

Financial Services (Collective Investment Schemes)
FINANCIAL SERVICES (COLLECTIVE INVESTMENT SCHEMES)
(CONDUCT OF BUSINESS) REGULATIONS 2011

2005-48
Repealed
Subsidiary
2011/193

Subsidiary Legislation made under s. 53 of the Financial Services (Collective Investment Schemes) Act 2011 and section 23(g)(i) of the Interpretation and General Clauses Act.

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Repealed by Act.2019-26 as from 15.1.2020

(LN. 2011/193)

Commencement **13.10.2011**

Amending enactments	Relevant current provisions	Commencement date
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EU Legislation/International Agreements involved:

Directive 2009/65/EC

Directive 2010/43/EU

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In exercise of the powers conferred on me by section 53 of the Financial Services (Collective Investment Schemes) Act 2011 and section 23(g)(i) of the Interpretation and General Clauses Act and in order to transpose into the law of Gibraltar Commission Directive 2010/43/EU of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards organisational requirements, conflicts of interest, conduct of business, risk management and content of the agreement between a depositary and a management company, I have made the following Regulations—

PART I

PRELIMINARY AND INTERPRETATION

Title and commencement.

1. These Regulations may be cited as the Financial Services (Collective Investment Schemes) (Conduct of Business) Regulations 2011 and come into operation on the day of publication.

Interpretation.

2.(1) In these Regulations and unless the context otherwise requires—

“board of directors” means the board of directors of a management company;

“CIS Regulations” means the Financial Services (Collective Investment Schemes) Regulations 2011;

“client” means any person or undertaking, including a UCITS, to whom a management company provides a service of collective portfolio management or services pursuant to regulation 4(3) of the CIS Regulations;

“counterparty risk” means the risk of loss for a UCITS resulting from the fact that the counterparty to a transaction may default on its obligations prior to the final settlement of the transaction’s cash flow;

“liquidity risk” means the risk that a position in a UCITS portfolio cannot be sold, liquidated or closed at limited cost in an adequately short time frame and that the ability of the UCITS to comply at any time with regulation 99(1) of the CIS Regulations is thereby compromised;

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“market risk” means the risk of loss for a UCITS resulting from fluctuation in the market value of positions in the UCITS’ portfolio attributable to changes in market variables, such as interest rates, foreign exchange rates, equity and commodity prices or an issuer’s credit worthiness;

“operational risk” means the risk of loss for a UCITS resulting from inadequate internal processes and failures in relation to people and systems of the management company or from external events, and includes legal and documentation risk and risk resulting from the trading, settlement and valuation procedures operated on behalf of the UCITS;

“relevant person” means any of the following in relation to a management company–

- (a) a director, partner or equivalent, or manager of a management company;
- (b) an employee of a management company and any other individual whose services are placed at the disposal and under the control of the management company and involved in the provision by the management company of collective portfolio management;
- (c) an individual who is directly involved in the provision of services to the management company by delegation to third parties, where the management company receives such services for the provision of collective portfolio management;

“senior management” means the person or persons who effectively conduct the business of a management company in accordance with regulation 5(1)(b) of the CIS Regulations;

“supervisory function” means the relevant persons or bodies responsible for the supervision of senior management and for the assessment and periodical review of the adequacy and effectiveness of the risk management process and of the policies, arrangements and procedures put in place to comply with the obligations under the CIS Regulations;

“unit-holder” means any person holding one or more units in a UCITS.

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(2) Where management companies have a dual structure composed of a board of directors and a supervisory board, the term “board of directors” in sub-regulation (1) is without prejudice to the supervisory board.

(3) Terms or expressions used by not defined in these Regulations that are also used in the CIS Regulations shall have the same meaning in these Regulations as they have in the CIS Regulations.

Scope and application of Regulations.

3.(1) These Regulations apply–

- (a) to procedures and arrangements referred to in regulation 12(1), and to structures and organisational requirements for minimising conflicts of interests referred to in regulation 12(1);
- (b) to the duty to act honestly, fairly and with due skill, care and diligence in the best interests of the UCITS and the criteria for determining the types of conflict of interests, specifying the principles required to ensure that the resources are employed effectively, defining the steps that should be taken to identify, prevent, manage or disclose conflicts of interests referred to in regulation 14(1) and (2);
- (c) to the particulars that need to be included in the agreements between the depository and management company in accordance with regulations 23(5) and 33(5); and
- (d) to the risk management process referred to in regulation 51(1) in particular, to criteria for assessing the adequacy of the risk management process employed by a management company and the risk management policy and processes and the arrangements, processes and techniques for risk measurement and management relating to such criteria.

(2) These Regulations apply as follows–

- (a) to management companies pursuing the activity of management of an undertaking for collective investment in transferable securities (UCITS);
- (b) Part V applies to depositaries carrying out functions pursuant to Part III and Chapter 3 of Part V of the CIS Regulations.

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(3) This Part, regulation 12 and Parts III, IV and VI apply to investment companies that have not designated a management company authorised pursuant to the CIS Regulations, and in those cases "management company" shall be read as "investment company".

PART II

ADMINISTRATIVE PROCEDURES AND CONTROL MECHANISM

CHAPTER 1

GENERAL PRINCIPLES

General requirements on procedures and organisation.

4.(1) The Authority shall not authorise a management company to offer services unless it is satisfied that the management company complies with the following requirements—

- (a) it has established, implemented and maintained decision-making procedures and an organisational structure which clearly and in a documented manner specifies reporting lines and allocates functions and responsibilities;
- (b) relevant persons of the management company are aware of the procedures which must be followed for the proper discharge of their responsibilities;
- (c) it has established, implemented and maintained adequate internal control mechanisms designed to secure compliance with decisions and procedures at all levels of the management company;
- (d) it has established, implemented and maintained effective internal reporting and communication of information at all relevant levels of the management company as well as effective information flows with any third party involved;
- (e) it has maintained adequate and orderly records of its business and internal organisation;
- (f) it takes into account the nature, scale and complexity of its business and the nature and range of services and activities undertaken in the course of that business.

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(2) The Authority shall not authorise a management company to offer services unless the management company establishes, implements and maintains systems and procedures that are adequate to safeguard the security, integrity and confidentiality of information, taking into account the nature of the information in question.

(3) The Authority shall not authorise a management company to offer services unless the management company establishes, implements and maintains an adequate business continuity policy aimed at ensuring, in the case of an interruption to the company's systems and procedures, the preservation of essential data and functions, and the maintenance of services and activities, or, where that is not possible, the timely recovery of such data and functions and the timely resumption of its services and activities.

(4) The Authority shall not authorise a management company to offer services unless the management company establishes, implements and maintains accounting policies and procedures that enable the management company, at the request of the Authority, to deliver in a timely manner to the Authority financial reports which reflect a true and fair view of the company's financial position and which comply with all applicable accounting standards and rules.

