Ireland will maintain its strong support for the funds industry which it views as key to promoting Ireland’s financial recovery.

The Central Bank has reported that the value of Irish domiciled investment funds had reached almost €899 billion for the first time as at the end of August. This figure represents a 20 per cent increase in the value of Irish domiciled investment funds since the beginning of 2010 (27 per cent year on year) and is a new high for the total value of Irish domiciled funds.

It has confirmed that assets under administration now exceeds €1.8 trillion.

Dillon Eustace have prepared a brochure on the AIFMD's Third Country Provisions which is available on our website: www.dilloneustace.ie

(l) Credit Rating Agencies

Article 4(1) of Regulation (EC) No 1060/2009 on credit rating agencies came into force on 7 December, 2010. The second paragraph of Article 4(1) contains the following requirement which applies to any credit rating mentioned in a prospectus:

“Where a prospectus published under Directive 2003/71/EC and Regulation (EC) No 809/2004 contains a reference to a credit rating or credit ratings, the issuer, offeror, or person asking for admission to trading on a regulated market shall ensure that the prospectus also includes clear and prominent information stating whether or not such credit ratings are issued by a credit rating agency established in the Community and registered under this Regulation.”

As such, all documents seeking approval under the Prospectus Directive must state whether or not a credit rating agency is registered in the Community and registered under Regulation (EC) No 1060/2009.

(m) CESR Consultation on Structured UCITS

With a view to the implementation of UCITS IV In July 2011, CESR has issued Final Guidelines on the risk measurement, calculation of global exposure and counterparty risk for UCITS.

The Final Guidelines deal with a range of issues including calculations for the commitment approach, procedures in respect of VaR calculations, stress testing, back testing and regulatory reporting. They also provide guidelines on hedging, collateral and netting.

“CESR has provided a definition of structured UCITS (which is different from the definition for key investor information (KII) requirements). In summary, structured UCITS are passively managed and offer investors a predefined payoff depending on different scenarios based on the value of the underlying assets. The investor can only be exposed to one scenario at any time during the life of the UCITS.

CESR has come to the conclusion that, rather than introducing a specific regime per se for the calculation of the global exposure for these structured UCITS, it would be more appropriate to have an alternative approach to the application of the existing guidelines.

The specific approach as proposed by CESR consists of the calculation, for each scenario to which investors can be exposed at any one time, of the global exposure using the commitment approach. Under this approach, each scenario must comply at all times with the 100% global exposure limit using the existing CESR Guidelines. CESR have set out a very useful set of examples in this regard.

There is a risk that some existing structured UCITS will not comply with these proposals and also that it may limit the types of products that can be made available. Note for example the CESR comment that “UCITS which use derivatives that incorporate a barrier-type feature are required to ensure that the maximum loss the UCITS can suffer when the payoff switches from one scenario to another is limited.”

In this regard, CESR’s proposal is that existing structured UCITS will not need, as regards global exposure, to comply with CESR’s July Guidelines on Risk measurement, Calculation of Global exposure and counterparty risk, but that in this case, such structured UCITS will no longer be able to actively market their UCITS. However, this is provided that such UCITS comply with whatever provisions have been put in place by Member States.”

(n) Amendments to the Prospectus Directive and Transparency Directive

Directive 2010/73/EU which will amend certain provisions of the Prospectus Directive and the Transparency Directive became effective on 31 December, 2010. Ireland has until July 1, 2012, to implement the relevant directive into domestic law.

Of particular note is the replacement of Article 8(1)(b) of the Transparency Directive and the additional paragraph (4) of the same article. Article 8 is amended as follows:

- ▣ in paragraph 1, point (b) is replaced by the following:
 - ‘(b) an issuer exclusively of debt securities admitted to trading on a regulated market, the denomination per unit of which is at least EUR 100 000 or, in the case of debt securities denominated in a currency other than euro, the value of such denomination per unit is, at the date of the issue, equivalent to at least EUR 100 000.’;
- ▣ the following paragraph (4) is added to Article 8:

'By way of derogation from paragraph (1)(b), Articles 4, 5 and 6 shall not apply to issuers of exclusively debt securities the denomination per unit of which is at least EUR 50 000 or, in the case of debt securities denominated in a currency other than euro, the value of such denomination per unit is, at the date of the issue, equivalent to at least EUR 50 000, which have already been admitted to trading on a regulated market in the Union before 31 December 2010, for as long as such debt securities are outstanding.'

