

INVESTMENT SERVICES RULES FOR ALTERNATIVE INVESTMENT FUNDS

PART B: STANDARD LICENCE CONDITIONS APPLICABLE TO ALTERNATIVE INVESTMENT FUNDS

APPLICABILITY OF PART B OF THE INVESTMENT SERVICES RULES

Part B of the Investment Services Rules for Alternative Investment Funds shall apply as follows:

- [I] Sections 1 to 7 shall apply to all AIFs whether these have appointed an external AIFM or are self-managed AIFs;
- [II] Section 8 shall apply **exclusively** to self-managed AIFs. Therefore, self-managed AIFs are expected to comply with **all** the sections prescribed in this Part B of the Rules.

APPLICABILITY OF REGULATION (EU) NO. 345/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL OF 17 APRIL 2013 ON EUROPEAN VENTURE CAPITAL FUNDS AND OF REGULATION (EU) NO. 346/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL OF 17 APRIL ON EUROPEAN SOCIAL ENTREPRENEURSHIP FUNDS

An AIF established as:

- [I] a European Venture Capital Fund in terms of Regulation (EU) No 345/2013 of the European Parliament and of the Council of 17 April 2013 on European Venture Capital Funds; or
- [II] a European Social Entrepreneurship Fund in terms of Regulation (EU) No 346/2013 of the European Parliament and of the Council of 17 April 2013 on European Social Entrepreneurship Funds

shall also refer to and comply with the applicable provisions prescribed in the aforementioned Regulations in addition to the SLCs prescribed in this Rulebook.

1. GENERAL REQUIREMENTS

- 1.01 Every AIF shall comply with the provisions of the Investment Services Act, the Regulations and the Investment Services Rules issued thereunder. An AIF may be managed in one of two ways :
- a) By an external manager, which is the legal person appointed by the AIF or on behalf of the AIF and which through this appointment is responsible for managing the AIF also referred to as “external AIFM”; or
 - b) Where the legal form of the AIF permits an internal management, and where the AIF’s governing body chooses not to appoint an external AIFM, by the AIF itself, which shall be licenced as a self-managed AIF.
- 1.02 Apart from the conditions listed in this Part of the Rules, where the AIF adopts different structures and strategies it shall also be subject to the supplementary conditions applicable to specific types of AIFs as prescribed in Appendix 1. In the case of umbrella AIFs, reference to the AIF shall be construed, where applicable, as reference to the sub-funds of the AIF.
- 1.03 The AIF shall commence its activities within 12 months of the date of issue of the Collective Investment Scheme Licence. If, for any reason the AIF is not in a position to comply with this condition, it shall notify the MFSA in writing setting out the reason(s) for such a delay indicating the proposed date of commencement of business. On the basis of the information provided and the circumstances of the case, the MFSA may decide to suspend or cancel the Licence in accordance with the relevant provisions of the Act.
- 1.04 The AIF shall co-operate in an open and honest manner with the MFSA and inform it promptly of any relevant information. The AIF shall supply the MFSA with such information and returns as the MFSA requires to monitor compliance with the conditions referred to in the Act and any rules and regulations issued thereunder.
- 1.05 Where a Standard Licence Condition demands that the AIF notifies the MFSA of an event, such notification shall be made to the MFSA formally, in a durable medium. The request to notify the MFSA of an event shall not be satisfied merely by the fact that the information which ought to be notified to the MFSA is included in a standard regulatory return.
- 1.06 The AIF shall notify the MFSA in writing of:
- a) a change in the AIF’s name or business name (if different) at least one month in advance of the change being made;
 - b) a change of address: at least one month in advance;

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- c) any material changes to the conditions for initial authorisation, in particular material changes to the information provided during the application process at least one month in advance of the change being made;
- d) the departure of a Director or Senior Manager, Portfolio Manager, Compliance Officer, Money Laundering Reporting Officer and Risk Manager within 14 days of the departure. The AIF shall also request the Director or Senior Manager to confirm to MFSA that their departure had no regulatory implications or to provide relevant details as appropriate. A copy of such request shall be provided to MFSA together with the AIF's notification of departure;
- e) any proposed material change to its business (whether that business constitutes licensable activity under the Act or not) – at least one month before the change is to take effect (where a new or amended Investment Services Licence/Collective Investment Scheme Licence is required, the new business shall not begin until the new Investment Services Licence/Collective Investment Scheme Licence has been granted or the amendment has been approved);
- f) a decision to make a material claim on any insurance policy held in relation to the AIF's business. Notification should be provided as soon as the decision is taken;
- g) any actual or intended legal proceedings of a material nature by or against the AIF immediately after the decision has been taken or on becoming aware of the matter;
- h) the fact, where applicable, that it has not provided any Investment Service or carried out any investment activity for the preceding six months, setting out the reasons for such inactivity and providing a business plan for future activity; and
- i) any other material information concerning the AIF, its business or its officials in Malta or abroad – immediately upon becoming aware of the matter.

1.07 The AIF shall obtain the written consent of the MFSA before:

- a) taking any steps to cease its operations;
- b) agreeing to sell or merge the whole or any part of its undertaking;
- c) making an application to a Regulator abroad to undertake any form of licensable activity outside Malta;

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- d) the appointment of a Director or Senior Manager, Compliance Officer, Money Laundering Reporting Officer and (and where the AIF is self-managed, also of a Risk Manager, Investment Committee Member, Portfolio Manager and Investment Advisor - where the Investment Advisor is an individual) in advance. The request for consent shall be accompanied by a Personal Questionnaire in the form set out in Schedule 2 to Part A of these Rules – duly completed by the person proposed. The individual proposed as investment advisor (to a self-managed AIF) need not complete the Personal Questionnaire.

In the case of a proposed Portfolio Manager, Compliance Officer, Money Laundering Reporting Officer (and where the AIF is self-managed, also of a Risk Manager, Investment Committee Member, Portfolio Manager and Investment Advisor - where the Investment Advisor is an individual) - the request shall also be accompanied by the Competency Form set out in Schedule 3 to Part A of these Rules duly completed by the person proposed.

Where the person proposed had within the previous five years submitted a PQ to the MFSA, the request for consent need not be accompanied by a new PQ. In such instances, it shall be accompanied by a confirmation by the proposed person as to whether the information included in the PQ previously submitted is still current, and indicating any changes or up-dates thereto. This confirmation is to be countersigned by an authorised official of the Licence Holder, confirming that he/she has seen the said PQ.

For the purposes of (d) above and (e) below, ‘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.

- e) the change in the responsibilities of a Director or Senior Manager in advance. The request for consent of the change in responsibilities of a Director or Senior Manager shall be accompanied by a PQ unless the individual concerned had within the previous three years submitted a PQ to the MFSA in connection with another role occupied by such individual with the same AIF, in which case it shall be accompanied by a confirmation by the Director or Senior Manager as to whether the information included in the PQ previously submitted is still current, and indicating any changes or updates thereto:

Provided that a change in the responsibilities of a Director or Senior Manager should only be notified to the MFSA when such a change is material, which shall include a change in the status or seniority of the person concerned (upwards or downwards).

- 1.08 The AIF shall co-operate fully with any inspection or other enquiry carried out by, or on behalf of the MFSA and inform it promptly of any relevant information. The AIF shall provide the MFSA with such information as the MFSA may require.

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- 1.09 The AIF shall pay promptly all amounts due to the MFSA. The Supervision Fee shall be payable by the AIF on the day the Licence is first issued and, thereafter annually within one week from the anniversary of that date.
- 1.10 The MFSA shall be notified of any breach of the Licence Conditions or of any of the provisions of the Offering Document or Constitutional Documents of the AIF as soon as the AIF becomes aware of the breach.
- 1.11 The AIF – or the AIFM or Administrator on its behalf – shall submit copies of the AIF’s annual audited financial statements.
- 1.12 The AIF shall disclose the identity of the regulated entity and its regulator or regulators in all correspondence, advertisements and other documents. Wording similar to the following shall be used: “Licenced by the MFSA as an Alternative Investment Fund.”
- 1.13 The MFSA shall not be liable in damages for anything done or omitted to be done unless the act or omission is shown to have been done or omitted to be done in bad faith.
- 1.14 The MFSA has the right from time to time, and following advance notification to the AIF, to vary or revoke any Licence Condition or impose new conditions.
- 1.15 The AIF shall not be required to make public the issue and redemption prices of its Units or Shares. However, these must be made available to unit-holders upon request.
- 1.16 If the dealings in the Units or Shares are suspended, the AIF – or the AIFM or the Administrator on its behalf – shall inform the MFSA forthwith stating the reason for this suspension.
- 1.17 The AIF, its AIFM or Administrator on its behalf shall keep such accounting and other records as are necessary to enable it to comply with these conditions and to demonstrate that compliance has been achieved. Accounting records shall be retained for a minimum period of ten years. During the first two years, they shall be kept in a place from which they can be produced within two working days of their being requested. After the first two years, they shall be kept in a place from which they can be produced within five working days of their being requested.
- 1.18 In the event of a winding up, the AIF must give the MFSA at least two weeks’ notice of this intention. The prior approval of the MFSA shall be obtained for the approach to be adopted. If requested to do so by the MFSA, the AIF shall do all in its power to delay the winding-up or to proceed with the winding up in accordance with the conditions imposed by the MFSA.

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- 1.19 Any changes to the financial year-end of the AIF shall be notified to the MFSA and disclosed in the Offering Document.

2. Governing Body of the AIF

- 2.01 The Governing Body of the AIF (which includes the Board of Directors, Trustee, or General Partners where applicable) shall be responsible for ensuring that the AIF complies with its obligations under these Rules.
- 2.02 The Governing Body of the AIF shall be composed of one or more directors independent of the AIFM and the Custodian.
- 2.03 The MFSA shall be satisfied on a continuing basis of the fitness and properness of the members of the Governing Body.
- 2.04 The members of the Governing Body shall act honestly and in good faith in what they consider to be the best interests of the AIF and its investors.
- 2.05 The members of the Governing Body shall exercise reasonable care, skill and diligence.
- 2.06 The members of the Governing Body have, both collectively as a Board and individually, an obligation to acquire and maintain sufficient knowledge and understanding of the AIF's business to enable them to discharge their functions as directors.
- 2.07 The Governing Body must not merely carry out a vetting function with regards to all the documents which are submitted for its attention. It is the duty of the Governing Body of an AIF to inform itself of its investment activities and have a proper understanding of its financial condition.
- 2.08 The Members of the Governing Body shall exercise the powers they have for the purposes for which such powers were conferred and they shall not misuse such powers.
- 2.09 The Governing Body shall exercise its powers independently without subordinating such powers to the will of others.
- 2.10 Whilst the Governing Body of an AIF may be entitled under the memorandum and articles of association to delegate particular functions, the delegation of such functions shall not absolve the Governing Body from the duty to supervise the discharge of such delegated functions.
- 2.11 The members of the Governing Body shall carry out all the necessary checks to satisfy themselves that the overall structure of the AIF is consistent with the standards prescribed in the Act and in these Rules and that the terms agreed to in the contracts with the service providers are reasonable and consistent with the standards adopted by the industry. Furthermore, the Governing Body must ensure that all the service providers appointed in relation to the AIF create an overall structure which will ensure an adequate division of responsibilities in relation to the fund.

