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Memorandum

To: CESR – Committee on European Securities Regulators

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CALL FOR EVIDENCE ON POSSIBLE IMPLEMENTING MEASURES CONCERNING THE FUTURE UCITS DIRECTIVE – CONTRIBUTION BY STUDIO LEGALE CIERI CROCENZI – ROME AND MILAN

A Background

The EC Commission has requested the assistance of CESR on the contents of the measures to be issued by the Commission for implementing certain provisions of Directive no 85/611/EEC (also known as "UCITS Directive") as amended following a proposal adopted by the European Parliament on January 13, 2009 (known as "UCITS IV") to be finally approved by the EC Council.

The request for assistance made by the Commission to the CESR focuses on the matters for which under UCITS IV the Commission will have - or will be entitled - to issue implementing provisions, and these matters include the notification procedure.

With regard to the notification procedure, the Commission may issue implementing provisions under article 95(1) and (2) of UCITS Directive. In this context, article 95(1) b) provides that these measures may concern "the facilitation of access for the competent authorities of the UCITS host Member State to the information and/or documents referred to in Article 93(1), (2) and (3) as required by Article 93(7)". These "information and/or documents" are the memorandum and articles of association of a UCITS or its regulation, its prospectus, key investor information, annual and semi-annual reports (collectively referred to as "Fund Documentation"), as well as the notification letter by means of which the UCITS declares the intention of selling its units/shares in another Member State ("MS"). For the purpose of this memo, "home MS" shall designate the MS in which the UCITS is established, and "host MS" shall designate the MS other than the home MS in which the UCITS intends to sell its units/shares; any reference to an article shall be referred to an article of UCITS IV, unless otherwise specified.

The purpose of this memo is to suggest a few solutions in order to adequately protect the investors of the host MS, given that this category of investors isn't even mentioned in the rules of UCITS IV governing the UCITS which market their units/shares in MS other than those in which they are established.

On the contrary, in the present situation of market turmoil, any new measure should focus on the protection of investors that will actually purchase a given product and a full transparency, in order to avoid an evident "information asymmetry" between the rules of MiFID, which have increased the standard of information for investment services, and those of UCITS IV, which in some cases have decreased this standard: it is to evidence that making available to Italian (or Spanish, or German) retail investors a full prospectus only in English is a lower degree of information with respect to the previous regulatory framework which allowed the host MS to require translation also of the full prospectus.

B Summary

We are of the opinion that the principles of transparency and investors protection which underlie UCITS Directive require – *inter alia* - that the investors in the host MS should always exactly know which sub-funds and share/unit classes of a UCITS are available for offering in their jurisdiction, either for a direct retail distribution or wrapped in discretionary managed portfolios.

In order to adequately protect the investors in the host MS without adversely affecting the principle of the direct notification, the offering of a UCITS in a host MS could be divided in two steps:

step one, direct notification which gives to the UCITS an *abstract* qualification for being sold ("The UCITS *may* access the market of the UCITS host Member State as of the date of this notification" – article 93(3) last sentence) ; and

step two, a notification by the UCITS to the host MS regulator on when is such UCITS willing to actually start the offering of its units/shares (as previously notified) in the host MS.

Such distinction is necessary because market practice shows that not necessarily a UCITS, after having been qualified for selling its units/shares in a host MS, immediately starts to sell them, while a clear information to the investors of the host MS on the products which can be purchased at a given moment should always be available. This information could be given by simply requiring the UCITS to communicate to the regulators of the host MS the date in which the offering will start, maybe depositing with such host MS regulator the same Fund Documentation that it received from the home MS with an effective date affixed on it.

In the last part of this memo, we will also deal with the contents of the notification letter, in particular to the part concerning the arrangements made for marketing the UCITS in the host MS.

C The protection of the investors of the host MS

In issuing level 2 provisions under article 95(1) and (2), the Commission could allow the host MS to have a national data base containing the details of the UCITS, their sub-funds, share classes actually sold to the investors in such host MS according to the marketing procedure allowed in such host MS. The legal basis for this is the requirement set out under UCITS IV that the host MS must be "facilitated" in having access to the information on the UCITS sold in its territory; for this purpose, article 93(7) provides that the home MS "shall ensure" that the competent authorities of the host MS have access to the Fund Documentation. Accordingly, the home MS regulators may require the UCITS seeking notification for selling in another MS to communicate, directly to the host MS regulators, the initial date of the offering. Of course, such initial date could also be communicated by the UCITS to its home MS regulator for subsequent notification to the host MS, but at the moment in which the UCITS seeks notification it is likely that it isn't aware of such date for not still having implemented the arrangements for the distribution in the host MS.

