



## COMMITTEE OF EUROPEAN SECURITIES REGULATORS

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Date: 17 September 2009  
Ref: CESR/09-785

### CONSULTATION PAPER

# **CESR's technical advice to the European Commission on level 2 measures relating to mergers of UCITS, master-feeder UCITS structures and cross-border notification of UCITS**

**Deadline for contributions:** CESR invites responses to this consultation paper by 17 November 2009. All contributions should be submitted online via CESR's website under the heading 'Consultations' at [www.cesr.eu](http://www.cesr.eu). All contributions received will be published following the close of the consultation, unless the respondent requests their submission to be confidential.



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## Introduction

1. In March 2007, the European Commission announced a series of targeted enhancements to the UCITS Directive (85/611/EC). Following further work and consultation, the Commission adopted a proposal for the revised UCITS Directive in July 2008, an amended version of which was approved by the European Parliament in January 2009 and adopted by the Council in June 2009. The final text of the revised Directive is expected to be published shortly in the Official Journal.
2. In the light of the approval of a compromise text by the European Parliament and the Council early in 2009, the Commission prepared a provisional request to CESR for technical advice on possible implementing measures concerning the future UCITS Directive (“the mandate”). The mandate is split into three parts as set out below. This consultation paper sets out CESR’s proposals under Part III.
3. Part I concerns measures related to the management company passport, while Part II covers implementing measures on the form and content of key investor information disclosures for UCITS. CESR’s draft advice on these implementing measures are set out in two consultation papers published on 8 July 2009 (Ref. CESR/09-624 and Ref. CESR/09-552 respectively). The deadline for delivery of CESR’s advice on Parts I and II is 30 October 2009.
4. Part III concerns measures related to mergers of UCITS, master-feeder structures and the notification procedure for cross-border marketing. The Commission is not under a legal obligation to adopt implementing measures in any of these areas. As such, the Commission encouraged CESR to focus firstly on the advice for Parts I and II. However, the Commission invited CESR to reflect on the best way to organise its work such that all necessary level 2 measures, including those under Part III of the mandate, are adopted in time to be implemented by Member States within the timeframe imposed by the level 1 Directive.
5. Following receipt of the mandate, CESR published a call for evidence on 17 February 2009 (Ref. CESR/09-179) to which it received 30 responses. These responses, which are available on CESR’s website, have been taken into account in the preparation of CESR’s advice. The advice has been prepared by the Investment Management Expert Group which is chaired by Mr Lamberto Cardia, Chairman of the Italian securities regulator, the Commissione Nazionale per le Società e la Borsa (CONSOB).

### Impact of the proposed approach

6. CESR is mindful of the impacts of its proposals. In order to develop a better understanding of the possible costs and benefits of CESR’s approach, stakeholders are invited to give specific input on likely impacts – including quantitative estimates wherever possible – of the draft advice. For this purpose, questions on costs and benefits are included throughout the document. This approach is in line with the request in the Commission’s mandate that CESR should present appropriate impact assessments in support of its advice.

### Next steps

7. CESR invites responses to this consultation from all stakeholders by 17 November 2009. During the consultation, an open hearing will be held at CESR’s premises, full details of which will be made available on CESR’s website in due course.

## Definitions

### *Directive*

The draft UCITS Directive (2009/65/EC) adopted by the European Parliament and the Council in 2009

### *feeder*

a feeder UCITS within the meaning of Article 58(1) of the Directive

### *feeder auditor*

the auditor of a feeder UCITS

### *feeder depositary*

the depositary of a feeder UCITS

### *fund documents*

the documents required to be drawn up for every UCITS, specifically its:

- fund rules or instrument of incorporation
- prospectus
- key investor information
- annual and half-yearly reports

### *home State*

the UCITS home Member State as defined in Article 2(1)(e) of the Directive

### *home State authority*

any or all of the competent authorities of the UCITS home Member State

### *host State*

the UCITS host member State as defined in Article 2(1)(f) of the Directive

### *host State authority*

any or all of the competent authorities of the UCITS host Member State

### *KID*

Key Information Document, CESR's proposal for the form that key investor information required by Article 78 should take

### *master*

a master UCITS within the meaning of Article 58(3) of the Directive

### *master auditor*

the auditor of a master UCITS

### *master depositary*

the depositary of a master UCITS

Where a UCITS is a self-managed investment company, references in this paper to the management company of the UCITS should be read as references to the UCITS itself.

## SECTION I – MERGERS OF UCITS

1. The first section of Part III of the mandate relates to implementing measures in Chapter VI concerning mergers of UCITS. There is only one set of implementing measures provided for in that chapter, which relates to Article 43. Where a merger is to be proposed or effected, Member States must require both the merging and the receiving UCITS to provide information so that the unitholders of both funds can make informed judgements about its impact on their investment. Paragraph (3) of Article 43 sets out four specific areas which the information must address, and also requires a copy of the key investor information of the receiving UCITS to be provided.
2. The Commission has the power to adopt implementing measures specifying the detailed content, format and way of providing this information. CESR is invited to advise on each of these aspects.
3. Responses to this part of the call for evidence came mainly from trade associations representing asset management firms, and individual firms. There were also some comments from associations representing credit institutions acting as depositaries.

### 1.1 Contents and format of the information

4. CESR is invited to advise on what additional detail could be specified in relation to the four specific areas of information listed in Article 43(3)(a) to (d), and whether the key investor information should be provided as a stand-alone document or as an integral part of the merger information. CESR is encouraged to specify the format of the letter<sup>1</sup> and provide a draft for this purpose.
5. Respondents to the call for evidence were mixed in their views about the need for level 2 measures. Some thought that none were needed as there is sufficient detail at level 1, and any supplementary matters could be dealt with effectively at level 3. Some respondents supported harmonisation of content, and suggested a list of specific subjects which they thought should be covered in the information, such as differences in investor rights, allocation of merger costs, treatment of accrued income in the merging UCITS, or whether there was to be any cash payout. Some wanted to see the essential points of the merger summarised in a concise, plain language format along the lines of the Key Information Document (KID) proposed in CESR's consultation (Ref. CESR/09-552).
6. Most of those respondents who commented on the provision of the KID would prefer to see it attached to any information letter rather than being provided as an integral part of the document.
7. Some respondents supported harmonisation of the format of the information (generally they were in favour of harmonising content as well), but the majority were against any prescription at level 2 in relation to the format.

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<sup>1</sup>The mandate refers to provision of an 'information letter' although no such term appears in the level 1 text, which refers only to 'information'.

## Level 2 advice

### Box 1

1. The information to be provided to unitholders shall be written, as far as possible, in a brief manner and in non-technical language that is reasonably likely to enable them to understand the nature of the proposal.
2. Since Article 43 does not require the unitholders of the merging and receiving UCITS to be given identical information, the sets of information should reflect their different needs. The information to be provided to the unitholders of the merging UCITS shall be sufficiently detailed and comprehensive to meet the reasonable needs of investors who have no prior knowledge of the features of the receiving UCITS or the manner of its operation. Where a cross-border merger is proposed, the merging UCITS shall take particular care to provide explanations in plain language of any terms or procedures relating to the receiving UCITS that are commonly used in its home State, but are unlikely to be familiar to investors in the home State of the merging UCITS.
3. The information to be provided to the unitholders of the receiving UCITS shall assume that those unitholders are already reasonably familiar with the features of the UCITS, the rights they enjoy in relation to it, and the manner of its operation. It shall focus on the operation of the merger and its potential impact on the receiving UCITS.
4. The information to be provided in accordance with paragraph (b) of Article 43(3) shall include, in addition to the points specifically mentioned in paragraph (b):
  - (a) details of any differences in the rights of unitholders;
  - (b) in the context of the investment policy and strategy, a profile of the typical investor for whom the UCITS is designed;
  - (c) in the context of costs, a statement of all charges and expenses for both UCITS, based on the amounts disclosed in their respective KIDs;
  - (d) if either UCITS applies a performance-related fee, an explanation of how it will be applied up to the point at which the merger becomes effective and, if the receiving UCITS applies such a fee, how it will subsequently be applied to ensure fair treatment of those unitholders who previously held units in the merging UCITS;

It shall explicitly draw the attention of unitholders to the KID and emphasise the desirability of reading it.
5. The information to be provided in accordance with paragraph (c) of Article 43(3) shall include in particular:
  - (a) how any accrued income in the merging UCITS is to be treated;
  - (b) if the terms of the merger include provision for a cash payment representing a percentage of the net assets of the merging UCITS, details of that proposed payment;
  - (c) in cases where Article 46 permits any of the costs of the merger to be charged to either the merging or the receiving UCITS or any of their unitholders, details of how those costs are to be allocated;
  - (d) an indication of how the report of the independent auditor or the depositary referred to in Article 42(3) may be obtained.
6. The information to be provided in accordance with paragraph (d) of Article 43(3) shall include:

- (a) where relevant under national law for the particular UCITS structure, the procedure by which unitholders should approve the merger proposal;
  - (b) how long unitholders will be able to continue making subscriptions and redemptions of units in the merging UCITS, and the details of any intended suspension of dealing in units to enable the merger to be carried out efficiently;
  - (c) when the merger will become effective in accordance with Article 47(1);
  - (d) when the unitholders of the merging UCITS will be able to exercise their rights as unitholders of the receiving UCITS (if different to (c)) and, if applicable, when and how they will receive the cash payment.
7. In cases where unitholders in the merging UCITS have the right to vote on the proposed merger, the information to be provided in accordance with paragraph (c) of Article 43(3) shall state:
- (a) that in the event the proposal is approved by the necessary majority, those unitholders who vote against the proposal or who do not vote at all, and who do not exercise their right to dispose of their units before the merger is effected, shall be issued units in the receiving UCITS in accordance with the terms of the merger;
  - (b) what arrangements will be made to inform all unitholders of the outcome of the vote.
8. The copy of the KID to be provided in accordance with paragraph (e) of Article 43(3) may be an integral part of the information document, or a free-standing document that is despatched or transmitted together with the main information document. If the KID is included in a larger document, it must appear in a prominent position. Its design and appearance must comply with all relevant requirements set out in KID rules.
9. Between the date when the information required by paragraphs 2 and 3 is provided to the unitholders of the merging and receiving UCITS and the date when the merger is effective, a copy of the relevant set of information shall be provided to each person that buys units in either UCITS, and to any potential investor who asks to receive copies of any of the fund documents of either UCITS.

