

STANDARDS BOARD FOR ALTERNATIVE INVESTMENTS

SBAI AND ITS TRUSTEES

EXPLANATORY MEMORANDUM

No responsibility, duty of care or liability whatsoever (whether in contract or tort or otherwise including, but not limited to, negligence) is or will be accepted by the SBAI, the Board of Trustees of the SBAI, any Investor Chapter Member or any Core Supporter to Signatories, investors or any other person in connection with the Standards or any Conformity Statement or Disclosure Statement made by any Signatory.

Neither the SBAI nor its Board of Trustees is a regulator of the alternative investment industry and their role does not extend beyond being a custodian of the Standards. None of the SBAI, its Board of Trustees, the Investor Chapter Members and the Core Supporters will seek to enforce compliance with the Standards by Signatories. The fact that a manager is a Signatory to the Standards is not and should not be taken as an endorsement of such manager by the SBAI, the Board of Trustees, the Investor Chapter Members or the Core Supporters or as a representation by the SBAI, the Board of Trustees, the Investor Chapter Members or the Core Supporters that such Signatory operates in conformity with the Standards. In determining whether to accept a manager's application to become a Signatory (or whether to revoke a manager's status as a Signatory), the Board of Trustees will be entitled to rely on the information provided to it by such manager without further investigation or verification. Further, subject to any duties a Trustee may have under applicable law, it is not envisaged, or expected, that a Trustee will when participating in any such decision of the Board of Trustees take into consideration information which it may possess otherwise than in its capacity as a Trustee. For the avoidance of doubt, Trustees are acting as individuals.

None of the SBAI, the Board of Trustees of the SBAI, the Investor Chapter Members and the Core Supporters accepts any responsibility or liability for any loss or damage caused to any person who acts or refrains from acting as a result of anything contained in or omitted from the Standards or any Conformity Statement or Disclosure Statement made by any Signatory or in reliance on the provisions of or material in the Standards or any Conformity Statement or Disclosure Statement made by any Signatory, whether such loss or damage is caused by negligence or otherwise.

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The purpose of this memorandum is to provide prospective signatories to the standards (the "**Standards**") of the Standards Board for Alternative Investments Limited ("**SBAI**") with information on the establishment, structure and aims of the SBAI and its board of trustees (the "**Board of Trustees**").

1. SBAI AND THE BOARD OF TRUSTEES

- 1.1 In common with similar non-profit making bodies, the body established to perform the role of "guardian" of the Standards is a company limited by guarantee. The company is incorporated in England and Wales and its name is Standards Board for Alternative Investments Limited.
- 1.2 The Board of Trustees for the Standards is the board of directors of the SBAI. These directors will also be the sole members of the SBAI and in this capacity will each provide a guarantee of a nominal amount of £1, but will have no further funding obligation in respect of the SBAI. The further funding requirements of the SBAI are met as described in section 4 below.
- 1.3 The Board of Trustees is required to promote the objectives of the SBAI as set out in the mandate described in section 2 below and, in so doing, have regard to stakeholder interests, including those of managers, investors and intermediaries. The intention is that the Board of Trustees, being the only members of the SBAI, will be able to exercise their independent judgement free from external constraints.

2. SBAI'S/THE BOARD OF TRUSTEES' MANDATE

2.1 The Mandate

The Mandate is reflected in the Memorandum and Articles of Association of the SBAI.

2.2

- To be an independent body to be the guardian or custodian of standards for the alternative investment industry. (Initially those standards will be the standards set out in the Hedge Fund Working Group Final Report published in January 2008.)
- Not to act as a regulator and not to interpose itself in any way between managers and their regulators.
- To produce an annual report on conformity with the Standards by the industry.
- Not act as a trade association, which is the role of AIMA.
- To maintain a register of signatory firms available for public inspection.
- To maintain Standards which in the judgement of the Board of Trustees:
 - are up to date;
 - are set at a level that reflects a high standard of conduct;
 - meet the aspirations and needs of the managers;
 - reflect the expectations of other stakeholders;
 - meet the requirements of public policy;
 - respond to changes in practice and expectation; and
 - are iterated and revised in the case of existing standards and so that new standards are developed where gaps are identified.
- To maintain links with stakeholders, including managers, industry users and suppliers, trade associations (including AIMA), the FCA and other regulatory and supervisory bodies, both within and outside the UK.
- To consider other guidelines (initiatives) which may be published or promulgated in jurisdictions outside the UK.
- To recognise that the industry operates on a global basis and evaluate opportunities for, and impediments to, convergence.
- To retain a Board of Trustees who:
 - have skills and experience in a wide variety of sectors;
 - are of independent mind;
 - have skills and experience in governance matters;
 - are of high standing and capable of commanding respect;
 - have experience and understanding of the international dimension;
 - have a personal commitment to the success of and reputation of the industry;
 - are capable collectively of fulfilling the mandate.
- To consult publicly with all relevant stakeholders on any proposed changes to the mandate.

