

17 November 2009

CESR
11-13 Avenue de Friedland
75008 Paris
France

Dear Sir

Consultation paper: Technical advice on level 2 measures relating to mergers of UCITS, master feeder UCITS structures and cross-border notification of UCITS

The IMA represents the asset management industry operating in the UK. Our members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the managers of occupational pension schemes. They are responsible for the management of over £3 trillion of assets, which are invested on behalf of clients globally. These include authorised investment funds, institutional funds (e.g. pensions and life funds), private client accounts and a wide range of pooled investment vehicles.

Our detailed response to the questions in the above consultation paper is attached. Our key concerns are as follows:

- The information requirements in Section 1 on mergers are far too prescriptive and will overload investors. If the merging fund has only a few investors and small AUM, and the receiving fund is far larger with thousands of shareholders, then it would be prohibitively expensive to justify the merger given the cost of sending information to the receiving unit holders. There is a danger that such onerous proposals could lead to fewer mergers, which would undermine the purpose of the Directive. It should be sufficient for fund managers to host the material for receiving unit holders on their website.
- On master feeders, we have a number of concerns relating to the master-feeder agreement; the depositary agreement; and the process for liquidation/merger of the master feeder.
- The requirement in relation to notifications, which states that a UCITS has to stop marketing if the regulators have made an error in the notification process, is unacceptable. In practice this could be almost impossible to comply with (e.g. where newspaper adverts have been placed) and could

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entail significant costs. It is not the fault of the UCITS if supervisors cannot get their communications right.

- Finally, we welcome CESR's recognition in paragraph 21 that tax issues can act as a barrier for cross-border fund mergers. Without clear European rules, a cross-border fund merger can result in a taxable event in the hands of the unit holder and therefore crystallise an unrealised gain. This fact can completely nullify the benefits of the UCITS IV provisions on fund mergers unless they are resolved by the Commission with legislative action. We urge CESR to stress clearly to the Commission in the final advice that real action is needed by the Commission to solve the problems regarding taxation of fund mergers. The Taxation of Mergers Directive (90/434/EEC) sets an example for this.

Please do not hesitate to contact us should you require further information.

Yours faithfully

A handwritten signature in black ink, reading 'Alwine Jones'. The signature is written in a cursive, flowing style.

Alwine Jones
Adviser, Regulation

IMA response - UCITS mergers

SECTION I: MERGERS OF UCITS

1.1 Contents and format of the information

1. *Do you agree with CESR's proposals for specifying the information to be given to unit holders? Is there any other information that is essential for them?*

No; we feel that these requirements are far too prescriptive and would overload investors.

It is important to get some sense of proportion when it comes to what, if any, information should be sent to unit holders in the receiving UCITS. After all, when a very large deal is placed in a UCITS there is no requirement to inform existing investors. If (as is often the case) the merging fund has only a few investors and small AUM, and the receiving fund is far larger with thousands of shareholders, then it would be prohibitively expensive and difficult to justify the merger on cost benefit grounds, (to the point where the costs of printing and postage alone might outweigh the benefits). Moreover, merging funds may re-align portfolios to match that of the receiving fund, so there is no material effect on the continuing fund.

We urge CESR not to overload investors by requiring too much information to be provided. The information should be proportionate, short and clear. Providing the KID, and informing them where other information can be found (via web links) should be enough.

Moreover, the proposals seem to require items that are already provided for in Level 1. Specifically:

- Box 1 paragraph 4 (a) seems to add little, if anything, to the requirement contained in Article 43(3)(c).
- Box 1 paragraph 4(b) &(c) does not seem to be necessary as the KID of the receiving UCITS will be provided to unit holders.
- The suggestion that the information highlights the need to read the KID would also appear to be unnecessary given that (according to the last CESR consultation on the contents of the KID), the KID would need to include the statement:

‘This document provides you with key investor information about this fund. This information is required by law. You are advised to read it before deciding whether to invest.’

- Box 1 paragraph 4(d) also seems unnecessary as such information will be provided in the KID.
- The final paragraph of 4 suggests that the letter provides reference to the KID and the need to read it – which implies that the KID will not be in a format or design that makes it attractive to an investor.

2. *Do you agree that a summary of the key points of the merger proposal should be optional?*

Yes.

3. *Should there be more detail at Level 2 about what ought to be included in the description of the rights of unit holders?*

No – see our response to 1 above. Additional points here include:

- Box 1 - paragraph 3, last sentence. What if there is no potential impact? This should mean that it is not necessary to send anything.

