30 March 2009

Mr. Carlo Comporti
Secretary General
The Committee of European Securities Regulators
11-13 Avenue de Friedland
75008 Paris
France

Dear Carlo

**CALL FOR EVIDENCE ON POSSIBLE IMPLEMENTING MEASURES CONCERNING THE FUTURE UCITS DIRECTIVE**

Please find attached the Investment Management Association's (IMA)[1] response to the call for evidence. We are very pleased that CESR has offered the industry the opportunity to contribute at an early stage of this important exercise. We stress, however, the need to give the industry sufficient time to also comment on CESR's draft advice in the coming months. Given the amount of issues raised in the Commission mandates to CESR we can only properly comment in detail after having seen CESR's drafting. As the timetable is tight, ongoing dialogue with the industry is important to get the approach right.

We call on CESR to remember that the aim of UCITS IV is to bring the fund industry into this millennium in terms of competitiveness of UCITS funds against substitute products. The detailed implementing measures must not introduce unnecessary red tape to issues like cross-border notification procedures. The achievements in the Directive itself must not be watered down by the implementing measures. Therefore the level 2 measures should focus on only the essential elements needed to make the new system work smoothly and efficiently. Unnecessary hard-coding of current regulatory practices into level 2 legislation should be avoided. Level 3 guidance is most often the appropriate tool for harmonising regulatory practices, and this allows CESR to ensure over time that UCITS maintain their existing high standard of investor protection. Additionally, CESR ought to keep in mind that the institutional

[1] 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 £3.4 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. In particular, our Members represent 99% of funds under management in UK-authorised investment funds (i.e. unit trusts and open-ended investment companies).

framework is under review and the role of level 3 is about to be further strengthened.

It is crucial that both CESR and the Commission devote enough resources in preparing the level 2 measures so that the implementation deadline does not slip from 1 July 2011. We cannot afford any more delays to get these efficiency tools into use as the fund industry is struggling in the worst economic climate in living memory.

We are concerned about the public comments made by CESR in the press on risk measurement methodologies and urge CESR to take into account when drafting the advice the impacts on existing UCITS, including those using VaR-methodologies. Rather than de facto ruling out some methodologies at level 2, CESR should give clear Level 3 guidance to facilitate convergence in Member States' ways to measure risk for UCITS.

Please find below IMA's detailed responses to the questions raised in the call for evidence.

Yours sincerely

Jarkko Syyrilä
Director, International Relations

# IMA'S DETAILED RESPONSE

## Part I – Request for technical advice on the level 2 measures related to the management company passport

As a general policy CESR should not go further than the relevant requirements in the MiFID implementing measures. There should be consistency in the approach between UCITS and MiFID as far as possible. The MiFID requirements already exist and have been proving their worth during the time of crisis, and UCITS can only be inspired by this. There is no need to reinvent the wheel.

*1.2.1. Prudential rules and conflict of interest (Article 12)*

There should be consistency in the approach between UCITS and MiFID and CESR should not go further for UCITS than the MiFID implementing measures.

*1.2.2. Rules of conduct including conflict of interests (Article 14)*

There should be consistency in the approach between UCITS and MiFID and CESR should not go further for UCITS than the MiFID implementing measures. Guidance on issues such as churning, soft commission arrangements, timely allocation of transactions/market timing, late trading, underwriting etc. mentioned in the call for evidence should be rather given at level 3. IMA have detailed guidelines for UK fund managers dealing with market timing and we believe that level 3, or even industry guidelines can adequately deal with these potential issues and level 2 rules are not necessary.

There are activities undertaken by a management company which have no MiFID counterpart (such as legal services and filing of tax returns). In such instances we would support an overarching standard rather than any detailed rules of conduct. Also there needs to be clarity about the identity of the client. We would take the view that the client (in a MiFID-type sense) is the fund and not the individual unitholders. If the individual shareholders would be characterised as clients then there would be significant problems with rules of conduct relating to best execution and appropriateness as well as complicating the conflicts of interest issue. It would be helpful therefore if the concept of client was limited, and if that were not possible to have some guidance from CESR of the priority that should be applied to the fund as opposed to its individual unitholders.