#### Explanatory text

8. The advice emphasises the importance of presenting the information clearly and in plain language. Where a cross-border merger is planned, the management companies of the two UCITS have a particular responsibility to consider how the constitution and operation of UCITS may differ between their States, and to explain to the unitholders in the home State of the merging UCITS any significant differences they ought to be aware of.
9. Article 43 does not state or imply that the information provided to the unitholders of the merging and the receiving UCITS must be identical. Indeed, it would be illogical to do so as existing unitholders in the receiving UCITS should already have sufficient information about its aims and manner of operation. The information given to these unitholders should be suitably concise and should focus on the operation and potential impact of the merger (e.g. whether the UCITS may receive assets from the merging UCITS that are likely to affect its risk profile). The information needs of unitholders in the merging UCITS, on the other hand, are likely to be more substantial.
10. CESR's advice takes account of the fact that Article 43(3) is detailed and specific about the requirements for the content of the information. The advice elaborates certain points, for example that any differences between the two UCITS in terms of unitholder rights should be spelt out; this could be important if, for example, an investment company conferring shareholder rights on its unitholders under national law were to merge with a common fund where such rights do not apply. The description of differences should enable investors to compare the

features of the two UCITS easily; this could be done, for example, by setting them out side-by-side in a table.

11. The requirement in Box 1 paragraph 1 for the information to be brief and written in plain language applies in all cases. There may be situations where the proposal is complex and requires a relatively lengthy explanation (although it is to be hoped that such cases would be comparatively rare). If so, the full explanation might be supplemented by providing a short summary of the key points of the merger proposal at the beginning of the letter or document, with signposting to the parts of the document where full details are provided. The inclusion of a summary would not relieve UCITS of the obligation to avoid the use of long, legalistic explanations in the rest of the document.
12. Regarding Box 1 paragraph 4, examples of differences in unitholder rights might include the effect of merging a common fund into an investment company (or vice versa), the provision of information to unitholders, the circumstances in which an extraordinary general meeting of unitholders may be convened, or the rights and powers that unitholders may exercise at such meetings.
13. The KID could be included as an annex to the information document provided it is clearly visible and not mixed with other material (this could be achieved for example by putting it on a fold-out back page).
14. Once existing unitholders in both UCITS have been informed of the merger, it is important that anyone who subsequently buys units in either fund, or who is thinking of investing and asks for full product information, should be similarly informed. Paragraph 9 requires copies of the relevant set of information to be provided to these groups of investors.

#### Questions:

1. *Do you agree with CESR's proposals for specifying the information to be given to unitholders? Is there any other information that is essential for them?*
2. *Do you agree that a summary of the key points of the merger proposal should be optional?*
3. *Should there be more detail at level 2 about what ought to be included in the description of the rights of unitholders?*
4. *Do you agree with the proposed treatment of the KID of the receiving UCITS?*
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)?*

## **1.2 Providing the information**

15. The mandate notes that, with the exception of key investor information, the Directive does not prescribe how information should be provided. CESR is invited to advise on what priority should be given to this particular issue, and to consider whether it is necessary to be specific about the medium in which the information is to be supplied.
16. Most of the respondents to the call for evidence who commented on this point were not in favour of any prescription or harmonisation at level 2. One respondent commented on the need to consider the fact that many unitholders are mere nominees for underlying investors, so it is important that information is provided in a form that can be quickly and effectively passed on to them.
17. CESR notes that, in both the home State of the UCITS and each host State where it is marketed, the national law already makes provision for how documents and other information may be



delivered to existing investors. Some Member States require notifications of events or changes to the UCITS to be sent to unitholders whose names are entered on the register; in other States the UCITS has no such record of its unitholders, so notice must be given in a newspaper or other widely-circulated publication where investors are likely to read it. Also, where there is a register, the registered unitholder may be a nominee for multiple underlying investors, in which case national law and regulation would govern the relationship between those parties.

18. Any proposal to harmonise the manner of providing unitholder information would either have to be adaptable to the differing requirements of Member States' national laws (in which case it would probably add little or no value) or it would have to impose new requirements for the specific situation of a merger, which would generate costs for UCITS in several States. CESR does not consider that the benefits of legislation to harmonise the way in which information should be provided in the particular case of a merger, are likely to justify the costs of implementing and maintaining it, and therefore does not intend to provide advice on how this might be done.
19. CESR recommends that industry participants should consider whether and how the provision of information to existing investors might be improved, so as to achieve more consistency in the effectiveness and timeliness of communications.

#### Question

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?*

### **1.3 General remarks**

20. CESR notes that the Directive procedure for cross-border mergers is as yet untested, and that experience may indicate the need for additional implementing measures or refinements to those proposed in this paper. CESR recommends that the Commission should carry out a post-implementation review of the effectiveness of the mergers regime, after a suitable interval or once a sufficient number of mergers has taken place, in order to determine whether improvements could be made to it.
21. Some respondents to the call for evidence noted that UCITS and their management companies may be deterred from using the procedures because of potential adverse tax implications. CESR recommends that the Commission should keep this issue under review.

## SECTION II – MASTER-FEEDER STRUCTURES

1. The second section of Part III of the mandate relates to implementing provisions in Chapter VIII concerning master-feeder structures. The mandate envisages eight areas in which it may be appropriate to introduce implementing measures, which are addressed in turn in this section of the consultation paper.
2. The mandate notes that the implementing measures should be justified on three investor protection grounds:
  - that any changes in the investment policy of the master UCITS have a significant impact on the feeder UCITS;
  - that the feeder UCITS is dependent on the master UCITS in order to fulfil its information and reporting obligations to its unitholders;
  - that the feeder UCITS requires information from the master UCITS to carry out necessary monitoring activities.
3. Responses to this part of the call for evidence came mainly from trade associations representing asset management firms, trade associations representing depositaries, and individual asset management firms. A common theme in many of the responses was a request to provide sufficient flexibility for commercial negotiation to take place and to avoid too much prescription at level 2.

### 2.1 Agreement between feeder and master UCITS

4. Article 60(1) requires the feeder UCITS to enter into an agreement with the master UCITS to ensure the feeder is provided with all documents and information necessary to discharge its Directive obligations. If master and feeder are to be managed by the same management company, internal conduct of business rules may be established in place of an agreement. The provision applies equally in cases where the feeder and master UCITS are established in the same Member State.
5. CESR is invited to advise on what the agreement should cover and which legal regime should apply to cross-border agreements, and to consider providing a draft model agreement.
6. Respondents to the call for evidence were split in their views on these issues. Some wanted prescriptive level 2 measures, and suggested a considerable number of topics that might be addressed in some detail by the agreement. Others said that differences in legal and regulatory regimes would make detailed prescription on this issue too complex, and that consequently it would be more proportionate to indicate in general terms which topics the agreement should cover. It was pointed out that many firms already have such agreements in place and CESR should not set out to re-invent them. Level 3 guidance on the contents and format of the agreement could supplement such measures.
7. There were also differences of opinion on the applicable legal regime for cross-border agreements. Some suggested that there should be no prescription on this point, since there are already protocols in other fields of European law to address such situations. That would enable the parties to agree to be bound by the laws of a third “neutral” Member State. A fair number favoured the regime that applies to the feeder UCITS, arguing that the feeder is more likely to need to enforce the agreement in the event of non-compliance so should benefit from being able to take legal action in its home State. Some others, however, suggested that the law of the master UCITS should apply, as a master could have several feeders, each in a different Member

State, so it would be onerous for the master to be operating under several different legal regimes. These considerations also apply to the agreements between depositaries (section 2.4) and auditors (section 2.6).

#### Level 2 advice

##### Box 2

Without prejudice to the provisions of Chapter VIII of the Directive, the terms of the agreement between the master UCITS and the feeder UCITS referred to in Article 60(1) shall not be materially inconsistent with the prospectus of either UCITS. The agreement shall include, but not be limited to, the following:

1. Access to information:
  - (a) the basis on which the master is to make new versions of its fund documents available;
  - (b) whether and how the master is to make available any internal operational documents (e.g. its risk management process, or its compliance reports);
  - (c) what details of breaches by the master will be made available to the feeder and, if the master undertakes to notify the feeder of them, the manner and timing of such notifications;
  - (d) in order to allow the feeder, when using financial derivative instruments for hedging purposes, to comply with its obligations under Article 58(2) in connection with Article 51(3), how and when the master will make available information about its actual exposure to such instruments to enable the feeder to calculate its own global exposure as envisaged by Article 58(2)(a);
  - (e) any other information-sharing arrangements, including with third parties.
2. Basis of investment by the feeder UCITS:
  - (a) the charges and expenses to be borne by the feeder, including (if applicable) a statement of which share class(es) of the master is/are available for investment, and details of any rebate or retrocession of charges or expenses by the master;
  - (b) if applicable, the terms on which any initial or subsequent transfer of assets in kind may be made from the feeder to the master.
3. Standard dealing arrangements:
  - (a) co-ordination of the frequency and timing of the NAV calculation process and the publication of prices; this part of the agreement shall contain appropriate measures to ensure compliance with the requirements of Article 60(2);
  - (b) co-ordination of transmission of dealing orders by the feeder, including (if applicable) the role of transfer agents or any other third party;
  - (c) if applicable, any arrangements necessary to take account of the fact that either or both UCITS are listed or traded on a secondary market;
  - (d) if the feeder and the master are denominated in different currencies, the basis for conversion of dealing orders;
  - (e) settlement cycles and payment details for purchases and redemptions of units of the master (including, if desired, the terms on which the master may settle redemptions by a transfer of assets in kind to the feeder);
  - (f) procedures to ensure enquiries and complaints from investors are handled appropriately (e.g. handling of mis-directed correspondence);
  - (g) if the fund rules or instrument of incorporation and prospectus of the master give it certain rights or powers in relation to unitholders (e.g. the right to refuse to accept investments), and the

master chooses to limit or forego the exercise of all or any such rights and powers in relation to the feeder, a statement of the terms on which it does so.

4. Contingent events affecting dealing arrangements:

- (a) manner and timing of notification by the master of the suspension and resumption of dealings in units;
- (b) arrangements for notifying and resolving pricing errors in the master (e.g. possible co-ordination of thresholds for recalculating the NAV).

5. Standard arrangements for the accounting period end:

- (a) where the feeder and the master have the same accounting period end, the co-ordination of the production of their periodic reports;
- (b) where the feeder and the master have different accounting period ends, arrangements for the feeder to obtain any necessary information from the master to enable it to produce its periodic reports.

6. Changes to standing arrangements:

- (a) timing and manner of notice to be given by the master of proposed or effective revisions to its fund rules / instrument of incorporation / prospectus / KID, if different to the standard arrangements for notification of unitholders;
- (b) timing and manner of notice by the master of a proposed liquidation, merger, or division;
- (c) notice by either UCITS that it has ceased or will cease to meet the qualifying conditions to be a feeder UCITS or a master UCITS respectively;
- (d) notice by either UCITS that it is changing its management company, its depositary or its auditor;
- (e) any notification of changes not covered above that the master undertakes to provide (e.g. changes to operational matters not described in the fund documents).