Box 1 paragraph 5(c) - with reference to the interpretation of Article 46, we need to ensure that the costs of alignment of the portfolios can be charged to the fund.

We need to ensure that fund managers are left to choose the most appropriate method of providing information, particularly to receiving fund investors, be this by post, email or on a website page. There must be as much flexibility as possible – managers should be free to decide on materiality and whether investors need be sent anything at all.

4. *Do you agree with the proposed treatment of the KID of the receiving UCITS?*

It is helpful that CESR has acknowledged that it is illogical for unit holders in the merging and receiving UCITS to be provided with identical information. But we would like to see an explicit statement from CESR that Article 43(3) can be construed as not requiring the KID of the receiving UCITS to be sent to the receiving UCITS unit holders.

In practice most mergers will take place without any impact on the continuing UCITS. Requiring re-papering of receiving UCITS unit holders with a document they would have already received would, as noted above, be of no benefit. A better approach would be for the KID to be available on a website, unless the regulator(s) have determined there is a material significance affecting both sets of unit holders.

5. *Would the proposals in Box 1 lead to additional costs for UCITS or management companies? Please quantify your estimates for one-off and ongoing costs. What would be the benefits of the proposals (e.g. compared to no prescription at Level 2 on this issue)?*

The requirement in the Level 1 text to inform the receiving UCITS unit holders in all cases will lead to increased printing and postage costs for the UCITS where national rules require unit holders to be sent information through a durable medium.

1.2 Providing the information

6. *Do you agree with CESR's assessment that the potential costs and benefits of a harmonised procedure do not support the case for providing advice on Level 2 measures on this issue?*

We strongly agree that the procedure for provision of information should not be harmonised. This would allow Member States more flexibility, for example the use of the internet as a more cost-effective medium to inform unit holders.

SECTION II MASTER-FEEDER STRUCTURES

2.1 Agreement between feeder and master UCITS

7. Do you agree with CESR's proposals for specifying the content of the agreement?

No; there is too much detail required to be included here, and much of this should be included in a service level agreement. In our view, only points 1 and 6 should be included in the master-feeder agreement. The other issues can be dealt with in a separate contract between the parties which does not need to be filed with the regulator.

In general the proposals look far too complicated for what ought to be a simple way of creating master/feeder structures. The regulators are in real danger of creating something that is not worthwhile doing and so losing the whole benefit of this efficiency. We also need to ensure that any proposals do not lead to continually changing agreements and filing those with the regulator.

8. Are all the points listed in Box 2 appropriate elements to be included in an agreement? Are there others that should be required to be included?

No – see above. And in Box 2 paragraph 1(c), "breaches" must be limited to material pricing errors only.

9. Which option do you prefer in relation to the national law and jurisdiction applicable to cross-border agreements?

Option B, which provides for flexibility over the applicable law. It should also be possible to have a third country (still within the EU) being used as the jurisdiction of the applicable law (e.g. domicile of the management company).

10. Do you agree that measures to protect the interests of other unit holders in a master UCITS should be left to national law and regulation?

Yes.

11. What would be the additional costs of the proposals in Boxes 2 and 3? Please quantify your estimates for one-off and ongoing costs. What would be the benefits of the proposals, compared to no prescription at Level 2 on this issue?

In general the proposals look far too complicated for what ought to be a simple way of creating master/feeder structures. The regulators are in real danger of creating something that is not worthwhile doing and so losing the whole benefit of this efficiency.

12. Do you agree with CESR's proposals in relation to internal conduct of business rules? If not, what should be required by such rules?

Yes. As a general point, feeder funds should not have an advantage that is unfair on other unit holders in the master fund.

13. *What would be the additional costs of the proposals in Box 4? Please quantify your estimates for one-off and ongoing costs. What would be the benefits of the proposals, compared to no prescription at Level 2 on this issue?*

We believe the costs should be minimal here.

2.2 Measures to avoid market timing

14. *Do you agree with CESR's proposed approach to prevention of market timing?*

Yes.

2.3 Liquidation, merger or division of a master UCITS

Liquidation of the master UCITS

15. *Do you agree with CESR's analysis of the issues relating to liquidation, merger or division of a master UCITS?*

Yes, although given that most master-feeder structures will be operated by the same management company, the presence of a feeder fund will naturally be factored in when determining the course of action should a decision be made to liquidate the master.

