



Date: 17 July 2008
Ref.: CESR/08-572

CALL FOR EVIDENCE ON THE REQUEST FOR ADVICE TO CESR ON THE UCITS ASSET MANAGEMENT COMPANY PASSPORT

Background:

In its 2006 White Paper on enhancing the Single Market framework for investment firms, the Commission undertook to examine the possibility of establishing an effective management company passport as part of its package of targeted legislative amendments to the UCITS Directive.

A management company passport would allow a UCITS fund to be managed by a management company authorised and supervised in a Member State other than the UCITS home Member State.

On Wednesday 16 July 2008, the Commission adopted a proposal for a directive containing amendments to the UCITS Directive (85/611/EEC). This proposal does not include any provision in that respect. The reason for this is that the Commission still needs to determine how the current high level of investor protection provided by the UCITS framework can be maintained in the context of such cross-order management arrangements (see explanatory text of the Commission proposal).

Therefore, in parallel, the European Commission requested CESR to provide advice that will help the Commission to develop provisions permitting the introduction of a management company passport under conditions that are consistent with a high level of investor protection.

CESR is invited to advise on the structure and principles which should guide potential future amendments to the Level 1 UCITS Directive which may be needed to give effect to a UCITS Management Company Passport, and to indicate the fields that could be addressed through Level 2 implementing legislation.

In particular, CESR is asked to propose the necessary supervisory and technical conditions to ensure that the cross-border management of a UCITS fund does not weaken the ability of the competent supervisor or other responsible bodies to monitor and enforce compliance of the fund with its governing law and rules.

CESR is therefore asked to set out the following:

- A clear and systematic allocation of regulatory responsibilities between the competent authorities responsible for all relevant entities (management company, UCITS fund and depositary);
- Conditions needed to ensure that the respective competent authorities have the means necessary to verify, monitor and enforce (directly or indirectly) the regulatory requirements for which they are responsible;
- Obligations incumbent on competent authorities to provide information and other assistance to partner authorities or other entities having responsibilities for the oversight of the fund/management company;
- Conditions needed to ensure that all relevant entities are subject to effective enforcement action for breaches of the law governing the fund or fund rules.



This will also require clarification of the rules governing the activities of the management company and of the UCITS fund, and the respective areas of responsibility of the different competent authorities and actors.

The expected content of the advice is described in more detail in the attached request for advice from the Commission.

CESR has been asked to deliver its advice by **1 November 2008**.

The advice will be discussed and developed by the Investment Management Expert Group, chaired by Lamberto Cardia, Chairman of the Italian Commissione nazionale per le società e la Borsa (CONSOB).

Call for evidence:

CESR invites all interested parties to submit their views as to what CESR should consider in its advice to the European Commission.

All contributions can be submitted online via CESR's website under the heading Consultations at www.cesr.eu by **22 August 2008**.

Due to the tight timeline, CESR will not be able to organise extensive public consultation nor to undertake any impact assessment in relation to its advice, but will make all reasonable efforts to identify how best to interact with market stakeholders under those constraints. CESR will keep market participants informed about the arrangements made in this respect.



EUROPEAN COMMISSION
Internal Market and Services DG

The Director-General

Brussels, 16th July 2008 **14623**
MARKT/G4/PS/D(2008) 19064

Mr Eddy WYMEERSCH
Chairman
CESR
11-13 avenue de Friedland
75008 Paris

Subject: Request for assistance on UCITS Management Company Passport

Dear Mr Wymeersch,

I write to request the assistance of CESR on supervisory issues which would arise in the event that a UCITS fund was managed by a management company situated in another Member State (Management Company Passport).

Today (July 16th), the Commission has published a proposal to amend the UCITS Directive in order to facilitate increased efficiency and consolidation in the fund industry and to enhance investor disclosures (Key investor Information). During the preparation of its proposals, the Commission has given careful consideration to the possibility of introducing new provisions in respect of the Management Company Passport. Preliminary versions of work on Management Company Passport have been made public, and were the subject of discussion with CESR Investment Management Expert Group in summer 2007.