(5) The Authority shall require a management company to monitor and, on a regular basis, evaluate the adequacy and effectiveness of the company's systems, internal control mechanisms and arrangements established in accordance with sub-regulations (1) to (4), and to take appropriate measures to address any deficiencies.

Resources.

5.(1) The Authority shall authorise a management company to offer services subject to the requirement that it employs personnel with the skills, knowledge and expertise necessary for the discharge of the responsibilities allocated to them.

(2) The Authority shall authorise a management company to offer services subject to the requirement that it retains the necessary resources and expertise so as to effectively monitor the activities carried out by third parties on the basis of an arrangement with the management company, especially with regard to the management of the risk associated with those arrangements.

(3) The Authority shall authorise a management company to offer services subject to the requirement that it ensures that the performance of multiple functions by relevant persons does not and is not likely to prevent

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those relevant persons from discharging any particular function soundly, honestly, and professionally.

(4) The Authority shall authorise a management company to offer services subject to the requirement that for the purposes laid down in sub-regulations (1), (2) and (3), it takes into account the nature, scale and complexity of its business and the nature and range of services and activities undertaken in the course of that business.

CHAPTER 2

ADMINISTRATIVE AND ACCOUNTING PROCEDURES

Complaints handling.

6.(1) The Authority shall authorise a management company to offer services subject to the requirement that it establishes, implements and maintains effective and transparent procedures for the reasonable and prompt handling of complaints received from investors.

(2) Such complaints and the measures taken for their resolution shall be recorded by the management company.

(3) Investors shall be able to file such complaints free of charge and the information regarding procedures referred to in sub-regulation (1) shall be made available to investors free of charge.

Electronic data processing.

7.(1) The Authority shall authorise a management company to offer services subject to the requirement that it makes appropriate arrangements for suitable electronic systems to permit a timely and proper recording of each portfolio transaction or subscription or redemption order in order to be able to comply with regulations 14 and 15.

(2) Management companies shall take the necessary steps to ensure a high level of security during electronic data processing as well as integrity and confidentiality of the recorded information, as appropriate.

Accounting procedures.

8.(1) The Authority shall authorise a management company to offer services subject to the requirement that—

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- (a) it operates accounting policies and procedures as referred to in regulation 4(4) that ensure the protection of unit-holders;
- (b) UCITS accounting is kept in such a way that all assets and liabilities of the UCITS can be directly identified at all times;
- (c) where a UCITS has different investment compartments, separate accounts are maintained for those investment compartments.

(2) The Authority shall authorise a management company to offer services subject to the requirement that it operates accounting policies and procedures established, implemented and maintained, in accordance with the accounting rules of the UCITS' home EEA State, so as to ensure that the calculation of the net asset value of each UCITS is accurately effected, on the basis of the accounting, and that subscription and redemption orders can be properly executed at that net asset value.

(3) The Authority shall authorise a management company to offer services subject to the requirement that it establishes appropriate procedures to ensure the proper and accurate valuation of the assets and liabilities of the UCITS, as consistent with the applicable rules referred to in regulation 100 of the CIS Regulations.

CHAPTER 3

INTERNAL CONTROL MECHANISMS

Control by senior management and supervisory function.

9.(1) The Authority shall authorise a management company to offer services subject to the requirement that, when allocating functions internally, the management company ensures that senior management and, where appropriate, the supervisory function, are responsible for the management company's compliance with its obligations under the CIS Regulations.

(2) For the purposes of sub-regulation (1), the management company shall ensure that its senior management—

- (a) is responsible for the implementation of the general investment policy for each managed UCITS, as defined, where relevant, in the prospectus, the fund rules or the instruments of incorporation of the investment company;

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- (b) oversees the approval of investment strategies for each managed UCITS;
 - (c) is responsible for ensuring that the management company has a permanent and effective compliance function, as referred to in regulation 10, even if this function is performed by a third party;
 - (d) ensures and verifies on a periodic basis that the general investment policy, the investment strategies and the risk limits of each managed UCITS are properly and effectively implemented and complied with, even if the risk management function is performed by third parties;
 - (e) approves and reviews on a periodic basis the adequacy of the internal procedures for undertaking investment decisions for each managed UCITS, so as to ensure that such decisions are consistent with the approved investment strategies;
 - (f) approves and reviews on a periodic basis the risk management policy and arrangements, processes and techniques for implementing that policy, as referred to in regulation 38, including the risk limit system for each managed UCITS.
- (3) For the purposes of sub-regulation (1), the management company shall also ensure that its senior management and, where appropriate, its supervisory function -
- (a) assesses and periodically review the effectiveness of the policies, arrangements and procedures put in place to comply with the obligations in the CIS Regulations;
 - (b) takes appropriate measures to address any deficiencies.
- (4) For the purposes of sub-regulation (1), management companies shall ensure that—
- (a) their senior management receives on a frequent basis, and at least annually, written reports on matters of compliance, internal audit and risk management indicating in particular whether appropriate remedial measures have been taken in the event of any deficiencies;
 - (b) their senior management receives on a regular basis reports on the implementation of investment strategies and of the internal

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procedures for taking investment decisions referred to in sub-regulation (2)(b) to (e);

- (c) the supervisory function, if any, receives on a regular basis written reports on the matters referred to in paragraph (a) above.

Permanent compliance function.

10.(1) The Authority shall authorise a management company to offer services subject to the requirement that—

- (a) it establishes, implements and maintains adequate policies and procedures designed to detect any risk of failure by the management company to comply with its obligations under the CIS Regulations, as well as the associated risks, and puts in place adequate measures and procedures designed to minimise such risk and to enable the Authority to exercise its powers effectively under the CIS Regulations;
- (b) it takes into account the nature, scale and complexity of the business of the company, and the nature and range of services and activities undertaken in the course of that business;
- (c) it establishes and maintains a permanent and effective compliance function which operates independently and which has the following responsibilities—
 - (i) to monitor and, on a regular basis, to assess the adequacy and effectiveness of the measures, policies and procedures put in place in accordance with paragraph (a) and the actions taken to address any deficiencies in the management company's compliance with its obligations;
 - (ii) to advise and assist the relevant persons responsible for carrying out services and activities to comply with the management company's obligations under the CIS Regulations.

(2) To enable the compliance function referred to in sub-regulation (1) to discharge its responsibilities properly and independently, management companies shall ensure that the following conditions are satisfied—

- (a) the compliance function must have the necessary authority, resources, expertise and access to all relevant information;

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- (b) a compliance officer must be appointed and must be responsible for the compliance function and for any reporting on a frequent basis, and at least annually, to the senior management on matters of compliance, indicating in particular whether the appropriate remedial measures have been taken in the event of any deficiencies;
- (c) the relevant persons involved in the compliance function must not be involved in the performance of services or activities they monitor;
- (d) the method of determining the remuneration of the relevant persons involved in the compliance function must not compromise their objectivity and must not be likely to do so,

but a management company shall not be required to comply with paragraphs (c) or (d) where it is able to demonstrate that, in view of the nature, scale and complexity of its business, and the nature and range of its services and activities, that requirement is not proportionate and that its compliance function continues to be effective.