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- 2.12 The Governing Body shall continuously monitor the execution of the functions delegated to the service providers and shall be satisfied that they are performing their functions in accordance with their contractual obligations.
- 2.13 The members of the Governing Body shall hold regular board meetings and shall ensure that detailed minutes are taken to record accurately the matters discussed and considered. The agenda should be well structured and prepared, giving sufficient time to allow for the input of all the notice parties and service providers before the meeting.
- 2.14 Minutes of the meetings of the Governing Body must be held in Malta at the registered office of the AIF or at any other place as may be agreed with the MFSA.
- 2.15 The Governing Body shall also be guided by the provisions of the Corporate Governance Manual for Directors of Investment Companies and Collective Investment Schemes which has been issued by the Authority.

3. SERVICE PROVIDERS

- 3.01 An AIF may appoint service providers as it deems necessary. The AIF is obliged to appoint an AIFM, a Custodian, an Auditor, a Compliance Officer and a Money Laundering Reporting Officer.
- 3.02 The MFSA shall be satisfied on a continuing basis of the fitness and properness of any service provider appointed by the AIF.
- 3.03 The AIF together with the service providers appointed shall comply with the applicable laws whether Maltese or EU Related to which they may respectively be subject.

The AIFM

- 3.04 The AIF may appoint a single external AIFM with responsibility for portfolio management and risk management of the AIF and other permitted services. The AIFM shall be duly authorised in terms of the AIFMD.
- 3.05 The AIFM may either have an established place of business in Malta or be a European AIFM. If established in Malta, it shall be in possession of a Category 2 Investment Services Licence issued in terms of Article 6 of the Act and authorised by the MFSA as an AIFM in terms of the AIFMD.
- 3.06 Where an AIF does not appoint an external AIFM, it shall be subject to all the Standard Licence Conditions prescribed in this Part to the Rules, including the supplementary conditions applicable to Self-Managed AIFs prescribed in Section 8 of these Rules.
- 3.07 The AIFM shall have sufficient financial resources and liquidity at its disposal to enable it to conduct its business, and such organisation, systems, experience and expertise deemed necessary by the MFSA for it to act as AIFM. The AIF shall be required to satisfy the MFSA that the proposed AIFM meets the above requirements on a continuing basis.
- 3.08 An AIF may appoint a European AIFM in accordance with the Investment Services Act (Alternative Investment Fund Manager Passport) Regulations, 2013. A European AIFM may seek to establish a branch in Malta or provide services pursuant to Regulations 6 and 7 of the said Regulations.
- 3.09 The appointment and/ or replacement of any party who is to be the AIFM of the AIF, the terms of that appointment and the contents of the agreement to which the appointment is subject, shall be agreed with the MFSA. The MFSA shall have the right to require the replacement of the AIFM.

- 3.10 The AIF shall be subject to investment objectives, policies and restrictions outlined in its Offering Document. The AIFM shall take all reasonable steps to comply with the investment policies and restrictions of the AIF.

Fund Administrator

- 3.11 The AIF (including self-managed AIF) or the AIFM may appoint an Administrator. Where an Administrator is not appointed, the AIFM shall be responsible for the Administration function (subject to the AIFM being authorised to undertake fund administration activities).
- 3.12 Where the proposed Fund Administrator is established in Malta, it should be in possession of a Fund Administration Recognition Certificate issued in terms of Article 9A of the Act.
- 3.13 The Fund Administrator shall have the business organisations, systems, experience and expertise deemed necessary by the MFSA for it to act as a Fund Administrator. The AIF shall satisfy the MFSA that the proposed Fund Administrator meets the above requirements.

Custodian

- 3.14 A single Custodian shall be appointed for each AIF in accordance with the following SLCs.

~~3.15~~ The Custodian shall ensure compliance with the applicable provisions of the Investment Services Act (Control of Assets) (Amendment) Regulations, 2016

~~shall be the holder of a Category 4 Investment Services Licence issued by the Authority or a Credit Institution having its registered office in the EU and authorised in accordance with Directive 2006/48/EC.~~

~~3.153.16~~ AIFs which have no redemption rights exercisable during the period of 5 years from the date of the initial investments and which in accordance with their core investment policy, generally do not invest in assets that must be held in custody in accordance with their core investment policy, or generally invest in issuers or non-listed companies in order to potentially acquire control over such companies, may appoint an entity which carries out depository functions as part of its professional or business activities in respect of which such entity is subject to mandatory professional registration or to legal or regulatory rules of professional conduct and which can provide sufficient financial and professional guarantees to meet the commitments inherent in carrying out its depository functions.

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~~3.163.17~~ The appointment of the Custodian shall be evidenced by a written contract. This contract shall *inter alia* regulate the flow of information deemed necessary to allow the Custodian to perform its functions for the AIF for which it has been appointed as Custodian.

~~3.173.18~~ The Custodian shall be separate and independent from the AIFM and shall act independently and solely in the interests of the Unit or Shareholders. Any facts, relationships, arrangements or circumstances which may at any stage bring that independence into question shall be declared to the MFSA as soon as the AIF becomes aware of such a matter.

~~3.183.19~~ The Custodian appointed for an AIF shall not be appointed as an External Valuer of that AIF, unless it has functionally and hierarchically separated the performance of its custodial functions from its tasks as External Valuer and the potential conflicts of interest are properly identified, managed, monitored and disclosed to the investors of the AIF.

~~3.193.20~~ The written consent of the MFSA shall be obtained before the appointment or replacement of any party to act in the capacity of Custodian to the AIF. The MFSA reserves the right to object to the proposed replacement or appointment and to require such additional information it considers appropriate.

Prime Broker and Counterparties

~~3.203.21~~ The AIF may appoint one or more prime brokers or counter parties.

~~3.213.22~~ Upon selecting and appointing counterparties and prime brokers, the AIFM on behalf of the AIF, shall enter into a written contract outlining the applicable terms. The contract shall also provide that the custodian be informed thereof. In particular any possibility of transfer and reuse of AIF assets shall be provided for in the contract and shall comply with the AIF's articles of association and Offering Document.

~~3.223.23~~ The AIF or the AIFM on behalf of the AIF shall exercise due skill, care and diligence before entering into an agreement and on an on-going basis thereafter taking into account the full range and quality of their services.

~~3.233.24~~ When selecting prime brokers or counterparties of an AIFM or an AIF in an OTC derivatives transaction, in a securities lending or in a repurchase agreement, the AIFM on behalf of the AIF shall ensure that those prime brokers and counterparties fulfil all of the following conditions:

- a) they are subject to on-going supervision by a public authority;
- b) they are financially sound;

- c) they have the necessary organisational structure and resources for performing the services which are to be provided by them to the AIF or AIFM.

3.243.25 When appraising the financial soundness referred to in SLC 3.24(b), the AIFM on behalf of the AIF shall take into account whether or not the prime broker or counterparty is subject to prudential supervision, including sufficient capital requirements and effective supervision.

3.253.26 The list of selected prime brokers shall be approved by the AIFM's senior management. In exceptional cases, prime brokers not included in the list may be appointed, provided they fulfil the requirements prescribed in SLC 3.24 and subject to approval by the AIFM. The AIFM shall be able to demonstrate the reasons for such choice and the due diligence that it exercised in selecting and monitoring the prime brokers which had not been listed.

Compliance Officer

3.263.27 Responsibility for the AIF's compliance with its licence conditions rests with the Board of Directors in the case of an AIF set up as an investment company; with the General Partner(s) in the case of an AIF set up as a limited partnership; or with the AIFM in the case of an AIF set up as a unit trust or a common contractual fund.

3.273.28 In order to enable the compliance functions to be properly carried out, the AIF shall establish, implement and maintain adequate policies and procedures designed to detect any risk of failure by the AIF to comply with its obligations under the Act, the Regulations issued thereunder and these Rules, as well as with its obligations under other applicable legislation, in particular the Prevention of Money Laundering Act, 1994, the Prevention of Financial Markets Abuse Act, 2005, and Regulations issued thereunder, as well as to detect the associated risks, and shall put in place adequate measures and procedures designed to minimize such risk and to enable the MFSA to exercise its powers effectively.

3.283.29 In order to enable the compliance function to discharge its responsibilities properly, the AIF shall ensure that a Compliance Officer is appointed to assume responsibility for the compliance function and for any reporting as to compliance required by these Rules.

3.293.30 The AIF shall obtain the written consent of the MFSA before the appointment or replacement of a Compliance Officer in advance. The request for consent of the appointment or replacement of a Compliance Officer shall be accompanied by a Personal Questionnaire ("PQ"), in the form set out in Schedule 2 to Part A of these Rules and by a Competency Form as set out in Schedule 3 to Part A of these Rules – duly completed by the person proposed. The MFSA reserves the right to object to the proposed appointment or replacement and to require such additional information it considers appropriate.

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- ~~3.303.31~~ The AIF shall notify the MFSA of the resignation or removal of its Compliance Officer upon becoming aware of the proposed resignation or removal. The AIF shall also request the Compliance Officer to confirm to the MFSA that his departure had no regulatory implications or to provide relevant details, as appropriate. A copy of such request shall be provided to the MFSA together with the AIF's notification of departure.
- ~~3.313.32~~ The AIF shall request its Compliance Officer to prepare a Compliance Report at least on a six monthly basis, which in the case of an AIF taking the form of:
- an investment company, should be presented to the Board of Directors; or
 - a limited partnership, should be presented to the General Partner; or
 - a unit trust or a common contractual fund should be presented to the AIFM and the Trustee.
- ~~3.323.33~~ The Compliance Report should indicate any:
- breaches to the Investment and Borrowing Restrictions;
 - complaints from Unit or Shareholders in the AIF and the manner in which these have been handled (for AIFs sold to retail investors, the manner in which complaints shall have been handled should be in accordance with Appendix 10 to these Rules);
 - material valuation errors (higher than 0.5% of NAV) and the manner in which these have been handled; and
 - material compliance issues during the period covered by the Compliance Report.
- ~~3.333.34~~ The Compliance Report should also include a confirmation that all the local Prevention of Money Laundering requirements have been satisfied. This confirmation should be obtained from the AIF's Money Laundering Reporting Officer.
- ~~3.343.35~~ A copy of the Compliance Report should be held in Malta at the registered office of the AIF and made available to the MFSA during compliance visits.

Money Laundering Reporting Officer

- ~~3.353.36~~ Responsibility for the AIF's compliance with its Prevention of Money Laundering obligations rests with the Board of Directors in the case of an AIF set up as an investment company; with the General Partner(s) in the case of an AIF set up as a limited partnership; or with the AIFM in the case of an AIF set up as a unit trust or a common contractual fund.
- ~~3.363.37~~ The AIF shall at all times have a Money Laundering Reporting Officer.

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~~3.373.38~~ The AIF shall obtain the written consent of the MFSA before the appointment or replacement of a Money Laundering Reporting Officer in advance. The request for consent of the appointment or replacement of a Money Laundering Reporting Officer shall be accompanied by a Personal Questionnaire (“PQ”), in the form set out in Schedule 2 to Part A of these Rules and by a Competency Form as set out in Schedule 3 to Part A of these Rules – duly completed by the person proposed. The MFSA reserves the right to object to the proposed appointment or replacement and to require such additional information it considers appropriate.

~~3.383.39~~ The AIF shall notify the MFSA of the resignation or removal of its Money Laundering Reporting Officer upon becoming aware of the proposed resignation or removal. The AIF shall also request the Money Laundering Reporting Officer to confirm to the MFSA that his departure had no regulatory implications or to provide relevant details, as appropriate. A copy of such request shall be provided to the MFSA together with the AIF’s notification of departure.