*1.2.3. Measures to be taken by a depositary of a UCITS managed by a management company on an investment company situated in another Member State (Articles 23 and 33)*

Regarding the agreement between the management company and the depositary CESR should limit to listing the issues that should be covered by the agreement. It is in fact an agreement between two commercial entities and the regulators should satisfy themselves with listing the issues that need to be covered in the agreement. Dictating the content of the agreement would be too far-reaching an approach. We would propose that the agreement contains the obvious, e.g.:

- What the custodian must do - comply with regulations, set up accounts, settle deals, corporate actions, proxy votes etc.

- Details of the persons who provide instructions

- Details of borrowings and foreign exchange transactions

- Stocklending clause

- Fees

- Appointment of corresponding banks (Sub-custodians) and liabilities

- Applicable law

- Termination terms

There should not be detailed requirements here so the contents should not be an exhaustible list.

*1.2.4. Risk management (Article 51)*

**1 What should be the conditions that govern risk management processes that can be employed by management/investment companies?**

**Establish the criteria that competent authorities should take into account when determining whether the risk management process employed by the management company is adequate for monitoring and measuring at any time the risk of a position and its contribution to the overall risk profile of the portfolio.**

The recent market events have shown that all manners of risk management and mitigation have been tested within UCITS (and other funds). It is therefore pleasing to note that the vast majority of UCITS have "weathered" and continue to "weather" the unprecedented "climate" experienced. Nevertheless, the introduction of the management company passport and the continuing move to a single market necessitates a harmonised approach for many aspects in the operation of a UCITS. We therefore welcome the Commission's proposals to strengthen and harmonise Members States' approach to risk management, not just at the level of the management company and the UCITS, but also at regulator level i.e. how the regulator of each Member State monitors and reacts to risk management and sets out appropriate regulatory limits.

**a) to advise on the categories of material risks that are relevant for UCITS (the identification of types of risks that should be addressed),**

Whilst the CESR risk management principles state that a manager must consider the material risks attributable to the UCITS, we do not believe that providing an exhaustive, or detailed, list at level 2 will be of any benefit. Risks of historically low importance have, in some circumstances, become material and may, perhaps, reduce to a lesser importance in the future. The dynamic nature of the markets and of funds

will continually introduce new risks which will need to be dealt with quickly and not subject to lengthy negotiations. We recommend that CESR considers these matters by way of separate consultation and aims to introduce level 3 guidelines, if appropriate.

**b) to advise on principles governing the identification of the particular material risks relevant for a particular UCITS related to each portfolio position and their contribution to the overall risk profile of the portfolio,**

As CESR has acknowledged in the Call for Evidence, the advice of February 2009[2] (which was consulted on in August 2008) suggests risk management principles detailing governance and organisation, identification and measurement of risks, management of risks, monitoring and reporting. We believe that this advice provides enough detail to advise the Commission on level 2 provisions. Any more detail at level 2 would not be helpful.

**c) to advise, to the extent possible, on requirements concerning risk measurement methods, such as the conditions for the use of different methodologies in relation to the identified types of risk and the specific criteria under which these methodologies might be used,**

It has been noted that risk management methodologies vary amongst Member States which has led to differences in the types of UCITS that have been authorised in Member States. However, this topic requires careful consideration and we recommend a separate consultation is appropriate, to include a review of the EU Recommendations on Derivatives (2004). The outcome should not form part of the level 2 measures for the reasons noted in (a) and (b), but appropriate matters could be included in Level 3 Guidance.

**d) to establish principles for risk management processes to be employed in order to mitigate or otherwise manage and monitor the identified risks related to each portfolio position and their contribution to the overall risk profile of the portfolio. This could include requirements for management companies to ensure proper functioning of risk management processes, establishment of criteria for assessing the effectiveness of risk management processes, setting out principles for systems for operating risk limits, and / or the definition of reporting and monitoring obligations. This list is not intended to be exhaustive or a final indication of the necessary elements, and CESR should consider the best overall packaged of measures necessary for ensuring sound risk management**

as (b) and (c) above.

[2] Risk Management Principles for UCITS

**2. What should be the content of the detailed rules regarding the accurate and independent assessment of the value of OTC derivatives as referred to in Article 51(1)?**

We believe that the guidance in the Eligible Assets Directive is sufficient in determining the accurate and independent assessment of the value of OTC derivatives.

**3. What detailed rules should govern the content and the procedure to be followed by the management company for communicating the information mentioned in Article 51(1) to the competent authorities of its home Member State?**

We believe rules governing the content and procedure should be produced as guidelines within level 3.