However, this preparatory work revealed important uncertainties and difficulties regarding:

- the allocation of responsibilities for ensuring compliance with the various obligations laid by UCITS between the authorities responsible for the fund and the management company where these are located in different Member States;
- the practical and technical conditions that would be necessary to enable both authorities (and other entities such as depositary or Board of Governors) to monitor compliance with the relevant requirements, and to support effective cooperation between the respective competent authorities;
- the ability of the UCITS fund's competent authority to enforce its rules on the fund when the fund is managed from another Member State.

The consultative and preparatory work did not succeed in identifying fully satisfactory answers to these concerns. As a result, the Commission considered that the inclusion of such provisions could give rise to supervisory, legal and operational risk which could be detrimental to the operation of funds making use of the Management Company Passport. The Commission has therefore decided not to include such provisions in its proposal for amendments to the UCITS Directive.

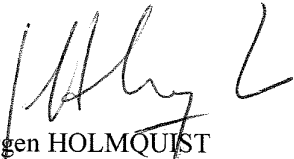
In recognition of the interest that a Management Company Passport may hold for some market participants, the Commission would like to request CESR's technical advice in respect of the questions set out in the attached mandate. Following CESR's advice the Commission would be able to consider an amendment to the UCITS proposal to introduce a viable Management Company Passport.

This advice should be guided by the principle that investors in funds that are managed on a cross-border basis should not be exposed to additional legal, operational risk or lower standards of supervision than investors in domestically managed UCITS. The mandate seeks advice on the conditions that are needed to ensure that Management Company Passport is consistent with this objective.

In particular, the advice should contain clear guidance on the allocation of responsibilities for monitoring and compliance of UCITS provisions between the authorities responsible for the UCITS fund and the management company. The advice should ensure that a competent authority is clearly designated as responsible for the different fields of activity, and avoid situations where responsibilities are not attributed to one authority or where responsibilities are duplicated. It should also provide clear guidance on the conditions and systems that the respective competent authorities will need to monitor and enforce compliance with the relevant requirements of the Directive for which they are responsible.

I would like to request CESR to submit its advice no later than 1 November 2008. The Commission is very grateful to CESR for its assistance in this matter, as well as for ongoing work on key investor information. My services remain at your disposal in respect of any questions arising from the present letter and accompanying mandate.

Yours sincerely,



Jörgen HOLMQUIST

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Cc: Mr L. Cardia, Chairman, Mr V. Conti Commissioner, Ms N. Giusto, Director International Relations CONSOB; Mr C. Comporti, Secretary General, CESR

REQUEST FOR ASSISTANCE ON UCITS MANAGEMENT COMPANY PASSPORT

1. BACKGROUND TO THE REQUEST FOR ADVICE

Under current approaches to implementation of the UCITS Directive, a UCITS, its management company, and its depositary must be located in the same Member State. All activities related to collective portfolio management and administration of the fund are subject to the law of one Member State and accountable to a single enforcement authority.¹

It has been suggested that the requirement to domicile all entities involved in the management and administration of a UCITS fund in one Member State represents a disproportionate and costly restriction on fund business. In its 2006 White Paper on enhancing the Single Market framework for investment firms, the Commission undertook to examine the possibility of establishing an effective management company passport as part of its package of targeted legislative amendments to the UCITS Directive. A management company passport would allow a UCITS fund to be managed by a management company authorised and supervised in a Member State other than the UCITS home Member State. An effective management company could avoid a double layer of capital charges. In the longer term, it could lead to greater specialisation benefits and scale economies and increase the quality of customer service and risk management.

Throughout the preparation of amendments to the UCITS Directive, the Commission services have consistently stressed the need to ensure that the management company maintains the current high level of investor protection provided by the UCITS framework. An investor investing in a UCITS fund which is managed on a cross-border basis should not be exposed to additional legal, operational or other risks compared to an investor investing in a fund whose management company is domiciled locally. In preliminary working documents foreshadowing possible amendments to the UCITS Directive², the Commission services identified considerations of a legal and supervisory nature that would need to be addressed when legislating for a management company passport. Any amendments to the UCITS Directive should "*allow fund managers to manage funds (of both contractual and corporate type) domiciled in another Member State, without generating fiscal or supervisory uncertainty which might undermine the effective oversight or tax-efficiency³ of the management company/fund chain.*"

2. THE KEY FOCUS OF THE REQUEST FOR ADVICE:

The Commission requests CESR advice on the supervisory and technical conditions that must be put in place to ensure that the cross-border management of a UCITS fund does

¹ The UCITS Directive (Article 5g of the UCITS Directive) allows activities to be delegated to parties in other Member States and third countries. However, the authorised entity which made the delegation remains fully liable for delegated functions and continues to be accountable for all authorised activities (including delegated functions) to the single supervisor.

