

19 August 2016

Attn: The Directors and Compliance Officers of Collective Investment Schemes, Fund Managers, Custodians and Fund Administrators

Dear Sir/ Madam,

Re: Circular on Offsite Supervision - Correspondence with the Funds Supervision Team

Introduction

The Funds Supervision Team (which forms part of the Securities and Markets Supervision Unit ("SMSU") at the MFSA) is responsible for the supervision of collective investment schemes ("CISs") and their service providers, namely Fund Managers, Custodians and Fund Administrators (collectively referred to as the "Licence Holders" or "Investment Services Providers"). The Funds Supervision Team receives a large volume of correspondence relating to offsite supervision on an ongoing basis and such correspondence covers a variety of topics/issues including breaches, pricing errors, resignations, requests for derogations and other compliance, risk and governance issues. The volumes of correspondence that we receive are increasing, and the levels of standard of such correspondence vary, whereby some requests are comprehensive and contain well-grounded recommendations and in other cases the Funds Supervision Team has to engage in lengthy correspondence with the Licence Holders and/ or their advisors.

The purpose of this letter is to set out below a number of recommendations that address common deficiencies that we have identified when we receive correspondence from Licence Holders and their advisors. Naturally the list below is not exhaustive and for the avoidance of doubt, it is not to be interpreted that if one adheres to the guidance set out herein, an approval from MFSA would be forthcoming or that no further documentation would be requested.

1. Submission for Annual Report and Audited Financial Statements and Interim Financial Statements (collectively referred to as "Financial Statements")

The Authority expects that Financial Statements are submitted within the deadline/ the periods set out in the relevant Investment Services Rules. Moreover, no submission of Financial Statements is to be made to the Authority until a full set of the required documents is available and all the required signatures have been obtained. Where,



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exceptionally, the submission of the Financial Statements is going to be justifiably delayed, the Funds Supervision Team should be informed and requested to consider such delay. The request is to be accompanied by:

- a) a Board of Directors Resolution from the Scheme/ Fund Manager/ Custodian/ Fund Administrator setting out clearly the reasons which justify the delay and requesting MFSA to grant the proposed extension period which should be clearly stated in the Resolution;
- b) (in case of a financial statements of CISs) written confirmation from the Fund Administrator that the underlying investors of the Scheme have been informed of the delay and the reasons for such delay; and
- c) written confirmation from the external auditor of the Scheme/ Fund Manager/ Custodian/ Fund Administrator stating that it supports the request for extension and that the audit will be completed within the proposed extended deadline.

Licence Holders should aim to submit such request to the MFSA at least one week prior to the submission deadline. Where the delay is only minor (say a few days), documents (a) to (c) need not be submitted.

2. Breaches

Communication to the MFSA informing us of breaches should, as a minimum, include:

- a) the SLC or investment restriction breached (in case of advertent breaches) and what it briefly states;
- b) date/period when breach occurred, and when/by whom it was discovered;
- c) nature of the breach (how it occurred);
- d) impact of the breach on the Scheme/ Sub-Fund and its underlying investors – if there was a loss to the Scheme/ Sub-Fund and/or investors, this should be quantified;
- e) remedial measures being adopted / proposed;
- f) in the case of retail CISs, confirmation from the Custodian that this entity has checked workings and is in agreement with remedial measures being adopted; and
- g) action taken to prevent recurrence of the breach.

3. Suspension of Dealings and NAV

Communication informing the Authority of the suspension of dealings and determination of NAV of a Scheme/ Sub-Fund should *inter alia* include:

- a) reason for suspension of dealings and NAV determination;
- b) confirmation from the Fund Administrator that the underlying investors of the Scheme/ Sub-Fund have been informed of the suspension;

- c) supporting resolution of the Scheme confirming that the suspension has been approved by the Board of Directors;
- d) confirmation that any provisions relating to the suspension of dealings and NAV determination in the offering documentation and constitutional documents of the Scheme have been fully adhered to;
- e) envisaged time frame by when the suspension of dealings and NAV is expected to be lifted.

Please note that documents (b) and (c) need not be submitted when the suspension of dealing is for one day/ few days as a result of closures of the main markets where the Scheme/ Sub-Fund invests in, or closures of the main exchanges where the assets of the Scheme/Sub-Fund are traded.

4. Valuation (NAV Calculation) Errors

The Authority applies a materiality concept of 0.5% in the context of valuation errors which require notification.

Communication informing the Authority of a valuation error should, *inter alia*, include:

- a) how the valuation occurred;
- b) date of identification and full details of Dealing Day affected;
- c) details of the financial impact of the valuation error and/or where subscriptions/ redemptions were dealt with wrong prices/ valuations;
- d) details of any remedial measures which result from the valuation errors for the Scheme/ Sub-Fund and/or its investors; and
- e) the communications to be made to the investors (particularly if remedial measures are adopted).

5. Derogation from Investment Services Rules

A request for a derogation from any specific Rule should include:

- a) specific SLC and what it briefly states;
- b) reason why a derogation is being requested;
- c) (in case of derogation from the Rules applicable to CISs) what are the risks to the Scheme/ Sub-Fund and the investors if the derogation is approved and how can these risks be mitigated;
- d) expected duration of the derogation. Please note that open ended derogations will be not be issued and we would ordinarily expect a derogation not to exceed two years. In this respect, it is the Licence Holder's ongoing responsibility to assess whether the derogation is still required at the time it expires. In case the Licence Holder deems that

the derogation is still appropriate and required, it is expected to formally submit to the Funds Supervision Team an updated assessment prior to the expiry date of such derogation; and

- e) resolution from the Board of Directors of the Scheme confirming its support for the request.

6. Resignations

It is a regulatory requirement to inform the Authority in case of a departure of a Director or Senior Manager¹, Committees Member, Portfolio Manager, Compliance Officer, Money Laundering Reporting Officer or Risk Manager, as stipulated by the applicable Standard Licencing Conditions under the relevant Rulebook. The following documents are to be submitted to the Funds Supervision Team:

- a) Formal notification in writing from the Licence Holder of the departure of any of the officials indicated above within 14 days of the departure. This notification should include the following:
 - i. the name and role of the official departing;
 - ii. reason of departure (resignation, dismissal, organisational structure change etc.);
 - iii. the effective date of resignation; and
 - iv. the proposed replacement.
- b) The Licence Holder shall also request the departing official **to confirm in writing directly to the Funds Supervision Team** whether the departure has any regulatory implications, or if otherwise to provide any relevant details. Furthermore, the departing official shall confirm in writing to the Fund Supervision Team points (i) to (iii) above. The communication from the departing official shall be submitted to the Authority in original.

Approvals of replacements of departing officials of Collective Investment Schemes, Fund Managers, Custodian and Fund Administrators need to be directed to the Authorisations Unit.

The Licence Holder shall ensure that the relevant forms related to the departure and approval of officials (where applicable) are filed with the Registry of Companies.

¹ 'Senior Manager' should be interpreted as the person occupying the most senior role following that of Director, so that in the case where there are various management grades, it is the most senior manager who will require the MFSA's authorisation.

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Conclusion

We trust that the contents of this circular provide a good insight of what the Authority expects as minimum standards in respect of offsite supervision correspondence. Adherence by Licence Holders these minimum standards would help improve operational effectiveness, efficiency and response time. We thank you in advance for your co-operation.

Contacts

Any queries or requests for clarifications in relation to this circular are to be addressed to Mr Joseph J Agius - Deputy Director, Securities & Markets Supervision Unit, on +356 2548 5535 or jagius@mfsa.com.mt.



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Director
Securities & Markets Supervision Unit