Auditor

~~3.393.40~~ The AIF shall appoint an auditor approved by the MFSA. The Auditor shall be a person empowered to audit accounts in terms of Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts.

~~3.403.41~~ The AIF shall replace its auditor if requested to do so by the MFSA. The MFSA’s consent shall be sought prior to the appointment or replacement of an auditor.

~~3.413.42~~ The AIF shall make available to its auditor the information and explanations he/she needs to discharge his/her responsibilities as an auditor and in order to meet the MFSA’s requirements.

~~3.423.43~~ The AIF shall not appoint an individual as an auditor, nor appoint an audit firm where the individual directly responsible for the audit, or his/her firm is:

- a) a director, partner, qualifying shareholder, officer, representative or employee of the AIF;
- b) a partner of, or in the employment of, any person in (a) above;
- c) a spouse, civil partner, parent, step-parent, child, step-child or other close relative of any person in (a) above;
- d) a person who is not otherwise independent of the AIF;
- e) a person disqualified by the MFSA from acting as an auditor of an AIF.

For this purpose, an auditor shall not be regarded as an officer or an employee of the AIF solely by reason of being an auditor of that AIF.

~~3.433.44~~ The AIF shall obtain from its auditor a signed letter of engagement defining clearly the extent of the auditor’s responsibilities and the terms of his appointment. The AIF

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shall confirm in writing to its auditor its agreement to the terms in the letter of engagement.

3.443.45 The letter of engagement shall include terms requiring the auditor:

- a) to provide such information or verification to the MFSA as the MFSA may request;
- b) to vacate his/her office if he becomes disqualified to act as auditor for any reason;
- c) if he/ she resigns, or is removed or not reappointed, to advise the MFSA of that fact and of the reasons for his ceasing to hold office. The auditor shall also be required to advise the MFSA if there are matters he/ she considers should be brought to the attention of the MFSA;
- d) in accordance with article 18 of the Act, to report immediately to the MFSA any fact or decision of which he becomes aware in his capacity as auditor of the AIF which:
 - i. is likely to lead to a serious qualification or refusal of his/ her audit report on the accounts of the AIF; or
 - ii. constitutes or is likely to constitute a material breach of the legal and regulatory requirements applicable to the AIF in or under the Act; or
 - iii. gravely impairs the ability of the AIF to continue as a going concern; or
 - iv. relates to any other matter which has been prescribed.

3.453.46 If at any time the AIF fails to have an auditor in office for a period exceeding four weeks, the MFSA shall be entitled to appoint a person to fill the vacancy; the fees and charges so incurred being payable by the AIF.

3.463.47 In respect of each annual accounting period, the AIF shall require its auditor to prepare its management letter in accordance with International Standards on Auditing.

External Valuer

3.473.48 The valuation function shall be performed by:

- a) An External Valuer, being a legal or natural person independent from the AIF, the AIFM and any other persons with close links to the AIF or the AIFM; or
- b) The AIFM, provided that the valuation task is functionally independent from the portfolio management and the remuneration policy and other measures ensure that conflicts of interest are mitigated and that undue influence upon employees is prevented.

3.483.49 The External Valuer shall be appointed by the AIFM or by the AIF where this is self-managed.

4. INVESTMENT OBJECTIVES, POLICIES AND RESTRICTIONS

GENERAL

- 4.01 For the purposes of this chapter of the rules, the Standard Licence Conditions prescribed therein shall be applicable as follows:
- i. SLC 4.02 to SLC 4.13 shall be applicable to **all** AIFs;
 - ii. SLCs 4.14 to SLC 4.40 shall be applicable **solely** to AIFs which are sold exclusively to retail investors;
 - iii. SLC 4.42 to SLC 4.60 shall be applicable **solely** to AIFs which are sold to Experienced Investors;
 - iv. SLC 4.61 to SLC 4.65 shall be applicable **solely** to AIFs which are sold to Qualifying Investors;
 - v. SLC 4.66 to SLC 4.70 shall be applicable **solely** to AIFs which are sold to Extraordinary Investors; and
 - vi. SLC 4.71 to SLC 4.74 shall be applicable **solely** to AIFs which are sold to Professional Investors.
- 4.02 The AIF shall be subject to the investment objectives, policies and restrictions outlined in its Offering Document. The AIFM or the AIF, where the fund is self-managed, shall take all reasonable steps to comply with the investment policies and restrictions of the AIF. The Custodian shall supervise the operation of the AIF to ensure that the AIFM complies with the investment policies and restrictions of the AIF.
- 4.03 Changes to the investment policies and restrictions of the AIF shall be notified to the investors in advance of the change.

Distributions of Income

- 4.04 An AIF shall effect any distributions of income in accordance with the provisions of its Constitutional Documents and/ or Offering Document.
- 4.05 Where the AIF is sold to retail investors it shall further comply with the SLCs prescribed in Appendix 2 on Distributions of Income which in the event of conflict with the provision of the Constitutional Documents and or Offering Document shall take precedence.

Side Letters

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- 4.06 Side letters to be entered into by the AIF must be circulated to and approved by the Board of Directors (where the AIF is set up as an investment company)/ General Partner(s) (where the AIF is set up as a limited partnership)/ AIFM of the AIF (where the AIF is set up as a unit trust or a common contractual fund) prior to issue.
- 4.07 The fact that side letters detailing preferential treatment of certain investors may be issued shall be disclosed in the Constitutional Documents and/or Offering Document.
- 4.08 Side letters issued by the AIF should be retained in Malta at the registered office of the AIF and should be available for inspection by the MFSA during compliance visits.

Side Pockets

- 4.09 Side pockets to be entered into by an AIF must conform to the Guidance Note on the use of Side Pockets by Collective Investment Schemes issued by the Authority.
- 4.10 The fact that side pockets may be used shall be disclosed in the Constitutional Documents and/or Offering Document.

Licence Conditions applicable to AIFs engaged in foreign currency lending

- 4.11 The AIF shall, in as far as these may be applicable to any foreign currency lending which it may carry out, abide by the high level principles on foreign currency lending as outlined in [MFSA Rule 1 of 2012](#) on foreign currency lending, which is modelled on the Recommendation of the European Systemic Risk Board on lending in foreign currencies (ESRB/2011/1).
- 4.12 Foreign currency lending means lending in any currency other than the legal tender of the country in which the borrower is domiciled. This includes situations where the Euro is the foreign currency due to the borrower's domicile being outside the euro zone.
- 4.13 When the AIF has engaged in any form of foreign currency lending during the period under review, it shall submit a confirmation to this effect together with its annual report. Any foreign currency lending activity shall be indicated as a percentage of the scheme's total NAV. An AIF which has not carried out any foreign currency lending during the period under review is not required to submit a 'nil' return.

SUPPLEMENTARY LICENCE CONDITIONS APPLICABLE TO AIFs SOLD EXCLUSIVELY TO RETAIL INVESTORS

Breach of Investment Restrictions

- 4.14 The AIF shall comply with the investment restrictions within six months from the launch of the AIF or upon reaching a value equivalent to EUR 2,500,000 whichever is sooner. However, provided it considers this to be in the best interest of its shareholders and that it observes the principle of risk spreading, the AIF will not be required to comply with its investment restrictions upon reaching a value equivalent to EUR 2,500,000 subject to it complying with such restrictions within a maximum of six months from launch. The AIF shall take all reasonable steps to comply with the investment restrictions. The Custodian shall supervise the operation of the AIF or the AIFM to ensure that the AIF complies with the investment restrictions.
- 4.15 The following shall be the rules applicable in the event of an inadvertent breach of the AIF's investment restrictions:
- i. If one or more of the AIF's investment restrictions are at any time contravened for reasons beyond the control of the AIFM or the AIF, the AIFM or the AIF shall take such steps as are necessary to ensure a restoration of compliance with such restriction(s) as soon as is reasonably practicable having regard to the interests of the unit-holders and, in any event, within the period of six months beginning on the date of discovery of the contravention of such restriction(s).
- The above is aimed at addressing circumstances which may arise following acquisition of the AIF's assets and include market price movements of the AIF's underlying assets or market illiquidity. The above is without prejudice to the duty of the AIFM and the AIF to comply with the AIF's investment restrictions and to ensure that such restrictions are not contravened as a direct result of any acquisition of its underlying assets.
- ii. Forthwith upon the Custodian becoming aware that circumstances of a kind described above have arisen, the Custodian shall take such steps as are necessary to ensure that the AIF or the AIFM comply with the requirement imposed by (i) above.
 - iii. A contravention of an investment restriction which may arise due to the circumstances outlined in (i) above shall not be considered as a breach of a Licence Condition and will therefore not be subject to the MFSA's notification requirements. However, where the contravention is not remedied by the AIFM or AIF within the maximum six month period stipulated in (i) above, a breach of this Licence Condition is deemed to arise and the relevant notification requirements will apply.
- 4.16 The AIF's investment policies shall be clearly defined in its Prospectus, and sufficient information shall be given to ensure that holders of Units are fully aware of the risks to which they will be exposed.

Ancillary Liquid Cash

4.17 The AIF may hold ancillary liquid assets irrespective of its investment objective and policy.

Investments in Securities

4.18 The AIF shall not invest more than 10 per cent of its assets in securities which are not traded in or dealt on a market which:

- i. the Custodian and AIFM have agreed between themselves as being appropriate for the AIF;
- ii. is listed in the Offering Document;
- iii. is regulated, operates regularly, is recognised and is open to the public;
- iv. has adequate liquidity and adequate arrangements in respect of the transmission of income and capital; and
- v. is not the subject of an MFSA restriction.

4.19 The AIF shall not invest more than 10 per cent of its assets in Securities issued by the same body.

4.20 The AIF shall not hold more than 10 per cent of any class of Security issued by any single issuer.

4.21 The AIF may, subject to approval from the MFSA, invest up to 100 per cent of its assets in Securities issued or guaranteed by any State, its constituent States, its local authorities, or public international bodies of which one or more States are members.

4.22 The AIF may invest in nil paid or partly paid shares and subscribe for placing or underwriting as long as the amount due to be paid does not exceed 5 per cent of the value of the AIF, except that, if the amount exceeds that figure, cash not required for other purposes or for the efficient management of the portfolio shall be available to cover the full amount outstanding.

4.23 The AIF and its AIFM, taking into account all of the AIFs which the latter manages, shall not acquire sufficient instruments to give it the right to exercise control over 20 per cent or more of the share capital or votes of a company, or sufficient instruments to enable it to exercise significant influence over the management of the issuer.

Deposits with Credit Institutions

4.24 No more than 10 per cent of the assets of the AIF shall be kept on deposit with any one body. This limit may be increased to 30 per cent in respect of money deposited

with a credit institution licensed in Malta or in any other EEA State, or with any other credit institution which has been approved by the MFSA.

Investments in Other UCITS and/ or Other Collective Investment Schemes

- 4.25 The AIF may acquire the Units of other Collective Investment Schemes subject to the following:
- i. not more than 20 per cent of the AIF's assets shall be invested in any one scheme;
 - ii. where the AIF invests in the Units of another AIF managed by the same AIFM, the AIFM of the AIF into which the investment is made shall waive all charges which it is entitled to charge for its own account in relation to the acquisition or disposal of Units;
 - iii. where a commission is received by the AIFM of the AIF by virtue of an investment in the Units of another scheme, that commission shall be paid into the property of the AIF.

