



**Financial Services
Commission**

Information page

Alternative Investment Fund Managers Directive Operating conditions – Conflicts of interest

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Any advice or interpretation covered in this information page represents the views of the FSC as to its expectations of how the requirements of the AIFMD are to be complied with and/or how it fails to be applied. This however is not intended as a definitive interpretation of the AIFMD which is ultimately a matter for the courts to determine. The FSC does not provide, or purport to offer, legal advice.



1. Introduction

- 1.1 In this information page, reference is made to the Alternative Investment Fund Managers Directive 2011/61/EU (“AIFMD”) and to the supplementing Level 2 Delegated Regulation (“Level 2”).
- 1.2 The AIFMD requires Alternative Investment Fund Managers (“AIFMs”) to operate in accordance with conditions set out in the AIFMD and Level 2. The purpose of this information page is to provide AIFMs with clear information, based on the information on the AIFMD and Level 2, on what requirements and conditions they must comply with in relation to identifying, preventing, managing and monitoring conflicts of interest that arise in the course of managing an AIF.
- 1.3 AIFMs should consider the contents of this information page together with the remainder of the AIFMD as provisions on conflicts of interest also appear in other areas such as, for example, delegation, depositaries and risk management. For further information on all areas of the AIFMD, please visit the FSC’s AIFMD informational website: www.fsc.gi/firms/aifmd.htm.

2. Conflicts of interest

Article 14 of the AIFMD

- 2.1 AIFMs must take all reasonable steps to identify conflicts of interest that arise in the course of managing AIFs between:
 - (a) the AIFM, including its managers, employees or any person directly or indirectly linked to the AIFM by control, and the AIF managed by the AIFM or the investors in that AIF;
 - (b) the AIF or the investors in that AIF, and another AIF or the investors in that AIF;
 - (c) the AIF or the investors in that AIF, and another client of the AIFM;
 - (d) the AIF or the investors in that AIF, and a UCITS managed by the AIFM or the investors in that UCITS; or
 - (e) two clients of the AIFM.
- 2.2 AIFMs must maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps designed to identify, prevent, manage and monitor conflicts of interest in order to prevent them from adversely affecting the interests of the AIFs and their investors.
- 2.3 AIFMs must segregate, within their own operating environment, tasks and responsibilities which may be regarded as incompatible with each other or which may potentially generate systematic conflicts of interest.
- 2.4 AIFMs must assess whether their operating conditions may involve any other material conflicts of interest and disclose them to the investors of the AIFs.
- 2.5 Where organisational arrangements made by an AIFM to identify, prevent, manage and monitor conflicts of interest are not sufficient to ensure, with reasonable confidence, that risks of damage to investors’ interests will be prevented, the AIFM must clearly disclose the general nature or sources of

conflicts of interest to the investors before undertaking business on their behalf, and develop appropriate policies and procedures.

- 2.6 Where the AIFM on behalf of an AIF uses the services of a prime broker, the terms shall be set out in a written contract; and:
- (a) in particular, any possibility of transfer and reuse of AIF assets must be provided for in that contract and must comply with the AIF rules or instruments of incorporation, and
 - (b) the contract must provide that the depositary be informed of the contract.
- 2.7 AIFMs must exercise due skill, care and diligence in the selection and appointment of prime brokers with whom a contract is to be concluded.
- 2.8 In summary, AIFMs must take all reasonable steps to avoid conflicts of interest and, where such conflicts cannot be avoided, to identify, manage, monitor and, where applicable, disclose those conflicts of interest in order to prevent them from adversely affecting the interests of the AIFs and their investors and to ensure the fair treatment of the AIFs and the investors of the AIFs.

3. Types of conflicts of interest

Article 30 of Level 2

- 3.1 For the purpose of identifying the types of conflicts of interest that arise in the course of managing an AIF, AIFMs shall take into account, in particular, whether the AIFM, a relevant person or a person directly or indirectly linked by way of control to the AIFM:
- (a) is likely to make a financial gain, or avoid a financial loss, at the expense of the AIF or its investors;
 - (b) has an interest in the outcome of a service or an activity provided to the AIF or its investors or to a client or of a transaction carried out on behalf of the AIF or a client, which is distinct from the AIF's interest in that outcome;
 - (c) has a financial or other incentive to favour:
 - the interest of a UCITS, a client or group of clients or another AIF over the interest of the AIF;
 - the interest of one investor over the interest of another investor or group of investors in the same AIF;
 - (d) carries out the same activities for the AIF and for another AIF, a UCITS or client; or
 - (e) receives or will receive from a person other than the AIF or its investors an inducement in relation to collective portfolio management activities provided to the AIF, in the form of monies, goods or services other than the standard commission or fee for that service.
- 3.2 The 'relevant person' in relation to an AIFM means any of the following:
- (a) a director, partner or equivalent, or manager of the AIFM;
 - (b) an employee of the AIFM, or any other natural person whose services are placed at the disposal and under the control of the AIFM and who is

involved in the provision of collective portfolio management services by the AIFM;

- (c) a natural or legal person who is directly involved in the provision of services to the AIFM under a delegation arrangement to third parties for the purpose of the provision of collective portfolio management by the AIFM.