2.3 Guardians or Custodians

The Board of Trustees is the guardian or custodian of the Standards.

2.4 Not a Regulator

Neither the SBAI nor its Board of Trustees is a regulator (or a self-regulatory industry) of the alternative investment industry and their role does not extend beyond being a custodian of the Standards. In particular, neither the Board of Trustees nor the SBAI will stand between fund managers and their regulatory authority, whether the FCA or any overseas regulator. Neither the SBAI nor its Board of Trustees will seek to enforce compliance with the Standards by signatories; it is expected that compliance will be achieved through market pressure, as described in more detail in the HFWG Final Report. The fact that a manager is a signatory to the Standards is not and should not be taken as an endorsement of such manager by the SBAI or the Board of Trustees or as a representation by the SBAI or the Board of Trustees that such signatory operates in conformity with the Standards.

2.5 Annual Report

The Board of Trustees will produce an annual report which will review and report on the status of conformity with the Standards by the industry over the previous year. The report's approach is intended to be qualitative not quantitative.

2.6 Not a trade association

The SBAI will not be a trade association. AIMA already fulfils this function and there is no intention that the SBAI should compete with AIMA. The Board of Trustees will instead seek to co-operate and work closely with AIMA. Further details of the proposed relationship between the two organisations are set out in section 10.1 of the HFWG Final Report. In particular, it is envisaged that AIMA will produce guidance on compliance with the Standards.

2.7 Register of signatories

The SBAI will maintain a register of all firms who become signatories to the Standards. All 14 members of the HFWG have been signatories to the Standards from the start. The register will be made available for inspection on the SBAI's website.

2.8 Maintenance and development of the Standards

The mandate will require the Board of Trustees to review the Standards on a rolling basis and consider where changes may be needed in order to keep them, in the judgement of the Board of Trustees:

- up to date;
- recognised and respected as an important component of the financial landscape by industry members, users and suppliers, and by regulatory and supervisory bodies;
- set at a level that reflects high standards of conduct, modified as the expected standards of conduct rise over time;
- meeting the aspirations and the needs of the managers and taking into account the practical realities they face;
- reflecting the expectations of other stakeholders, in particular those of investors; and
- meeting the public policy requirements of the day.

The Board of Trustees will need to be mindful not just of the need for iteration and revision of existing Standards, but also of the need to identify gaps in the Standards and produce new or amended Standards, as appropriate, to address them.

The Board of Trustees will consult the industry and the wider public on proposed changes and/or additions to the Standards.

2.9 Liaison with stakeholders

In order to maintain the Standards in the way described above, the Board of Trustees will need to maintain links with all of the stakeholders in the industry. In addition to the fund manager community and its users and suppliers, other key stakeholders include the FCA and other regulatory and supervisory bodies elsewhere in Europe and globally.

2.10 Supervisory issues

In maintaining the Standards, the Board of Trustees will also need to consider issues of greatest concern to public policy, such as financial stability, investor protection and market integrity.

2.11 Changes to the mandate

The mandate of the SBAI and its Board of Trustees as set out in section 2.1 above will be reflected as appropriate in the SBAI's constitution and as such will be a matter of public record. It will also be made available on the SBAI's website. The constitution of the SBAI will require the Board of Trustees to consult publicly with

all relevant stakeholders on any changes to the mandate which the Trustees may propose to make from time to time. However, the final decision on any changes to the mandate will remain with the Trustees.