These amendments will result in an increase in the minimum denomination to at least €100,000 for Issuers wishing to avail of the exemptions set out in Article 8 and also to state that in order to rely on the grandfathering provisions for securities issued with a minimum denomination of at least €50,000, they must have been issued before 31 December 2010.

The exemptions from the periodic financial reporting requirements of the Transparency Directive for "wholesale" issuers will only continue to apply if they exclusively issue securities with a minimum denomination of €100,000.

(o) Consultation on legislative changes to the UCITS depository function and to UCITS managers' remuneration

The European Commission intends to publish a new legislative proposal in order to review the current framework applicable to UCITS depositories and to introduce new provisions on UCITS' managers' remuneration with a view to improving the level of UCITS investor protection and has issued a consultation document in that regard. The consultation document and relevant information can be found on the European Commission's website at the following link:

http://ec.europa.eu/internal_market/consultations

The Consultation is open until 31 January 2011.

UCITS IV

The European Council voted on 22 June, 2009 for the adoption of the UCITS IV Directive (the "Directive"), as already adopted by the European Parliament in plenary session on 13 January, 2009. The Directive has now been finally adopted in accordance with the co-decision procedure, thus marking the end of the first step for the implementation of a European text.

The UCITS IV proposal containing amendments to the UCITS Directive 85/611/EC was first proposed by the EC on 16 July, 2008. This proposal did not take into account the management company passport which, after having been debated at CESR level, was reintroduced in December 2008.

According to the Lamfalussy process, there remains three levels before the transposition of the Directive shall be considered as fully completed among Member States. Similar to MiFID, the Directive provides that the details of certain provisions should be covered by Level 2 implementing measures to be adopted by the EC with a view to harmonising the implementation of the text. On 13 February, 2009 the EC submitted to CESR a provisional request for technical advices on the new UCITS Directive implementing measures.

The consultation paper that CESR published on 8 July, 2009 provides technical advice on the level 2 measures related to the UCITS management company passport. CESR's draft advice covers the organisational requirements that companies managing UCITS need to fulfil, and conflicts of interest those companies must avoid. The advice also includes details on the companies' rules of conduct, depositaries and risk management, as well as on supervisory cooperation. The majority of the suggestions made in the CESR Advices were carried through into the Commission Directive 2010/43/EU of 1 July 2010 implementing the UCITS IV Directive as regards organizational requirements, conflicts of interest, conduct of business, risk management and content of the agreement between a depositary and a management company.

The final two steps of the Lamfalussy process will take place during and after the period of transposition of the Directive. Under level 3, CESR will be in charge of issuing interpretation recommendations to national authorities and under level 4 the EC will control and advise Member States as to a proper interpretation and application of the Directive. Member States will have until 1 July, 2011 to implement the text into national legislation.

The following is a summary of the key implications of the UCITS IV Directive:

Management Company Passport

The concept of a management company passport ("MCP") was first introduced in Directive 2001/107/EC (the "Man Co Directive"). The Man Co Directive introduced an authorisation framework for Man Cos which is similar to that applied to investment firms under MiFID imposing requirements relating to minimum capital, internal management control

mechanisms, probity and experience of the directors and management and conduct of business rules.

These measures were intended to harmonise the authorisation process of Man Cos in all EU Member States which in theory would enable the MCP provided for in the Man Co Directive (as explained below) to operate effectively whereby a Man Co established in one Member State could be appointed as Man Co of UCITS schemes domiciled in other Member States.