Transactions in Financial Derivative Instruments – for efficient portfolio management purposes

- 4.26 The AIF may employ techniques and instruments for the purpose of efficient portfolio management. These operations may concern the use of Financial Derivative Instruments.

The reference in this SLC to techniques and instruments for the purpose of efficient portfolio management shall be understood as a reference to techniques and instruments which fulfil the following criteria:

- i. they are economically appropriate in that they are realised in a cost-effective way;
 - ii. they are entered into for one or more of the following specific aims:
 - a. reduction of risk; or
 - b. reduction of cost.
- 4.27 The AIF shall only hold Financial Derivative Instruments for the purposes of efficient portfolio management in terms of SLC 4.26 and shall not hold Financial Derivative Instruments for investment purposes nor shall it be leveraged or geared in any manner through the use of Financial Derivative Instruments.

- 4.28 In order to assure it is not leveraged or geared through the use of Financial Derivative Instruments, the Scheme shall calculate its exposure relating to Financial Derivative Instruments on the basis of the Commitment Approach. The Scheme shall convert its derivatives positions into the equivalent positions of the underlying assets embedded in those Financial Derivative Instruments. The commitment calculation for certain Financial Derivative Instruments may be adjusted by a probability factor that aims to reflect the probability of the Financial Derivative Instrument's commitment occurring. For options and warrants, the delta approach may be used. Where it is not possible to calculate a probability factor on a scientific and objective basis, the factor is assumed to be 1. Reference should be made to Appendix VI to Part B of the Investment Services Rules for Retail Collective Investment Schemes which set out the Commitment Rules for a non-exhaustive list of commonly traded Financial Derivative Instruments.
- 4.29 The AIF's maximum exposure to one counterparty in an OTC-derivative transaction shall not be more than 5 per cent of value of the assets of the AIF. This limit may be increased to 10 per cent in respect of OTC-derivative transactions made with a counterparty which is a credit institution. The exposure per counterparty of an OTC-derivative should not be measured on the basis of the notional value of the OTC-derivative, but on the maximum potential loss incurred by the Scheme if the counterparty defaults.
- 4.30 The exposure to one counterparty in an OTC-derivative transaction may be reduced where the counterparty provides the AIF with collateral which satisfies the following criteria:
- i. the collateral falls within one of the following categories:
 - a. cash;
 - b. government or other public securities;
 - c. certificates of deposit issued by Relevant Institutions; and
 - d. bonds/commercial paper issued by Relevant Institutions;
 - ii. collateral is:
 - a. marked to market daily;
 - b. transferred to the custodian, or its agent; and
 - c. immediately available to the AIF, without recourse to the counterparty, in the event of a default by that entity;
 - iii. in the case of non-cash collateral, the collateral:
 - a. cannot be sold or pledged;
 - b. has a minimum credit rating of A or equivalent;
 - c. is held at the credit risk of the counterparty; and
 - d. is issued by an entity independent of the counterparty;
 - iv. in the case of cash collateral, the collateral may not be invested other than in the following:

- a. deposits with relevant institutions, which are capable of being withdrawn within 5 working days;
- b. government or other public securities which have a minimum credit rating of A or equivalent;
- c. certificates of deposit issued by relevant institutions, which have a minimum credit rating of A or equivalent; and
- d. daily dealing Qualifying Money Market Funds which have a minimum credit rating of AAA or equivalent.

Invested cash collateral which is held at the credit risk of the AIF, other than cash collateral invested in government or other public securities or Qualifying Money Market Funds, shall be diversified so that no more than 20 per cent of the collateral is invested in the securities of, or placed on deposit with, one institution. Invested cash collateral may not be placed on deposit with, or invested in securities issued by the counterparty or a related entity.

- 4.31 The AIF may net the mark-to-market value of its OTC-derivative positions with the same counterparty, thus reducing the AIF's exposure to its counterparty, provided that the AIF has a contractual netting agreement with its counterparty which creates a single legal obligation such that, in the event of the counterparty's failure to perform owing to default, bankruptcy, liquidation or any other similar circumstance, the AIF would have a claim to receive or an obligation to pay only the net sum of the positive and negative mark-to-market values of included individual transactions.
- 4.32 Derivative transactions which are performed on an exchange where the clearing house meets the following conditions, shall be deemed to be free of counterparty risk:
- i. is backed by an appropriate performance guarantee;
 - ii. is characterised by a daily mark-to-market valuation of the derivative positions; and
 - iii. is subject to at least daily margining.
- 4.33 The AIF shall only enter into OTC-derivatives for the purposes of efficient portfolio management with counterparties who:
- i. are not the AIFM or Custodian of the AIF; and
 - ii. form part of a group whose head office or parent company is licensed, registered or based in Malta, any member of the OECD, the EU or the EEA and is subject to prudential supervision; and
 - iii. have a credit rating of at least A (Standards & Poor's) or A2 (Moody's) or an equivalent rating by another internationally renowned credit rating agency.

Such counterparty shall satisfy the AIFM or the AIF that it has:

- agreed to value the transaction at least weekly; and
- will close out the transaction at the request of the AIFM or the AIF at fair value.

4.34 When the AIF holds a Financial Derivative Instrument which automatically or at the AIF's or counterparty's discretion, requires cash or physical settlement on maturity or exercise, the AIF shall hold the underlying instrument as cover. The level of cover should be calculated on the basis of the Commitment Approach as indicated in SLC 4.28.

4.35 When in view of the nature of the Financial Derivative Instrument, the AIF cannot hold the underlying as cover (e.g. in the case of index based financial derivative instruments), SLC 4.34 shall not apply and the AIF shall hold any of the following assets as cover:

- i. cash;
- ii. liquid debt instruments (e.g. government bonds of first credit rating) prudently adjusted by appropriate haircuts (minimum of 5 per cent);
- iii. other highly liquid assets which are correlated with the underlying of the Financial Derivative Instruments, prudently adjusted by appropriate haircuts (minimum 5 per cent).

The level of cover should be calculated on the basis of the Commitment Approach as indicated in SLC 4.28.

For the purposes of the above, the instruments held as cover should be considered as 'liquid' when they can be converted into cash at no more than 7 business days at a price closely corresponding to the current valuation of the financial instrument. It has to be ensured that the respective cash amount is at the AIF's disposal at the maturity/ expiry or exercise date of the Financial Derivative Instrument.

Uncovered Sales

4.36 The AIF may not carry out uncovered sales of Securities or other financial instruments. Uncovered sales are all transactions in which the AIF is exposed to the risk of having to buy securities at a higher price than the price at which the securities are delivered, thus making a loss, and the risk of not being able to deliver the underlying for settlement at the time of the maturity of the transaction.

General Restrictions – Single Issuer Exposures

4.37 Notwithstanding the individual limits laid down in SLC 4.19, 4.24 and 4.29, the AIF may not combine:

- i. investments in Securities issued by;
- ii. deposits made with; and/or
- iii. counterparty exposures arising from OTC-derivative transactions undertaken with;

a single body in excess of 35 per cent of its assets.

Borrowing Limits

4.38 An AIF may borrow up to a maximum of 10 per cent of:

- i. its assets, when the AIF is set up as an investment company or limited partnership; or
- ii. the value of the AIF, when the AIF is set up as a unit trust or common contractual fund.

Provided that the borrowing is on a temporary basis and such that the AIF's overall risk exposure does not exceed 110 per cent of its assets under any circumstances.

Provided further that the AIF may acquire foreign currency by means of a 'back to back' loan. Foreign currency obtained in this manner is not classed as borrowings for the purposes of this SLC provided that the offsetting deposit:

- a. is denominated in the base currency of the AIF; and
- b. equals or exceeds the value of the foreign currency loan outstanding.

Miscellaneous

4.39 An AIF cannot enter into cross sub-fund investments.

4.40 Material changes to the Investment Policies and Restrictions of the AIF shall be notified to investors in advance of the change.

4.41 Changes to the Investment Objectives of the AIF shall be subject to the prior approval of the Unit holders of the AIF. The change in the investment objectives should only become effective after all pending redemptions linked to the change in the investment objectives have been satisfied. Any applicable redemption fees would also need to be waived accordingly.

INVESTMENT POLICIES, OBJECTIVES AND RESTRICTIONS APPLICABLE TO ALTERNATIVE INVESTMENT FUNDS WHICH ARE SOLD TO EXPERIENCED INVESTORS

Investment Restrictions

- 4.42 The minimum investment which the AIF may accept is EUR 10,000. Once the minimum investment has been made, any additional amount may be invested but the total amount invested must not at any time be less than EUR 10,000 unless this is the result of a fall in the net asset value. In the case of an umbrella AIF, the EUR 10,000 threshold may apply on a per scheme basis rather than on a per sub-fund basis.
- 4.43 The AIF shall comply with the investment restrictions within six months from the launch of the AIF or upon reaching a value equivalent to EUR 2,500,000 whichever is sooner. However, provided it considers this to be in the best interest of its shareholders and that it observes the principle of risk spreading, the AIF will not be required to comply with its investment restrictions upon reaching a value equivalent to EUR 2,500,000 subject to it complying with such restrictions within a maximum of six months from launch.
- 4.44 The AIF may only enter into repurchase/reverse repurchase and stock lending or borrowing agreements:
- i. When in the opinion of the AIF or the AIFM, the entering into such agreements by the AIF is appropriate and in the interest of the AIF, and entails an acceptable level of risk; and
 - ii. In accordance with good market practice, which involves the provision of adequate collateral to the satisfaction of the AIF or the AIFM.
- 4.45 Investment by the AIF in Financial Derivative Instruments as part of the investment policy in order to obtain exposure to underlying assets shall be without prejudice to the limits prescribed in these Investment Services Rules which apply in the case of direct investments in such underlying assets. The exposure to the underlying assets should be calculated using the Commitment Approach.
- 4.46 Direct borrowing for investment purposes and leverage via the use of derivatives is restricted to 100% of the NAV. The AIF's exposure relating to derivative instruments is calculated taking into account:
- i. the current value of the underlying asset;
 - ii. the counterparty risk;
 - iii. future market movements; and
 - iv. the time available to liquidate positions.

The AIF's exposure relating to borrowing for investment purposes is the amount so borrowed.

The assessment of the AIF's global exposure to derivative investments should be assessed on the basis of the Value at Risk Approach or the Commitment Approach.

- 4.47 The AIFM or (in the case of a self-managed AIF), the AIF, must take reasonable steps to ensure that the AIF, is managed according to the principle of risk spreading. In particular, the AIF shall be required to adhere to the diversification requirements prescribed hereunder. In the case of an AIF investing in alternative assets, the Authority may impose tailored investment restrictions. Such AIF may utilise SPVs subject to the conditions prescribed in Appendix 1 and subject to such other conditions as the Authority may consider appropriate imposing, taking into account the nature of the underlying assets, and their proposed custody arrangements.
- 4.48 The AIF may invest up to 20% of its total assets in securities issued by the same body and up to 30% of its assets in money market instruments issued by the same body provided that:
- i. The 20% / 30% limit set out above may be increased to a maximum of 100% in the case of securities and money market instruments issued or guaranteed by an OECD or EU/EEA Member State, its local authorities or public international bodies of which one or more such States are members;
 - ii. The 20% / 30% limit set out above may be increased to a maximum of 35% in the case of securities and money market instruments guaranteed by a credit institution authorised in the EEA or which is subject to equivalent prudential requirements;
 - iii. The 20% limit set out above may be increased up to a maximum of 30% in the case of transferable securities traded in or dealt on a regulated market which operates regularly, is recognised and is open to the public.
- 4.49 The AIF may invest up to a maximum of 35% of its total assets in deposits held with a single body.
- 4.50 The AIF is not subject to any investment restrictions with respect to investments in a single collective investment scheme provided that the underlying scheme is a UCITS or other open ended collective investment scheme subject to risk spreading requirements which are at least comparable to those applicable to the AIF itself.
- 4.51 The AIF may invest up to a maximum of 30% of its total assets in any single collective investment scheme which does not satisfy the conditions indicated in SLC 4.51 above.
- 4.52 Where the AIF is a fund of hedge funds it shall invest in at least five hedge funds.
- 4.53 Where the AIF enters into OTC derivative transactions, it shall ensure that its exposure to a single counterparty is limited to 20% of its total assets.