An additional aspect that needs to be considered is that currently certain non-EU regulators require any changes to a UCITS' Prospectus (and the necessary supporting documentation such as a notice of an EGM) to be approved by themselves either in advance of, or simultaneous to, the home regulator's approval. With the current timeline it would be difficult to secure such approval in the 3 weeks allowed for home regulator approval.

16. *Do you consider it likely that in practice a feeder UCITS would not become aware of the master's intention to liquidate, merge or sub-divide before receiving formal notice of the proposal?*

It is unlikely that a feeder would be unaware before notification.

17. *Do you agree with CESR's proposals in Box 5 for dealing with the liquidation of a master UCITS?*

No. We believe that advance notification of a liquidation or merger to the feeder, under a confidentiality agreement, would allow for more equal treatment of the Feeder's shareholders and the other shareholders of the master.

Such an agreement would allow the feeder to prepare the necessary documentation to support its response to a proposed merger or liquidation. The key part which seems to be missing from these proposals is allowing time for the feeder fund to hold an EGM of its shareholders, which it is assumed would be necessary if the fund is to change its investment policy to allow it to invest in a new master fund, whether as a result of a merger or liquidation.

Putting in place an agreement would allow the feeder more time to prepare changes to its Prospectus and also to draft a shareholder circular. As soon as the formal

notice of 3 or 2 months (as applicable) is given, the feeder will be able to file for approval of its proposal with its home Regulator, for example the day after receiving notice from the master. Approval is then received 3 weeks later and the feeder can mail its shareholders with notice of the EGM. Presuming a successful EGM is held, the feeder would then be able to align the timing of the change to its investment policy with the liquidation/merger of the master.

This would appear to be a much improved position for the shareholders of the feeder fund as they would continue to be fully invested rather than the feeder holding cash for around a month which could happen under the current proposals.

The confidentiality agreement would allow for a more equal treatment of the Feeder's shareholders and the other shareholders of the master. If it is not possible to achieve such fairness, the feeder vehicle will prove to be unattractive to potential investors and the proposed structure will never come to fruition.

18. Does the proposed procedure in Box 5 make it more or less likely that feeder UCITS would pursue an alternative option to liquidation? What would be the additional costs of the proposals? Please quantify your estimates for one-off and ongoing costs. What would be the benefits of the proposals, compared to no prescription at Level 2 on this issue?

The procedure in Box 5 would make it difficult for a feeder to pursue an alternative to liquidation whereas the above process would leave other alternatives open.

Merger or sub-division of the master

19. Do you agree with CESR's proposals in Box 6 for dealing with the merger or division of a master UCITS? In particular:

No. We believe that advance notification of a merger to the feeder, under a confidentiality agreement, would allow for more equal treatment of the feeder's unit holders and the other unit holders of the master.

(a) is one month long enough in which to prepare a proposal for an option other than liquidation of the feeder?

Yes – but see (b) below.

(b) how quickly can the feeder make information for unit holders available once the competent authority's approval is received?

5 days is too short a period to inform all unit holders of a proposed change; given the diverse unit holder base of many UCITS, more time is certainly required here. We suggest that this is extended to 10 days and then the one month period in (a) above could be reduced to 23 days (however this timeframe would only be feasible if a confidentiality agreement is put in place so as to allow the feeder to prepare the necessary documents supporting its proposal in advance).

(c) would you expect the feeder to suspend subscriptions during any period in which it is unable to make new investments?

This should be an option available for the manager of the feeder UCITS.

(d) does the proposed time extension in paragraph 10 strike a fair balance between the interests of investors and the practical needs of the feeder UCITS?

Yes.

20. Does the proposed procedure in Box 6 make it more or less likely that feeder UCITS would pursue an alternative option to liquidation? What would be the additional costs of the proposals? Please quantify your estimates for one-off and ongoing costs. What would be the benefits of the proposals, compared to no prescription at Level 2 on this issue?

The procedure in Box 6 would make it difficult for a feeder to pursue an alternative to liquidation, whereas the above process would leave other alternatives open.

2.4 Agreements between depositaries

21. Do you agree with CESR's proposals for defining the content of the depositaries' agreement?

No – see below. In any case, this section needs to take into account the feedback to the Commission's Depositary consultation.

22. Does Box 7 cover the right issues? Should other issues be addressed?

No; too much detail is required here which is inappropriate for inclusion in this agreement, including the technical procedures for NAV calculation. We do not understand the reference to a 'depositary's report to unit holders' in paragraph 4, and do not support the introduction of new reports of this kind under Level 2.