However, despite the new authorisation process and the provision of a MCP contained in the Man Co Directive, the MCP has not worked under the existing legal framework. This failure was attributed to the fact that the definition of “UCITS Home Member State” in the Man Co Directive meant that it was not possible for a Man Co to passport its services in the context of UCITS funds established as unit trusts.

The Directive enables European funds created under the UCITS regime to be managed by a management company authorised and supervised in a Member State other than the home Member State of the Fund.

Fund Mergers

The Directive establishes a unified regime for both cross-border and domestic mergers of Funds. Pursuant to the Directive, all Funds are entitled to merge regardless of their structure (corporate, unit trust, or contractual type of funds).

Master Feeder Structure

The Directive sets out the first European regulation concerning the setting-up of master feeder funds. A feeder fund is defined in the Directive as a UCITS or a sub-fund thereof which has been approved to invest at least 85% of its assets in units of another fund. It can also set aside 15% of its assets to invest in derivative instruments or liquid assets etc. As far as the master fund is concerned, it cannot itself be a feeder fund, nor hold units of a feeder fund.

Key Investor Information

The key investor information (“KII”) shall replace the simplified prospectus which failed to provide investors with all basic information to enable them to make an informed investment choice. It is intended to be a short pre-contractual document written in a brief manner and in

a non-technical language which shall provide easily understandable, fair, clear and not misleading information on the fund to contemplated or actual investors.

The European Commission has now published a Regulation 583/2010 implementing the UCITS IV Directive as regards the key investor information and conditions to be met when providing key investor information or the prospectus in a durable medium other than paper or by means of the website (the “Commission Regulation”).

On 1 July, CESR issued level 3 Guidelines on the methodology for the calculation of the synthetic risk and reward indicator in the KII document. Such an indicator should be based on the volatility of the fund using weekly or monthly returns concerning the previous five years.

Simplified Notification Procedure

A fund wishing to market its units in a Member State different than its country of incorporation will notify its supervisory authority of such project, through a notification procedure which will then be transferred by its home regulator to the competent supervisory authorities of the contemplated host country (new “regulator-to-regulator” procedure).

Enhanced Cooperation between Supervisory Authorities

The proposed amendments to the Directive will result in increased cross-border operations necessitating a full and timely cooperation between supervisory authorities. The Directive encourages the exchange of information, harmonises the powers of the supervisory authorities and allows for the possibility of immediate verifications and investigations, consultation and mutual help mechanisms.

The enhance cooperation between supervisory authorities is expected to result in a more simplified Regulator-to-Regulator notification. This will permit a UCITS to begin marketing its units in another Member State (the “Host Member State”) no later than 10 working days after the date of receipt of the required standard notification letter accompanied by complete documentation required in the application. It also greatly simplifies the documentation required, and significantly the only document which requires translation in the language of the Host Member State is the KII.

The notification procedures in the UCITS IV Directive have been broadly welcomed by the European funds industry as it is believed that they will improve administrative efficiency and facilitate more efficient marketing and reduce translation costs.

For detailed information on UCITS IV, please refer to Brian Higgins of Dillon Eustace and the following publications which can be read on our website:-

- ▣ UCITS IV – Management Company
- ▣ UCITS IV – Key Investor Information Document
- ▣ UCITS IV – Cross-Border Notifications

▣ MiFID 2

In April, 2010 CESR published three consultation papers which were seen by industry as a steps towards reviewing and amending certain aspects of MiFID. The consultation papers included proposed technical advice by CESR on investor protection and intermediaries (CESR/10-417), equity markets (CESR/10-394) and transaction reporting (CESR/10-292).

The consultation papers addressed areas of the MiFID legal framework needing improvement, including quality, cost and consolidation of post-trade transparency data and delays in the publication of such data.

CESR published its recommendations to the European Commission in late July, which related to key issues both CESR and market participants had identified. The recommendations take into account market developments since MiFID was originally drafted and full details of which can be read at <http://www.cesr.eu/popup2.php?id=7009>.