The exposure to one counterparty in an OTC derivative transaction may be reduced where the counterparty provides the AIF with acceptable collateral in accordance with good market practice to the satisfaction of the AIF or its AIFM.

The exposure per counterparty of an OTC derivative should not be measured on the basis of the notional value of the OTC derivative, but on the maximum potential loss incurred by the AIF if the counterparty defaults.

The AIF may net the mark-to-market value of its OTC derivative positions with the same counterparty, thus reducing its exposure to its counterparty, provided that the AIF has a contractual netting agreement with its counterparty which creates a single legal obligation such that, in the event of the counterparty's failure to perform owing to default, bankruptcy, liquidation or any similar circumstance, the AIF would have a claim to receive or an obligation to pay only the net sum of the positive and negative mark-to-market values of included individual transactions.

- 4.54 The AIF shall limit its aggregate maximum exposure (through securities, money market instrument, deposits and OTC derivatives transactions) to a single issuer/counterparty to 40% of its total assets.
- 4.55 Where the AIF has been set up as a Feeder Fund, the underlying fund shall satisfy the leverage restrictions applicable to the AIF.
- 4.56 Changes to the investment policies and restrictions of the AIF shall be notified to investors in advance of the change.
- 4.57 Changes to the investment objectives of the AIF shall be notified to investors in advance of the change. The notice period should be sufficiently long to allow for redemption requests to be submitted by investors and processed prior to the change being effected. The change in the investment objectives should only become effective after all pending redemptions linked to the change in the investment objectives have been satisfied. Any applicable redemption fees would also need to be waived accordingly.
- 4.58 The following shall be the rules applicable in the event of an inadvertent breach of investment restrictions:
- i. if one or more of the AIF's investment restrictions are at any time contravened for reasons beyond the control of the AIFM or the AIF, the AIFM or the AIF must take such steps as are necessary to ensure a restoration of compliance with such restriction(s) as soon as is reasonably practicable having regard to the interests of the unit-holders and, in any event, within the period of six months beginning on the date of discovery of the contravention of such restriction(s);

The above is aimed at addressing circumstances which may arise following acquisition of the AIF's assets and include market price movements of the

AIF's underlying assets or market illiquidity. The above is without prejudice to the duty of the AIFM and the AIF to comply with the AIF's investment restrictions and to ensure that such restrictions are not contravened as a direct result of any acquisition of its underlying assets.

- ii. a contravention of an investment restriction which may arise due to the circumstances outlined in (i) above shall not be considered as a breach of a licence condition and will therefore not be subject to MFSA's notification requirements. However, where the contravention is not remedied by the AIFM or the AIF within the maximum six month period stipulated in (i) above, a breach of this Licence Condition is deemed to arise and the relevant notification requirements will apply.

4.59 Where the AIF invests directly or indirectly in immovable property, the following supplementary conditions shall apply:

- i. The AIF may invest up to a maximum of 25% of its total assets directly or indirectly (through an SPV) in any one single immovable property. Subject to the AIF being operated according to the risk spreading principle, it will not be required to comply with this restriction before three years from its launch. For the purposes of this restriction, a property whose economic viability is linked to another property is not considered as a separate item of property for this purpose.
- ii. Where the AIF invests solely in immovable property (rather than also in property funds and/ or other securities), it should be exposed to not less than 5 different properties.
- iii. The AIF may invest 100% of its total assets in any single property fund provided that such fund complies with the investment, borrowing and leverage conditions applicable to AIFs targeted to Experienced Investors, established as property funds and which are set out in these Rules and in the MFSA's Property Fund Policy.
- iv. The AIF may invest up to 100% of its assets in a Special Purpose Vehicle provided that the applicable investment, borrowing and leverage restrictions are satisfied at the level of the Special Purpose Vehicle.

4.60 An AIF cannot enter into cross sub-fund investments.

INVESTMENT POLICIES, OBJECTIVES AND RESTRICTIONS APPLICABLE TO ALTERNATIVE INVESTMENT FUNDS WHICH ARE SOLD TO QUALIFYING INVESTORS

Investment Restrictions

MFSA

MALTA FINANCIAL SERVICES AUTHORITY

- 4.61 The minimum investment which the AIF may accept is EUR 75,000 per investor. Once the minimum investment has been made, any additional amount may be invested but the total amount invested must not at any time be less than EUR 75,000 unless this is the result of a fall in the net asset value. In the case of an umbrella AIF, the EUR 75,000 may apply on a per scheme basis rather than on a per sub-fund basis.
- 4.62 The AIF shall be subject to the investment objectives, policies and restrictions outlined in its Offering Document. In addition, where the AIF intends effecting its investments through the use of Trading Companies or Special Purpose Vehicles, it shall also be subject to the supplementary conditions regarding the use of such vehicles set out in Appendix 1 to these Rules. The AIFM or the AIF shall take all reasonable steps to comply with the investment policies and restrictions of the AIF.
- 4.63 Changes to the investment objectives of the AIF shall be notified to investors in advance of the change. The notice period should be sufficiently long to allow for redemption requests to be submitted by investors and processed prior to the change being effected. The change in the investment objectives should only become effective after all pending redemptions linked to the change in the investment objectives have been satisfied. Any applicable redemption fees would also need to be waived accordingly.
- 4.64 The following shall be the rules applicable in the event of an inadvertent breach of investment restrictions:
- i. if one or more of the AIF's investment restrictions are at any time contravened for reasons beyond the control of the AIFM or the AIF, the AIFM or the AIF must take such steps as are necessary to ensure a restoration of compliance with such restriction(s) as soon as is reasonably practicable having regard to the interests of the unit-holders and, in any event, within the period of six months beginning on the date of discovery of the contravention of such restriction(s);

The above is aimed at addressing circumstances which may arise following acquisition of the AIF's assets and include market price movements of the AIF's underlying assets or market illiquidity. The above is without prejudice to the duty of the AIFM and the AIF to comply with the AIF's investment restrictions and to ensure that such restrictions are not contravened as a direct result of any acquisition of its underlying assets.

- ii. a contravention of an investment restriction which may arise due to the circumstances outlined in (i) above shall not be considered as a breach of a licence condition and will therefore not be subject to MFSA's notification requirements. However, where the contravention is not remedied by the AIFM or the AIF within the maximum six month period stipulated in (i) above, a

breach of this Licence Condition is deemed to arise and the relevant notification requirements will apply.

Cross Sub-Fund Investments

- 4.65 A sub-fund may invest in units of one or more sub-funds within the same scheme, subject to this being permitted in the constitutional documents and the Offering Memorandum of the said AIF and subject to the following:
- a. the investment company should in its memorandum of association elect to have the assets and liabilities of each sub-fund comprised in that company treated as a patrimony separate from the assets and liabilities of each other sub-fund of such company in terms of Regulation 9 of the Companies Act (Investment Companies with Variable Share Capital) Regulations;
 - b. the sub-fund is allowed to invest up to 50% of its assets into another sub-fund within the same scheme;
 - c. the target sub-fund/s may not themselves invest in the sub-fund which is to invest in the target sub-fund/s;
 - d. in order to avoid duplication of fees, where the AIFM of the sub-fund and the AIFM of the target sub-fund is the same or (in the case of different AIFMs) where one AIFM is an affiliate of the other, only one set of management (excl. performance fees), subscription and/or redemption fees applies between the sub-fund and the target sub-fund, provided that this restriction shall apply only in respect of and to the extent (up to the portion) of the investment of the sub-fund in the target sub-fund;
 - e. for the purposes of ensuring compliance with any applicable capital requirements, cross-investments will be counted once;
 - f. any voting rights acquired by the sub-fund from the acquisition of the units in the target sub-fund shall be disapplied as appropriate.

INVESTMENT POLICIES, OBJECTIVES AND RESTRICTIONS APPLICABLE TO ALTERNATIVE INVESTMENT FUNDS WHICH ARE SOLD TO EXTRAORDINARY INVESTORS

Investment Restrictions

- 4.66 The minimum investment which the AIF may accept is EUR 750,000 per investor. Once the minimum investment has been made, any additional amount may be invested but the total amount invested must not at any time be less than EUR 750,000 unless this is the result of a fall in the net asset value. In the case of an

umbrella AIF, the EUR 750,000 may apply on a per scheme basis rather than on a per sub-fund basis.

- 4.67 The AIF shall be subject to the investment objectives, policies and restrictions outlined in its Offering Document. In addition, where the AIF intends effecting its investments through the use of Trading Companies or Special Purpose Vehicles, it shall also be subject to the supplementary conditions regarding the use of such vehicles set out in Appendix I to these Rules. The AIFM or the AIF shall take all reasonable steps to comply with the investment policies and restrictions of the AIF.
- 4.68 Changes to the investment objectives of the AIF shall be notified to investors in advance of the change. The notice period should be sufficiently long to allow for redemption requests to be submitted by investors and processed prior to the change being effected. The change in the investment objectives should only become effective after all pending redemptions linked to the change in the investment objectives have been satisfied. Any applicable redemption fees would also need to be waived accordingly.
- 4.69 The following shall be the rules applicable in the event of an inadvertent breach of investment restrictions:
- i. if one or more of the AIF's investment restrictions are at any time contravened for reasons beyond the control of the AIFM or the AIF, the AIFM or the AIF must take such steps as are necessary to ensure a restoration of compliance with such restriction(s) as soon as is reasonably practicable having regard to the interests of the unit-holders and, in any event, within the period of six months beginning on the date of discovery of the contravention of such restriction(s);

The above is aimed at addressing circumstances which may arise following acquisition of the AIF's assets and include market price movements of the AIF's underlying assets or market illiquidity. The above is without prejudice to the duty of the AIFM and the AIF to comply with the AIF's investment restrictions and to ensure that such restrictions are not contravened as a direct result of any acquisition of its underlying assets.

- ii. a contravention of an investment restriction which may arise due to the circumstances outlined in (i) above shall not be considered as a breach of a licence condition and will therefore not be subject to MFSA's notification requirements. However, where the contravention is not remedied by the AIFM or the AIF within the maximum six month period stipulated in (i) above, a breach of this Licence Condition is deemed to arise and the relevant notification requirements will apply.