2.12 Skills and qualities required

The mandate also includes requirements as to the composition and membership of the Board of Trustees as a whole. The Board must consist of members who demonstrate the following attributes and qualities:

- a broad range of **skill sets and experience** derived from the alternative investment world, other areas of investment management and public policy related to financial services;
- an **independent mind**, and an ability to place their specialist understandings of, for example, the world of fund management in a broader context
- skills and experience in **governance** matters;
- be of **high standing** and capable of commanding the respect of the alternative investment community as well as its users and regulators;
- include individuals with **international understanding**; and
- include individuals with a **personal commitment** to the success of the industry and its good reputation.

2.13 Consideration of standards in other jurisdictions

The mandate requires the Board of Trustees, when considering whether the Standards should be updated to consider other relevant guidelines (initiatives) which may be published or promulgated in jurisdictions outside the UK. The purpose is to see what might be learnt from them and where convergence may be appropriate. In so doing, the Trustees will need to be mindful of proper differences stemming from variations in law and regulation and in business practice.

2.14 Convergence over time

Equally, the Board of Trustees should evaluate opportunities for, and impediments to, convergence with standards in other jurisdictions. This will be of particular importance in areas such as valuation and risk management, which are of direct relevance to financial stability. Clearly, much could be gained by minimising the differences between standards which emanate from different jurisdictions. Convergence would improve clarity for stakeholders and promote confidence in the industry in the UK and globally.

2.15 **President's Working Group of the USA**

The Board of Trustees assessed the findings of the US President's Working Group report into the alternative investment industry and incorporated them in the Standards

3. HOW WILL THE TRUSTEES BE APPOINTED?

- 3.1 The Board of Trustees has the power to nominate and appoint new Trustees and to reappoint Trustees who retire and put themselves forward for re-appointment at any annual general meeting of the SBAI. Signatories will be entitled to attend an annual meeting of signatories at which, commencing in 2010, the signatories will consider and, if thought fit, indicate their approval of the appointment or reappointment of the Trustees who have been appointed or reappointed as Trustees at the annual general meeting of the SBAI held in that year. Signatories will thereby be offered the opportunity as a group to express their view on such appointments and reappointments. In the event that a resolution to indicate approval of any such appointment or reappointment is not passed by the signatories, this will not affect the appointment or reappointment of the relevant Trustee by the members of the SBAI.
- 3.2 There will be no prescribed groups from which the Board of Trustees should be drawn and only the Board of Trustees will be able to make nominations. However, for practical reasons the number of Trustees is limited to 20.

4. HOW WILL MANAGERS SIGN UP TO THE STANDARDS?

- 4.1 Managers will be invited to sign up to the Standards by completing a simple application form issued by the SBAI. A brief explanatory memorandum will accompany the form. By signing up to the Standards, fund managers will undertake to adopt the comply or explain regime set out in the Standards and to publicise this on their websites and elsewhere as further detailed in the Final HFWG Report. Managers who sign up to the Standards will be expected to bear a share of the costs of the SBAI calculated on what is intended to be an equitable basis, but with a smaller contribution expected from smaller managers.
- 4.2 In the event that a signatory fails to comply with any of the undertakings given by the signatory in the application form, the Board of Trustees may, at its sole discretion, revoke its acceptance of that manager as a signatory to the Standards. In the event that a manager does so cease to be a signatory to the Standards, it will not hold itself out in any way as a signatory to the Standards and in particular will cease to communicate in its marketing materials and/or to display on its website that it is a signatory to the Standards.

5. HOW WILL INVESTORS JOIN THE SBAI?

- 5.1 Investors will be invited to join the SBAI Investor Chapter by completing a simple application form issued by the SBAI. By joining the Investors Chapter, investors will undertake to promote the Standards, encourage managers to achieve conformity with the Standards, integrate the Standards in their due diligence process and interact with the Board of Trustees, managers and investors to provide recommendations on

improving the Standards. Investors will also provide funding towards the working capital of the SBAI.

5.2 **Register of investors**

The SBAI will maintain a register of all firms who joined the Investor Chapter. The register will be made available for inspection on the SBAI's website.

Standards Board for Alternative Investments

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