7. Applicable law:

- (a) where the feeder and the master are established in the same Member State, a statement that the applicable law shall be the law of that Member State (or any part of it), and both parties agree to the exclusive jurisdiction of the courts of that Member State (or the relevant part of it).
- (b) where the feeder and the master are established in different Member States, a statement:

**OPTION A**

[that the applicable law shall be the law of the Member State (or any part of it) in which the feeder is established, and that both parties agree to the exclusive jurisdiction of the courts of that Member State (or the relevant part of it).]

**OPTION B**

[either that the applicable law shall be that of the Member State (or any part of it) in which the feeder is established or that it shall be that of the Member State (or any part of it) in which the master is established, as the parties may choose. Both parties agree to the exclusive jurisdiction of the courts of the Member State (or the relevant part of it) whose law is applicable to the agreement.]

Explanatory text

- 8. CESR's advice is intended to set out the areas to be covered by an agreement without being prescriptive about either the exact content or the format of such an agreement. This will allow



feeders and masters a suitable degree of flexibility, bearing in mind the variety of situations that might arise (e.g. depending on whether both UCITS are established in the same Member State or not, and whether their management companies are part of the same group or are entirely unconnected).

9. CESR recognises that, since both UCITS have a fiduciary duty to protect the interests of their unitholders, it does not need to specify all the possible protections that each party may wish to include in the agreement, having obtained suitable legal advice. CESR's advice covers only the areas which unitholders would reasonably expect to be explicitly addressed in the agreement.

#### Applicable law

10. CESR has taken account of responses to its call for evidence which, as described in paragraph 2.1.4, did not indicate any consensus on the question of the law applicable to the agreement. There are four possible options for addressing this issue:
  - prescribe the law of the feeder's home State;
  - prescribe the law of the master's home State;
  - prescribe a choice between the laws of the home State of either UCITS;
  - allow complete flexibility, including the possibility of applying the law of a third country.
11. CESR sees merit in the first option, and to a lesser extent in the second. It does not believe that it would be appropriate to compel every agreement to be under the law applicable to the master, but the third option seems to offer a degree of flexibility that might be beneficial, depending on the particular circumstances of the two UCITS. There might, for instance, be advantageous cost savings to the feeder if the applicable law is that of the master, and there might be adverse tax implications for one or other of the parties depending on the decision.
12. However, CESR does not think that the fourth option of complete flexibility is appropriate. Although it is acceptable in some areas of European law for the parties to a contract to apply the law of a third country, CESR considers that the interests of the underlying investors would not be best served by such an arrangement. It would also be illogical to allow a feeder and a master established in the same home State to operate under the law and jurisdiction of a different Member State.
13. Consequently, CESR seeks views on whether the applicable law of the feeder home State should apply in all cases, or whether there should be a choice between the laws of the feeder and master home States.

#### Fair treatment of unitholders

##### Level 2 advice

###### Box 3

Member States may, in their national laws, regulations and provisions, require any master UCITS established in their jurisdiction to ensure that the arrangements between the master and its feeder UCITS shall not unfairly prejudice the interests of any other unitholder of the master that is not itself a feeder UCITS.

14. CESR has considered whether the agreement needs to take account of the interests of any other investors in the master that are not themselves feeder UCITS. For example, arrangements to provide particular information to the feeder, or to provide it sooner than to other investors, could



be seen as giving the feeder and its investors an unfair advantage over other direct investors in the master.

15. Although CESR regards the fair treatment of all unitholders in a UCITS as a matter of great importance, its view is that the duties of the master, in this respect, are provided for in national law. However, if Member States consider it appropriate, they could supplement the requirements of Box 2 with the measure in Box 3. It is also open for the master and feeder to include a provision on this issue in their agreement if they so wish.

#### Questions

7. *Do you agree with CESR's proposals for specifying the content of the agreement?*
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?*
9. *Which option do you prefer in relation to the national law and jurisdiction applicable to cross-border agreements?*
10. *Do you agree that measures to protect the interests of other unitholders in a master UCITS should be left to national law and regulation?*
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?*

#### Internal conduct of business rules

16. CESR's understanding is that the provision for internal conduct of business rules to replace the full agreement applies only where a single legal entity acts as the management company for both the feeder and the master. It does not apply where the two UCITS are managed by separate legal entities forming part of the same management group.

#### Level 2 advice

##### Box 4

Where the feeder UCITS and the master UCITS are managed by the same management company and elect not to enter into an agreement, as provided for in the third paragraph of Article 60(1), the management company's internal conduct of business rules shall include appropriate measures to:

1. Ensure compliance with the requirements of Article 60(2), including in situations where units of the feeder are dealt in on a secondary market;
2. Mitigate conflicts of interest that may arise between the feeder and the master, to the extent that these are not addressed by the general requirements of [cross-reference to L2 material on conflicts of interest]. These may include, but are not limited to, any of the matters identified in Box 2 above.

#### Questions

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?*
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?*



## 2.2 Measures to avoid market timing

17. Article 60(2) requires the master and the feeder to co-ordinate the timing of their NAV calculations and price publication to avoid market timing in their unit dealings. CESR is invited to advise on what measures are needed to avoid market timing or other arbitrage opportunities, taking into account the situation of UCITS whose units may or will be bought and sold through secondary trading.
18. While respondents to the call for evidence expressed general support for the need to implement effective measures to prevent market timing, few considered that additional level 2 measures in this regard would be necessary. There was considerable support for the view that this matter could be dealt with effectively through the agreement between feeder and master, covered in section 2.1.
19. CESR recognises that the activities of market timers can be detrimental to all UCITS, so it is necessary to address such risks through appropriate procedures. Although the congruity between the prices of a master and its feeder might make the feeder more vulnerable to such activities than other UCITS, CESR does not consider the risk would be so great that legislative measures applicable only to feeders would be necessary. Indeed, it would be inconsistent to legislate for feeder UCITS on this matter while remaining silent on the possibility of other dealings in units of UCITS being subject to market timing abuses.
20. CESR notes that UCITS and their management companies must determine how to combat the risk of market timing, in the light of their particular dealing arrangements. Consequently, CESR recommends that the agreement between feeder and master UCITS or the internal conduct of business rules covered in section 2.1 above should specifically address what appropriate measures are necessary to ensure compliance with the level 1 text in Article 60(2). This should include appropriate measures where the units of either or both UCITS are traded on a secondary market.

### Question

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

## 2.3 Liquidation, merger or division of a master UCITS

21. When a master UCITS either goes into liquidation, or undergoes a merger or division, Article 60 paragraphs (4) and (5) respectively set out the choices available to a feeder UCITS investing in that fund. In each case it is foreseen that the feeder will be liquidated unless its competent authority approves one of the prescribed alternative courses of action (e.g. re-investment into another master, or conversion from a feeder to a non-feeder UCITS).
22. CESR is invited to advise on detailed procedures for approving the alternative courses of action, considering in particular the timing implications and the requirements for exchange of information between competent authorities.
23. Several respondents to the call for evidence had suggestions on specific points of detail, although a few questioned the need for any level 2 measures. It was suggested that some matters could be dealt with in the agreement between the two UCITS. Some respondents asked for there to be a simplified procedure in cases where a master merges or sub-divides and the continuing UCITS has the same (or substantially the same) investment objective and policy.
24. In each of the situations covered by this part of the mandate, the actions of all parties are subject to time constraints imposed by the Directive. The feeder's proposal for dealing with the liquidation of the master UCITS must reflect the fact that the master is not obliged to give the feeder more than three months' notice of the binding decision to liquidate. Likewise, a feeder

has no right to receive earlier notice of a proposed merger or division of its master than the 60 days provided for in Article 60(5). Nevertheless, CESR considers that master UCITS should be encouraged to provide longer notice periods where possible.

25. Any proposals that CESR makes on these procedures should take account of the interests of each of the affected parties where these time constraints apply. The feeder, especially if it has not been forewarned of the master's intentions, will need to consider the options available to it, choose one and prepare a proposal to put it into effect, so that it can obtain its competent authority's decision within the necessary timescale. The competent authority should have sufficient time to consider the proposal, especially if it involves a significant change (e.g. a feeder opting to become a non-feeder UCITS). The unitholders of the feeder should be informed of any proposed change that will affect their investment and given an appropriate opportunity to react, whether through a vote (if national law requires it) or by exercising the right to redeem on non-prejudicial terms.
26. CESR considers that its advice should reflect standards set down in the level 1 text for comparable situations. Article 59, setting out the process by which a feeder UCITS is approved for the first time, grants the competent authority 15 working days to approve the application, once it has received a completed file. Where the UCITS is already in existence and wishes to become a feeder or to switch to a different master, Article 64(1) sets out the information that must be provided to unitholders and allows them at least 30 days before the new investment takes effect, in which to redeem their units without charge. Therefore, these provisions could be copied for the purpose of the situations described here.
27. CESR recognises, however, that an exact copy-out of the above-mentioned provisions might severely limit the amount of time the feeder could spend considering various options for re-investment. This could make it more likely that the feeder would have to be liquidated, which would not achieve the objective of the level 1 text to provide the feeder with a choice of possible courses of action. Competent authorities could assist in this regard by considering whether to undertake to review certain types of application in a shorter time period than the 15 working days provided for in the level 1 text, although this would have to be for each authority to decide individually.
28. CESR notes that Article 60 does not set a time period after which the feeder must be liquidated. Consequently, if the feeder is unable to obtain the necessary approval to re-invest before the master is liquidated, merged or sub-divided, the feeder should request redemption of its units (provided the master has not suspended all redemptions) or receive the proceeds of the liquidation. The feeder could remain open for redemptions until such time as it is able to re-invest, but could suspend new subscriptions during that period.
29. CESR has prepared its advice on the understanding that, where the feeder's competent authority would consider any resulting breach of Article 58(1) and (2) to fall within the exemption provided by Article 57(2), it could sanction the exception on the basis that it would be beyond the control of the feeder, and could be remedied within a reasonable timeframe taking due account of the interests of unitholders.