Cross Sub-Fund Investments

- 4.70 A sub-fund may invest in units of one or more sub-funds within the same scheme, subject to this being permitted in the constitutional documents and the Offering Memorandum of the said AIF and subject to the following:
- a. the investment company should in its memorandum of association elect to have the assets and liabilities of each sub-fund comprised in that company treated as a patrimony separate from the assets and liabilities of each other sub-fund of such company in terms of Regulation 9 of the Companies Act (Investment Companies with Variable Share Capital) Regulations;
 - b. the sub-fund is allowed to invest up to 50% of its assets into any sub-fund within the same scheme;
 - c. the target sub-fund/s may not themselves invest in the sub-fund which is to invest in the target sub-fund/s;
 - d. in order to avoid duplication of fees, where the AIFM of the sub-fund and the AIFM of the target sub-fund is the same or (in the case of different AIFMs) where one AIFM is an affiliate of the other, only one set of management (excl. performance fees), subscription and/or redemption fees applies between the sub-fund and the target sub-fund, provided that this restriction shall apply only in respect of and to the extent (up to the portion) of the investment of the sub-fund in the target sub-fund;
 - e. for the purposes of ensuring compliance with any applicable capital requirements, cross-investments will be counted once;
 - f. any voting rights acquired by the sub-fund from the acquisition of the units in the target sub-fund shall be disappplied as appropriate.

INVESTMENT POLICIES, OBJECTIVES AND RESTRICTIONS APPLICABLE TO ALTERNATIVE INVESTMENT FUNDS WHICH ARE SOLD TO PROFESSIONAL INVESTORS

Investment Restrictions

- 4.71 The AIF shall be subject to the investment objectives, policies and restrictions outlined in its Offering Document. In addition, where the AIF intends effecting its investments through the use of Trading Companies or Special Purpose Vehicles, it shall also be subject to the supplementary conditions regarding the use of such vehicles set out in Appendix I to these Rules. The AIFM or the AIF shall take all reasonable steps to comply with the investment policies and restrictions of the AIF.
- 4.72 Changes to the investment objectives of the AIF shall be notified to investors in advance of the change. The notice period should be sufficiently long to allow for redemption requests to be submitted by investors and processed prior to the change being effected. The change in the investment objectives should only become

effective after all pending redemptions linked to the change in the investment objectives have been satisfied. Any applicable redemption fees would also need to be waived accordingly.

4.73 The following shall be the rules applicable in the event of an inadvertent breach of investment restrictions:

- i. if one or more of the AIF's investment restrictions are at any time contravened for reasons beyond the control of the AIFM or the AIF, the AIFM or the AIF must take such steps as are necessary to ensure a restoration of compliance with such restriction(s) as soon as is reasonably practicable having regard to the interests of the unit-holders and, in any event, within the period of six months beginning on the date of discovery of the contravention of such restriction(s);

The above is aimed at addressing circumstances which may arise following acquisition of the AIF's assets and include market price movements of the AIF's underlying assets or market illiquidity. The above is without prejudice to the duty of the AIFM and the AIF to comply with the AIF's investment restrictions and to ensure that such restrictions are not contravened as a direct result of any acquisition of its underlying assets.

- ii. a contravention of an investment restriction which may arise due to the circumstances outlined in (i) above shall not be considered as a breach of a licence condition and will therefore not be subject to MFSA's notification requirements. However, where the contravention is not remedied by the AIFM or the AIF within the maximum six month period stipulated in (i) above, a breach of this Licence Condition is deemed to arise and the relevant notification requirements will apply.

Cross Sub-Fund Investments

4.74 A sub-fund may invest in units of one or more sub-funds within the same scheme, subject to this being permitted in the constitutional documents and the Offering Memorandum of the said AIF and subject to the following:

- i. the investment company should in its memorandum of association elect to have the assets and liabilities of each sub-fund comprised in that company treated as a patrimony separate from the assets and liabilities of each other sub-fund of such company in terms of Regulation 9 of the Companies Act (Investment Companies with Variable Share Capital) Regulations;
- ii. the sub-fund is allowed to invest up to 50% of its assets into any sub-fund within the same scheme;

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- iii. the target sub-fund/s may not themselves invest in the sub-fund which is to invest in the target sub-fund/s;
- iv. in order to avoid duplication of fees, where the AIFM of the sub-fund and the AIFM of the target sub-fund is the same or (in the case of different AIFMs) where one AIFM is an affiliate of the other, only one set of management (excl. performance fees), subscription and/or redemption fees applies between the sub-fund and the target sub-fund, provided that this restriction shall apply only in respect of and to the extent (up to the portion) of the investment of the sub-fund in the target sub-fund;
- v. for the purposes of ensuring compliance with any applicable capital requirements, cross-investments will be counted once;
- vi. any voting rights acquired by the sub-fund from the acquisition of the units in the target sub-fund shall be disapplied as appropriate.

5. TRANSPARENCY REQUIREMENTS

Constitutional Documents

- 5.01 Any changes to the Constitutional Document of the AIF must be approved by the MFSA in advance of implementation.
- 5.02 The Constitutional Documents shall contain at least the information prescribed in Appendix 3.

Offering Document

- 5.03 The AIF shall publish an Offering Document, which shall be dated and which shall be kept up to date. The Offering Document shall be offered to investors free of charge before they become committed to investing.
- 5.04 The Offering Document shall contain sufficient information for investors to make an informed judgement about the investment proposed to them and shall contain at least the information prescribed in Appendix 4.
- 5.05 The AIF shall approve the Offering Document including any amendments thereto, and confirm its approval to the MFSA.
- 5.06 The Offering Document and any amendments thereto shall be sent to and agreed with the MFSA before publication. The AIFM must submit a copy of its approval of the Offering Document, when this is submitted for the MFSA's approval.

Annual Report

- 5.07 The AIF or the AIFM or Administrator on its behalf shall submit copies of the AIF's annual audited financial statements to the MFSA and such other information, as the MFSA may from time to time request. The annual reports shall be published and provided to investors in the AIF upon request. The annual reports shall be submitted to the MFSA within six months respectively of the end of the period concerned.

Where applicable, the AIF or the AIFM or Administrator on its behalf shall also include with the annual report a confirmation in terms of SLC 4.13 of these Rules on the involvement of the AIF in foreign currency lending.

- 5.08 The annual report shall be accompanied by a report by the Custodian on whether the AIF has been managed:
- a. in accordance with the limitations imposed on the investment and borrowing powers of the AIF by the Constitutional Documents and by the MFSA; and

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b. in accordance with its Constitutional Document and its Licence Conditions.

In the case of non-compliance with (a) or (b) above, the Custodian's Report should outline the steps taken to rectify the situation.

- 5.09 The accounting information given in the annual report shall be prepared in accordance with the IFRS as adopted by the EU and with the accounting rules laid down in the Constitutional Documents.
- 5.10 The accounting information given in the annual report shall be audited by a certified auditor in accordance with SLC 3.44. The auditor's report, including any qualifications, shall be reproduced in full in the annual report.
- 5.11 The AIF shall also submit to the MFSA, on the following e-mail address: fundreporting@mfsa.com.mt, any statistical returns which may be required by the Central Bank of Malta to fulfil European and other relevant reporting obligations.
- 5.12 In complying with the requirements prescribed in this section above, the AIF shall also refer and comply with the applicable provisions of the Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision outlining the content and format of the annual report. The content and format of the annual report shall be adapted to the type of AIF to which it applies.

6. DEALINGS BY OFFICIALS OF AN AIF

- 6.01 Where the AIF allows its officials to deal for their own account, it is responsible for ensuring that such a practice does not lead to abuse. The standards and procedures to be adopted should include the following:
- a) The AIF must take appropriate steps to ensure that officials act in conformity with the statutory requirements concerning insider dealing and market abuse.
 - b) Internal mechanisms should be established to prompt the Compliance Officer's intervention if and when in respect of any staff member, abnormal behaviour or patterns concerning investment transactions are observed.
- 6.02 All transactions undertaken by officials on their own account should be at "arm's length" – but this does not preclude discounts being allowed to officials.

7. **MARKETING OF AN AIF**

- 7.01 The marketing of the AIF is subject to the provisions of Section 11 of the Act.
- 7.02 The AIF may only be marketed with a passport in jurisdictions outside Malta if it satisfies the relevant provisions prescribed in the Investment Services Act (Alternative Investment Fund Manager Passport) Regulations and the Investment Services Act (Marketing of AIFs) Regulations. The marketing of an AIF in jurisdictions outside Malta to investors other than Professional Investors as defined in this Rulebook is not automatic and may be allowed subject to national provisions applicable in the respective jurisdiction as prescribed in Article 43 of the AIFM Directive.

8. SUPPLEMENTARY LICENCE CONDITIONS APPLICABLE TO SELF-MANAGED AIFS

For the purposes of this section, the term ‘the AIF’ shall be understood as referring to a ‘Self-Managed AIF’.

Permissible Activities

8.01 A self-managed AIF may only be authorised to provide the licensable activities which consist in the internal management of the AIF as provided hereunder:

- (a) Investment management functions which the AIF shall at least perform:
 - [i] Portfolio management;
 - [ii] Risk management.

- (b) Other functions that an AIF may additionally perform in the course of the collective management thereof:
 - [i] Administration
 - legal and fund management accounting services;
 - customer inquiries;
 - valuation and pricing, including tax returns;
 - regulatory compliance monitoring;
 - maintenance of Unit or Shareholder register;
 - distribution of income;
 - unit/shares issues and redemptions;
 - contract settlements including certificate dispatch;
 - record keeping.
 - [ii] Marketing;
 - [iii] Activities related to the assets of the AIF, namely services necessary to meet the fiduciary duties of the AIF, facilities management, real estate administration activities, advice to undertakings on capital structure, industrial strategy and related matters, advice and services relating to mergers and the purchase of undertakings and other services connected to the management of the AIF and the companies and other assets in which it has invested.

8.02 Without prejudice to the generality of Article 6(6) of the Act, in the case of an application for a licence as a self-managed AIF, the MFSA shall inform the applicant in writing within three months of the submission of a complete application, whether or not the licence has been granted. The MFSA may prolong this period for up to

three additional months, where it considers necessary due to the specific circumstances of the case and after having notified the applicant accordingly.

Provided that for the purpose of this SLC, an application is deemed to be complete if the applicant has at least submitted the information referred to in the Checklist to the Application Form in Schedule 1 to Part A of these Rules to the satisfaction of the Authority.

The AIF shall commence its activities as soon as the licence has been granted.

- 8.03 A self-managed AIF may start providing an investment service in Malta with investment strategies described in accordance with the Application Form submitted to the MFSA as soon as the licence is granted, but not earlier than 1 month after having submitted any missing information referred to hereunder:
- (a) Information on arrangements made for the delegation and sub-delegation to third parties of functions referred to in SLCs 8.65 to 8.73 of this Part of the Rules;
 - (b) The memorandum and articles of association of the AIF;
 - (c) Information on the arrangements made for the appointment of the custodian in accordance with Part BIV of the Investment Services Rules for Investment Services Providers;
 - (d) Any additional information referred to in SLC 8.74 of this Part of the Rules.
- 8.04 The MFSA may restrict the scope of the authorisation in particular as regards the investment strategies an AIF is allowed to adopt.

Financial Resources Requirements

- 8.05 The AIF shall have sufficient financial resources at its disposal to enable it to conduct its business effectively, to meet its liabilities and to be prepared to cope with the risks to which it is exposed.
- 8.06 Without prejudice to the generality of SLC 8.05, the AIF must have own funds which are equivalent to an initial capital of at least EUR 300,000.
- 8.07 The financial resources of the AIF shall at all times exceed the level prescribed. The AIF shall maintain own funds equal to or in excess of its capital resources requirement and these shall constitute the AIF's financial resources requirement.
- 8.08 Where the value of the portfolio of the AIF exceeds EUR 250 million, the AIF will be required to provide an additional amount of own funds which is equal to 0.02% of the amount by which the value of the portfolio of the AIF exceeds EUR 250 million:

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Provided that the required total of the initial capital and the additional amount of own funds shall not exceed EUR 10 million.