A senior regulator with the FSA in the UK has been chosen to chair a committee of 16 experts from European stock markets, execution venues and investment banks to work with CESR by assisting it advise the European Commission who will then go and draft MiFID 2.

It is expected that MiFID 2 will take effect in 2012 and is aimed at tightening the rules that govern stock exchanges, electronic trading systems, investment banks and high frequency trading hedge funds.

Please contact a member of the Regulatory and Compliance Department in Dillon Eustace should you need further information on MiFID 2.

ISE adopts New Rules on Corporate Governance

On the 17 December 2010, the Irish Stock Exchange (“the ISE”) published the new Listing Rules (“the Rules”) which require Irish listed companies to comply or explain against additional corporate governance provisions which arise from the recommendations contained in the report on Compliance with the Combined Code on Corporate Governance by Irish listed companies (“the ISE/IAIM Commissioned Report”). These Rules, contained in a new Irish Corporate Governance Annex, supplement the existing provisions which require Irish listed companies to comply or explain against the requirements of the UK Corporate Governance Code.

The new Rules are effective immediately, therefore Irish listed companies with accounting periods commencing on or after the 18 December 2010, will be required to comply or explain against the Irish specific corporate governance provisions.

The requirement to comply with the UK Corporate Code is already in place, having applied to Irish listed companies with accounting periods beginning on or after 30 September 2010.

Dodd Frank Wall Street Reform and Consumer Protection Act

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Act”) was signed into law by the US President on 21 July, 2010.

Non U.S. investment advisers to private funds may be required to register with the SEC and comply with certain rules and requirements that are applicable only to SEC registered investment advisers. These requirements include rules and provisions relating to performance fee arrangements, custody of client assets, marketing of advisory services and products, disclosures to the SEC, clients and investors on Form ADV, establishment of a compliance program and appointment of a chief compliance officer.

However, the Act exempts certain foreign private advisers from SEC registration and reporting/recordkeeping requirements. To qualify, advisers must meet all of the following criteria:

-  have no place of business in the United States;

- ▣ have fewer than 15 clients and investors in the United States in private funds advised by the adviser at any time;
- ▣ have assets under management attributable to U.S based clients and investors in private funds it advises of less than \$25 million or such higher amount as the SEC may, by rule, deem appropriate; and
- ▣ neither hold itself out to the public in the United States as an investment adviser, nor act as a business development company or an investment adviser to a registered investment company.

Accordingly, any non U.S. adviser with more than 14 U.S. clients and U.S. investors in private funds, or that manages \$25 million or more of the assets attributable to U.S. clients and U.S. investors, may be required to register with the SEC if they do not qualify for any other exemption.

Our client brochure highlights the potential impact of certain provisions of the Act on non U.S. investment advisers to private funds, in particular the requirement that non U.S. investment advisers who manage assets greater than \$25 million attributable to U.S. clients may need to register with the SEC by 21 July, 2011.

Please contact Andrew Bates should you need further information in relation to the Act.

▣ The Central Bank of Ireland

(i) Change of Name

Following the commencement of the Central Bank Reform Act 2010, the Irish Financial Services Regulatory Authority has been renamed the “Central Bank of Ireland” with effect from 1 October, 2010.

The Central Bank has confirmed that it does not require approved documents or contracts to be updated immediately in order to reflect this change in name. Such updates can be implemented when documents next come up for review.

(ii) Annual Report and Strategic Plan

On 16 July, 2010, the Central Bank published its 2009 Annual Report and Strategic Plan for 2010 to 2012.

The major new measures and initiatives featured in the Strategic Plan include:

- ▣ A refocused approach to strengthening the financial system including a new approach to financial stability assessment;
- ▣ The development of a new regulatory model with an enhanced supervisory capacity for the detection and correction of problems with an active and challenging approach;
- ▣ Interacting with new EU supervisory bodies, such as the European Systemic Risk Board and the European System of Financial Supervisors;
- ▣ Building on consumer protection including a review of the Consumer Protection Code;
- ▣ Greater attention in our economic research on the functioning of the financial system and fuller collaboration with the universities, ESRI and the wider public service; and
- ▣ Moving towards a 100% charge back arrangement on the costs to industry to reduce the cost to the taxpayer.