Permanent internal audit function.

11.(1) The Authority shall authorise a management company to offer services subject to the requirement that, where appropriate and proportionate in view of the nature, scale and complexity of the management company's business and the nature and range of collective portfolio management activities undertaken in the course of that business, it establishes and maintains an internal audit function which is separate and independent from the other functions and activities of the management company.

(2) For the purposes of sub-regulation (1), the internal audit function shall have the following responsibilities—

- (a) to establish, implement and maintain an audit plan to examine and evaluate the adequacy and effectiveness of the management company's systems, internal control mechanisms and arrangements;
- (b) to issue recommendations based on the result of work carried out in accordance with paragraph (a);
- (c) to verify compliance with the recommendations referred to in paragraph (b);

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- (d) to report in relation to internal audit matters in accordance with regulation 9(4).

Permanent risk management function.

12.(1) The Authority shall authorise a management company to offer services subject to the requirement that it establishes and maintains a permanent risk management function.

(2) The permanent risk management function referred to in sub-regulation (1) shall be hierarchically and functionally independent from operating units, but the Authority may permit a management company not to comply with that obligation where it is appropriate and proportionate in view of the nature, scale and complexity of the management company's business and of the UCITS it manages.

(3) For the purposes of sub-regulation (1), a management company shall be able to demonstrate to the Authority that appropriate safeguards against conflicts of interest have been adopted so as to allow an independent performance of risk management activities and that its risk management process satisfies the requirements of regulation 48 of the CIS Regulations.

(4) The permanent risk management function referred to in sub-regulation (1) shall—

- (a) implement the risk management policy and procedures;
- (b) ensure compliance with the UCITS risk limit system, including statutory limits concerning global exposure and counterparty risk in accordance with regulations 41, 42 and 43;
- (c) provide advice to the board of directors as regards the identification of the risk profile of each managed UCITS;
- (d) provide regular reports to the board of directors and, where it exists, the supervisory function, on -
 - (i) the consistency between the current levels of risk incurred by each managed UCITS and the risk profile agreed for that UCITS;
 - (ii) the compliance of each managed UCITS with relevant risk limit systems;

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- (iii) the adequacy and effectiveness of the risk management process, indicating in particular whether appropriate remedial measures have been taken in the event of any deficiencies;
- (e) provide regular reports to the senior management outlining the current level of risk incurred by each managed UCITS and any actual or foreseeable breaches to their limits, so as to ensure that prompt and appropriate action can be taken;
- (f) review and support, where appropriate, the arrangements and procedures for the valuation of OTC derivatives as referred to in regulation 44.

(5) The permanent risk management function shall have the necessary authority and access to all relevant information necessary to fulfil the tasks set out in sub-regulation (4).

Personal transactions.

13.(1) The Authority shall authorise a management company to offer services subject to the requirement that it establishes, implements and maintains adequate arrangements aimed at preventing the following activities in the case of any relevant person who is involved in activities that may give rise to a conflict of interest, or who has access to inside information within the meaning of Article 1(1) of Directive 2003/6/EC of the European Parliament and of the Council of 28 January 2003 on insider dealing and market manipulation, or to other confidential information relating to UCITS or transactions with or for UCITS by virtue of an activity carried out by him on behalf of the management company—

- (a) entering into a personal transaction which fulfils at least one of the following criteria—
 - (i) that person is prohibited from entering into that personal transaction within the meaning of Directive 2003/6/EC;
 - (ii) it involves the misuse or improper disclosure of confidential information;
 - (iii) it conflicts or is likely to conflict with an obligation of the management company under the CIS Regulations or under Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments;

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- (b) advising or procuring, other than in the proper course of his employment or contract for services, any other person to enter into a transaction in financial instruments which, if a personal transaction of the relevant person, would be covered by paragraph (a) above, or by Article 25(2)(a) or (b) of Commission Directive 2006/73/EC of 10 August 2006 implementing Directive 2004/39 as regards organisational requirements and operating conditions for investment firms and defined terms for the purpose of that Directive, or would otherwise constitute a misuse of information relating to pending orders;
- (c) disclosing, other than in the normal course of his employment or contract for services and without prejudice to Article 3(a) of Directive 2003/6/EC, any information or opinion to any other person if the relevant person knows, or reasonably ought to know, that as a result of that disclosure that other person will, or would be likely to, take either of the following steps -
 - (i) to enter into a transaction in financial instruments which, where a personal transaction of the relevant person would be covered by paragraph (a) above or by Article 25(2)(a) or (b) of Directive 2006/73/EC, or would otherwise constitute a misuse of information relating to pending orders;
 - (ii) to advise or procure another person to enter into such a transaction,

provided that for the purposes of paragraph (b), where certain activities are performed by third parties, the management company shall ensure that the entity performing the activity maintains a record of personal transactions entered into by any relevant person and provides that information to the management company promptly on request.

(2) The arrangements referred to in sub-regulation (1) shall in particular be designed to ensure that—

- (a) each relevant person covered by sub-regulation (1) is aware of the restrictions on personal transactions and of the measures established by the management company in connection with personal transactions and disclosure, in accordance with that sub-regulation;

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- (b) the management company is informed promptly of any personal transaction entered into by a relevant person, either by notification of that transaction or by other procedures enabling the management company to identify such transactions;
- (c) a record is kept of the personal transaction notified to the management company or identified by it, including any authorisation or prohibition in connection with such a transaction.

(3) Sub-regulations (1) and (2) do not apply to the following kinds of personal transactions—

- (a) personal transactions effected under a discretionary portfolio management service where there is no prior communication in connection with the transaction between the portfolio manager and the relevant person or other person for whose account the transaction is executed;
- (b) personal transactions in UCITS or units in collective undertakings that are subject to supervision under the law of a EEA State which requires an equivalent level of risk spreading in their assets, where the relevant person and any other person for whose account the transactions are effected are not involved in the management of that undertaking.

(4) For the purposes of this regulation, "personal transaction" has the same meaning as in Article 11 of Directive 2006/73/EC.

Recording of portfolio transactions.

14.(1) The Authority shall authorise a management company to offer services subject to the requirement that for each portfolio transaction relating to UCITS, a record of information which is sufficient to reconstruct the details of the order and the executed transaction can be produced without delay.