#### Questions

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



## Liquidation of the master UCITS

### Level 2 advice

#### Box 5

1. The feeder UCITS, as soon as it receives notification that the master UCITS is to be liquidated, shall inform its competent authority of the fact, indicating the proposed date of the liquidation, and whether it expects to suspend the repurchase, redemption or subscription of its units in accordance with Article 60(3) before that date.
2. The feeder shall submit to its competent authority, no later than two months after the date on which it received notification that the master UCITS is to be liquidated, one of the following:
  - (a) its proposal to invest in another master UCITS in accordance with Article 60(4)(a), together with the documents required under Article 59(3);
  - (b) its proposal to convert to a UCITS that is not a feeder UCITS in accordance with Article 60(4)(b), together with its revised fund rules or instrument of incorporation, prospectus, and key investor information; or
  - (c) confirmation of its intention to be liquidated.
3. The competent authority shall, if the application under 2(a) or (b) complies with the requirements of the UCITS Directive, grant approval within 15 working days of receipt of the proposal and all necessary supporting documents. It shall immediately inform the feeder UCITS of this fact.
4. On receiving the competent authority's approval, the feeder UCITS shall take appropriate action to notify the master UCITS, either by requesting repurchase or redemption of its investment or (if the master UCITS has already suspended redemption of units) confirming the basis on which the proceeds of liquidation will be transmitted to it.
5. The feeder UCITS shall, no later than five working days after receiving approval from its competent authority in accordance with (3), provide information to its unitholders about the course of action to be taken. In the case where a proposal under (2)(a) is approved, the feeder shall comply with Article 64. In the case where a proposal under (2)(b) is approved, the feeder shall comply with paragraph (6) below.
6. A feeder UCITS that is converting to a non-feeder UCITS:
  - (a) shall provide at least the following information to its unitholders:
    - (i) a statement that the competent authorities of the feeder UCITS home Member State approved the new investment objectives and policy of the UCITS;
    - (ii) the revised key investor information;
    - (iii) the date when the UCITS is to start to invest in accordance with its new objectives and policy;
    - (iv) a statement that unitholders have the right to request within 30 days the repurchase or redemption of their units without any charges other than those retained by the UCITS to cover disinvestment costs; that right shall become effective from the moment the UCITS has provided the information referred to in this paragraph.
  - (b) shall comply with Article 64(2) as if the reference in it to paragraph 1 of Article 64 were instead a reference to this paragraph;

- (c) shall not invest in accordance with its new objectives and policy before the period of 30 days referred to in sub-paragraph (a)(iv) has elapsed.
7. In the event that liquidation of the master UCITS commences before the date on which the feeder UCITS is to begin investing either in a different master UCITS or in accordance with its new objectives and policy (“the reinvestment date”), the feeder shall either:
- (a) receive the proceeds of the liquidation in cash; or
  - (b) receive some or all of the proceeds of the liquidation as a transfer in kind where both the agreement between the feeder and master UCITS and the terms of the liquidation provide for it, and if both parties so agree; in this event the feeder UCITS may realise any part of the transferred assets for cash at any time;
- provided that any cash held or received under (a) or (b) may be re-invested for the purpose of efficient cash management but not otherwise until the reinvestment date.
8. In the event that the feeder UCITS is holding assets received through a transfer in kind, and is to begin investing in a different master UCITS at the reinvestment date, it shall either:
- (a) realise all the assets for cash before the reinvestment date; or
  - (b) transfer some or all of the assets to the new master UCITS as a transfer in kind on the reinvestment date, but only where the agreement between the feeder and the new master UCITS provides for it and if both parties so agree.
9. The feeder UCITS may, between the commencement date of liquidation of its former master UCITS and the reinvestment date, suspend subscriptions into its own units. It may not suspend the repurchase or redemption of its own units during the period provided for by Article 64(1)(d) and paragraph (6)(a)(iv) above, unless it is directed to do so by its competent authority. A competent authority shall give such a direction only if it considers the suspension necessary to protect the interests of unitholders. If the feeder is unable to pay its unitholders the proceeds of their redemptions because it has not yet received the proceeds of the master’s liquidation, it shall immediately inform its competent authority of the situation.
10. By way of derogation from (2), the feeder UCITS may defer the submission of its proposal under (2)(a) or (b) if the following conditions are satisfied:
- (a) the commencement date of liquidation of the master UCITS is to be more than three months after it has given notice in accordance with Article 60(4); and
  - (b) the feeder UCITS can determine on reasonable grounds that the reinvestment date defined in (7) will fall no later than the next working day after the commencement date of the liquidation.
- The feeder UCITS shall in this case, no later than the two-month deadline in (2), inform its competent authority in writing of the date by which it expects to submit its proposal, setting out its reasons for believing that it is able to comply with (b) above.

#### Explanatory text

30. The procedure in Box 5 is designed on the assumption that the master UCITS will give the minimum notice that is required under Article 60(4), i.e. no more than three months. CESR proposes to allow the feeder UCITS two months to reach a decision as to what course of action it will take, and to prepare revised documentation for whichever option it chooses.
31. The competent authority of the feeder will have 15 working days to consider the application and reach a decision, in line with the time allowed it in the case of a UCITS being authorised as a feeder for the first time. It will inform the feeder immediately; the feeder must then begin the process of informing its unitholders. Since Chapter VIII of the Directive does not specify how soon it must provide this information after receiving approval, CESR proposes a maximum

period of 5 working days in which to make the necessary notification in accordance with the national laws and regulations of the feeder's home State (and any State in which it is notified under Article 93).

32. Article 64, concerning provision of information and a 30-day free redemption period, already applies to a feeder transferring its investments to a different master UCITS. CESR proposes in paragraph 6 that equivalent provisions should apply in the case of a feeder that converts to a non-feeder UCITS. Where national law requires it, the information to be provided would include details of the meeting of unitholders to be convened to consider the proposal.
33. Paragraph 7 recognises the possibility that, where the feeder requires two months to submit its proposal and the third month is accounted for by the competent authority's review and the subsequent provision of information to unitholders, liquidation may have already commenced by the time the 30-day redemption period begins. If so, during that time the feeder can no longer comply with its old investment objectives, but neither can it invest in accordance with its new mandate until the 30 days are ended.
34. CESR proposes that a feeder UCITS in this situation should be either wholly invested in cash, or should retain any combination of assets that it has received as a transfer in kind from the former master. It may use the cash, and if necessary sell other assets, in order to meet unitholder redemption requests, and may make investments to manage the cash efficiently, but it should not undertake any new long-term investment during the period. CESR would not consider the rolling over of an existing derivative or forward contract to be a new investment.
35. The feeder may decide it is not desirable to accept money from investors that cannot be invested before the end of the period, in which case it may suspend subscriptions during the period. However, since level 1 confers the right on investors to redeem their units during a specified period, the feeder should not normally be permitted to over-ride that right by suspending redemptions. A suspension of redemptions should be allowed only if the competent authority considers there is an over-riding investor protection issue that makes it necessary temporarily to prevent unitholders from exiting the feeder.
36. Paragraph 10 is intended to provide some flexibility in cases where the master UCITS has given a longer period of notice than the minimum requirement, prior to liquidation. In principle, the feeder should if it wishes be able to make use of the extra time to prepare its proposal under Article 60(4)(a) or (b). However, CESR considers that it is important to minimise the delay between the actual liquidation of the master and the re-investment by the feeder following the 30-day redemption period.
37. Consequently, CESR proposes that the maximum two-month period for submitting a proposal to the competent authority could be extended only where it is foreseeably possible for the entire process required under the proposal to be completed by the time the proceeds of the liquidation are paid to the feeder. This would ensure that any extra time provided by the master is used in the first instance to minimise the disruption caused to investors in the feeder. Only if the delay between liquidation and re-investment can be entirely eliminated, will the feeder itself be allowed to take more time preparing its application.
38. It may be helpful to read this section in conjunction with the hypothetical timelines in Annex III.

#### Questions

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

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

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

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

(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?

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?

### Merger or sub-division of the master UCITS

39. Article 60(5) outlines three options which the feeder UCITS can pursue as an alternative to liquidation. Option (a) allows the feeder to continue investing in the master UCITS or another UCITS resulting from the merger or division; it can be refined into four variants, as set out in Box 6. Options (b) and (c) are the same as those available when the master is liquidated.

### Level 2 advice

#### Box 6

1. The feeder UCITS, as soon as it receives notification that the master UCITS is to be subject to a merger or division, shall inform its competent authority of the fact, indicating the proposed effective date of the merger or division, and whether it expects to suspend the repurchase, redemption or subscription of its units in accordance with Article 60(3) before that date.
2. The feeder UCITS shall submit to its competent authority, no later than one month after the date on which it received notification that the master UCITS is to be merged or sub-divided, one of the following:
  - (a) its proposal to continue to invest in the master UCITS in accordance with Article 60(5)(a), in situations where the proposed change to the master is:
    - (i) a merger in which the master is the receiving UCITS;
    - (ii) a sub-division of the master in which the master is to continue materially unchanged as one of the resulting UCITS;
  - (b) its proposal to invest in another UCITS resulting from the merger or division of the master UCITS in accordance with Article 60(5)(a), in situations where the proposed change to the master is:
    - (i) a merger in which the master is the merging UCITS and the feeder is to begin investing in the receiving UCITS;
    - (ii) a sub-division of the master where the feeder is to begin investing in a resulting UCITS that is materially different to the master (e.g. which has a different investment objective and policy);
  - (c) its proposal to invest in another master UCITS not resulting from the merger or division in accordance with Article 60(5)(b);
  - (d) its proposal to convert to a UCITS that is not a feeder UCITS in accordance with Article 60(5)(c); or
  - (e) confirmation of its intention to be liquidated.

3. In the case of option (2)(a):
  - (a) if any revision to the feeder UCITS' fund rules or instrument of incorporation, prospectus or key investor information is necessary, it shall attach the revised version to the proposal;
  - (b) the competent authority of the feeder UCITS shall, if the proposal complies with the requirements of the Directive, grant approval within 15 working days of receipt of the proposal and any necessary supporting documents, and shall immediately inform the feeder of this fact;
  - (c) the feeder shall inform the master that it will continue to invest;
  - (d) the feeder shall, if required by the laws and regulations of its home State, inform its unitholders of the decision.
4. In the case of options (2)(b) and (c):
  - (a) the documents required under Article 59(3) shall be attached to the proposal;
  - (b) the competent authority of the feeder UCITS shall, if the proposal complies with the requirements of the Directive, grant approval within 15 working days of receipt of the proposal and all necessary supporting documents, and shall immediately inform the feeder of this fact;
  - (c) the feeder shall take appropriate action to notify the master, either by confirming the basis on which it wishes to participate in the merger or division, or by confirming that it intends to repurchase or redeem its investment before the effective date, or by taking immediate steps to disinvest;
  - (d) the feeder shall, no later than five working days after receiving approval from its competent authority, provide information to its unitholders in compliance with Article 64.
5. In the case of option (2)(d):
  - (a) the revised fund rules or instrument of incorporation, prospectus and key investor information shall be attached to the proposal;
  - (b) the competent authority of the feeder UCITS shall, if the proposal complies with the requirements of the UCITS Directive, grant approval within 15 working days of receipt of the proposal and all necessary supporting documents, and shall immediately inform the feeder of this fact;
  - (c) the feeder shall take appropriate action to notify the master, either by confirming that it intends to repurchase or redeem its investment before the effective date, or by taking immediate steps to disinvest;
  - (d) the feeder shall, no later than five working days after receiving approval from its competent authority, provide information to its unitholders in compliance with paragraph 6 of Box 5.
6. Where the feeder has selected option (2)(b), (c) or (d), it shall exercise its right under Article 60(5) third sub-paragraph to repurchase or redeem all its units in the master in the following circumstances:
  - (a) the competent authority of the feeder has not yet given its approval to the feeder's proposal by the last day on which units in the master can be repurchased or redeemed before the merger or division is effected; or
  - (b) the feeder has received the necessary approval, but the merger or division of the master is to be effected before the "reinvestment date", being the date on which the feeder:
    - (i) if it has selected options (2)(b) or (c), is to begin investing in a different master UCITS; or
    - (ii) if it has selected option (2)(d), is to begin investing in accordance with its new objective and policy.