23. Which option do you prefer in relation to the national law and jurisdiction applicable to cross border agreements? Would you prefer the law of the master depositary's home State to be applicable in every case?

We prefer option B as it allows for more flexibility.

24. What would be the additional costs of the proposals in Box 7? Please quantify your estimate of one-off and ongoing costs. What would be the benefits of these proposals, compared to no prescription at Level 2 on this issue?

No comment.

2.5 Reporting by the master UCITS depositary

25. Do you agree with CESR's proposals in relation to the irregularities to be reported by the depositary?

The wording in paragraph 2 should include the concept of materiality, e.g. 'a material breach of the master fund's NAV. Items (d) and (e), if material, would also affect the NAV calculation. Where there are material breaches unit-holders who are entering or leaving the fund may be affected. Since a feeder UCITS is likely by its nature to be subscribing on a daily basis to the master, it would seem appropriate for the feeder's depositary (and management company) to be notified.

26. Do you agree that the interests of other unit holders in a master UCITS will be adequately protected under national laws if these proposals are implemented?

Each Member State will have rules regarding the correction of errors which have a material impact on the fund's unit holders. The feeder fund is in reality just another unit holder and so should be treated accordingly.

27. What would be the additional costs of the proposals in Box 8? Please quantify your estimate of one-off and ongoing costs. What would be the benefits of these proposals, compared to no prescription at Level 2 on this issue?

Provided the wording is amended to include the concept of materiality, there would appear to be no difference between meeting these requirements and relying on national rules (which will treat a feeder as any other unit holder).

2.6 Agreement between auditors

28. Do you agree with CESR's proposals in relation to auditor agreements?

No comment.

29. Which option do you prefer in relation to the national law and jurisdiction applicable to cross border agreements?

Option B allows for more flexibility.

30. Do you foresee that feeder UCITS will generally align their accounting periods with those of their master, or are there good reasons for having different accounting year-end dates?

Yes; in general accounting periods will be aligned.

31. What would be the additional costs of the proposals in Box 9? Please quantify your estimate of one-off and ongoing costs. What would be the benefits of these proposals, compared to no prescription at Level 2 on this issue?

No comment.

2.7 Change of feeder UCITS objective

32. Do you agree that it is not necessary for CESR to provide advice on Level 2 measures on this issue?

Yes.

2.8 Transfer of assets in kind

33. Do you agree that it is not necessary for CESR to provide advice on Level 2 measures on this issue?

Yes.

SECTION III – NOTIFICATIONS

34. Do you agree with CESR's proposals in relation to publication of marketing information?

It would be extremely helpful if the Member States were required to state clearly whether marketing material is required to be pre-approved by the competent authority (and whether such pre-approval is also required for non-fund financial advertising).

Moreover, UCITS and their management companies should be able to rely entirely on the information published by Member States and should not be held liable if they fail to comply with a requirement that was not published.

Additionally, we have the following points on Box 10:

- there should be a requirement for the information to be kept up-to-date and the date of last update be on the website.
- Box 10, para 2 (page 32). Could we add in "and published in a language customary in international finance"?
- Box 10 para 3 (d) or (e) - could we add in "and details of where any marketing material requires pre-approval by the authorities" (Belgium require this and we understand France has just gone this way too).
- Box 10 para 3(f) - the process for paying fees is very unclear (see also para 33 on page 38). Could we get some more clarity around this? Does UCITS pay the home state regulator or pay directly? There should be a statement that fees are "reasonable".

35. What would be the additional costs of the proposal in Box 10? Please quantify your estimates for one-off and ongoing costs. What would be the benefits of this proposal, compared to no prescription at Level 2?

The benefit would be to allow for a smoother marketing process and potentially reduced legal costs.

3.2 Facilitating host state access to notification documentation.

36. Do you support the development of a centralised IT system to facilitate the notification procedure and provide a central repository for fund documents? Could the OAM developed under the Transparency Directive be adapted for this purpose?

We see no need for a centralised IT system. In a modern technological age most management companies operate websites that have all the necessary documentation as well as systems that provide intermediaries and regulators with up-to-date copies of documents. A central database would seem unnecessary and if introduced the cost will be borne by unit holders indirectly. A regulatory requirement to publish on a firm's website is therefore a better option both for firms and investors.

37. What are the current costs of the notification process? What would be the additional costs (direct or indirect) to stakeholders other than competent authorities of developing a centralised system? Please quantify your estimate of one-off and ongoing costs.