- (2) The record referred to in sub-regulation (1) shall include—
 - (a) the name or other designation of the UCITS and of the person acting on account of the UCITS;
 - (b) the details necessary to identify the instrument in question;
 - (c) the quantity;

- (d) the type of the order or transaction;
- (e) the price;
- (f) for orders, the date and exact time of the transmission of the order and name or other designation of the person to whom the order was transmitted, or for transactions, the date and exact time of the decision to deal and execution of the transaction;
- (g) the name of the person transmitting the order or executing the transaction;
- (h) where applicable, the reasons for the revocation of an order;
- (i) for executed transactions, the counterparty and execution venue identification and, for these purposes, an "execution venue" means a regulated market as referred to under Article 4(1)(14) of Directive 2004/39/EC, a multilateral trading facility as referred to in Article 4(1)(15) of that Directive, a systematic internaliser as referred to in Article 4(1)(7) of that Directive, or a market maker or other liquidity provider or an entity that performs a similar function in a non-EEA state to the functions performed by any of the foregoing.

Recording of subscription and redemption orders.

15.(1) The Authority shall authorise a management company to offer services subject to the requirement that it takes all reasonable steps to ensure that the received UCITS subscription and redemption orders are centralised and recorded immediately after receipt of any such order.

(2) The record referred to in sub-regulation (1) shall include information on the following—

- (a) the relevant UCITS;
- (b) the person giving or transmitting the order;
- (c) the person receiving the order;
- (d) the date and time of the order;
- (e) the terms and means of payment;

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- (f) the type of the order;
- (g) the date of execution of the order;
- (h) the number of units subscribed or redeemed;
- (i) the subscription or redemption price for each unit;
- (j) the total subscription or redemption value of the units;
- (k) the gross value of the order including charges for subscription or net amount after charges for redemption.

Record-keeping requirements.

16.(1) The Authority shall authorise a management company to offer services subject to the requirement that the managements company retains the records referred to in regulations 14 and 15 for a period of at least 5 years or, in exceptional circumstances, such longer period as the Authority may determine by the nature of the instrument or portfolio transaction, where it is necessary to enable the Authority to exercise its supervisory functions under the CIS Regulations.

(2) Where—

- (a) the authorisation of a management company expires, the Authority may require the management company to retain the records referred to in sub-regulation (1) for the outstanding term of the 5-year period;
- (b) a management company transfers its responsibilities in relation to the UCITS to another management company, the Authority may require that arrangements are made so that such records for the past 5 years are accessible to that company,

in default of which the Authority may impose a fine of £10,000 recoverable as a civil debt.

(3) The records referred to in this regulation shall be retained in a medium that allows the storage of information in a way accessible for future reference by the Authority, and in such a form and manner that the following conditions are met—

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- (a) the Authority must be able to access them readily and to reconstitute each key stage of the processing of each portfolio transaction;
- (b) it must be possible for any corrections or other amendments, and the contents of the records prior to such corrections or amendments, to be easily ascertained;
- (c) it must not be possible for the records to be otherwise manipulated or altered.

PART III

CONFLICT OF INTERESTS

Criteria for the identification of conflicts of interest.

17.(1) The Authority shall authorise a management company to offer services subject to the requirement that, in order to identify the types of conflict of interest that arise in the course of providing services and activities and whose existence may damage the interests of a UCITS, the management company takes into account the question of whether the management company or a relevant person, or a person directly or indirectly linked by way of control to the management company, is in any of the following situations, whether as a result of providing collective portfolio management activities or otherwise—

- (a) the management company or that person is likely to make a financial gain, or avoid a financial loss, at the expense of the UCITS;
- (b) the management company or that person has an interest in the outcome of a service or an activity provided to the UCITS or another client or of a transaction carried out on behalf of the UCITS or another client, which is distinct from the UCITS interest in that outcome;
- (c) the management company or that person has a financial or other incentive to favour the interest of another client or group of clients over the interests of the UCITS;
- (d) the management company or that person carries on the same activities for the UCITS and for another client or clients which are not UCITS;

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- (e) the management company or that person receives or will receive from a person other than the UCITS an inducement in relation to collective portfolio management activities provided to the UCITS, in the form of monies, goods or services, other than the standard commission or fee for that service.

(2) For the purposes of sub-regulation (1), when identifying the types of conflict of interests, a management company shall take into account—

- (a) the interests of the management company, including those deriving from its belonging to a group or from the performance of services and activities, the interests of the clients and the duty of the management company towards the UCITS;
- (b) the interests of two or more managed UCITS.

Conflicts of interest policy.

18.(1) The Authority shall authorise a management company to offer services subject to the requirement that it establishes, implements and maintains an effective conflicts of interest policy as follows—

- (a) the policy must be set out in writing and be appropriate to the size and organisation of the management company and the nature, scale and complexity of its business; and
- (b) where the management company is a member of a group, the policy shall take into account any circumstances of which the company is or should be aware which may give rise to a conflict of interest resulting from the structure and business activities of other members of the group.

(2) The conflicts of interest policy established in accordance with sub-regulation (1) shall include the following—

- (a) the identification of, with reference to the collective portfolio management activities carried out by or on behalf of the management company, the circumstances which constitute or may give rise to a conflict of interest entailing a material risk of damage to the interests of the UCITS or one or more other clients;
- (b) procedures to be followed and measures to be adopted in order to manage such conflicts.

Independence in conflicts management.

19.(1) The Authority shall authorise a management company to offer services subject to the requirement that the procedures and measures provided for in regulation 18(2)(b) are designed to ensure that relevant persons engaged in different business activities involving a conflict of interest carry on those activities at a level of independence appropriate to the size and activities of the management company and of the group to which it belongs and to the materiality of the risk of damage to the interests of clients.

(2) The procedures to be followed and measures to be adopted in accordance with regulation 18(2)(b) shall include the following where necessary and appropriate for the management company to ensure the requisite degree of independence—

- (a) effective procedures to prevent or control the exchange of information between relevant persons engaged in collective portfolio management activities involving a risk of a conflict of interest where the exchange of that information may harm the interests of one or more clients;
- (b) the separate supervision of relevant persons whose principal functions involve carrying out collective portfolio management activities on behalf of, or providing services to, clients or to investors whose interests may conflict, or who otherwise represent different interests that may conflict, including those of the management company;
- (c) the removal of any direct link between the remuneration of relevant persons principally engaged in one activity and the remuneration of, or revenues generated by, different relevant persons principally engaged in another activity, where a conflict of interest may arise in relation to those activities;
- (d) measures to prevent or limit any person from exercising inappropriate influence over the way in which a relevant person carries out collective portfolio management activities;
- (e) measures to prevent or control the simultaneous or sequential involvement of a relevant person in separate collective portfolio management activities where such involvement may impair the proper management of conflicts of interest; and

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- (f) where the adoption or the practice of one or more of the measures and procedures set out in paragraphs (a) to (e) does not ensure the requisite degree of independence, such alternative or additional measures and procedures as are necessary and appropriate for those purposes.