(iii) New Chairperson of Takeover Panel

On the 19 October, Mr Denis McDonald, S.C. was announced, as the Chairperson of the Irish Takeover Panel for a three year period.

The Irish Takeover Panel is the statutory body responsible for monitoring and supervising takeovers and other relevant transactions in relevant companies in Ireland.

Mr McDonald was called to the Bar in July 1986 and called to the Inner Bar in October 2000. He practices primarily in commercial law.

(iv) Consultation Paper 45 – amendments to the Minimum Competency Requirements (“CP45”)

During the second quarter, the Central Bank published CP45 regarding the Minimum Competency Requirements and sought industry views on the proposals by the 13 August, 2010. The Central Bank was expected to publish their findings in the final quarter of this year but it is more likely to be in the New Year. In summary, CP45 proposes the following:

- ▣ changing the 3 year CPD cycle to an annual 15 formal hour requirement;
- ▣ phasing out ‘grandfathering arrangements’ over a 4 year period whereby a recognised qualification must be achieved by 2015;
- ▣ amendment to making public the register of accredited individuals on request; and

- ▣ detailed requirements are proposed regarding records to be maintained to demonstrate compliance with the Requirements.

The Central Bank is aiming at introducing the new requirements in the second quarter of 2011.

(v) Consultation paper 47 – Review of Consumer Protection Code (“CP47”)

In late October, the Central Bank issued a consultation paper on amendments to the Consumer Protection Code. The strategic plan for 2008 – 2010 had earlier suggested such a consultation process commencing in 2009.

The closing date for submissions is 10 January, 2011 and full details of CP47 can be found on www.financialregulator.ie.

(vi) Draft Directive Deposit Guarantee Scheme

In November 2010, the Head of Payments and Securities Settlements in the Central Bank (Paul Molumby) welcomed the proposals set out in the draft recast Deposit Guarantee Schemes Directive.

The proposal is a comprehensive reform of EU Deposit Guarantee Schemes and follows on from the EU “emergency measures” taken in 2009, through Directive 2009/14/EC, which principally dealt with increasing the level of coverage to €100,000 for all schemes.

The four key elements of the draft directive are:

1. The simplification and harmonisation of the scope of coverage;
2. Faster payout times;
3. Revisions to funding arrangements; and
4. Enhanced cooperation between deposit guarantee schemes across Europe.

The proposals are beneficial from a depositor’s perspective and give confidence that Deposit Guarantee Schemes can assist in maintaining financial stability. In particular, depositors would receive compensation quicker than was previously the case.

While payout times will be reduced from three months to 20 working days with effect from the 1 January 2011 under Directive 2009/14/EC, the draft directive proposes reducing this to seven calendar days by the end of 2013.

This is a draft directive, and certain aspects may be clarified or changed as it progresses through the EU approval process. The Central bank continue to closely monitor developments.

(vii) Consultation Paper 48 - Minimum activities of Irish-domiciled investment Funds (“CP48”)

Having regard to the imminent implementation of UCITS IV (and particularly the UCITS Management Company Passport), the Central Bank has issued a consultative paper regarding the minimum activities regime for Irish authorised funds.

The issues raised from an industry perspective were:

- ▣ Proposal of a definition for maintenance of the shareholder register within the state;
- ▣ Request grandfathering/transitional arrangements for current derogations;
- ▣ Separate outsourcing requirements where that outsourcing is being carried out intra-group as opposed to outsourcing to a third-party;
- ▣ Recognition that for administration services provided to non-Irish funds it may not be possible to require the core administration activities as outlined in CP48, if the administration company is not contracted to provide all core administration functions; and
- ▣ Highlight that the BCP requirements in CP48 go further than the CEBS BCP requirements and should therefore be made more flexible and proportionate.