7. Following the repurchase or redemption of units in the master UCITS, the feeder UCITS shall either:
  - (a) receive the redemption proceeds in cash; or
  - (b) receive some or all of the redemption proceeds as a transfer in kind where the agreement between the feeder and master provides for it and if both parties so agree; in this event the feeder may realise any part of the transferred assets for cash at any time;

provided in either case that any cash held or received shall not be invested in further assets until the reinvestment date.
8. In the event that the feeder UCITS is holding assets received through a transfer in kind, and is to begin investing in a different master UCITS at the reinvestment date, it shall either:
  - (a) realise all the assets for cash before the reinvestment date; or
  - (b) transfer some or all of the assets to the new master UCITS as a transfer in kind on the reinvestment date, but only where the agreement between the feeder and the new master UCITS provides for it and if both parties so agree.
9. The feeder UCITS may, between the date it repurchases or redeems its units in the master UCITS and the reinvestment date, suspend subscriptions into its own units. It may not suspend the repurchase or redemption of its own units during the period provided for by Article 64(1)(d) and Box 5 paragraph (6)(a)(iv), unless it is directed to do so by its competent authority. A competent authority shall give such a direction only if it considers the suspension necessary to protect the interests of unitholders. If the feeder is unable to pay its unitholders the proceeds of their redemptions because it has not yet received the proceeds of its own redemption from the master, it shall immediately inform its competent authority of the situation.
10. By way of derogation from (2), the feeder UCITS may defer the submission of its confirmation under (2)(a) or its proposal under (2)(b), (c) or (d) if the following conditions are satisfied:
  - (a) the effective date of the merger or division of the master UCITS is to be more than two months after it has given notice in accordance with Article 60(5); and
  - (b) either:
    - (i) for a proposal under (2)(b), the feeder can determine on reasonable grounds that the last date on which its unitholders can exercise their rights under Article 64(1)(d) will fall no later than the day before the effective date of the merger or division; or
    - (ii) for a proposal under (2)(c) or (d), the feeder can determine on reasonable grounds that the reinvestment date under (6) above will fall no later than the latest day on which it should expect to receive settlement of the repurchase or redemption of units in the master.

The feeder UCITS shall in this case, no later than the one-month deadline in (2), inform its competent authority in writing of the date by which it expects to submit its proposal, setting out (where applicable) its reasons for believing that it is able to comply with (b) above.

#### Explanatory text

40. The procedure in Box 6 for dealing with a merger or division is aligned as closely as possible with that for liquidations in Box 5. It starts from the assumption that the master UCITS gives no more than the minimum 60 days' notice required under Article 60(5).
41. Where the feeder proposes to continue investing in the master and there is no material change in the master's investment objectives and policy (i.e. in the situations described above in paragraph (2)(a)), the process should be simple. The review of the proposal by the feeder's competent authority should be straightforward, and there is no obligation under the Directive to inform



unitholders or enable them to redeem their units free of charge. CESR considers that immaterial changes to the fund documents of the feeder may be made under this option if, in the judgement of the relevant competent authority, they will not affect unitholders' participation in the fund.

42. Where the feeder proposes to continue investing in a different master UCITS resulting from the merger or division (i.e. in the situations described above in paragraph (2)(b)), the process is slightly more complex. The competent authority may need to carry out a much fuller review of the proposal, and the change falls within the scope of Article 64 requiring information to be provided to unitholders in the feeder. The feeder must, in that situation, comply with the obligation under Article 64(3) to ensure that it does not invest in a master with different objectives until its own investors have had the opportunity to exit the feeder in accordance with Article 64(1)(d). To do so, it may be obliged to redeem its investment in the master before the merger or division is effected, and then reinvest at a later date.
43. Where the feeder proposes to invest in accordance with options (b) or (c) of Article 60(5), the process described in Box 6 paragraphs 6 to 9 largely follows that for liquidations set out in Box 5. The only significant difference is that the feeder must exercise its right to exit the master before the merger or division becomes effective, whether or not it has completed the process of informing its unitholders and allowing them the right of redemption without charge. If that right remains in force, the feeder must refrain from reinvesting its assets during that period, as explained in paragraphs 2.3.13 to 2.3.15 above.
44. In these cases, if the master has given the minimum 60 days' notice to the feeder and puts the merger or division into effect at the earliest possible date, it will be quite difficult for the feeder to meet the timetable. It will need to discuss the matter with its own competent authority at the earliest possible opportunity to agree a timetable for the process that will ensure all Directive obligations are complied with.
45. If, however, the master allows a longer period of notice, Box 6 paragraph 10 allows the feeder to take more time to prepare its proposal but, as with Box 5 paragraph 10, the interests of investors must be given priority. For a feeder that wishes to invest in a different UCITS under the terms of the merger or division, it must prepare a timetable that ensures its unitholders' right of redemption under Article 64(1)(d) will have expired before the effective date of the merger or division. For a feeder that intends to invest in a completely different UCITS or to become a non-feeder UCITS, it must devise a timetable that eliminates any delay between the end of its own unitholders' right to redeem free of charge, and the settlement (in cash or by transfer in kind) of the disinvestment from the old master.
46. As with the description of liquidation procedures, it may be helpful to read this section in conjunction with the hypothetical timelines in Annex III.

#### Questions

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

- (a) is one month long enough in which to prepare a proposal for an option other than liquidation of the feeder?*
- (b) how quickly can the feeder make information for unitholders available once the competent authority's approval is received?*
- (c) would you expect the feeder to suspend subscriptions during any period in which it is unable to make new investments?*
- (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?*

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?

## 2.4 Agreements between depositaries

47. Article 61 requires that, if the feeder and the master have different depositaries, both depositaries must enter into an information-sharing agreement in order to ensure they can fulfil their respective duties. CESR is invited to advise on the elements of the agreement, taking account of whether or not the two depositaries are established in the same Member State and which legal regime should apply to cross-border agreements. It should consider providing a draft model agreement.
48. It will always be the case that a feeder and a master established in different Member States will have different depositaries (although potentially those depositaries could be Members of the same corporate group). The feeder depositary, in order to carry out its functions effectively, has to have access to information which only the master can provide, and such an agreement would enable the feeder depositary to get that some of that information directly from the master depositary. Article 61(1) makes clear that both depositaries, when acting in accordance with the Directive's requirements, may disclose information to each other without incurring any legal liability for breach of confidentiality.
49. Respondents to the call for evidence generally supported the concept of level 2 measures on this issue, though a few thought that the scope and contents should be left to be negotiated by the parties concerned. Many respondents noted that since the duties of a depositary are not harmonised, it would be difficult for level 2 measures for such an agreement to be prescriptive and comprehensive. Several expressed concerns that any information released to the feeder depositary should be available to other unitholders as well, to ensure fair treatment of all investors. There were also concerns that the limits of the feeder depositary's liability should be made clear, i.e. that it is not responsible for failures by the master UCITS, its management company or its depositary.
50. As noted under section 2.1, the issue of the applicable law for cross-border agreements is a priority. Some respondents suggested that there should be complete flexibility in this regard; others that the agreement should conform to the law applicable to the agreement between the two UCITS.

### Level 2 advice

#### Box 7

The agreement between the depositaries of the master UCITS and the feeder UCITS referred to in Article 61(1) shall include, but not be limited to, the following:

1. The identification of the documents and categories of information which are to be routinely shared, and whether such information / documents are to be notified by one depositary to the other or made available on request.
2. The manner and timing (including any applicable deadlines) of the transmission of information by the master depositary to the feeder depositary.



3. Co-ordination of the involvement of both depositaries, to the extent appropriate in view of their respective mandatory duties under national law (but excluding where acting as a delegate on a contractual basis), in relation to:
  - a. the procedure for calculating the NAV of each UCITS, including any measures appropriate to protect against the activities of market timers as envisaged by Article 60(2);
  - b. the processing of instructions by the feeder to buy / sell units in the master, and the settlement of such transactions, including any arrangement to transfer assets in kind.
4. The co-ordination of accounting period-end procedures, including in particular the preparation of each depositary's report to unitholders.
5. The basis on which the feeder depositary may have access to records of breaches kept by the master depositary.
6. The procedure for handling ad hoc requests for assistance from one depositary to the other.
7. Identification of particular contingent events which ought to be notified by one depositary to the other on an ad hoc basis (e.g. the master depositary to notify a proposed change to the investment objectives or policy of the master), and the manner in which this will be done.
8. A statement of the applicable law and jurisdiction in the following terms:
  - (a) if the feeder UCITS and the master UCITS have concluded an agreement in accordance with Article 60(1), the law of the Member State (or any part of it) identified as the applicable law in that agreement shall also be applicable to the present agreement, and both parties agree to the exclusive jurisdiction of the courts of that Member State (or the relevant part of it);

#### OPTION A

- (b) [If no such agreement is in place between the two UCITS, as envisaged by the third paragraph of Article 60(1), a statement that the applicable law shall be the law of the Member State (or any part of it) in which the feeder UCITS is established, and both parties agree to the exclusive jurisdiction of the courts of that Member State (or the relevant part of it).]

#### OPTION B

- (b) [If no such agreement is in place between the two UCITS, as envisaged by the third paragraph of Article 60(1), a statement either that the applicable law shall be that of the Member State (or any part of it) in which the feeder UCITS is established, or that it shall be that of the Member State (or any part of it) in which the master UCITS is established, as the parties may choose. Both parties agree to the exclusive jurisdiction of the courts of the Member State (or the relevant part of it) whose law is applicable to the agreement.]