Management of activities giving rise to detrimental conflict of interest

20.(1) The Authority shall authorise a management company to offer services subject to the requirement that it updates a record of the types of collective portfolio management activities undertaken by or on behalf of the management company in which a conflict of interest entailing a material risk of damage to the interests of one or more UCITS or other clients has arisen or, in the case of an ongoing collective portfolio management activity, may arise.

(2) Where the organisational or administrative arrangements made by the management company for the management of conflicts of interest are not sufficient to ensure, with reasonable confidence, that risks of damage to the interests of UCITS or of its unit-holders will be prevented, senior management or other competent internal body of the management company shall be promptly informed in order for them to ensure that management company acts in the best interests of the UCITS and of its unit-holders.

(3) A management company shall report situations referred to in sub-regulation (2) to investors by any appropriate durable medium and give reasons for its decision.

Strategies for the exercise of voting rights

21.(1) The Authority shall authorise a management company to offer services subject to the requirement that it develops adequate and effective strategies for determining when and how voting rights attached to instruments held in the managed portfolios are to be exercised, to the exclusive benefit of the UCITS concerned.

(2) The strategy referred to in sub-regulation (1) shall determine measures and procedures for -

- (a) monitoring relevant corporate events;
- (b) ensuring that the exercise of voting rights is in accordance with the investment objectives and policy of the relevant UCITS;

- (c) preventing or managing any conflicts of interest arising from the exercise of voting rights.

(3) A summary description of the strategies referred to in sub-regulation (1) shall be made available to investors, and details of the actions taken on the basis of those strategies shall be made available to the unit-holders free of charge and on their request.

PART IV

RULES OF CONDUCT

CHAPTER 1

GENERAL PRINCIPLES

Duty to act in the best interests of UCITS and their unit-holders

22.(1) The Authority shall authorise a management company to offer services subject to the requirement that unit-holders of managed UCITS are treated fairly and that the management company refrains from placing the interests of any group of unit-holders above the interests of any other group of unit-holders.

(2) For the purposes of sub-regulation (1), management companies shall apply appropriate policies and procedures for preventing malpractices that might reasonably be expected to affect the stability and integrity of the market.

(3) For the purposes of sub-regulation (1), and in order to comply with the duty to act in the best interests of the unit-holders, a management company shall ensure that fair, correct and transparent pricing models and valuation systems are used for the UCITS it manages and it must be able to demonstrate that the UCITS portfolios have been accurately valued.

(4) For the purposes of sub-regulation (1), a management company must act in such a way as to prevent undue costs being charged to the UCITS and its unit-holders.

Due diligence requirements

23.(1) The Authority shall authorise a management company to offer services subject to the requirement that it ensures a high level of diligence in the selection and ongoing monitoring of investments, in the best interests of UCITS and the integrity of the market.

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(2) For the purposes of sub-regulation (1) a management company shall—

- (a) ensure it has adequate knowledge and understanding of the assets in which the UCITS are invested;
- (b) establish written policies and procedures on due diligence and implement effective arrangements for ensuring that investment decisions on behalf of the UCITS are carried out in compliance with the objectives, investment strategy and risk limits of the UCITS;
- (c) formulate forecasts and perform analyses concerning the investment's contribution to the UCITS portfolio composition, liquidity and risk and reward profile before carrying out an investment when implementing their risk management policy, and where it is appropriate after taking into account the nature of a foreseen investment. Such analyses shall only be carried out on the basis of reliable and up-to-date information, both in quantitative and qualitative terms;
- (d) exercise due skill, care and diligence when entering into, managing or terminating any arrangements with third parties in relation to the performance of risk management activities, and subject to the following principles –
 - (i) before entering into such arrangements, the management company shall take the necessary steps in order to verify that the third party has the ability and capacity to perform the risk management activities reliably, professionally and effectively; and
 - (ii) the management company shall establish methods for the on-going assessment of the standard of performance of the third party.

CHAPTER 2

HANDLING OF SUBSCRIPTION AND REDEMPTION ORDERS

Reporting obligations in respect of execution of subscription and redemption orders

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24.(1) The Authority shall authorise a management company to offer services subject to the requirement that where it has carried out a subscription or redemption order from a unit-holder, it notifies the unit-holder, by means of a durable medium, confirming execution of the order as soon as possible, and no later than the first business day following execution or, where the confirmation is received by the management company from a third party, no later than the first business day following receipt of the confirmation from the third party; save that the foregoing does not apply where the notice would contain the same information as a confirmation that is to be promptly dispatched to the unit-holder by another person.

(2) The notice referred to in sub-regulation (1) shall, where applicable, include the following information -

- (a) the management company identification;
- (b) the name or other designation of the unit-holder;
- (c) the date and time of receipt of the order and method of payment;
- (d) the date of execution;
- (e) the UCITS identification;
- (f) the nature of the order (subscription or redemption);
- (g) the number of units involved;
- (h) the unit value at which the units were subscribed or redeemed;
- (i) the reference value date;
- (j) the gross value of the order including charges for subscription or net amount after charges for redemptions;
- (k) a total sum of the commissions and expenses charged and, where the investor so requests, an itemised breakdown.

(3) For the purposes of sub-regulation (1) –

- (a) where orders for a unit-holder are executed periodically, a management company shall either take the action set out in that sub-regulation or provide the unit-holder, at least once every 6

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months, with the information listed in sub-regulation (2) in respect of those transactions; and

- (b) a management company shall supply the unit-holder, upon request, with information about the status of his order.

CHAPTER 3

BEST EXECUTION

Execution of decisions to deal on behalf of the managed UCITS

25.(1) The Authority shall authorise a management company to offer services subject to the requirement that it acts in the best interests of the UCITS it manages when executing decisions to deal on behalf of the managed UCITS in the context of the management of their portfolios.

(2) For the purposes of sub-regulation (1), a management company shall take all reasonable steps to obtain the best possible result for the UCITS, taking into account price, costs, speed, likelihood of execution and settlement, order size and nature, or any other consideration relevant to the execution of the order, and the relative importance of such factors shall be determined by reference to the following criteria -

- (a) the objectives, investment policy and risks specific to the UCITS, as indicated in the prospectus or as the case may be in the fund rules or articles of association of the UCITS;
- (b) the characteristics of the order;
- (c) the characteristics of the financial instruments that are the subject of that order;
- (d) the characteristics of the execution venues to which that order can be directed.

(3) For the purposes of sub-regulation (1) a management company shall—

- (a) establish and implement effective arrangements for complying with the obligation referred to in sub-regulation (2) in particular, it shall establish and implement a policy to allow it to obtain, for UCITS orders, the best possible result;

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- (b) obtain the prior consent of the investment company on the execution policy and shall make available appropriate information to unit-holders on the policy established in accordance with this regulation and on any material changes to its policy;
- (c) monitor on a regular basis the effectiveness of its arrangements and policy for the execution of orders in order to identify and, where appropriate, correct any deficiencies and shall review the execution policy on an annual basis and whenever a material change occurs that affects the management company's ability to continue to obtain the best possible result for the managed UCITS; and
- (d) be able to demonstrate that they have executed orders on behalf of the UCITS in accordance with the management company's execution policy.

