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Ireland bolsters processes after EU delegation focus

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Asset managers seeking authorisation in Ireland will have to submit extra documents justifying their planned use of delegation to non-EU countries.

The Irish regulator yesterday announced plans to amend its authorisation procedures for funds and management companies seeking to delegate functions out of the country – one of the first signs that an EU drive to prevent letterbox entities is being followed by national regulators.

In future the Central Bank of Ireland will require firms seeking authorisation to provide “details and rationale for the geographical distribution of planned activities” and an “objective justification for delegation arrangements in relation to critical functions”.

Asset managers will also have to document information such as the remuneration paid to their non-EU delegates, the assessment of legal risk and how they undertake due diligence during the selection process.

They will also have to state “how best execution obligations continue to be met when dealing with execution outside of the EU”.

The planned changes to the central bank’s application forms and internal procedures are intended to reflect principles set out by the EU’s main securities regulator in guidelines published last year on asset managers’ use of delegation arrangements in the context of Brexit.

The European Securities and Markets Authority issued the guidance in response to fears that some national supervisors were engaging in a “race to the bottom” to attract Brexit-related business by allowing firms to establish lightly resourced structures in their jurisdiction and delegating key activities back to the UK.

The central bank says the changes to its internal procedures will ensure that “in relation to the Esma opinions, relevant facts underpinning outcomes are formally documented during our authorisation process”.

The Irish regulator’s move underlines that the EU’s Brexit-inspired scrutiny of delegation is being embedded in national regulatory practices, experts say.

Monica Gogna, partner at Dechert, says the central bank’s changes are “an indication that the review of delegation by EU regulators is not going to disappear”.

The move may spark fears that fund managers will increasingly face added “red tape” when seeking to delegate activities to non-EU countries.

The Esma opinion was fiercely criticised by some parts of the fund industry, notably the UK, for tightening the rules on delegation without justification.

David Morrey, partner at Grant Thornton in the UK, says: “The fact is that the wording on delegation expressed in the opinion is not how current delegation rules are applied in practice in most of the EU.”

John Adams, London-based partner at Shearman and Sterling, says the requirement in the Esma opinion for firms to justify the geographic distribution of their activities was “very odd”.

Mr Adams says: “Why shouldn't [...] a UK manager, or a US manager, or an Asian manager, be able to sub-manage a fund that focuses on continental EU markets?”

He expresses concern about the Irish regulator’s decision to incorporate that requirement into its authorisation procedures.

Mr Morrey says the central bank’s review of its processes could represent “a genuine toughening” of the regulator’s authorisation process, which “may make it harder for delegation to take place in practice”.

The Irish regulator “could look at the reasons firms give for delegating to the UK and say there is not a strong enough geographical basis for that delegation, and it needs to be changed”, he says.

However, Mr Morrey adds that it is equally possible that the Irish regulator is “window dressing [in other words] tweaking its forms to show it is considering the Esma opinion by asking the right questions”.

Despite the specification of new requirements, it is possible that the central bank “[will not] be any harder on delegation than they have been historically”, says Mr Morrey.

Neil Simmonds, partner at London law firm Simmons & Simmons, says the central bank’s statement is a formalisation of existing practices rather than a significant tightening of standards.

“We would not expect much in the way of practical implications affecting the ability of Ireland-regulated management companies to delegate portfolio management to managers in the UK, the US or other sensible jurisdictions,” says Mr Simmonds.

But Attilio Veneziano, founder of London-based law firm Veneziano & Partners, says the central bank’s stance shows that the EU’s scrutiny of delegation and substance is “here to stay”.

He says requirements for more explicit justification of delegation arrangements should not be seen “as a barrier, rather an organic evolution within the EU financial services rulebook”.

For example he notes that the Alternative Investment Fund Managers Directive, which came into force in 2013, contained requirements for managers to explain the geographic location of their activities.

But Ms Gogna warns that fund firms’ long-term priority will be ensuring this extra scrutiny does not go too far and explicitly limit the use of delegation by global asset managers.

There are already signs that the EU intends to continue to look at delegation and take steps in addition to the Esma opinion.

The bloc is currently [working](#) on legislation that, if approved, would give Esma the ability to review asset managers' use of delegation to non-EU countries.

The commission also [indicated](#) last year that it is open to the idea of enshrining stricter rules on delegation to the Ucits directive – a move that would aim to mirror AIFMD, which has a definition of what constitutes a letterbox entity.

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