The rationale of this "facilitation" of access to the Fund Documentation granted to the host MS' regulator under UCITS IV isn't the knowledge of the Fund Documentation *per se*, but, we understand, the protection of the investors of the host MS. This because the full availability of the Fund Documentation allows the regulators of the host MS to concentrate their supervision on the relevant products

and protect the investors of their jurisdiction. In addition, the host MS regulator should also be aware of which products are sold at a given time in its jurisdiction. There is also another way in which the availability of the Fund Documentation can help the host MS regulators to protect their investors, and this manner is setting up a data base managed by the regulator of the host MS with the documentation of all the local and foreign funds *actually* sold in such host MS. This solution, as we will see, seems confirmed and allowed by article 93(7), last paragraph and (8), which provide for a direct notification by the UCITS to the regulator of the host MS in case, respectively, of changes to the prospectus or to the share classes sold in such host MS. Accordingly, it is to evidence that under UCITS IV a host MS should be aware of what products are sold in its territory at any time. In addition, an adequate information to the concerned investors on what is actually available for them and its features – as shown in the Fund Documentation – is also in line with the requirements of information to the clients on the relevant financial instruments set out under MiFID in connection with investment services, including placing of UCITS.

The above mentioned data base is particularly important in consideration of a possible discrepancy between the products which are liable to be sold in the host MS because the notification procedure under article 93 of UCITS IV has been successfully completed and those which are *actually* sold in such host MS, maybe because, once authorized, the UCITS didn't find a distributor or a local paying agent. Indeed, one of the ways in which the principles of transparency which inspire UCITS IV can be implemented is by giving to the investors of the host MS a full information on the sub-funds and share classes which are available in their country for retail clients, and, e.g., on the sub-funds and/or share classes which are only available for institutional investors (keeping in mind that as far as distribution in its territory is concerned, the definition of "institutional investor" is governed by the *host* MS).

On the basis of this situation, and in order to allow a full information of the investors in the host MS, a reasonable compromise would be that without arguing the principle of the abstract qualification of a UCITS to be sold in the host MS through the mere notification procedure, and in this sense article 93(3) last sentence is very clear, the UCITS simply *communicates* to the host MS : (i) the date from which such marketing will start, (ii) the sub-funds that it will actually sell in such host MS, by specifying the type of investors (i.e., retail and/or institutional) and (iii) the share classes offered to the various categories of investors. This type of information would be greatly protective for the investors of the host MS, which would have a clear idea of the products which they can actually purchase, and would bring the information allowed to the investors in funds governed by UCITS at a level comparable with the information that MiFID allows to the users of investment services, thus avoiding the risk of the above mentioned "information asymmetry" between the two Directives.

As we pointed out, information on the starting date of the offering could also be transmitted by the regulator of the home MS of the UCITS when making the notification of the first offering under article 93(3). In this case, such transmission should take place by input of the UCITS, which should therefore already know the starting date of the offering in the host MS: all the market players know that this is very difficult to know.

The alternative, as pointed out, is that a UCITS, once authorized for being sold in a host MS after the regulator-to-regulator notification, communicates – for information purposes only – to the host country regulator, the sub-funds and share classes to be sold and the initial offering date, by also depositing the Fund Documentation to be used in the host MS, which shall be the same transmitted to the home MS with the addition of an effective date for the host MS, at least in the KII which is translated in such host MS language. It is to evidence that this second deposit would be made for information purposes only and wouldn't affect in any manner the timing for the offering of the UCITS in the host MS as scheduled by the promoter.

If there is a central depository of Fund Documentation for a given MS, additional benefits for the local investors will be possible, because the Fund Documentation could then be made available to the investors in the host MS by the local regulator, as it shall be the case of Italy which is setting up a publicly available data base ordered on the ISIN code of the various products.