#### Explanatory text

51. CESR has followed the same principle in relation to this agreement as it has with the agreement between the feeder and master UCITS, namely that the advice should indicate the areas to be covered by the agreement without being prescriptive as to the precise content or format. The advice seeks to recognise that there are considerable differences between the detailed mandatory duties of a depositary in each Member State, and the extent to which a depositary may be permitted (if at all) to carry out activities delegated to it by another person. Co-operation can take place only to the extent that there is harmonisation at national level. A depositary cannot be required, under the terms of this Article of the Directive, to carry out any function that is forbidden or not provided for under the national law of its home State.

52. Box 7 proposes that where there is an agreement between the feeder and master UCITS, the agreement between their depositaries should conform to its provisions concerning the applicable law and jurisdiction of the courts. Where there is no such agreement (i.e. feeder and master have the same management company but different depositaries), CESR foresees two options for prescribing the applicable law of the depositaries' agreement; either that it must always be the law of the feeder depositary home State, or that the parties may choose the law of the home State of either depositary. In practice, however, it is likely that a master and feeder with the same management company will also share the same depositary.
53. An alternative approach to the question of the applicable law has been proposed, namely that in all cases it should be that of the master depositary's home State. The grounds for this proposal are that the agreement will predominantly cover information that the master depositary should provide to the feeder depositary. Since the majority of the activities in relation to the agreement will be undertaken by the master depositary, it can be argued that – in the event of a dispute between them – it is in the interests of the master depositary to be able to obtain a resolution in its home State.
54. It should be noted that comments relating to depositaries are based on the current text of the amended Directive and do not take account of any possible future revision of the role of the depositary in relation to UCITS.

#### Questions

21. *Do you agree with CESR's proposals for defining the content of the depositaries' agreement?*
22. *Does Box 7 cover the right issues? Should other issues be addressed?*
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?*
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?*

### **2.5 Reporting by the master UCITS depositary**

55. Article 61(2) requires the depositary of the master UCITS, if it detects any "irregularities" in the master UCITS that are "deemed to have a negative impact on the feeder UCITS", immediately to inform its own regulator, together with the feeder UCITS or its management company and depositary.
56. CESR is requested to advise on a list of the "types of irregularities" that should fall within the scope of this requirement, and whether any issues that lie outside of the depositary's legal duties of oversight should be reported.
57. Representatives of depositaries who responded to the call for advice stated that, in accordance with existing practice, any irregularities should firstly be reported to the master UCITS and its management company. They should be reported under Article 61 only if the management company has failed to address them properly within a reasonable time. Some of the representatives suggested the requirement should relate only to problems in the NAV calculation of the master that could significantly affect the feeder's NAV. It was pointed out that all other investors in the master should be informed of any issue reported under this requirement.
58. Asset managers and their representative associations voiced similar views, emphasising the need for the master UCITS to be given the opportunity to address any perceived issues before they are reported more widely. Requests were made for an exhaustive list of irregularities,

bearing in mind that depositaries in different Member States differ in the extent of their responsibilities for oversight of funds.

#### Level 2 advice

##### Box 8

1. Irregularities which are deemed to have a negative impact on a feeder UCITS, as envisaged by Article 61(2), are matters which the master depositary is required by its national law or regulations to report to the master UCITS or its management company, and to the master UCITS home State competent authority.
2. The matters referred to in (1) may include but are not limited to:
  - (a) Errors in the NAV calculation of the master;
  - (b) Errors in transactions for the sale or repurchase on units in the master undertaken by the feeder;
  - (c) Errors in the payment or capitalisation of income arising from the master, or in the calculation of any related withholding tax;
  - (d) Breaches of the master's investment objectives, policy or strategy as described in its fund documents;
  - (e) Breaches of investment and borrowing limits set out in national law or in the fund documents.
3.
  - (a) The master depositary, within a reasonable time of having informed the feeder UCITS (or its management company) and its depositary of an irregularity, shall inform the feeder depositary of how the master UCITS has resolved or proposes to resolve the irregularity.
  - (b) The feeder depositary, if it is not satisfied that the resolution approved by the master depositary is in the interests of the feeder UCITS' unitholders, shall seek to agree an acceptable resolution with the master depositary. If it is unable to do so, it shall inform the feeder UCITS or its management company of that fact.
4. Member States may make provision in national law requiring the master UCITS or its management company to notify or otherwise inform those of its unitholders that are not feeder UCITS of any of the matters listed above.

#### Explanatory text

59. CESR's advice recognises, as explained in section 2.4 above, that the differing duties of depositaries in each Member State make it impractical to specify exhaustively what irregularities should be reported. A depositary can be expected to report only on what it is required to oversee in accordance with its national law and regulations. That does not of course prevent depositaries from choosing to extend the scope of their oversight under the terms of the depositaries' agreement.
60. The management company of the feeder UCITS, when first setting up a link to a master in another State, should ascertain in conjunction with its depositary whether the master depositary would be required to report the same types of irregularity that the feeder depositary would be required to report. The feeder management company and depositary can then judge for themselves whether the arrangement is in the best interests of the feeder's investors and whether they need to try to secure additional disclosure under the terms of the respective agreements.
61. In relation to paragraph 3 of Box 8, the procedure would operate on the basis of any problems being resolved through discussion between depositaries in the first instance. Possible

alternatives would be either for the master depositary to communicate simultaneously with the feeder UCITS (or its management company) and its depositary, or for the agreements between them to specify how the resolution of irregularities should be addressed. Notification to the competent authority of the feeder UCITS would be made as and when required by the national law and regulation of the feeder UCITS' home State.

62. Although no reference is made in the level 1 text to informing the master UCITS or its management company, CESR is satisfied that national law provisions requiring the master depositary to inform the master UCITS first would not necessarily conflict with the Directive requirement. Similarly, the requirement to provide information to the feeder UCITS may be supplemented by national law requirements to provide the same information to other unitholders.

#### Questions

25. *Do you agree with CESR's proposals in relation to the irregularities to be reported by the depositary?*
26. *Do you agree that the interests of other unitholders in a master UCITS will be adequately protected under national laws if these proposals are implemented?*
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?*

### **2.6 Agreements between auditors**

63. Article 62 requires that, if the feeder UCITS and master UCITS have different auditors, they must enter into an information-sharing agreement in order to ensure that both can fulfil their duties. This mirrors the requirement in Article 61 concerning depositaries. Auditors also enjoy the same exemption from confidentiality rules as depositaries when sharing information under the agreement.
64. CESR is invited to advise on the elements of the agreement, and in particular what arrangements would be needed to allow the feeder auditor to take account of the audit report of the master auditor.
65. Respondents to the call for evidence raised similar issues to those mentioned under section 2.4. Indeed, similar considerations apply both in terms of the applicable law for cross-border agreements, and the scope of items to be covered in the agreement.

#### Level 2 advice

##### **Box 9**

The agreement between the auditors of the master UCITS and the feeder UCITS referred to in Article 62(1) shall include, but not be limited to, the following:

1. The identification of the documents and categories of information which are to be routinely shared, and whether such information / documents are to be notified by one auditor to the other or made available on request.
2. The manner and timing (including any applicable deadlines) of the transmission of information by the master auditor to the feeder auditor.
3. The co-ordination of the involvement of each auditor in the accounting period-end procedures for the UCITS, including in particular the preparation of the auditor's report to unitholders. Where

the feeder and the master UCITS have different accounting year-end dates, these provisions shall include the procedure and timing by which the master auditor is to make the ad hoc report required by the first paragraph of Article 62(2).

4. Identification of matters that should be treated as irregularities in the audit report of the master auditor, for the purposes of the second paragraph of Article 62(2).
5. The procedure and timing for handling ad hoc requests for assistance from one auditor to the other.
6. A statement of the applicable law and jurisdiction in the following terms:
  - (a) if the feeder UCITS and the master UCITS have concluded an agreement in accordance with Article 60(1), the law of the Member State (or any part of it) identified as the applicable law in that agreement shall also be applicable to the present agreement, and both parties agree to the exclusive jurisdiction of the courts of that Member State (or the relevant part of it);

#### OPTION A

- (b) [If no such agreement is in place between the two UCITS, as envisaged by the third paragraph of Article 60(1), a statement that the applicable law shall be the law of the Member State (or any part of it) in which the feeder UCITS is established, and both parties agree to the exclusive jurisdiction of the courts of that Member State (or the relevant part of it).]

#### OPTION B

- (b) [If no such agreement is in place between the two UCITS, as envisaged by the third paragraph of Article 60(1), a statement either that the applicable law shall be that of the Member State (or any part of it) in which the feeder UCITS is established, or that it shall be that of the Member State (or any part of it) in which the master UCITS is established, as the parties may choose. Both parties agree to the exclusive jurisdiction of the courts of the Member State (or the relevant part of it) whose law is applicable to the agreement.]

#### Explanatory text

66. CESR's advice for this section of the mandate is in line with its proposals in sections 2.1 and 2.4, in terms of both the degree of prescription of content and format of the agreement, and the approach to the question of applicable law for cross-border agreements.
67. The experience of Member States where master-feeder structures for non-harmonised funds are already common, suggests that the funds use the same auditor or (in the case of cross-border arrangements) auditors in the same group. Where that is not the case, the feeder auditor either has to obtain the information it needs from the master auditor or carry out its own ad hoc audit of the master, without however having access to the master's books and records at that point in time. Consequently, it is nearly always the case that the accounting year-end date of the feeder is aligned with that of the master.

#### Questions

28. *Do you agree with CESR's proposals in relation to auditor agreements?*
29. *Which option do you prefer in relation to the national law and jurisdiction applicable to cross-border agreements?*
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?*
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?*

## 2.7 Change of feeder UCITS objective

68. Under the amended Directive, any existing UCITS will be able to convert itself into a feeder UCITS subject to the approval of its competent authority. Likewise, an existing feeder will be able to cease to feed into one master and begin to feed into a different one, again subject to regulatory approval. Article 64(1) requires a UCITS to give certain specified pieces of information to its unitholders notifying its intention to take either of these courses of action.
69. CESR is invited to specify the format of the information<sup>2</sup> and the way in which it should be provided. The mandate notes that the Directive does not harmonise the way other documents should be provided, and that no express reference is made to the use of a durable medium.
70. Views of respondents to the call for evidence were mixed; some made specific proposals in relation to the matters mentioned in the mandate, whereas others considered that there is no need for level 2 measures and that level 3 guidelines would be sufficient. It was pointed out that the situation envisaged here is not substantively different to that of any UCITS that proposes a change to its investment objectives and policy, and that national laws and regulations may already prescribe requirements in that regard (e.g. there may be a requirement to seek prior approval from unitholders or the competent authority).
71. Since the national laws of each Member State provide for the manner in which a UCITS should notify investors of its intention to modify its investment objective or policy, CESR does not consider that any additional investor protection measures are necessary in the case of a feeder UCITS.

