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## 9 PRODUCT OVERSIGHT AND GOVERNANCE

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### 9.1 Introduction

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This section of the Manual sets out the Firm's approach to the FCA's product oversight and governance regime, the rules of which are set out in the [PROD](#) sourcebook. Appendix Q can be found in the Manual Appendices and provides assessment questionnaires for both the AR and Firm to complete in respect of each new and existing product and service as to their current compliance with the PROD rules, and thus an indication of further action that may be required.

The PROD assessment should be completed when any new product or service is launched and also on an ad hoc basis (fund closes etc). Although much of the focus is on products, the rules also capture investment services and should be applied accordingly.

### 9.2 Background

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The FCA's product oversight and governance rules came into force on 3 January 2018 in line with the introduction of MiFID II. Although the FCA had product governance requirements before the introduction of MiFID II, these were narrower in scope than the new rules in terms of the financial instruments they covered.

In simple terms, the product governance element of MiFID II is aimed at ensuring advisers are offering their clients suitable solutions, by requiring product manufacturers and distributors, such as advisers, to identify target markets. It is therefore vital that firms to which the PROD rules apply ensure they have structured their business approach accordingly and are able to demonstrate the application of these rules.

### 9.3 The Product Oversight and Governance Regime

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#### 9.3.1 Definitions

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Product oversight and governance means the systems and controls firms have in place for the design, approval, marketing and ongoing management of products and services throughout their lifecycle, to ensure they meet legal and regulatory requirements. If these systems and controls are working effectively then products will:

- Meet the needs, characteristics and objectives of one or more identifiable target markets.
- Be sold to clients in the target markets by appropriate distribution channels.
- Deliver appropriate client outcomes.

The FCA define a manufacturer as a person creating, developing, issuing and/or designing an investment, including when advising corporate issuers on the launch of new investments.

The definition of a distributor is a person offering, recommending, or selling an investment, or providing an investment service to a client.

#### 9.3.2 PROD Sourcebook

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The FCA's PROD sourcebook is split into 4 sections, but only the first 3 apply to the Firm and its ARs:

- PROD 1. Product intervention and product governance sourcebook, providing a summary of each of the 4 PROD sections.

- PROD 2. Statement of policy with regards to making of temporary product intervention rules, is the FCA's position on when it will intervene with regards to a product and apply temporary restrictions.
- PROD 3. Product governance: MiFID sets out the rules to be applied for both the manufacture and distribution of a product that falls under the MiFID umbrella.
- PROD 4. Product governance for insurance-based investment (IDD) products.

In summary, PROD 1 and 2 provide information, whilst PROD 3 sets out action to be taken. This Manual only considers PROD 3 requirements as the Firm does not have the regulatory permissions to conduct insurance-related business. PROD 3 thus applies to MiFID investment firms, CRD credit institutions, MiFID optional investment firms, and branches of third-country investment firms. For non-MiFID firms that manufacture or distribute financial instruments, the FCA has stated that these firms should (as opposed to must) follow the PROD rules. Therefore, the Firm has opted to apply the principles of the PROD regime to non-MiFID business which includes acting as an AIFM for an AIF.

As a principal, the Firm has the responsibility to oversee the regulated activities of its ARs, and ensure these activities fall within the perimeter of its authorised permissions. This then means that any AR which manufactures, and/or distributes a financial instrument or investment service must comply with the PROD 3 sourcebook.

For manufacturers and distributors in scope of PROD 3, there are several overarching key elements that must be complied with, as follows:

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### 9.3.3 Manufacturers

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For manufacturers of financial instruments:

- The product is designed to meet the needs, characteristics and objectives of the client target market (i.e. Professional Clients and/or Eligible Counterparties' business clients).
- That the strategy for the distribution of the product is compatible with this target market.
- That the product is actually distributed to the target market.
- That where new products have been developed or existing products are being significantly modified, a process of approval has been followed.
- That risks associated with the design of the product and its intended target market have been assessed and mitigated.
- That where products have been manufactured in collaboration with other firms, a written agreement outlining mutual responsibilities must be in place.
- That products undergo scenario testing and analysis to assess the risks of poor outcomes for clients and the circumstances in which those poor outcomes arise.
- That sufficient information is available to intended and existing distributors of new and existing products covering the functioning of the product, the approval process, the target market, and appropriate distribution channels.
- That the product manufacturer has a robust review process in place to ensure the product remains fit for the purpose of its intended target market.
- Where product alignment issues are identified, prompt action is taken to address them.
- That the product manufacturer has considered and reviews potential and actual conflicts of interest to ensure no client is adversely impacted and market integrity issues are not created.
- That sufficient oversight and training mechanisms are in place to enable sufficient governance of the manufacturing process and the knowledge of personnel involved in this.
- That monthly compliance reports include details of the products manufactured and the distribution strategy.

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### 9.3.4 Distributors

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For distributors of financial instruments:

- That a comprehensive understanding and knowledge of the product being provided is obtained via information provided by the manufacturer.
- That the target market is clearly identified, even if not specified by the manufacturer, and this aligns with the target market of the distributor.
- That a distribution strategy is set out, considering wider FCA rules, as necessary.
- That appropriate governance arrangements are in place.
- That personnel involved in the distribution of the product have the necessary knowledge and understanding of the product to do so effectively.
- That compliance reports include details of the products distributed by the firm.
- That a robust review process is in place to ensure the product remains fit for the purpose of its intended target market, and its governance arrangements provide sufficient oversight.
- That a process is in place to provide feedback to the manufacturer on sales and reviews undertaken.
- That where the distribution of a product is to another distributor, the responsibilities in this chain are understood. Where this applies, please refer to section 9.5 below, which contains the policy and procedure for the appointment of introducers and placement agents.

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## 9.4 PROD Annex Assessment Questionnaire

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### 9.4.1 Assessment Questionnaire

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The Firm will provide each new AR with a blank PROD assessment questionnaire to complete once the AR entity has been appointed by the FCA. The PROD assessment questionnaire is also available on Leo. Once the AR has completed the PROD assessment, the Firm will review it to establish the AR's current level of compliance with the rules and whether the AR is conducting its regulated activity as a manufacturer and/or a distributor. The Firm's review will be recorded in the Firm's version of the assessment questionnaire in Appendix Q. ARs should complete the required sections of the assessment themselves, as this will be reviewed as part of monitoring, and report material changes (such as the appointment of an introducer) to the Firm. Existing ARs will be required to update and/or complete a new PROD assessment on an ad hoc basis also (launch of new product/fund, initial and subsequent fund closes, etc).

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### 9.4.2 Follow-Up

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If on completion of the assessment questionnaire there are identified compliance gaps, the AR must report these to the Firm and take the necessary action to address the issues at hand. There is no defined solution as it is dependent on the context of each AR firm. However, actions may require, but are not limited to:

- Putting in place policies.
- Training staff.
- Defining a process.
- Identifying the product target market.
- Identifying conflicts of interest.
- Establishing appropriate management information.
- Establishing a monitoring regime.
- Establishing a product review mechanism.
- Establishing a feedback loop.

Sign-off for implemented actions to address any gaps will be undertaken by the Compliance Officer or a member of the compliance team, as delegated by the Compliance Officer.

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## 9.5 Third-Party Placement Agents/Introducers

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### 9.5.1 General Requirements

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As set out in section 3.15 of the Manual, outsourcing should not:

1. Create additional operational risk.
2. Jeopardise internal controls.
3. Delegate responsibility or change client relationships.
4. Hinder the FCA or internal/Firm compliance monitoring.
5. Prevent continued compliance with the Firm's threshold conditions or Principles for Businesses.

The Firm/AR and its senior management remain fully responsible for discharging all of its obligations under the regulatory system in relation to any outsourced function. In other words, **the activity can be outsourced but not the responsibility.**

The Firm/AR must make sure that any service provider:

- Is competent and capable to carry out the activity.
- Has the necessary authorisation(s)/licence(s) or arrangement(s) to enable the activity to be carried out lawfully.
- Signs a valid, written agreement with the Firm/AR that clearly allocates and sets out rights and responsibilities, and which ensures effective performance against agreed standards, e.g. service level agreement, regular review and monitoring, escalations, service credits, confidentiality of information, etc.

[SYSC 8.1.8 R](#) contains necessary steps for certain regulated firms to take when outsourcing critical or important operational functions. However, these are considered as good practice guidance for other firms and in relation to other types of outsourced activity and should be considered prior to the appointment of every third-party service provider. The remainder of this policy relates to the systems and controls regarding third-party placement agents and/or introducers.

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### 9.5.2 Placement Agents and Introducers

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Placement agents typically assist fund managers with fundraising by helping structure the transaction and/or find potential investors that are willing and able to invest in offered securities. The agent acts on behalf of the fund manager and does not purchase the offered securities directly.

Introducers have a much more limited scope of appointment than placement agents and their activities tend to be limited to effecting introductions to the fund manager or other members of the fund group and distributing approved communications on behalf of the fund manager.

Both types of firm/individual work on behalf of the fund manager, therefore, these firms/individuals must not provide any advice on the transactions/offerings to which their activities relate, and the fund manager is ultimately responsible for the activities of these firms/individuals and must, therefore, be involved in the appointment process including the putting in place of an appropriate agreement.

The activities of placement agents and introducers are likely to fall within scope of the regulated activities of arranging investments and making arrangements with a view to transactions in investments. Therefore, placement agents and introducers will need to have the necessary authorisation, licence or arrangement in

place to enable them to conduct this activity lawfully. Where a placement agent or introducer has no authorisation, licence or arrangement, this should be investigated under the direction of the Firm's Compliance Officer. It's important to note that the 'all crimes' approach of POCA means that any advantage gained through unlawful activity would constitute proceeds of crime.

Legislation relevant to the fund and/or fund manager will also impose restrictions and limitations on the activities of placement agents and introducers. For example, UK AIFs can only be marketed, directly and indirectly, outside the UK in accordance with local rules and regulations, such as the third-country rules under National Private Placement Regimes in EU member states.

As mentioned in chapter 8a of this Manual, the FCA's SDR Regime extends beyond FCA-authorised firms and applies to distributors such as introducers and placement agents. Therefore, the rules in chapter 8a for distributors will also apply to introducers and placement agents in respect of both labelled and unlabelled products.

As well as general outsourcing risks, the use of placement agents and introducers creates additional compliance and legal risks for the fund manager and connected parties. Therefore, a procedure (see below) was implemented to mitigate these risks and must be followed by all ARs and TPMM firms.

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### 9.5.3 Procedure for Appointing Placement Agents and Introducers

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When the Firm/AR is considering appointing a placement agent or introducer, it must first notify the Firm's Compliance Officer of the proposed scope of appointment and provide an updated PROD assessment that takes into account the proposed appointment. Any directions given by the Compliance Officer must be followed.

General outsourcing requirements, as set out above and in section 3.15 of the Compliance Manual, and the following steps specific to the appointment of a placement agent/introducer, must then be followed by the Firm/AR:

1. Notify the Compliance Officer of the names of the firms/individuals it wishes to appoint and provide the Compliance Officer with the due diligence conducted on the proposed appointments (including relevant AML checks), which demonstrate the proposed appointments are suitable in respect of the general outsourcing requirements.
2. The Compliance Officer will review the information provided and may conduct or request further due diligence be carried out.
3. The Compliance Officer will then confirm whether or not the proposed appointments are appropriate. If they are, the Firm/AR should provide the Compliance Officer with the proposed agreement so that the agreement can be checked for appropriateness, required terms and conditions.
4. Where an AR is permitted to appoint a placement agent or introducer, the AR must ensure:
  - a. The Firm is kept informed of all activities and involved in all decisions relating to the placement agent/introducer including approval of target recipients.
  - b. It holds regular (at least monthly), documented performance reviews/evaluations of the placement agent or introducer with respect to the terms of appointment, as set out in the relevant agreement.
  - c. Reports to the Firm on the activities and performance of all placement agents/introducers in the relevant sections of the monthly report templates.
  - d. Informs the Firm, without delay, of any issues or concerns regarding a placement agent or introducer.

When an AR is considering terminating or not renewing an agreement with a placement agent or introducer, it must do so in full compliance with the terms of the agreement and must notify the Firm of its intentions in advance and without delay, separately and in addition to monthly reporting.