Placing orders to deal on behalf of UCITS with other entities for execution

26.(1) The Authority shall authorise a management company to offer services subject to the requirement that it acts in the best interests of the UCITS it manages when placing orders to deal on behalf of the managed UCITS with other entities for execution, in the context of the management of their portfolios.

- (2) For the purposes of sub-regulation (1) –
 - (a) a management company shall take all reasonable steps to obtain the best possible result for the UCITS taking into account price, costs, speed, likelihood of execution and settlement, size, nature or any other consideration relevant to the execution of the order, and the relative importance of such factors are to be determined by reference to regulation 25(2);
 - (b) a management company shall establish and implement a policy to enable it to comply with the obligation referred to in paragraph (a) which shall identify, in respect of each class of instruments, the entities with which the orders may be placed and the management company shall only enter into arrangements for execution where such arrangements are consistent with obligations laid down in this regulation,

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and management companies shall make available to unit-holders appropriate information on the policy established in accordance with paragraph (b) and on any material changes to this policy.

- (3) Pursuant to sub-regulation (1), a management companies shall-
- (a) monitor on a regular basis the effectiveness of the policy established in accordance with sub-regulation (2)(b) and, in particular, the execution quality of the entities identified in that policy and, where appropriate, correct any deficiencies;
 - (b) review the policy on an annual basis or whenever a material change occurs that affects the management company's ability to continue to obtain the best possible result for the managed UCITS; and
 - (c) be able to demonstrate that it has placed orders on behalf of the UCITS in accordance with the policy established in accordance with sub-regulation (2)(b).

CHAPTER 4

HANDLING OF ORDERS

General principles

27.(1) The Authority shall authorise a management company to offer services subject to the requirement that it establishes and implements procedures and arrangements which provide for the prompt, fair and expeditious execution of portfolio transactions on behalf of the UCITS and satisfying the following conditions -

- (a) ensure that orders executed on behalf of UCITS are promptly and accurately recorded and allocated;
- (b) execute otherwise comparable UCITS orders sequentially and promptly unless the characteristics of the order or prevailing market conditions make this impracticable, or the interests of the UCITS require otherwise; and
- (c) financial instruments or sums of money, received in settlement of the executed orders are promptly and correctly delivered to the account of the appropriate UCITS.

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(2) For the purposes of sub-regulation (1), a management company shall not misuse information relating to pending UCITS orders, and shall take all reasonable steps to prevent the misuse of such information by any of its relevant persons.

Aggregation and allocation of trading orders

28.(1) The Authority shall authorise a management company to offer services subject to the requirement that it does not carry out a UCITS order in aggregate with an order of another UCITS or another client or with an order on its own account, unless the following conditions are met -

- (a) it must be unlikely that the aggregation of orders will work overall to the disadvantage of any UCITS or clients whose order is to be aggregated;
- (b) an order allocation policy must be established and implemented, providing in sufficiently precise terms for the fair allocation of aggregated orders, including how the volume and price of orders determines allocations and the treatment of partial executions.

(2) For the purposes of sub-regulation (1) –

- (a) where a management company aggregates a UCITS order with one or more orders of other UCITS or clients and the aggregated order is partially executed, it shall allocate the related trades in accordance with its order allocation policy;
- (b) where a management company which has aggregated transactions for own account with one or more UCITS or other clients' orders, it does not allocate the related trades in a way that is detrimental to the UCITS or another client;
- (c) where a management company aggregates an order of a UCITS or another client with a transaction for own account and the aggregated order is partially executed, it allocates the related trades to the UCITS or other client in priority over those for own account,

provided that where the management company is able to demonstrate to the UCITS or its other client on reasonable grounds that it would not have been able to carry out the order on such advantageous terms without aggregation, or at all, it may allocate the transaction for own account proportionally, in accordance with the policy as referred to in sub-regulation (1)(b).

CHAPTER 5

INDUCEMENTS

Safeguarding the best interests of UCITS

29.(1) A management company shall not be regarded for the purpose of these Regulations as acting honestly, fairly and professionally in accordance with the best interests of the UCITS if, in relation to the activities of investment management and administration to the UCITS, it pays or is paid any fee or commission, or provides or is provided with, any non-monetary benefit, other than the following -

- (a) a fee, commission or non-monetary benefit paid or provided to or by the UCITS or a person on behalf of the UCITS;
- (b) a fee, commission or non-monetary benefit paid or provided to or by a third party or a person acting on behalf of a third party, where the following conditions are satisfied -
 - (i) the existence, nature and amount of the fee, commission or benefit, or, where the amount cannot be ascertained, the method of calculating that amount, must be clearly disclosed to the UCITS in a manner that is comprehensive, accurate and understandable, prior to the provision of the relevant service;
 - (ii) the payment of the fee or commission, or the provision of the non-monetary benefit must be designed to enhance the quality of the relevant service and not impair compliance with the management company's duty to act in the best interests of the UCITS;
- (c) proper fees which enable or are necessary for the provision of the relevant service, including custody costs, settlement and exchange fees, regulatory levies or legal fees, and which, by their nature, cannot give rise to conflicts with the management company's duties to act honestly, fairly and professionally in accordance with the best interests of the UCITS.

(2) For the purposes of sub-regulation (1)(b)(i), a management company may disclose the essential terms of the arrangements relating to a fee, commission or non-monetary benefit in summary form, provided that the

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management company undertakes to disclose further details at the request of the unit-holder and provided that it honours that undertaking.

PART V

**PARTICULARS OF THE STANDARD AGREEMENT BETWEEN A
DEPOSITARY AND A MANAGEMENT COMPANY**

Elements related to the procedures to be followed by the parties to the agreement

30.(1) The parties to the agreement (as defined in sub-regulation (2)) shall include in the written agreement referred to in either regulation 20(5) or regulation 30(5) of the CIS Regulations the following particulars related to the services provided, and procedures to be followed, by the parties to the agreement—

- (a) a description of the procedures, including those related to the safe-keeping, to be adopted for each type of asset of the UCITS entrusted to the depositary;
- (b) a description of the procedures to be followed where the management company envisages a modification of the fund rules or prospectus of the UCITS, and identifying when the depositary should be informed, or where a prior agreement from the depositary is needed to proceed with the modification;
- (c) a description of the means and procedures by which the depositary will transmit to the management company all relevant information that the management company needs to perform its duties including a description of the means and procedures related to the exercise of any rights attached to financial instruments, and the means and procedures applied in order to allow the management company and the UCITS to have timely and accurate access to information relating to the accounts of the UCITS;
- (d) a description of the means and procedures by which the depositary will have access to all relevant information it needs to perform its duties;
- (e) a description of the procedures by which the depositary has the ability to enquire into the conduct of the management company and to assess the quality of information transmitted, including by way of on-site visits;

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- (f) a description of the procedures by which the management company can review the performance of the depositary in respect of the depositary's contractual obligations.