The 2006 expert group report stated that the costs are difficult to produce as delays in the amount of time to market a fund can mean missed opportunities.

In terms of a centralised system, any cost to competent authorities would undoubtedly be passed onto management companies who would pass this onto unit-holders.

38. What would be the benefits of these proposals, compared to no prescription at level 2?

There appears little benefit and potential costs involved – see above.

Standard notification letter and attestation

39. Do you consider the notification letter (Annex I) satisfactory? Are there any other matters that it ought to cover?

We would make two points for CESR to consider.

Firstly, the notification letter is now sent to the Home Member State for verification and onward transmission to the host state where marketing is to take place. (Article 93(3)).

The information produced by the UCITS in Part B of the notification letter – and verified by the home Member State competent authority – will be the information requirements disclosed at a distance by the host state competent authority under Article 91(3), but, as paragraph 9 on page 33 makes clear, this may not be up-to-date or complete.

Is there an obligation on the host Member State to check the relevant website – or to go further than that when verifying the information?

Secondly, we can see that there is scope for a host state to stop a notification because the information required to be sent in Part B might include some form of approval document from the host state, which, if not attached, would be seen as an incomplete notification and hence rejected. Thus the Directive's aim of ease of market access is thwarted by national regimes.

To avoid such measures we would prefer that the notification letter contain the information documents prescribed by Article 93(2) only and thereafter a general statement that the UCITS will abide by the host state marketing requirements described in Article 93(1).

Clearly if there are pre-approval requirements relating to marketing material etc the UCITS will need to comply with these, but this should not hold up the notification process.

It would be helpful if the model notification letter could be modified to include the request to market in multiple member states.

In particular, we disagree with the requirement to specify distribution channels (and certainly would not want to see specific distributors named). It should be sufficient

for a fund manager to confirm that it will distribute in accordance with and continue to comply with the rules of the host State, rather than having to set out detailed marketing plans. If the distribution is done via MiFID-compliant entities (as is most often the case), there should be no need for further information. It can then be left to supervisors to monitor post event. Also what happens if distribution arrangements change during the notification period or afterwards? There will be many cases where agreements are still in negotiation, or change, or new ones are added; therefore it doesn't make sense to list them all, as the list could change at any time.

Additional points here include:

- Annex 1 (page 41) – it should only be necessary to register sub-funds (first box) and not share classes of sub-funds. Therefore you should only have to notify a sub-fund and then supply an updated KID without further notification when a new share class comes along.
- Page 43 - Attachments - next to the report and accounts line add "(where relevant)".
- For paying agents this should read "Details of PROPOSED paying agent" as the agreement may not have been signed at the point of notification. This usually takes the longest time, so we would not want to lose the benefits of the new 10 day notification period.
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40. Do you have any comments on the draft attestation letter (Annex II)?

No.

41. Do you consider that use of the proposed letters would generate any additional costs, compared to the existing procedure following the CESR Guidelines? What would be the additional benefits, again compared to the existing procedure?

No, subject to the comments above.

3.4 Electronic transmission of notification files

42. Do you support the development of a dedicated electronic system to effect transmission of notifications between competent authorities? What would be the costs and benefits of such a system to UCITS and their management companies?

Box 11 paragraph 7 (page 37) - this is unacceptable. In practice it could be almost impossible to comply with (e.g. where newspaper adverts have been placed, where marketing material has been sent out etc.), could significantly hinder pan-EU marketing programmes (if there is a technical problem with one regulator but not others for example) and entail significant costs. It is not the fault of the UCITS if supervisors cannot get their communications right. The UCITS needs to have certainty otherwise it cannot plan, and then this defeats the purpose of reducing the notification period.

43. Do you agree with the proposed procedures in Boxes 11 and 12 for use of e-mail to transmit notifications, if no dedicated system is made available? Do you consider that any additional measures are desirable, and what would be their costs and benefits?

The e-mail approach is acceptable, although clarity on how the 10 days required in Article 93(3) fits in with paragraphs 7 and 8 would be useful.

44. Does the proposed procedure for transmission and acknowledgement of receipt give sufficient certainty to UCITS that wish to access the market of another Member State? Does it give adequate protection to investors in a host State, in the event that an incomplete notification takes place?

Yes. An e-mail can show both receipt by the recipient as well as a 'read receipt' automatically and with no system development.

45. Should CESR develop Level 3 guidelines in this area instead of advising the use of Level 2 measures?

This detail would sit better at Level 3.