### Question

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

## 2.8 Transfer of assets in kind

72. In the circumstances described in section 2.7, it is possible that the UCITS could transfer all or part of its assets in kind (in specie) to the new master UCITS in exchange for units. Although no level 1 provision applies any specific harmonisation requirement to this procedure, the comitology provision in Article 64(4) foresees that implementing measures may be established.
73. CESR is therefore invited to advise on the procedure for valuing and auditing a transfer of assets in kind and on what role the depositary should play in this process.
74. Respondents to the call for evidence offered mixed views. Some saw no need for any level 2 measures, and queried why they should be applied to transfers in kind in this situation alone when such transfers may also take place in other circumstances. Some acknowledged similarities with the merger procedure, but were concerned that alignment with mergers would impose additional costs with no corresponding benefit. A few respondents were however in favour and made specific proposals on implementing measures.
75. CESR notes that national regimes impose differing requirements (for example, some Member States assign a specific role to the auditor, and the degree of involvement by the depositary may vary significantly). That being so, CESR's view is that it would be difficult to prescribe a harmonised procedure applicable only to feeders when national procedures would continue to

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<sup>2</sup> The mandate refers to provision of an "information letter" although such a term is not used in the Directive.



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apply in all other cases. For that reason, CESR recommends that no level 2 measure should be introduced.

Question

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



## SECTION III - NOTIFICATIONS

1. The third section of Part III of the mandate relates to implementing provisions in Chapter XI concerning cross-border marketing of UCITS. The draft mandate envisages four areas in which it may be appropriate to introduce implementing measures, which are discussed in turn in this section of the consultation paper.
2. The mandate notes the value of the work already done by CESR to establish voluntary guidelines in 2006 in relation to notification procedures under the existing Directive (CESR 06/102b, referred to in this section of the paper as the “CESR Guidelines”). It suggests that the CESR Guidelines can serve as an inspiration for advice on suitable level 2 measures. The Commission asks CESR to “find balanced solutions that will ensure that supervisors can discharge their duties but also that will not compromise the objectives of the reform of the notification procedure”.
3. Responses to this part of the call for evidence came mainly from asset management firms, most of which emphasised the importance of ensuring an effective notification regime without artificial barriers or delays.

### 3.1 Scope of the information to be published by each Member State

4. Article 91(3) introduces a new obligation on Member States to ensure that complete information on laws, regulations and other provisions that relate specifically to the marketing of UCITS established in another Member State within their territories, is easily accessible at a distance and by electronic means. The information must be available in a language customary in the sphere of international finance, be provided in a clear and unambiguous manner, and be kept up to date. CESR is invited to advise on the scope of the relevant information.
5. This legislative provision reflects the aim of CESR Guideline 13, which requests Member States to prepare and maintain a list of relevant provisions and publish it on their websites. A standard template for Member States to complete and publish is provided in the Guidelines.
6. Several respondents to the call for evidence suggested points to consider in terms of accessibility of the information, such as each competent authority website having a specific area set aside for this purpose, and providing staff contact details to ensure any problems can be promptly addressed.

#### Level 2 advice

##### Box 10

1. Information to be provided in accordance with Article 91(3) must be specifically relevant to arrangements made for marketing units of UCITS in the Member State.
2. Information may be given in the form of a narrative description, or a series of references or links to source documents, or a combination of both.
3. The following non-exhaustive list, which is without prejudice to any other laws or regulations applicable in the relevant Member State, sets out categories of information to be provided if they fall within (1):
  - (a) definitions of the scope of marketing or the equivalent legal term;



- (b) requirements for the contents, format and manner of presentation of promotional material (if not otherwise harmonised by European legislation), including all compulsory warnings and restrictions on the use of certain words or phrases;
- (c) details of any additional information, not harmonised by European legislation, required to be disclosed to existing or potential unitholders or their agents;
- (d) details of any exemptions from marketing rules and requirements, or any variation in their applicability, in relation to certain UCITS or classes of UCITS, or certain categories of investors;
- (e) requirements for any reporting or transmission of information to the competent authorities of that Member State, and the procedure for lodging updated versions of required documents;
- (f) requirements for any fees or other sums to be paid to the competent authorities or any other statutory body in that Member State, either on the inception of marketing or periodically thereafter;
- (g) requirements in relation to the facilities to be made available to unitholders (or certain categories of unitholder) as required by Article 92;
- (h) requirements for the termination of marketing in that Member State.

#### Explanatory text

7. CESR's advice sets out several categories of information which, if covered under national law and regulation, will be directly relevant to the marketing of UCITS. Information that relates specifically to the marketing of UCITS would probably not include (for instance) references to precedents in case law that have no direct bearing on a UCITS.
8. Box 10 Paragraph 3(c) does not mean that a host State could require a UCITS to include additional information in its fund rules, instrument of incorporation or prospectus, since that would be contrary to Article 91(2).
9. A number of respondents to the call for evidence suggested that firms should be able to rely on the published information and should not be held liable if they fail to comply with a requirement that was not published by the authority (that is, as the result of an error on the part of the authority). This is a question of legal interpretation, but if it is considered that the text of the Directive does not confer such an indemnity from liability, then level 2 measures cannot provide one instead. CESR's understanding, based on Recital 65<sup>3</sup> of the Directive, is that such a list of information cannot be relied on as exhaustive and must be without prejudice to other provisions in the national law of the host State.

#### Questions

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

### **3.2 Facilitating host State access to notification documentation**

10. Article 93(7) introduces a new obligation on the UCITS home State competent authority to ensure the host State competent authority has access by electronic means to the supporting

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<sup>3</sup> "For the purpose of enhancing legal certainty there is a need to ensure that a UCITS which markets its units on a cross-border basis has an easy access....to complete information on the laws, regulations and administrative provisions applicable in the UCITS host Member State and that specifically relate to the arrangements made for marketing of UCITS. Liabilities with regard to such publication shall be subject to national laws."

documentation sent with the notification letter (as set out in Article 93(2)). The UCITS itself is then required to keep the documentation up-to-date and notify any amendments to the host State.

11. CESR is invited to advise on:
  - the definition of common standards and the content of procedures for facilitating the host State access, and in particular to assess the need for databases at national or EU level;
  - common standards and procedures for the notification by UCITS to host States of amendments to the relevant documents.
12. The reference in the Directive to “access by electronic means” could include a range of options, from email messages to an EU-wide database system. Email messaging is a basic communication tool, suitable for facilitating the filing of the notification documents and the exchange of information between competent authorities. The creation of an EU-wide database would represent a potentially more efficient solution by providing a central repository for the fund documents of notified UCITS. CESR Guideline 1 included a commitment for Members to “facilitate electronic filing of documents”.
13. Regarding the development of a centralised EU system, CESR notes that a similar type of electronic project, the Officially Appointed Mechanism (OAM) system, has already been introduced under the Transparency Directive although it is not yet operational Europe-wide. The OAM will essentially be used as a filing system for regulated information such as annual reports, prospectuses etc. Documents are filed by Information Providers and are available for anyone to view, including the general public. CESR plans to begin looking in late 2010 at a Europe-wide solution, i.e. a network of national OAMs able to communicate with one another.
14. In order to evaluate the merits and drawbacks of creating a centralised electronic notification procedure, CESR is undertaking an initial exercise to describe the possible scope and functionality of two elements: a database for storage of fund documents, and a process for electronic transmission of notification files (as discussed in section 3.4). Such a project would be without prejudice to the full functioning of the notification procedure foreseen in the Directive, as from the date of its entry into force.
15. One possible outcome of the review would be to use or adapt an existing system developed for other purposes relating to the European single market. The work already done for the OAM, for example, could be the basis for a medium-term solution to the storage of updated UCITS documents in an EU context, although it would not be a solution for the notification process. Whatever the recommended option, an essential pre-requisite in assessing the feasibility of the operation of the system (as noted by several respondents to the call for evidence) would be a thorough analysis of the potential benefits and costs (including development lead time). This would include consideration of whether the costs could be met directly from the budgets of competent authorities, or whether some costs might fall indirectly on UCITS and so on investors themselves. If so, it would be important to assess what benefits industry participants and investors, as well as regulators, would gain from such a system.
16. Another approach to achieving electronic access could be to require each competent authority to make all such documentation available on its own website. Although there is a relevant precedent under the Prospectus Directive, here a greater quantity of documents would be required to be published. Consequently, this option could prove burdensome in some Member States with large numbers of UCITS. Recital 60<sup>4</sup> of the Directive makes it clear that, in respect of key investor information, use of the competent authority’s website is not mandatory.

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<sup>4</sup> “The competent authorities of each Member State may make available to the public, in a dedicated section of their website, key investor information concerning all UCITS constituted and authorised in that Member State.”

17. Alternatively, level 2 measures could give Member States discretion to publish the information themselves or impose a requirement on each outwardly passporting UCITS to publish the information itself. The UCITS could do this on its own (or its management company's) website, or some other common location (such as a trade association website) designated for that purpose.
18. This suggestion might also address the second Commission question, about updates to the documents. Several replies to the call for evidence noted that Article 93(7) requires the UCITS itself, and not its home State authority, to notify any amendments in the documents to the host State authority. Some suggested that level 2 measures should nevertheless provide for this to be done via the home State authority, in the same way as for an initial notification, in order to provide a more streamlined process.
19. CESR does not intend to propose such measures at level 2, since to do so would directly contradict the level 1 provision and introduce a lack of clarity about the responsibilities of the respective parties.

#### Questions

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

### **3.3 Standard notification letter and attestation**

20. Article 93(1) requires a UCITS that wishes to passport into another Member State to submit a notification letter to the competent authority of its home State. In accordance with Article 93(3) the home State competent authority will support this notification with an attestation that the UCITS concerned fulfils the conditions of the Directive.
21. CESR is invited to advise on:
  - the exhaustive content of the notification letter, which clearly allows the host State to identify enclosed obligatory documents (which may be in a language not understood by that competent authority), and a format which will be easily adaptable for electronic communication;
  - the exhaustive design and content of the attestation, which should be easily adaptable for electronic communication.
22. Annexes I and II to the CESR Guidelines contain standard models for both the notification letter and attestation. CESR has reviewed these model documents and used them as the basis for its advice; proposed drafts of the notification and attestation letters are attached as Annexes I and II to this paper.
23. Part A of the notification letter has undergone only minor modifications compared to the version in the CESR Guidelines, but Part B covering non-harmonised requirements has been expanded. It now requires specific information to be given about the distribution channels to be employed (some authorities may in addition require names of individual firms), persons providing facilities under Article 92, how the requirement to publish prices will be complied with, and whether use is to be made of any applicable exemptions that may exist in the national marketing regime.