² http://ec.europa.eu/internal_market/investment/legal_texts/index_en.htm

³ In the above referenced documents (p.13 overview document), DG MARKT has set out the reasons which have led it to conclude that the scope for potential tax inefficiencies arising in the case of cross-border UCITS management is confined to some non-fiscally transparent structures (some contractual funds, limited partnerships).

not weaken the ability of the relevant supervisors or other responsible bodies to monitor and enforce compliance of the funds with its governing law and rules. There will be a need for clarity as regards the rules governing the activities of the management company and of the UCITS fund, the respective areas of responsibility of the different competent authorities and actors. In the absence of such clarity, operational and legal risk could compromise the smooth functioning of UCITS funds and the interests of unit-holders/investors.

CESR is invited to provide advice that will help the Commission to develop provisions permitting the introduction of management company passport under conditions which are consistent with high levels of investor protection. The advice should set out:

- A clear and systematic allocation of regulatory responsibilities between the competent authorities responsible for all relevant entities (management company, UCITS fund and depositary);
- Conditions needed to ensure that the respective competent authorities have the means necessary to verify, monitor and enforce (directly or indirectly) the regulatory requirements for which they are responsible;
- Obligations incumbent on competent authorities to provide information and other assistance to partner authorities or other entities having responsibilities for the oversight of the fund/management company;
- Conditions needed to ensure that all relevant entities are subject to effective enforcement action for breaches of the law governing the fund or fund rules.

In addition, CESR advice on management company passport should be mindful of the need to minimise compliance costs and complexity for business operators of the supervisory framework. The advice should, where consistent with the goal of underpinning the current high level of investor protection, avoid duplication of controls and excessively cumbersome administrative procedures.

CESR is invited to advise the Commission on the structure and principles which should guide potential future amendments to the level 1 UCITS Directive which may be needed to give effect to a UCITS management company passport. The advice should focus on high level principles and considerations that need to be enshrined in level 1 Directive, while indicating the fields that could be addressed through level 2 implementing legislation. The advice should specify the criteria according to which implementing legislation should be defined. CESR advice will be used to inform further reflections on any eventual adjustments to the existing UCITS Directive (level 1) to give effect to the management company passport.

3. CONTENT OF THE ADVICE

3.1. Definition of domicile:

The introduction of the management company passport will result in a situation whereby the home Member State of the management company will be different from the home Member State of the UCITS (fund).

CESR is asked to advise on the elements that could be used to distinguish the home Member State of the management company, that of the UCITS fund and that of the depositary in situations where use is made of the management company passport. Particular consideration should be given to the case of UCITS funds established under contractual or trust law.

3.2. Applicable law and allocation of supervisory responsibilities

The current UCITS Directive does not provide for a clear functional break-down of the services that constitute the activity of collective portfolio management (annex II) between the management company and the UCITS fund (Article 1(a)2). Cross-border management of a UCITS implies that at least some of these activities are performed by an entity, the management company, which is authorised (Article 5(1) of the UCITS Directive) by the authority of a Member State different from the one where the fund is itself situated and supervised.

The UCITS Directive distinguishes between the rules governing the establishment and on-going activities of the management company (Section III of the UCITS Directive for management companies, IV for investment companies) and those governing the constitution and functioning of the UCITS fund (Sections V to VIII). Currently, all of these provisions are enforced in one single Member State.

In the event that the management company is established in a Member State other than of the UCITS fund, there will be a need to ensure that the regulatory requirements applying to both the management company and the UCITS fund are clearly specified and that the respective responsibilities of the relevant competent authorities are clear. It will also be necessary to ensure that the cross-border organisation of the fund management/administration process does not compromise the full application of all requirements flowing from the UCITS Directive – through the creation of regulatory gaps.

