

# Depository Decoded: A comprehensive checklist for choosing a depository partner

*Choosing a strong depository partner is an important component of your fund's compliance matrix. Beyond this, the choice will feed into the overall success of your fund strategy. [Linda Morsia](#) and [Martin O'Brien](#) highlight the qualities you should be looking for before settling on a service provider.*

A strong depository partner is a strategic ally, safeguarding assets, optimizing operations, and supporting long-term growth alongside their clients. The right depository helps fund managers navigate evolving regulations, avoid costly errors, and instils confidence among investors, which is why selecting one is of vital importance for fund managers.

## What is a depository's duty?

A depository serves as a guardian and overseer for fund managers, ensuring regulatory compliance and investor protection. Their responsibilities include safeguarding fund assets by confirming proper ownership for non-custodial assets like private equity and real estate, and maintaining an independent inventory. A depository is also responsible for custody of financial instruments, such as stocks, bonds and other securities, and holds them in either physical or electronic custody.

In addition, depositaries monitor and reconcile cash flows daily to identify any discrepancies and verify that all transactions are processed in line with the fund's guidelines. Oversight extends to ensuring managers adhere to regulations and the fund's governing documents, covering matters such as valuations, calls and distributions, and investment restrictions.

With these duties, depositaries provide an independent layer of assurance for investors, helping to prevent fraud, mismanagement, and operational mistakes. In jurisdictions like the European Union (EU), such roles are clearly defined by legislation such as the Alternative Investment Fund Managers Directive (AIFMD), which requires depository involvement for alternative investment funds.

# What is the value-add a depositary should deliver?

Beyond the checks and balances and core services that follow, depositaries can also offer value added services such as collating and delivering market insights, and benchmarking data to help clients grow their business and adapt to changes in their operating environment. An example might be a depositary delivering regular updates to help clients make better informed decisions.

## The 4 core depositary services to quality check:

### 1. Extensive current compliance knowledge and regulatory expertise

A good depositary must have deep and wide knowledge of local, national and global regulations. They should proactively monitor regulatory changes and inform clients accordingly. An example of this might be supporting a fund manager to transition to the Sustainable Finance Disclosure Regulation (SFDR) or navigate jurisdictional nuances for an EU member state governed by the AIFMD. A poor depositary service might expose a client to regulatory penalties and reputation damage by failing to flag non-compliance.

#### Questions to ask:

- Is the depositary eligible under AIFMD regulations?
- Does the depositary work alongside, though independently from, the AIFM and fund administrator?
- Is the depositary located in the same jurisdiction as the fund (or permitted under AIFMD II cross-border rules)?
- Does the depositary meet capital adequacy and prudential supervision requirements?
- Can the depositary provide [Depositary Lite](#) services for non-EU funds marketed in the EU?

### 2. Robust risk management

Depositaries play a key role in safeguarding assets and monitoring risk. A strong risk framework includes oversight of counterparty risk, asset verification, and escalation protocols. For example, a depositary should be able to flag unusual

trading patterns in a hedge fund's portfolio and initiate a review to uncover a rogue trader, which would prevent significant losses. An example of how incorrectly applied risk management might disadvantage a client would be if a depositary overlooked concentration risk in a fund's holdings, which later contributed to a liquidity crisis during market volatility.

### **Questions to ask:**

- Does the depositary have specialist expertise in private markets asset classes?
- Does the depositary have appropriate risk assessments adapted to each asset class that are flexible and client centric?
- Does the depositary understand the specialist requirements for the transaction process that applies specifically to private markets?
- Does the depositary have appropriate measures in place regarding the strict liability for loss of assets in custody?
- Are there clear terms for delegation to custodians, including due diligence and segregation of assets?
- Is there clarity on discharge of liability in case of external events or custodian/sub-custodian issues?

## **3. Timely and efficient operations**

Efficiency in settlement, reconciliation, and reporting is a business necessity. A responsive partner can prevent delays and reduce operational risk, for example, by implementing automated reconciliation tools that reduce NAV errors, enabling faster reporting and fewer investor complaints. Conversely, manual processes might lead to unnecessary delays in trade settlement and so result in missed investment opportunities.

### **Does the depositary have:**

- Safekeeping of assets (custody of financial instruments and verification of ownership and record for other assets)?
- Cash flow monitoring to ensure proper handling of fund transactions?
- Oversight monitoring, including NAV calculation accuracy, investor register maintenance, transaction validation, income application, and compliance with fund documentation and valuation rules?
- A proven track record and experience in depositary services?

- A strong onboarding process and transitional support?
- The specialist ability to service complex private markets fund structures (e.g., private equity, real estate, venture capital)?
- A scalable service model to support fund growth and complexity?

## 4. Client service and communication

In the same way as a fund manager would provide clear, proactive communication and a dedicated relationship manager to investors, the same service from a depositary can make a significant difference in how fund managers experience the service. A good example of this might be a depositary assigning a multilingual client service team to a cross-border fund, which enhances communication and reduces potential friction in onboarding and daily operations.

### Questions to ask:

- Does the depositary have a dedicated relationship team with subject matter experts?
- Does it have a transparent fee structure with clarity on additional charges?
- Does it have a willingness to customize services based on fund needs?
- Does it have a strong governance culture and proactive issue resolution?

Beyond this, a depositary partner should also have a solid balance sheet and credit rating, have membership to relevant industry associations, be able to provide a range of client references and proof of low staff turnover, as well as broad experience across multi-jurisdictional operations, private markets asset classes and fund types. A modern depositary should also offer digital platforms to deliver real-time reporting, data analytics, and integration with a fund manager's systems. It should add value, mitigate and pre-empt risk, and support your growth and goals, all while ensuring flawless regulatory compliance.

For U.S. managers, once you've determined you need to [appoint](#) a depositary it is important to choose a service that best fits your needs. There is estimated to be \$750 billion in U.S.-promoted private capital in European centres, and U.S. managers navigating Europe's complex and highly regulated environment need an independent third-party provider with comprehensive private markets expertise and experience to streamline the journey. For more detail about fundraising in Europe read this [guide](#).

If you'd like more detailed information about your depositary needs or simply to discuss any of the questions raised in this article, please contact us.



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