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AIFMD Implementing Measures: Long Awaited Delegated Regulation Finally Published in the Official Journal

By [Orestis Omran](#), [Nora Wouters](#) on April 8, 2013

On March 22, 2013, the [Delegated Regulation](#) supplementing the [Alternative Investment Managers Directive](#) ("AIFMD") with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision was finally published in the official EU Journal.

The Regulation is expected to bring considerable changes to the way U.S. Alternative Investment Funds operate in Europe. Their managers need to study the changes brought about by both the AIFMD and the Delegated Regulation to avoid the risk of severe financial consequences that national legislations will impose for non-compliance. The most important provisions of the Regulation are set out below.

Calculation of Assets

The methods to be followed by investment managers when valuing assets under management are provided in detail. It must be emphasized that each derivative instrument position, including any derivative embedded in transferable securities, must be converted into its equivalent position in the underlying assets of that derivative. In addition, investments in other Alternative Investment Funds ("AIF") shall not be included. The assets under management will need to be revalued on an annual basis and continuous monitoring via periodic recalculation of values must take place.

Additional Professional Funds and Professional Indemnity Insurance

An AIFM is required to adopt and implement effective internal risk management policies and procedures in order to identify, measure, manage and monitor operational risks including professional liability risks to which the Alternative Investment Fund Manager ("AIFM") is or could be exposed. Moreover, AIFMs shall provide its own funds for professional negligence risks for a minimum of 0.01 % of the value of the portfolios of AIFs managed.

Operating Conditions

As a general rule, AIFMs shall apply a high standard of diligence in the selection and monitoring of investments. In particular, such diligence should apply when selecting and appointing counterparties and prime brokers, who are required to be financially sound, subject to ongoing supervision by a public authority and possess the necessary organizational structure and resources for the required services. Moreover, AIFMs have to act fairly and honestly in accordance with the best interests of AIFs they manage. The Regulation expressly sets out the protection against the risk of inducement if the AIFM receives any monetary or non-monetary benefit other than the fees and commissions by the AIF and third parties and sets out disclosure requirements for all benefits.

Valuation

AIFMs shall establish, maintain, implement and review, for each AIF they manage, written policies and procedures that ensure a sound, transparent, comprehensive and appropriately-documented valuation process. Any valuation policies adopted by the AIFM have to comply with the following: (i) the competence and independence of personnel carrying out the valuation of assets; (ii) the specific investment strategies of the AIF and the assets in which the AIF might invest; (iii) the controls over the selection of valuation inputs, sources and methodologies; (iv) the escalation channels for resolving differences in values for assets; (v) the valuation of any adjustments related to the size and liquidity of positions, or changes in the market conditions, as appropriate; (vi) the appropriate time for closing the books for valuation purposes; and (vii) the appropriate

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frequency for valuing assets.

Delegation

Fundamental decision-making functions, such as those related to the risks of portfolio management, shall remain with the AIFM in order for the AIFM to not become a mere “letter box” entity. In particular, the following need to be considered when assessing the objectives of a delegation structure: (a) optimizing of business functions and processes; (b) cost saving; (c) expertise of the delegate in administration or in specific markets or investments; (d) access of the delegate to global trading capabilities.

Conclusion

While many of these provisions seem common-sense, the devil is in the detail. The new compliance requirements are likely to result in increased operating costs. They may need time to be become fully effective and this may have an impact to a broad spectrum of activities of AIFMs. Managers of AIFs need to be prepared for the new regime and the changes that will need to be made in the operation of their AIFs if they are to remain fully compliant and avoid the risks of what will probably be serious penalties.



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