- 8.09 Without prejudice to the amounts prescribed in SLC 8.08 above, the own funds of the AIF shall never be less than the amount required under Article 21 of Directive 2006/49/EC i.e. one quarter of the preceding year's fixed overheads.
- 8.10 The MFSA may authorise an AIF not to provide up to 50% of the additional amount of own funds referred to in SLC 8.08 above, if it benefits from a guarantee of the same amount given by a credit institution or an insurance undertaking which has its registered office in Malta, in another Member State or EEA State or in a third country where it is subject to prudential rules considered by the MFSA as equivalent to those prescribed by Union Law.
- 8.11 The AIF shall comply with any further financial resources requirements set by the MFSA. If the MFSA so determines, the AIF will be given due notice in writing of the additional financial resources requirements which shall be applied.
- 8.12 The AIF shall immediately advise the MFSA if at any time it is in breach of its Financial Resources Requirement. In this case, the MFSA may, if the circumstances justify it, allow the AIF a limited period within which to restore its financial resources to the required level.

Professional Liability Cover

- 8.13 To cover professional liability risks resulting from activities which the AIF may carry out pursuant to these Rules, the AIF shall either:
- (a) have additional own funds which are appropriate to cover potential liability risks arising from professional negligence; or
 - (b) hold professional indemnity insurance against liability arising from professional negligence which is appropriate to the risks covered.
- 8.14 The AIF shall purchase the Professional Indemnity Insurance from an EU or non-EU undertaking authorised to provide professional indemnity insurance in accordance with Union law or Maltese law. The Professional Indemnity Insurance can also be provided by a third party entity.
- 8.15 For the purposes of demonstrating to the satisfaction of the MFSA that the above requirement is being complied with on an ongoing basis, the AIF shall submit a copy of the cover note or such other written evidence as the MFSA may require to establish compliance with these Rules.

- 8.16 The AIF shall, within two days from the date it becomes aware of any circumstances specified in (a) to (g) below, inform the MFSA in writing where:
- a. during the term of the policy, the AIF has notified insurers of an incident which may give rise to a claim under the policy;
 - b. during the term of a policy, the insurer has cancelled the policy or has notified its intention of doing so;
 - c. the policy has not been renewed or has been cancelled and another policy satisfying the requirements prescribed in this section has not been taken out from the day on which the previous policy lapsed or was cancelled;
 - d. during the term of a policy, the terms or conditions are altered in any manner so that the policy no longer satisfies the requirements prescribed in this section;
 - e. the insurer has intimated that it intends to decline to indemnify the insured in respect of a claim under the policy;
 - f. the insurer has given notice that the policy will not be renewed or will not be renewed in a form which will enable the policy to satisfy the requirements prescribed in this section;
 - g. during the term of a policy, the risks covered by the policy or the conditions or terms relating thereto are altered in any manner.
- 8.17 Own funds including any additional own funds as referred to in SLC 8.14(a), shall be invested in liquid assets or assets readily convertible to cash in the short term and shall not include speculative positions.
- 8.18 In complying with SLC 8.14 above, the AIF shall also refer and comply with the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

Operational arrangements

- 8.19 The AIF shall at all times use adequate and appropriate human and technical resources that are necessary for its proper management.
- 8.20 The AIF shall be required to have sound administrative and accounting procedures, control and safeguard arrangements for electronic data processing and adequate internal control mechanisms, in particular, having regard also to the nature of the AIF itself.

- 8.21 In particular these will include rules for personal transactions by its employees or for the holding or management of investments in order to invest on its own account and ensuring at least, that each transaction involving the AIF may be reconstructed according to its origin, the parties to it, its nature, and the time and place at which it was effected and that the assets of the AIF are invested according to the Constitutional Documents, the Offering Document and any other legal provisions in force.
- 8.22 In adhering with the requirements prescribed in SLCs 8.19 to 8.21 above, the AIF shall also refer and comply with the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

Investment Committee

- 8.23 The management of the assets of the AIF is entrusted with the Board of Directors, at least one member of whom must be resident in Malta.
- 8.24 The Board of Directors shall establish an in-house Investment Committee made up of at least three members, whose composition may include members of the Board of Directors. The Terms of Reference of this Investment Committee - The Terms of Reference of this Investment Committee – which regulate the proceedings of the Investment Committee – and any changes thereto are subject to the prior approval of the MFSA.
- 8.25 The majority of Investment Committee meetings – the required frequency of which should depend on the nature of the AIF’s investment policy, but which should be at least quarterly – are to be physically held in Malta. Investment Committee meetings are deemed to be physically held in Malta if the minimum number of members that form a quorum necessary for a meeting are physically present in Malta.
- 8.26 The minutes of meetings of the Investment Committee should be available in Malta for review during MFSA’s compliance visits.
- 8.27 The role of the Investment Committee will be to:
- a. Monitor and review the investment policy of the AIF;
 - b. Establish and review guidelines for investments by the AIF;
 - c. Issue of rules for stock selection;
 - d. Set up the portfolio structure and asset allocation; and
 - e. Make recommendations to the Board of Directors of the AIF

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- 8.28 Where the AIF has not appointed an Investment Committee, the functions mentioned in SLC 8.27 shall be undertaken by the Directors of the AIF and any reference to Investment Committee throughout this Section shall be construed as reference to the Board of Directors of the AIF.
- 8.29 The Investment Committee may delegate the day-to-day investment management of the assets of the AIF to one or more officials of the AIF referred to as “the Portfolio Manager/s”. The Portfolio Managers will effect day-to-day transactions within the investment guidelines set by the Investment Committee and in accordance with the investment objectives, policy and restrictions described in the AIF’s Offering Document/ Marketing Document.
- 8.30 The AIF shall obtain the written consent of the MFSA before the appointment or replacement a member of the Investment Committee or a Portfolio Manager. The MFSA reserves the right to object to the proposed replacement or appointment and to require such additional information it considers appropriate. The MFSA shall be entitled to be satisfied, on a continuing basis, of the fitness and properness, including competence, of the members of the Investment Committee and of the Portfolio Manager/s.
- The request for consent of the appointment of a member of the Investment Committee or a Portfolio Manager shall be accompanied by a PQ and Competency Form in the forms set out in Schedules 2 and 3 to Part A of these Rules together with a detailed CV of the person proposed.
- 8.31 The AIF shall notify the MFSA in writing of the departure of a Member of the Investment Committee and/ or a Portfolio Manager within 14 days of the departure. The AIF shall also request the Investment Committee and/ or the Portfolio Manager, as applicable, to confirm that his/ her departure has no regulatory implications or otherwise provide any relevant details, as appropriate. A copy of such request shall be provided to MFSA.
- 8.32 The AIF shall have adequate arrangements, in agreement with and subject to the approval of the MFSA, to ensure adequate monitoring of the activities of the Portfolio Manager/s and the Investment Committee.
- 8.33 The AIF shall on a continuing basis ensure that it has sufficient management resources to effectively conduct its business.

Permanent Risk Management Function

- 8.34 The AIF shall functionally and hierarchically separate the functions of risk management from the operating units including from the functions of portfolio management.

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8.35 The MFSA shall review the functional and hierarchical separation of the functions of risk management in accordance with SLC 8.35 above in accordance with the principle of proportionality, on the understanding that the AIF shall, in any event, be able to demonstrate that specific safeguards against conflicts of interest allow for the independent performance of risk management activities and that the risk management process satisfies the requirements of SLCs 8.34 to 8.40 and is consistently effective.

8.36 The AIF shall implement adequate risk management systems in order to identify, measure, manage and monitor appropriately all risks relevant to its investment strategy and to which it is or may be exposed.

8.37 The AIF shall review the risk management systems with appropriate frequency at least once a year and adapt them whenever necessary.

Provided that the frequency of the periodic review shall be decided by the senior management in accordance with the principle of proportionality given the nature, scale and complexity of the business of the AIF.

8.38 The AIF shall at least:

- a. Implement an appropriate, documented and regularly updated due diligence process, according to the AIF's investment strategy, objectives and risk profile;
- b. Ensure that the risks associated with each investment position of the AIF and their overall effect on the AIF's portfolio can be properly identified, measured, managed and monitored on an ongoing basis, including through the use of appropriate stress testing procedures;
- c. Ensure that the risk profile of the AIF shall correspond to the size, portfolio structure and investment strategies and objectives of the AIF as provided for in its Constitutional Documents and/or Offering Document.

Provided that in complying with SLC 8.38 above, the AIF shall submit to the MFSA the information prescribed in Annex 3 to Appendix 8 to these Rules dealing with results of stress tests and shall further comply with the applicable provisions of the Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

8.39 The AIF shall set a maximum level of leverage which it may employ as well as the extent of the right to reuse collateral or guarantee that could be granted under the leveraging arrangement, taking into account, *inter alia*:

- a. The type of the AIF;

- b. The investment strategy of the AIF;
- c. The sources of leverage of the AIF;
- d. Any other interlinkage or relevant relationships with other financial services institutions, which could pose systemic risk;
- e. The need to limit the exposure to any single counterparty;
- f. The extent to which the leverage is collateralised;
- g. The asset-liability ratio;
- h. The scale, nature and extent of the activity of the AIF on the markets concerned.

8.40 In complying with SLCs 8.34 to 8.39 above, the AIF shall also refer and comply with the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

Liquidity Management Policy

8.41 An AIF which is not an unleveraged closed-ended AIF shall employ an appropriate liquidity management system and adopt procedures which enable it to monitor the AIF's liquidity risk and to ensure that the liquidity profile of the investment of the AIF complies with its underlying obligations.

8.42 The AIF shall regularly conduct stress tests, under normal and exceptional liquidity conditions, which enable it to assess the AIF's liquidity risk and monitor it accordingly.

8.43 In complying with SLC 8.42 above, the AIF shall submit to the MFSA the information prescribed in Annex 3 to Appendix 8 to these Rules dealing with results of stress tests and shall further comply with the applicable provisions of the Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

8.44 The AIF shall ensure that the investment strategy, the liquidity profile and the redemption policy are consistent.

8.45 In complying with SLC 8.42 to SLC 8.44, the AIF shall also refer and comply with the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

Investment in securitisation positions

8.46 The AIF shall comply with the requirements on securitisation as prescribed in the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

Valuation

8.47 The AIF shall ensure that appropriate and consistent procedures are established so that a proper and independent valuation of the assets of the AIF can be performed in accordance with SLCs 8.47 to 8.62, the Constitutional Documents and/or Offering Documents.

8.48 The rules applicable to the valuation of assets and the calculation of the net asset value per Unit or Share of the AIF shall be those prescribed in the Investment Services Rules, the Constitutional Documents and/or Offering Documents.

8.49 The AIF shall also ensure that the net asset value per Unit or Share thereof is calculated and disclosed to investors in accordance with SLCs 8.47 to 8.62, the Constitutional Documents and/or Offering Documents.

8.50 The valuation procedures used shall ensure that the assets are valued and the net asset value per Unit or Share is calculated at least once a year.

8.51 If the AIF is an open-ended AIF, such valuations and calculations shall also be carried out at a frequency which is both appropriate to the assets held by the AIF and its issuance and redemption frequency.