*1.2.5. On-the-spot verification and investigation (Article 101)*

There should be consistency in the approach between UCITS and MiFID.

*1.2.6. Exchange of information between competent authorities (Article 105)*

There should be consistency in the approach between UCITS and MiFID.

**Part II – Request for technical advice on the level 2 measures related to key investor information – supplement to the Commission's April 2007 'request for assistance on key investor disclosures for UCITS'**

We do not comment this part of the call for evidence as CESR is consulting separately its drafting on the KII.

**Part III – Request for technical advice on the level 2 measures related to fund mergers, master-feeder structures and the notification procedure**

*The absolute key priority in IMA's view is that regarding notification, mergers and master-feeder structures, CESR should develop clear and unambiguous procedures for each of them. There must be one way of notifying, merging and setting up master-feeder structures a UCITS across Europe and not 27 varieties with this and that add-ons. Main principles should be at Level 2 but much of the practical issues like model letters and attestations could be developed at Level 3 as CESR has done in the past, to allow for flexibility to amend practices as markets and methods develop.*

Regulators should require UCITS managers to submit to them only the information which is absolutely necessary for the regulators to make informed decisions regarding those procedures.

*3.1. Merger of UCITS (Article 43(5))*

We urge CESR not overload the investors by requiring too much information to be included in the letter. Adequate information should be provided to ensure that the

unit-holders are aware of the impact of the merger, including information as to why the merger is taking place. The information should be proportionate, short and clear.

Rather than duplicating any information in the information letter or increase the complexity of such, it is preferred for the information letter to include and therefore focus on only those matters relevant to the merger. The KID can be attached as a separate document or the information can be incorporated in the letter, flexibility should be provided. A UCITS manager should be free to bind up all the documents in one if they so wish.

The information letter is a matter of communication between a UCITS manager and its clients. CESR or the Commission should in no case try and dictate the form of this by a model letter. It should be enough for the regulators to list issues that need to be covered, but the format needs to be left for the UCITS manager to decide. The information letter should be of free format with prescribed content rather than prescribed format.

*3.2. Master-feeder structures*

Regarding master-feeder structures we consider that the mandates are too many and too detailed. We doubt the necessity and usefulness for Level 2 measures on for example contribution in kind (3.2.8). On that the main issue is valuation which would seem to be quite straightforward using market prices at the relevant valuation point. This does not seem to necessitate Level 2 rules.

As CESR's time and resources are limited, priority should be on measures that really affect the every-day operation of the UCITS market like the smooth functioning of the notification procedure. Most of the issues covered in this section can be dealt at level 3.

Regarding *market timing* it should be noted that this is important for all UCITS, not just master/feeder structures. However, we do not believe that level 2 should provide detailed guidance on how to prevent or deter market timers as each case is unique. IMA has detailed guidelines[3] for UK fund managers to consider when dealing with market timing and we believe that level 3, or even industry guidelines can adequately deal with these potential issues.

*3.3. Notification procedure*

*3.3.1. Scope of the information on national law to be published by UCITS host Member State*

UCITS managers need to be able to rely on the information provided by Member States regarding their requirements on the non-harmonised area. This information needs to be accurate and kept up-to-date. Host Member State competent authorities should not be able to pose sanctions regarding possible breaches of national requirements on marketing by foreign UCITS if the requirements are not listed among the information as requested by Art. 91(3).

[3] MARKET TIMING - GUIDELINES FOR MANAGERS OF INVESTMENT FUNDS, July 2008

*3.3.2. Facilities and procedures providing for the access of a host Member States to statutory documents of a UCITS and other information as referred to in Article 93(1) to (3)*

Regarding the access to statutory documents of UCITS and a possible central database we strongly urge CESR to pay attention to the cost implications. Creating and maintaining this database would be an expensive project so making the documents available on the website of the UCITS manager would clearly be the preferable option at least on the short to medium term.

All in all the use of e-mail communication by the UCITS to deliver the documents to its home State competent authority and between the competent authorities should be accepted and favoured as the format of exchanging information.

*3.3.3. Standard model of the notification letter (Article 93(1) and the attestation (Article 93(3))*

We want to stress to CESR that balanced solutions which do not make the process too complex are required. For example it should be enough 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 the case most often, there should be no need for further information.

*3.3.4. Procedures for the electronic transmission of the notification file and the exchange of information between competent authorities for the purpose of the notification procedure*

We have no comments as this question deals with the communication between the competent authorities.