4. Conflicts of interest policy

Article 31 of Level 2

- 4.1 The AIFM shall establish, implement and apply an effective conflicts of interest policy. That policy shall be set out in writing and shall be appropriate to the size and organisation of the AIFM and the nature, scale and complexity of its business.
- 4.2 Where the AIFM is a member of a group, the policy shall also take into account any circumstances of which the AIFM 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.
- 4.3 The conflicts of interest policy established in accordance with section 4.1 shall include the following:
 - (a) with reference to the activities carried out by or on behalf of the AIFM, including activities carried out by a delegate, sub-delegate, external valuer or counterparty, identification of the circumstances which constitute or may give rise to a conflict of interest entailing a material risk of damage to the interests of the AIF or its investors;
 - (b) procedures to be followed and measures to be adopted in order to prevent, manage and monitor such conflicts.

5. Conflicts of interest related to the redemption of investments

Article 32 of Level 2

- 5.1 The AIFM that manages an open-ended AIF shall identify, manage and monitor conflicts of interest arising between investors wishing to redeem their investments and investors wishing to maintain their investments in the AIF, and any conflicts between the AIFM's incentive to invest in illiquid assets and the AIF's redemption policy in accordance with its obligations under section 2.1 above.

6. Procedures and measures preventing or managing conflicts of interest

Article 33 of Level 2

- 6.1 The procedures and measures established for the prevention or management of conflicts of interest shall be designed to ensure that the relevant persons

engaged in different business activities involving a risk of conflict of interest carry out these activities having a degree of independence which is appropriate to the size and activities of the AIFM and of the group to which it belongs, and to the materiality of the risk of damage to the interests of the AIF or its investors.

- 6.2 Where necessary and appropriate for the AIFM to ensure the requisite degree of independence, the procedures to be followed and measures to be adopted in accordance with section 4.3(b) above shall include the following:
- (a) effective procedures to prevent or control the exchange of information between relevant persons engaged in collective portfolio management activities or other activities pursuant to Article 6(2) and (4) of Directive 2011/61/EU (on the authorised activities and services of the AIFM) involving a risk of conflict of interest where the exchange of information may harm the interest of one or more AIFs or their investors;
 - (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 investors, whose interests may conflict, or who otherwise represent different interests that may conflict, including those of the AIFM;
 - (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 restrain 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 or other activities pursuant to Article 6(2) and (4) of Directive 2011/61/EU (on the authorised activities and services of the AIFM) where such involvement may impair the proper management of conflicts of interest.

Where the adoption or the application of one or more of those measures and procedures does not ensure the requisite degree of independence, the AIFM shall adopt such alternative or additional measures and procedures as are necessary and appropriate for those purposes.

7. Managing conflicts of interest

Article 34 of Level 2

- 7.1 Where the organisational or administrative arrangements made by the AIFM are not sufficient to ensure, with reasonable confidence, that risks of damage to the interests of the AIF or investors in the AIF are prevented, the senior management or other competent internal body of the AIFM shall be promptly informed in order to take any necessary decision or action to ensure that the AIFM acts in the best interests of the AIF or the investors in that AIF.

8. Monitoring conflicts of interest

Article 35 of Level 2

- 8.1 The AIFM shall keep and regularly update a record of the types of activities undertaken by or on behalf of the AIFM in which a conflict of interest entailing a material risk of damage to the interests of one or more AIFs or its investors has arisen or, in the case of an on-going activity, may arise.
- 8.2 Senior management shall receive on a frequent basis, and at least annually, written reports on activities referred to in section 8.1.

9. Disclosure of conflicts of interest

Article 36 of Level 2

- 9.1 The information to be disclosed to investors in accordance with section 2.1 and 2.2 above shall be provided to investors in a durable medium or displayed on a website.
- 9.2 Where information referred to in section 9.1 is displayed on a website and is not addressed personally to the investor, the following conditions shall be satisfied:
- (a) the investor has been notified of the address of the website, and the place on the website where the information may be accessed, and has consented to the provision of the information by such means;
 - (b) the information must be up to date;
 - (c) the information must be accessible continuously by means of that website for such period of time as the investor may reasonably need to review it.

10. Strategies for the exercise of voting rights

Article 37 of Level 2

- 10.1 An AIFM shall develop adequate and effective strategies for determining when and how any voting rights held in the AIF portfolios it manages are to be exercised, to the exclusive benefit of the AIF concerned and its investors.
- 10.2 The strategy referred to in section 10.1 shall determine measures and procedures for:
- (a) monitoring relevant corporate actions;
 - (b) ensuring that the exercise of voting rights is in accordance with the investment objectives and policy of the relevant AIF;
 - (c) preventing or managing any conflicts of interest arising from the exercise of voting rights.
- 10.3 A summary description of the strategies and details of the actions taken on the basis of these strategies shall be made available to the investors on their request.



11. Application of implementing measures

Any measures adopted by the European Union Commission under Article 14(4) of the AIFMD will also be applicable.