8.52 If the AIF is a closed-ended AIF, such valuations and calculations shall also be carried out in case of an increase or decrease of the capital by the AIF.

8.53 The AIF shall inform the investors of the valuations and calculations as prescribed in the Constitutional Documents and/or Offering Documents.

8.54 The AIF shall ensure that the valuation function is either performed by:

- (a) An external valuer, being a legal or natural person independent from the AIF and any other persons with close links to the AIF; or
- (b) The AIF itself, provided that the valuation task is functionally independent from the portfolio management and the remuneration policy and other measures ensure that conflicts of interest are mitigated and that undue influence upon employees is prevented.

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- 8.55 The custodian appointed for an AIF shall not be appointed as external valuer of such AIF, unless it has functionally and hierarchically separated the performance of its depositary functions from its tasks as external valuer and the potential conflicts of interest are properly identified, managed, monitored and disclosed to the investors of the AIF.
- 8.56 Where an external valuer performs the valuation function, the AIF shall demonstrate that:
- (a) The external valuer is subject to mandatory professional registration recognised by law or to legal or regulatory provision or rules of professional conduct;
 - (b) The external valuer can provide sufficient professional guarantees to be able to perform effectively the relevant valuation function in accordance with SLCs 8.47 to 8.53; and
 - (c) The appointment of the external valuer complies with the requirements of SLCs 8.76 to 8.78 and with the provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision on SLC 8.84.
- 8.57 The external valuer shall not delegate the valuation function to a third party.
- 8.58 The AIF shall notify the appointment of the external valuer to the MFSA. The MFSA may require that another external valuer be appointed instead, where the conditions prescribed in SLC 8.56 are not met.
- 8.59 The valuation shall be performed impartially and with all due skill, care and diligence.
- 8.60 Where the valuation function is not performed by an independent external valuer, the MFSA may require the AIF to have its valuation procedures and/or valuations verified by an external valuer or, where appropriate by an auditor.
- 8.61 The AIF shall be responsible for the proper valuation of its assets, the calculation of the net asset value and the publication of that net asset value. The AIF's liability towards the AIF and its investors shall, therefore not be affected by the fact that the AIF has appointed an External Valuer.
- 8.62 Notwithstanding SLC 8.61 and irrespective of any contractual arrangements providing otherwise, the External Valuer shall be liable to the AIF for any losses suffered by the AIF as a result of the External Valuer's negligence or intentional failure to perform its tasks.

8.63 In complying with the provisions prescribed in SLCs 8.48 to 8.62, the AIF shall comply with the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

Conduct of Business

8.64 The AIF shall comply with the conduct of business rules prescribed hereunder. In particular the AIF shall:

- a. act honestly, with due skill, care and diligence and fairly in conducting its activities;
- b. act in the best interests of the AIF, the investors and the integrity of the market;
- c. have and employ effectively the resources and procedures that are necessary for the proper performance of its business activities;
- d. take all reasonable steps to avoid conflicts of interest and, when they cannot be avoided, to identify, manage and monitor and, where applicable, disclose, those conflicts of interest in order to prevent them from adversely affecting the interests of the AIF and the investors and to ensure that the AIF is fairly treated;
- e. comply with all regulatory requirements applicable to the conduct of its business activities so as to promote the best interests of the investors and the integrity of the market;
- f. treat all investors fairly.

8.65 No investor in the AIF shall obtain preferential treatment unless such preferential treatment is disclosed in the relevant AIF's Constitutional Documents and/or Offering Documents.

8.66 In complying with SLCs 8.64 and 8.65 the AIF shall also refer and comply with the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

Remuneration

8.67 The AIF shall have remuneration policies and practices for those categories of staff, including senior management, risk takers, control functions, and any employees receiving total remuneration that takes them into the same remuneration bracket as

senior management and risk takers, whose professional activities have a material impact on the risk profile of the AIF, that are consistent with and promote sound and effective risk management and do not encourage risk taking which is inconsistent with the risk profiles, the Constitutional Documents and/or Offering Documents of the AIF.

- 8.68 The AIF shall determine the remuneration policy and practice in accordance with the principles outlined in Appendix 7.
- 8.69 The AIF shall further comply with any guidelines on sound remuneration policies which shall be issued by ESMA.

Conflicts of Interest

- 8.70 The AIF shall act honestly, fairly and with integrity – in the best interests of its investors/ shareholders and of the market. Such action shall include:
- i. avoiding conflicts of interest where this is possible and, where it is not, ensuring - by way of disclosure, internal procedures or otherwise – that investors are treated fairly.
 - ii. the following procedures should be followed during meetings (including but not limited to Investment Committee Meetings), where a member considers that s(he) has or may have a conflict of interest:
 - a. that person should declare that interest to the other members either at the Meeting at which the issue in relation to which s(he) has an interest first arises, or if the member was not at the date of the Meeting interested in the issue, at the next Meeting held after s(he) became so interested;
 - b. unless otherwise agreed to by the other members, a member shall avoid entering into discussions in respect of any contract or arrangement in which s(he) is interested and should withdraw from the meeting while the matter in which s(he) has an interest is being discussed;
 - c. the interested member should not vote at a Meeting in respect of any contract or arrangement in which s(he) is interested, and if s(he) shall do so, his/ her vote shall not be counted in the quorum present at the Meeting;
 - d. the minutes of the meeting should accurately record the sequence of such events.
 - iii. abiding by all relevant laws and regulations, including in respect of Prevention of Money Laundering;

- iv. not making any claim of independence or impartiality which is untrue or misleading; and
 - v. not making misleading or deceptive representations to investors.
- 8.71 The AIF shall 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 investors.
- 8.72 The AIF shall segregate within its operating environment, tasks and responsibilities which may be regarded as incompatible with each other or which may potentially generate systematic conflicts of interest.
- 8.73 The AIF shall assess whether its operating conditions may involve any other material conflicts of interest and disclose them to the investors.
- 8.74 Where organisational arrangements made by the AIF 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 AIF shall 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.
- 8.75 In complying with SLCs 8.70 to 8.74, the AIF shall also refer and comply with the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

Delegation and sub-delegation

- 8.76 An AIF which intends delegating to third parties the task of carrying out functions on its behalf shall notify the MFSA before the delegation arrangements become effective. The AIF shall comply with the following requirements:
- a. the AIF must be able to justify its entire delegation structure on objective reasons;
 - b. the delegate must possess sufficient resources to perform the respective tasks and the persons who effectively conduct the business of the delegate must be of sufficiently good repute and sufficiently experienced;
 - c. where the delegation concerns portfolio management or risk management, it must be conferred only on undertakings which are authorised or registered for

the purpose of asset management and subject to supervision, or where that condition cannot be met, only subject to prior approval by the MFSA;

- d. where the delegation concerns portfolio management or risk management and is conferred on a Third Country undertaking, in addition to the requirements outlined in point (c) above, there must be a cooperation agreement in place between the MFSA and the supervisory authority of the Third Country;
- e. the delegation must not prevent the effectiveness of supervision of the AIF, and in particular, must not prevent the AIF from being managed, in the best interests of its investors;
- f. the AIF must be able to demonstrate that the delegate is qualified and capable of undertaking the functions in question, that it was selected with all due care and that the AIF is in a position to monitor effectively at any time the delegated activity, to give at any time further instructions to the delegate and to withdraw the delegation with immediate effect when this is in the interest of investors.

8.77 The AIF shall review the services provided by each delegate on an ongoing basis.

8.78 No delegation of portfolio management or risk management shall be conferred on:

- a. The Custodian or a delegate of the Custodian; or
- b. Any other entity whose interests may conflict with those of the AIF or the investors of the AIF, unless such entity has functionally and hierarchically separated the performance of its portfolio management or risk management tasks from its other potentially conflicting tasks, and the potential conflicts of interest are properly identified, managed, monitored and disclosed to the investors of the AIF.

8.79 The liability of the AIF towards the investors shall not be affected by the fact that the AIF has delegated functions to a third party, or by any further sub-delegation, nor shall the AIF delegate its functions to the extent that in essence, it can no longer be considered to be the manager of the AIF and to the extent that it becomes a letter-box entity.

8.80 The delegate may sub-delegate any of the functions delegated to it provided that the following conditions are met:

- a. The AIF consented prior to the sub-delegation;
- b. The AIF notified the MFSA before the sub-delegation arrangements became effective;

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- c. The conditions prescribed in SLCs 8.76 to 8.77 are fulfilled on the understanding that all references to the 'delegate' are read and construed as referring to the 'sub-delegate'.
- 8.81 No sub-delegation of portfolio management or risk management shall be conferred on:
- a. The custodian or a delegate of the custodian; or
 - b. Any other entity whose interests may conflict with those of the AIF or the investors of the AIF, unless such entity has functionally and hierarchically separated the performance of its portfolio management or risk management tasks from its other potentially conflicting tasks, and the potential conflicts of interest are properly identified, managed, monitored and disclosed to the investors of the AIF.
- 8.82 The relevant delegate shall review the services provided by each sub-delegate on an ongoing basis.
- 8.83 Where the sub-delegate further delegates any of the functions delegated to it, the conditions prescribed in SLC 8.80 shall apply *mutatis mutandis*.
- 8.84 In complying with SLCs 8.76 to 8.83 above, the AIF shall also refer and comply with the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.

Additional transparency Requirements applicable to self-managed AIFs

Disclosure to investors

- 8.85 The AIF shall make available to investors, in accordance with the Constitutional Documents and/or Offering Documents, the information prescribed in Appendix 4 (Disclosure to Investors) before they invest in the AIF as well as any material changes thereto.
- 8.86 The AIF shall also make available an annual report as outlined in Appendix 8 (Annual Report). The annual report shall be provided to investors upon request.

Disclosure to the MFSA

- 8.87 The AIF shall regularly report to the MFSA on the principal markets and instruments in which it trades as outlined in Appendix 8 (Disclosure to the Competent Authority).

- 8.88 In exceptional circumstances and where required in order to ensure the stability and integrity of the financial system or to promote long-term sustainable growth, the MFSA may impose additional reporting requirements following a specific request by ESMA to do so.

Additional reporting obligations for leveraged AIFs - Use of information by the MFSA, supervisory cooperation and limits to leverage

- 8.89 The AIF shall demonstrate that the leverage limit set by it is reasonable and that it complies with that limit at all times. The MFSA shall assess the risks that the use of leverage by an AIF could entail, and, where deemed necessary in order to ensure the stability and integrity of the financial system, the MFSA, after having notified ESMA and the ESRB, shall impose limits to the level of leverage that the AIF is entitled to employ or other restrictions on the management of the AIF, to limit the extent to which the use of leverage contributes to the build-up of systemic risk in the financial system or risks of disorderly markets. The MFSA shall duly inform ESMA and the ESRB of actions taken in this respect, through the procedure stipulated in the MFSA Act and the Investment Services Act.
- 8.90 The notification referred to in SLC 8.89 shall be made not less than 10 working days before the proposed measure is intended to take effect or to be renewed.
- 8.91 The notification referred to in SLC 8.89 shall include details of the proposed measure, the reasons for the measure and when the measure is intended to take effect.
- 8.92 In exceptional circumstances, the MFSA may decide that the proposed measure takes effect within the period of 10 working days referred to in SLC 8.89.
- 8.93 In complying with SLCs 8.89 to 8.92 above, the AIF shall also refer and comply with the applicable provisions of Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision.