

LAW SOCIETY'S COMPANY LAW COMMITTEE

THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS

Consultation Paper on CESR's guidelines for supervisors regarding the transitional provisions of the amending UCITS Directives

November 2004

INTRODUCTION

1. The Law Society's Company Law Committee welcomes the Committee of European Securities Regulators' Consultation Paper ("the Paper"). The Paper states that the amending UCITS Directives, to be adopted by Member States by 13 February 2004, contained some ambiguities leading to differences of interpretation and implementation by regulators in Member States. The Committee welcomes harmonisation of implementation of Directives.
2. The Committee notes the introduction into the proposals in the Consultation Paper of implementation dates not contained in the Directives themselves. It assumes that such dates are a compromise between those regulators who, in the absence of reference to any particular transitional relief within the Directives, expect implementation by the deadline for adopting the Directives, and other regulators who consider applying transitional arrangements for the whole transitional period provided for in the Directives.

The Committee would make the general point that the reorganisation of retail funds which has to take place to implement Directives involves long-term planning and certainty; the introduction of intermediate deadlines for implementation, in addition to those in the terms of the Directives, should be treated cautiously and must provide the fund management industry with adequate timescales.

3. Turning to the specific questions raised in the Consultation Paper and following the same numbering:

QUESTIONS ON THE TRANSITIONAL TREATMENT

I UCITS I management companies

1. Can a grandfathered UCITS I management company i.e. authorised before 13 February 2004, launch “passportable” UCITS III funds?

The Paper states that CESR members propose that a grandfathered UCITS I management company is allowed to launch “passportable” UCITS III funds only until 30 April 2006 at the latest; after that final date, the management companies must be adapted to UCITS III. The Paper suggests that to be able to avail of this possibility, a grandfathered UCITS I management company has in any case to comply with the requirements of Article 21 as amended by Directive 2001/108/EC concerning an appropriate risk management process.

This is an area where an arbitrary date has been introduced. In the circumstances of this proposal, the Committee accepts the introduction of the date of 30 April 2006, although it sees no need to introduce a date earlier than 13 February 2007, the last transitional date in the Directive.

2. Can a grandfathered management company continue to launch “passportable” UCITS I funds after 13 February 2004?

In CESR’s view, a grandfathered management company cannot continue to launch passportable UCITS I funds after 13 February 2004.

The Committee agrees with this view.

II UCITS I Funds (single fund structure)

1. Can a UCITS I fund authorised between 13 February 2002 and 13 February 2004 and wishing to be marketed in another Member State obtain a UCITS I - product passport and benefit from a grandfathering period until 13 February 2007?

The Paper suggests that the situation was unclear from the date of entry into force of the amended UCITS Directive and so CESR members proposed to provide for a period until 31 December 2005 at the latest for UCITS I funds authorised between those two dates to be converted to the regime of the amended UCITS Directive.

The Committee agrees with this proposal in the interests of expediting compliance with the Directive.

III UCITS I umbrella funds

1. Can a “passportable” UCITS I sub-fund be launched in a grandfathered UCITS 1 umbrella fund?

As they consider the transitional treatment was unclear, CESR members propose a period until 31 December 2005 at the latest for UCITS I sub-funds to be launched in a grandfathered UCITS I umbrella fund. This is stated as being the period within which the overall UCITS I umbrella should have been converted to UCITS III. The latter is only introduced by proposal in this consultation process.

The Committee is not persuaded as to the reason for imposing this deadline earlier than the end of the transitional period under the Directive, namely 13 February 2007.

2. Can a “passportable” UCITS III sub-fund be launched in a grandfathered UCITS 1 umbrella fund?

In CESR’s view, this is not possible because the whole umbrella structure including all sub-funds should either be submitted to the regime of the 1985 Directive or that of the 2001 Directive.

The Committee agrees that a single legal basis should apply to the whole umbrella fund.

IV Simplified prospectus

1. Must a UCITS I have a simplified prospectus available in order to maintain its registration?

In CESR’s view, UCITS I funds launched before 13 February 2004 should have available a simplified prospectus as soon as possible and no later than 30 September 2005. In cases not meeting this deadline, host members states are not obliged to accept UCITS I funds without simplified prospectuses.

The process of introducing simplified prospectuses does not appear to be uniform. Whilst the concept of a uniform simplified prospectus is welcomed, it is essential that the information to be contained within it is certain sufficiently well in advance of any date of implementation to give a highly developed fund management industry, such as that in the United Kingdom, ample time to introduce it. The dateline of 30th September 2005 would seem to be the earliest date for harmonised implementation to suit this. The date should then be applied strictly, rather than “not obliged” as stated.

2. Is it possible for UCITS which have no simplified prospectus and which wish to be marketed in another Member State to obtain a UCITS III product passport?

The Paper suggests that as there is no transitional provision within the amending UCITS Directives, a UCITS III product passport requires the fund to have a simplified prospectus.

The Committee agrees with this conclusion.

QUESTIONS CONCERNING THE EUROPEAN PASSPORTS

I Management company passport

1. Are the product and management company passport issued separately or combined?

The Paper states that in CESR's view these passports are issued separately from each other.

The Committee agrees with this conclusion.

2. Does a management company which wants to distribute in a host Member State UCITS' units, without establishment of a branch only need a product passport or is a management company passport necessary in addition?

The Paper suggests this question is extremely complex. It promulgates two options, either (A) the need for both management company passport and product passport or (B) the need only for a product passport.