D <u>The consistency of the provisions on a national deposit for the *first* marketing in the host MS with the Level 1 provisions of UCITS IV on the direct deposit by the UCITS with the host MS regulator of *subsequent* versions of the Fund Documentation</u>

The procedure described in section C, which should be referred to the first marketing, is also consistent with the level 1 provisions of UCITS IV on the deposit of subsequent versions of the Fund Documentation: according to article 93(7), last sentence, any amendment to the Fund Documentation must be notified to the host MS *directly by the UCITS*.

Therefore, by combining the deposit of *subsequent* versions of the Fund Documentation made by the UCITS with the *initial* deposit also made by the UCITS (already qualified for being sold pursuant to the notification procedure), it would be possible to have national data bases for the benefit of the investors of the countries which "import" UCITS.

All the above arrangements should be allowed in level 2 rules of the Commission issued under article 95 (1) and (2), in particular the rules that entitle the Commission to govern "the facilitation of access for the competent authorities of the UCITS host Member State" to the Fund Documentation (see article 95(1) b)).

Indeed, a deposit made by the UCITS for information purposes only allows the host MS regulators to be "facilitated" in having access to the Fund Documentation. In addition, as it already happens or will happen in certain countries such as Italy, a deposit made with certain standards allows the host MS regulators to set up a data base accessible to the public, with a high degree of transparency.

D <u>The importance of the information on the "arrangements made for marketing the UCITS in the host Member State"</u>

Under the current regulations – i.e., pre-UCITS IV – a UCITS seeking registration in a host MS has to inform the local regulator about the arrangements made for selling its units/shares in such host MS. This information is very important for a number of reasons, mostly because the investors of the host MS need to know the channels of distribution, i.e. if they can purchase the units/shares of the UCITS directly from a distributor and/or wrapped in a discretionary segregated portfolio. In addition, the investors of the host MS need to know whether they have to bear additional costs with respect to those indicated in the prospectus: it is true that under MiFID these costs have to be disclosed by the intermediaries which carry out the above mentioned channels of distribution, i.e., the placing agent or the portfolio manager, since both carry out an investment service regulated by MiFID, but it may happen – as it is the case of Italy – that some providers aren't subject to MiFID, such as the "correspondent bank" and in general any local paying agent which may charge fees for its payment services. Therefore, in such case, by whom and where will investors be informed about these additional costs?

In addition, the fact that some intermediaries play a role in the distribution of the UCITS in a host MS, or the existence in a given jurisdiction of a cooling off period during which the investor may cancel the order, affect the timing for processing the transactions with respect to the ordinary procedure described the prospectus in relation to orders directly addressed to the UCITS and therefore the investors of a host MS may receive the units/shares for a NAV which is different to the one that would have been applied should the timing for sending orders as provided for in the prospectus have been applied.

Accordingly, we propose that the Commission, in exercising its powers under article 95(2) a) in connection with the requirements on the form and contents of the notification letter, requires that such letter contains at least the following information:

(i) entities involved in the marketing in the host MS, e.g., distribution through a retail placing agent with a paying agent and/or a discretionary segregated portfolio and/or distribution restricted to institutional investors for their own account;

(ii) procedures for selling the units/shares in the host MS, steps and timing for processing the orders and the payments from when the investor signs the application form to when the NAV of the order is actually determined;

(iii) contents of the confirmation of the order to the investor;

(iv) charges, not shown in the Fund Documentation, applicable to the investors of the host MS;

(v) places (e.g., websites and/or publication) where the investors of the host MS may find information, such as the NAV or Notices to Investors.

Under UCITS IV, these information should be transmitted between regulators, but it is to evidence that allowing access to them to the investors of the host MS would greatly increase the "transparency" of the UCITS.

F Conclusions

We are of the opinion that CESR should suggest to the Commission to issue Level 2 rules which must be a reasonable compromise between the interest of the fund management companies in reducing the costs for cross border selling of their UCITS products and the interest of the investors in the host MS country – which in most of cases are far more than those in the home MS of the UCITS – in exactly knowing which products are sold in their country and from when, and to have always available official versions of the offering documents consistent with those deposited with the regulator which will supervise the distribution of the UCITS in their country, i.e., the host MS. In addition, the Commission should elaborate a procedure for allowing the investors of the host MS access to the information transmitted to their regulator in connection with the arrangements made for marketing the UCITS in such host MS.

Thank you for the attention.

Respectfully submitted

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