(2) In this Part, "parties to the agreement" means a depositary and a management company.

Elements related to the exchange of information and to obligations on confidentiality and money-laundering

31.(1) Parties to the agreement referred to in either regulation 20(5) or regulation 30(5) of the CIS Regulations to include the following elements related to the exchange of information and obligations on confidentiality and money laundering in that agreement -

- (a) a list of all the information that needs to be exchanged between the UCITS, its management company and the depositary related to the subscription, redemption, issue, cancellation and repurchase of units of the UCITS;
- (b) the confidentiality obligations applicable to the parties to the agreement;
- (c) information on the tasks and responsibilities of the parties to the agreement in respect of obligations relating to the prevention of money laundering and the financing of terrorism, where applicable.

(2) The obligations referred to in sub-regulation (1)(b) shall be drawn up by the parties to the agreement so as not to impair the ability of either the competent authority of a management company's EEA home State or the competent authority of the UCITS EEA home State in gaining access to relevant documents and information.

Elements related to the appointment of third parties

32. Where the depositary or the management company envisage appointing third parties to carry out their respective duties, both parties to the agreement referred to either in regulation 20(5) or regulation 33(5) of the CIS Regulations shall include at least the following particulars in that agreement—

- (a) an undertaking by both parties to the agreement to provide details, on a regular basis, of any third parties appointed by the

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depository or the management company to carry out their respective duties;

- (b) an undertaking that, upon request by one of the parties, the other party will provide information on the criteria used for selecting the third party and the steps taken to monitor the activities carried out by the selected third party;
- (c) a statement that a depository's liability as referred to in regulation 21 or regulation 31 of the CIS Regulations shall not be affected by the fact that it has entrusted to a third party all or some of the assets in its safe-keeping.

Elements related to potential amendments and the termination of the agreement

33. The parties to the agreement referred to in either regulation 20(5) or regulation 30(5) of the CIS Regulations shall include, in the agreement itself, the following particulars related to amendments and the termination of that agreement –

- (a) the period of validity of the agreement;
- (b) the conditions under which the agreement may be amended or terminated;
- (c) the conditions which are necessary to facilitate transition to another depository and, in case of such transition the procedure by which the depository shall send all relevant information to the other depository.

Applicable law

34. Parties to the agreement referred to either in regulation 20(5) or regulation 30(5) of the CIS Regulations shall specify that the law applicable to that agreement is that of the UCITS' EEA home State.

Electronic transmission of information

35. Where the parties to the agreement referred to in either regulation 20(5) or regulation 30(5) of the CIS Regulations agree to the use of electronic transmission for part or all of information that flows between them, such an agreement shall contain provisions ensuring that a record is kept of such information.

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Scope of the agreement

36. An agreement referred to in either regulation 20(5) or regulation 30(5) of the CIS Regulations may cover more than one UCITS managed by the management company and, in such a case, the agreement shall list the UCITS covered.

Service level agreement

37. The parties to the agreement shall include details of means and procedures referred to in regulation 30(c) and (d) above, either in the agreement referred to in either regulation 20(5) or regulation 30(5) of the CIS Regulations or in a separate written agreement.

PART VI

RISK MANAGEMENT

CHAPTER 1

RISK MANAGEMENT POLICY AND RISK MEASUREMENT

Risk management policy

38.(1) The Authority shall authorise a management company to offer services subject to the requirement that it establishes, implements and maintains an adequate and documented risk management policy which identifies the risks the UCITS it manages are or might be exposed to.

(2) The risk management policy referred to in sub-regulation (1) shall-

- (a) comprise such procedures as are necessary to enable the management company to assess for each UCITS it manages the exposure of that UCITS to market, liquidity and counterparty risks and the exposure of the UCITS to all other risks, including operational risks, which may be material for each UCITS it manages;
- (b) address the following elements-
 - (i) the techniques, tools and arrangements that enables the management company to comply with the obligations set out in regulations 40 and 41;

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- (ii) the allocation of responsibilities within the management company pertaining to risk management.

(3) For the purposes of sub-regulation (1), the risk management policy shall state the terms, contents and frequency of reporting of the risk management function referred to in regulation 12 to the board of directors and to senior management and, where appropriate, to the supervisory function.

(4) For the purposes of sub-regulations (1) and (2), a management company shall take into account the nature, scale and complexity of its business and of the UCITS it manages.

Assessment, monitoring and review of risk management policy

39.(1) The Authority shall authorise a management company to offer services subject to the requirement that it assesses, monitors and periodically reviews -

- (a) the adequacy and effectiveness of the risk management policy and of the arrangements, processes and techniques referred to in regulations 40 and 41;
- (b) the level of compliance by the management company with the risk management policy and with arrangements, processes and techniques referred to in regulations 40 and 41;
- (c) the adequacy and effectiveness of measures taken to address any deficiencies in the performance of the risk management process.

(2) For the purposes of sub-regulation (1), where Gibraltar is the management company's EEA home State, the management company shall notify to the Authority any material changes to the risk management process.

(3) The requirements of sub-regulation (1) shall be subject to review by the Authority on an on-going basis and accordingly when granting authorisation.

CHAPTER 2

**RISK MANAGEMENT PROCESSES, COUNTERPARTY RISK
EXPOSURE AND ISSUER CONCENTRATION**

Measurement and management of risk

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40.(1) The Authority shall authorise a management company to offer services subject to the requirement that it adopts adequate and effective arrangements, processes and techniques in order to -

- (a) measure and manage at any time the risks which the UCITS it manages are or might be exposed to;
- (b) ensure compliance with limits concerning global exposure and counterparty risk, in accordance with regulations 41 and 43,

in a manner which is proportionate to the nature, scale and complexity of the business of the management company and of the UCITS it manages and consistent with the UCITS risk profile.

(2) For the purposes of sub-regulation (1), a management company shall take the following actions for each UCITS it manages -

- (a) put in place such risk measurement arrangements, processes and techniques as are necessary to ensure that the risks of taken positions and their contribution to the overall risk profile are accurately measured on the basis of sound and reliable data and that the risk measurement arrangements, processes and techniques are adequately documented;
- (b) conduct, where appropriate, periodic back-tests in order to review the validity of risk measurement arrangements which include model-based forecasts and estimates;
- (c) conduct, where appropriate, periodic stress tests and scenario analyses to address risks arising from potential changes in market conditions that might adversely impact the UCITS;
- (d) establish, implement and maintain a documented system of internal limits concerning the measures used to manage and control the relevant risks for each UCITS taking into account all risks which may be material to the UCITS as referred to in regulation 38 and ensuring consistency with the UCITS risk-profile;
- (e) ensure that the current level of risk complies with the risk limit system as set out in paragraph (d) for each UCITS;
- (f) establish, implement and maintain adequate procedures that, in the event of actual or anticipated breaches to the risk limit

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system of the UCITS, result in timely remedial actions in the best interests of unit-holders.