In the view of the Committee, option (B), only a product passport, is correct. It agrees with the statement that there would be little point in having a separate passport for UCITS and one for the management company, if the management company passport must always be used in addition to the product passport in these cases.

3. Does a management company which wants to distribute in a host Member State UCITS' units through an own branch need both the product and the management company passport?

The Paper states CESR's view that both the so-called product passport and the so-called management company passport are needed for this activity.

The Committee agrees with this view.

4. Which passports are needed when a management company wants to provide in a host member state only the so-called ISD services?

The Paper states that in CESR's view only the so-called management company passport is needed.

The Committee agrees with this view.

5. Does a management company which wishes to combine the provision of the so-called ISD services in a host Member State with the cross-border distribution of UCITS' units, either directly, by itself, or indirectly, entrusting a third party, need both the product and the management company passport?

The Paper states that in CESR's view the so-called product passport and the so-called management company passport are both needed for this activity.

The Committee agrees with this view.

6. Can an open-ended investment company designate a management company in another EU jurisdiction?

The Paper states that CESR members agree they would only permit an open-ended investment company to designate a management company in the same EU jurisdiction. The Paper sets out the reasoning of "almost all CESR members". Perhaps recognising that the Directive is not clear, or indeed produces a different conclusion on strict interpretation, the Paper states that CESR members agree that the European Commission should consider an amendment that would clarify the position on this issue under the UCITS Directive.

This is the most controversial of the proposals in the Paper. It appears to run contrary to specific terms of the directive and we suggest that implementation of the existing Directive in accordance with the view of "almost all CESR members" is outside the powers of the regulators.

It may be of assistance if we amplify our response in respect of this question. Article 6 of the Directive provides

"Member States shall ensure that the management company, authorised in accordance with this Directive by the competent authorities of another Member State, may carry on within their territories the activity for which it has been authorised, either by the establishment of a branch or under the freedom to provide services."

It seems to the Committee that these activities are much wider than mere collective portfolio management, as referred to in Recital 7 of the Amendment Directive, to which the Paper makes reference. With regard to Article 3, to which reference is also made, this merely provides the test for establishing where a UCITS is deemed to be “situated” and therefore needs to be authorised. It states that a unit trust is situated in the place where the management company has its registered office. Since the unit trust is not a separate legal entity, this necessarily means that the manager of a unit trust has to be situated in the same place as the fund is authorised and therefore does not permit the management company to act generally on a cross-border basis. With investment companies the position is different; Article 3 provides that the UCITS is situated where the investment company has its registered office and then provides that the head office of that investment company is situated in the same state as the registered office. With an investment company this simply means that the board of directors should meet and direct the operations of the investment company in the place where that investment company has its registered office. It is silent as to whether this precludes the management company providing services to that investment company being established in another Member State.

It is wrong to equate administrative functions with the head office function, being where the ultimate authority resides and, in the case of an investment company, being its board of directors.

In the view of the Committee, a branch which shows sufficient capability in the jurisdiction in question should be able to act as management company for a fund in that jurisdiction. This is particularly the case where, as in some jurisdictions, it is not necessary to have a management company if, in effect, the board of directors of a corporate fund have the responsibility for management. There are capital requirement benefits from the establishment of a single management company with branch operations and this presumably was part of the rationale within the Amending Directive.

Whilst the Committee accepts that an amendment may be properly made by the European Commission and European Parliament, it would question the power of regulators to overrule the terms of the Directive pending such amendment.

7. Does a management company which manages, based on an out-sourcing mandate, the portfolio of an open-ended investment company or of an investment fund domiciled in another EU jurisdiction, need a management company passport and if yes, for individual or for collective portfolio management?

The Paper expresses CESR's view that a bilateral delegation agreement subject to the safeguards of Article 5(g) should be sufficient.

The Committee agrees with this conclusion.

8. Is distribution of third party funds included in the scope of activity of a management company?

The Paper states CESR's view that the distribution of third party funds is included in the scope of activity of a management company.

The Committee agrees with this view.

9. Can a management company benefit from the management company passport (in particular for its ISD services) whilst it is no longer, at a given moment, managing harmonised UCITS or whilst it is not yet managing harmonised UCITS, but preparing an application procedure for approval of a harmonised UCITS or whilst it does not manage harmonised UCITS funds as designated management company in its home member state?

The Paper states that to avail of the management company passport, a management company must manage at least one harmonised UCITS as a designated management company.

The Committee agrees with this view.

II Product Passport

1. Do those non-UCITS funds, which pursuant to the national provisions of the host Member State have already been entitled to distribute their units in the host State and which now adapt to UCITS III lose their former permission?

The Paper suggests the marketing of the fund can in CESR's view continue uninterrupted in the host Member State. The two month period of Article 46 paragraph 2 does not apply, so even before the expiry of the two month period reserved for the host State, competent authorities to handle the notification, the distribution of fund units can continue on the basis of the former permission.

The Committee agrees with this view.

2. Do those UCITS I funds which adapt their registration to UCITS III, lose their UCITS I passport?

The Paper states that in CESR's view the UCITS passport will continue to be effective.

The Committee agrees with this view.

OTHER ISSUES

We refer to the two month notice period required to be given before a UCITS may begin to market its units in another Member State (Article 46 of 1985 Directive).

There is a lack of uniformity in Member States as to whether this applies to the launch of a sub-fund of an umbrella fund which has already given such notice to the relevant regulator in respect of the umbrella fund. The Committee considers the uniform position should be that the two month period applies at the fund level and not the sub fund level in an umbrella fund, so that the period does not apply to additional sub-funds, when launched.

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