CESR is asked to review the current specification of provisions of UCITS law that are binding at the level of the management company and at the level of the fund and depositary, and advise on whether the envisaged allocation of responsibilities are sufficiently complete and effective to cater for situations where the management company and UCITS fund are in different Member States.

In particular, CESR is asked to identify and propose solutions to any identified gaps in supervision or overlapping responsibilities that might arise if the management company and fund/depositary are located in different Member States.

CESR is asked to advise on whether formal structures (e.g. colleges of supervisors or MoUs) are needed to underpin cooperation between competent authorities responsible for management company and the UCITS fund.

3.3. Authorisation procedure for UCITS fund whose management company is established in another Member State

Once authorised as a management company in compliance with the UCITS Directive, the management company should be deemed eligible to provide services of collective portfolio management to UCITS funds in other Member States, or to establish a UCITS fund in another Member State.

There may also be a need for a mechanism which allows for verification that the management company employs the risk management procedures needed to manage effectively the full range of risks embodied in the UCITS investment policy. This will permit an assessment that the qualifications of the manager and its risk management systems are capable of ensuring that the UCITS fund operates in conformity with its fund rules and governing law, and that the risk management systems are commensurate with the risks embodied in the UCITS investment policy.

CESR is requested to advise on the need for and design of mechanism or process which will allow for checking that qualifications of the management company (authorised in another Member State) are commensurate with the demands/risks embedded in the investment policy of the UCITS fund.

CESR is asked to advise on any duly motivated circumstances under which a management company could be refused permission to manage/set up a fund in another Member State.

3.4. On-going supervision of the management of the fund

Having clarified the law applicable to the management company and the UCITS fund (under section 3.2 above), there will be a need to define the conditions needed to ensure that the respective competent authorities have the means to monitor and control compliance with the law governing the management company or fund, and to detect breaches of the governing law and fund rules. CESR is asked to advise on the conditions that may be required to ensure that the respective authorities are able to discharge effectively their responsibilities for monitoring and enforcing compliance with the law governing the fund.

It is essential for the smooth management and administration of the fund that all relevant commercial entities and the respective competent authorities work effectively together. Particular attention will be needed to ensure the adequate and timely flow of information between:

- the different commercial entities involved in the management, administration and oversight of the UCITS fund;
- the competent authorities responsible for ensuring compliance of the various commercial entities with the law governing their activities and the fund rules.

CESR is asked to advise on the conditions (e.g. in terms of direct or indirect access to or control of certain functions or processes) needed to ensure that the supervisor of the UCITS and the supervisor of its management company have sufficient means and information to discharge their duties effectively.

CESR is asked to advise on the obligations of information and conduct of business that the management company owes to the UCITS fund and depositary (and vice versa).

CESR is asked to advise on the mechanisms or procedures that should be envisaged to ensure the timely and effective exchange of information between a UCITS supervisor and a supervisor of a management company (or vice versa).

3.5. Dealing with breaches of rules governing the management of the fund

Provisions will be needed to clarify arrangements when failure of one party to comply with its obligations and responsibilities leads to an actor in another Member State being unable to comply with the rules applying to it. These provisions should in particular deal with the way competent authorities will be informed about relevant breaches and what measures they can take to deal effectively with them.

Additional complexities are related to cross-border enforcement actions against contractual funds. As contractual funds are not legal entities, they have no legal personality, independent of their management company. Therefore if the deeds or rules constituting a contractual fund are laid down under the law of a Member State different from that where the management company is located, there will be no legal entity present in the Member State where the fund is constituted who can be pursued by the relevant authorities in the case of material breach of fund rules. The question arises whether this particular situation presents additional risks in terms of supervision or investor protection and would therefore require specific treatment.

CESR is asked to advise on any mechanisms or information flows that are needed to ensure that the respective competent authorities are duly and quickly informed of any breach of the rules governing the management of the fund; and the conditions under which effective enforcement action can be undertaken.

CESR is invited to advise on the need for and form of any additional measures to facilitate effective enforcement action by authorities responsible for a contractual form UCITS fund when the management company is established in another Member State.

4. Timing

CESR is requested to transmit its final advice to the Commission on the above issues by no later than 1 November 2008.