- (3) For the purposes of sub-regulation (1), a management company shall—
- (a) employ an appropriate liquidity risk management process in order to ensure that each UCITS it manages is able to comply at any time with regulation 99(1) of the CIS Regulations;
 - (b) where appropriate, conduct stress tests which enable assessment of the liquidity risk of the UCITS under exceptional circumstances;
 - (c) ensure that for each UCITS it manages the liquidity profile of the investments of the UCITS is appropriate to the redemption policy laid down in the fund rules, the instruments of incorporation or the prospectus.

Calculation of global exposure

41.(1) The Authority shall authorise a management company to offer services subject to the requirement that it calculates the global exposure of a managed UCITS as referred to in regulation 48(3) of the CIS Regulations as either of the following -

- (a) the incremental exposure and leverage generated by the managed UCITS through the use of financial derivative instruments including embedded derivatives pursuant to regulation 48(4)(d) of the CIS Regulations, which may not exceed the total of the UCITS net asset value;
 - (b) the market risk of the UCITS portfolio.
- (2) For the purposes of sub-regulation (1) a management company –
- (a) shall calculate the UCITS global exposure on at least a daily basis;
 - (b) may calculate global exposure by using the commitment approach, the value at risk approach or other advanced risk measurement methodologies as may be appropriate, and for these purposes, "value at risk" shall mean a measure of the maximum expected loss at a given confidence level over a specific time period;

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- (c) shall ensure that the method selected to measure global exposure is appropriate, taking into account the investment strategy pursued by the UCITS and the types and complexities of the financial derivative instruments used, and the proportion of the UCITS portfolio which comprises financial derivative instruments,

provided that where a UCITS employs techniques and instruments including repurchase agreements or securities lending transactions in order to generate additional leverage or exposure to market risk in accordance with regulation 48(2) of the CIS Regulations, a management company shall take these transactions into consideration when calculating global exposure.

Commitment approach

42.(1) Where the commitment approach is used for the calculation of global exposure, a management company shall apply this approach to all financial derivative instrument positions including embedded derivatives as referred to in regulation 48(4)(d) of the CIS Regulations, whether used as part of the UCITS general investment policy, for purposes of risk reduction or for the purposes of efficient portfolio management as referred to in regulation 48(2) of the CIS Regulations.

(2) Where the commitment approach is used for the calculation of global exposure, a management company shall convert each financial derivative instrument position into the market value of an equivalent position in the underlying asset of that derivative (standard commitment approach), and, without prejudice to the foregoing, a management company may apply other calculation methods which are equivalent to the standard commitment approach.

(3) A management company shall take account of netting and hedging arrangements when calculating global exposure, where these arrangements do not disregard obvious and material risks and result in a clear reduction in risk exposure.

(4) Where the use of financial derivative instruments does not generate incremental exposure for the UCITS, the underlying exposure need not be included in the commitment calculation.

(5) Where the commitment approach is used, temporary borrowing arrangements entered into on behalf of the UCITS in accordance with regulation 98 of the CIS Regulations need not be included in the global exposure calculation.

Counterparty risk and issuer concentration

43.(1) The Authority shall authorise a management company to offer services subject to the requirement that it ensures that counterparty risk arising from an over-the-counter (OTC) financial derivative instrument is subject to the limits set out in regulation 49 of the CIS Regulations.

(2) When calculating the UCITS exposure to a counterparty within the limits referred to in regulation 49(1) of the CIS Regulations, a management company –

- (a) shall use the positive mark-to-market value of the OTC derivative contract with that counterparty;
- (b) may net the derivative positions of a UCITS with the same counterparty, provided that they are able to legally enforce netting agreements with the counterparty on behalf of the UCITS,

provided that netting shall only be permissible with respect to OTC derivative instruments with the same counterparty and not in relation to any other exposures the UCITS may have with that same counterparty.

(3) A management company may reduce the UCITS exposure to a counterparty of an OTC derivative transaction through the receipt of collateral which is sufficiently liquid to be sold quickly at a price that is close to its pre-sale valuation.

(4) A management company shall take collateral into account in calculating exposure to counterparty risk as referred to in regulation 49(1) of the CIS Regulations when the management company passes collateral to OTC counterparty on behalf of the UCITS, and collateral passed may be taken into account on a net basis only if the management company is able to legally enforce netting arrangements with this counterparty on behalf of the UCITS.

(5) A management company shall calculate issuer concentration limits as referred to in regulation 49 of the CIS Regulations on the basis of the underlying exposure created through the use of financial derivative instruments pursuant to the commitment approach.

(6) With respect to the exposure arising from OTC derivatives transactions as referred to in regulation 49(2) of the CIS Regulations a

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management company shall include in the calculation any exposure to OTC derivative counterparty risk.

CHAPTER 3

**PROCEDURES FOR THE VALUATION OF THE OTC
DERIVATIVES**

Procedures for the assessment of the value of OTC derivatives

44.(1) The Authority shall authorise a management company to offer services subject to the requirement that it verifies that UCITS exposures to OTC derivatives are assigned fair values that do not rely only on market quotations by the counterparties of the OTC transactions and which fulfil the criteria set out in Article 8(4) of Directive 2007/16/EC.

(2) For the purposes of sub-regulation (1), a management company shall—

- (a) establish, implement and maintain arrangements and procedures which ensure appropriate, transparent and fair valuation of UCITS exposures to OTC derivatives;
- (b) ensure that the fair value of OTC derivatives is subject to adequate, accurate and independent assessment;
- (c) ensure that the valuation arrangements and procedures are adequate and proportionate to the nature and complexity of the OTC derivatives concerned;
- (d) comply with the requirements set out in regulation 5(2) and regulation 23(4) when arrangements and procedures concerning the valuation of OTC derivatives involve the performance of certain activities by third parties.

(3) For the purposes of sub-regulations (1) and (2), the risk management function shall be appointed with specific duties and responsibilities.

(4) The valuation arrangements and procedures referred to in sub-regulation (2) shall be adequately documented by a management company.

CHAPTER 4

**TRANSMISSION OF INFORMATION ON DERIVATIVE
INSTRUMENTS**

Reports on derivative instruments

45.(1) The Authority shall authorise a management company to offer services subject to the requirement that it delivers to the Authority on an annual basis, reports containing information which reflects a true and fair view of the types of derivative instruments used for each managed UCITS, the underlying risks, the quantitative limits and the methods which are chosen to estimate the risks associated with the derivative transactions.

(2) The Authority shall review the regularity and completeness of information referred to in sub-regulation (1) and that it have an opportunity to intervene where appropriate.