Responses were due by 31 December, 2010.

Dillon Eustace will provide updates on the outcome of this consultation process in due course.

(viii) Enforcement Strategy and Risk Based Supervision

On the 21 December 2010, the Central Bank published its Enforcement Strategy which sets out the enforcement regime of the newly established Enforcement Directorate for 2011-2012.

The key objectives of the Enforcement Strategy include:

- ▣ Improving effective compliance through the robust application of the enforcement powers of the Central Bank;
- ▣ Enforcement activity prioritised in accordance with the risk profile of the financial institution to ensure that enforcement resources will be directed to those areas where it is perceived that the greatest risks lie; and
- ▣ An increased focus on the actions of persons involved in the management of financial institutions.

On the 22 December 2010, the Central Bank published its Consultation Paper on Impact Metrics for the Risk Based Supervision of Financial Firms by the Central Bank.

Interested parties are invited by this Consultation Paper to submit proposals as to what indicators the Central Bank should use to calibrate the impact of the circa 15,000 firms that it regulates. The result of this consultation will be used alongside the Central Bank's own analysis of the most pertinent indicators to determine the metrics which will be used in its approach to supervision of different entities as well as the fees' blocks into which different institutions should fall.

The consultation will run from 22 December until 24 February 2011. Responses should be sent to Risk@centralbank.ie or by post to Miss Helen Guinane, Risk Division, Central Bank of Ireland, PO Box No. 559, Dame Street, Dublin 2.

Dillon Eustace

This Funds Quarterly Legal and Regulatory Update is for information purposes only and does not constitute, or purport to represent, legal advice. It has been prepared in respect of the quarter (1 October, 2010 to 31 December, 2010) and, accordingly, may not reflect changes that have occurred subsequent to this period. If you have any queries or would like further information regarding any of the above matters, please refer to the author or your usual contact in Dillon Eustace

CONTACT US

Our Offices

Dublin

33 Sir John Rogerson's Quay,
Dublin 2,
Ireland.
Tel: +353 1 667 0022
Fax: +353 1 667 0042

Boston

26th Floor,
225 Franklin Street,
Boston, MA 02110,
United States of America.
Tel: +1 617 217 2866
Fax: +1 617 217 2566

New York

245 Park Avenue,
39th Floor,
New York, NY 10167,
United States of America.
Tel: +1 212 792 4166
Fax: +1 212 792 4167

Tokyo

12th Floor,
Yurakucho Itocia Building
2-7-1 Yurakucho, Chiyoda-ku
Tokyo 100-0006, Japan.
Tel: +813 6860 4885
Fax: +813 6860 4501

e-mail: enquiries@dilloneustace.ie
website: www.dilloneustace.ie

Contact Points

For more details on how we can help you, to request copies of most recent newsletters, briefings or articles, or simply to be included on our mailing list going forward, please contact any of the team members below.

Breeda Cunningham
Regulatory and Compliance

e-mail: breeda.cunningham@dilloneustace.ie
Tel : +353 1 6670022
Fax: + 353 1 6670042

Paula Kelleher
Regulatory and Compliance

e-mail: paula.kelleher@dilloneustace.ie
Tel : +353 1 6670022
Fax: + 353 1 6670042

Andrew Lawless
Regulatory and Compliance

e-mail: andrew.lawless@dilloneustace.ie
Tel: +353 1 6670022
Fax: +353 1 6670042

DISCLAIMER:

This document is for information purposes only and does not purport to represent legal advice. If you have any queries or would like further information relating to any of the above matters, please refer to the contacts above or your usual contact in Dillon Eustace.

Copyright Notice:
© 2011 Dillon Eustace. All rights reserved.

DILLON  EUSTACE

DUBLIN CORK BOSTON NEW YORK TOKYO

33 Sir John Rogerson's Quay, Dublin 2, Ireland.
www.dilloneustace.ie

In alliance with Arendt & Medernach