24. Since the marketing of UCITS is not a harmonised activity, CESR does not consider it practical to develop a list that reflects all the varying legal requirements of each Member State. The intention is that the pro-forma in Part B will be universally applicable, so there will be a harmonised template for all notification letters; but competent authorities will set out as part of the information disclosed under Article 91(3) the amount of detail they require under each heading.
25. The draft attestation letter also closely follows the version in the CESR Guidelines, with a few minor modifications.

#### Questions

39. *Do you consider the notification letter (Annex I) satisfactory? Are there any other matters that it ought to cover?*
40. *Do you have any comments on the draft attestation letter (Annex II)?*
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?*

### **3.4 Electronic transmission of notification files**

26. Article 93(5) is a new provision requiring Member States to ensure that their competent authorities will accept electronic transmission and filing of notification documents. The draft mandate notes that smooth electronic communication is crucial to achieve the expected benefits of the reformed notification procedure.
27. CESR is invited to advise on:
- the procedures for facilitating electronic communication for notification files, particularly regarding confirmation of transmission by the home State competent authority;
  - procedures for exchanging information between competent authorities for the purpose of the notification procedure;
  - technical arrangements regarding electronic communication and other information exchange regarding notification;
  - procedures to deal with the situation where there are technical problems or the host State competent authority establishes that the notification file is incomplete.
28. Some respondents to the call for evidence noted that existing procedures under (e.g.) the Prospectus Directive may provide a useful point of reference in considering implementing measures. CESR has an existing system, the Transaction Reporting Exchange Mechanism (TREM) which was introduced as part of the implementation of MiFID. It is a method for authorised firms to notify their competent authority of transactions in listed securities, which allows secure and confidential transmission of data between competent authorities. However, the system as it currently stands cannot be used to transmit documents as attachments.
29. As noted in section 3.2 above, CESR is undertaking an initial exercise to assess the possibility of developing a centralised system to deal with the notification procedure, and the resulting benefits and costs. This might include the adaptation of TREM to accept attached document files. CESR will keep stakeholders informed of the development and outcome of this work.
30. Although the outcome of that exercise should not be pre-judged, it may prove to be the case that a specialised system cannot be developed, or at least not in time for implementation of the



Directive in July 2011. If so, a basic electronic notification process using existing technology will be needed. Exchange of e-mails would be the minimum standard that would meet the level 1 requirement, so CESR's advice focuses on the development of such a process.

#### Level 2 advice

##### Box 11

1. Each transmission of a notification in accordance with Article 93(3) shall be carried out by e-mail.
2. Each competent authority shall designate an e-mail address for the purpose of receiving notifications. It shall inform all other authorities of its designated e-mail address, and shall ensure that any change to the address is immediately brought to their attention.
3. The home State authority shall send a notification only to the designated e-mail address of the relevant host State authority.
4. The notification e-mail shall list the documents which are being provided in support, indicating in each case either that the document is attached to the e-mail, or has previously been provided to the host State authority, indicating the date on which it was so provided. Any attachment shall be provided in a format in common use.
5. As soon as the home State authority has sent the e-mail, it shall inform the UCITS of its right to access the market of the host State with immediate effect.
6. A notification shall not be considered complete in cases where:
  - (a) a document listed as attached in the e-mail is missing, or the wrong document is attached, or the document is incapable of being viewed or printed;
  - (b) the home State authority uses an incorrect e-mail address;
  - (c) transmission fails as a result of a technical failure in the home State authority's own systems.
7. If the home State authority is informed or becomes aware that a notification it has transmitted is incomplete under (6), it shall immediately take steps to rectify the problem. If it is unable to do so within 24 hours of becoming aware of the problem, it shall immediately inform the UCITS that a complete notification has not taken place and instruct the UCITS to cease accessing the market in that State.
8. The UCITS shall comply with any instruction given under (7) until it receives confirmation from its home State authority that a successful notification has taken place. Notwithstanding this, it shall continue to provide facilities to, and accept redemption instructions from, any existing unitholder in the host State that acquired units before the instruction was given.
9. Notwithstanding (1), competent authorities may agree between themselves on a bilateral or multi-lateral basis to replace e-mail by an equivalent method of electronic transmission, or to implement additional procedures to enhance the security of e-mails transmitted between them. Any alternative method or enhanced procedure shall not delay the notification or inhibit the ability of the UCITS to access the market of the host State.

#### Explanatory text

31. For the new notification procedure to work, the home State authority needs to have assurance that it has successfully discharged its duties and that the UCITS can rely on the transmission it has sent in order to begin accessing the market in the host State. CESR considers that it is essential as a minimum for each authority to designate an e-mail address that all other authorities can rely on as a postbox for transmission of notifications. One possibility of ensuring that reliable information is available would be for CESR to maintain a list on its website showing the designated address of each authority.
32. The e-mail notification should contain the relevant documents as attachments; it will not be sufficient to provide a hyperlink to a website where they are published. Where they are already in the host State authority's possession (if, for example, an existing sub-fund (investment compartment) of an umbrella UCITS is to be marketed alongside other previously notified sub-funds, in which case the fund rules and prospectus of the umbrella will already have been sent), the message should state this, indicating when the document was sent.
33. The attachments should include any information required by the host State under its national provisions for marketing of UCITS, and confirmation of payment of any fee due to the host State authority. It might be necessary to send a particular document under separate cover to the rest of the notification, but the home State authority cannot treat the notification as complete until all documents have been transmitted. CESR considers that a Word document or a PDF would satisfy the requirement for a format in common use.
34. CESR proposes that the home State authority should be able to rely on its own systems as evidence of successful transmission. Problems could arise if the home State authority has mis-addressed the e-mail, or not included all the relevant documents. In some cases, the home State authority will become aware of the problem itself (for example, if it receives a message telling it the e-mail was undelivered). In other cases, the host State authority will inform it (for example, if a document is missing – see Box 12). Some problems may become apparent almost immediately, others not until some time has passed.
35. When the home State authority is informed by the host State authority of such a problem, or becomes aware of it through its own internal systems and procedures, it should take immediate steps to resolve the problem. This might be a simple matter that could be expedited immediately, e.g. resending a document; but if it cannot be resolved within 24 hours, then the UCITS must be informed at once and told to cease accessing the market in the host State until the problem is resolved. If the UCITS has already sold units to investors in the host State, it should however continue to fulfil its obligations to them by providing facilities and accepting redemption instructions from them.
36. The procedure is intended as a minimum standard, representing CESR's best efforts in the absence of a systematic means of verifying all notification transmissions. Individual Member States may choose to implement arrangements between themselves to enhance the procedure, especially in relation to systems security. Some authorities already use encryption mechanisms (e.g. use of public and private keys) to ensure notification messages are secure, and it is not the intention to oblige any authority to cease using such measures. CESR does not, however, consider that it is essential to have such safeguards in place since the information being transmitted (for example, a publicly available prospectus) is not of a nature to require the highest level of security in every case.



## Level 2 advice

### Box 12

1. Each competent authority shall implement a procedure to ensure that its designated e-mail address for receiving notifications is checked on each working day, and that any new transmissions are promptly opened and reviewed.
2. When the host State authority receives a new notification, it shall acknowledge receipt to the home State authority within five working days. An e-mail sent to the home State authority at an address designated by it for that purpose shall be sufficient to fulfil the obligation, although authorities may choose to agree another procedure between themselves.
3. The host State authority shall check the e-mail to ensure that it is a complete notification, i.e. that no listed attachment is missing and that every document is capable of being viewed or printed. If that is not the case, it shall inform the home State authority of the problem within five working days of receiving the notification, either as part of its acknowledgement of receipt or in a separate communication.
4. If the home State authority does not receive an acknowledgement from the host State authority within the specified time, it shall follow up the matter by contacting the host State authority.
5. Non-receipt by the host State authority in cases where the home State authority has complied with the requirements of Box 11, or failure by the host State authority to acknowledge receipt, does not affect the right of the UCITS to access the market of the host State with immediate effect.

### Explanatory text

37. CESR proposes that receipt of each notification should be acknowledged by the host State authority. This has no bearing on the exercise of the UCITS' right to market its units under the third sub-paragraph of Article 93(3), except in cases where the host State authority identifies that the notification is incomplete. Acknowledgement also provides a mechanism to warn the home State authority in the event that an unauthorised or fraudulent notification is provided to a host State authority.
38. The acknowledgement should be sent within five working days of receipt (an automated receipt generated by the host State authority's e-mail system is sufficient). Within that period, the host State authority should take active steps to check that the listed documents are attached and readable, but it is not under any obligation to review the documents in detail or to check that the UCITS complies with local marketing requirements.
39. It is recommended that the address for receipt of notifications should be one that can be accessed by more than one individual, so that undue delays do not arise from an individual being absent from the office or otherwise unable to access e-mail.
40. The procedures proposed in Boxes 11 and 12 do not cover every eventuality, and it is suggested that CESR could develop further guidelines to address situations that may arise, such as:
  - failure in transmission attributable to an external factor (i.e. not the fault of either authority);
  - the procedure to be followed if a host State authority does not send a prompt acknowledgement of receipt.

41. In any event, the successful implementation of the CESR Guidelines has demonstrated the ability of Member States to work together through day-to-day supervision processes to resolve difficulties in the notification process as they arise. CESR is confident that competent authorities would continue to co-operate in this field to achieve the intended outcome of an effective single market for UCITS.

#### Questions

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





## ANNEX I

### MODEL NOTIFICATION LETTER TO MARKET UNITS OF UCITS IN AN EEA MEMBER STATE

COMMUNICATION FOR MARKETING UCITS IN \_\_\_\_\_  
(the host Member State)

#### Part A Harmonised part

Name of the UCITS:

\_\_\_\_\_

Home State of the UCITS: \_\_\_\_\_

Legal form of the UCITS: common fund / unit trust / investment company  
(please circle or mark the correct choice)

Does the UCITS have sub-funds / compartments? Yes / No

Name of the UCITS and/or sub-fund(s) to be marketed in the host State <sup>5</sup>	Duration (if applicable)	Code numbers if applicable (e.g. ISIN)

Name of management company / Self-managed investment company

\_\_\_\_\_

Home State of management company: \_\_\_\_\_

Address, and registered office / domicile if different from address

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Details of company's website:

<sup>5</sup> If the UCITS intends to market only certain share classes, it should list only those classes.



Details of contact person at management company

Name / Position:

Telephone number:

E-mail address:

Fax number:

Duration of the company, if applicable: \_\_\_\_\_

Scope of activities of the management company in the host State

\_\_\_\_\_  
\_\_\_\_\_

Additional information about the UCITS (if necessary)

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

**Attachments**

☐ The latest version of the fund rules or instrument of incorporation (which need not be submitted separately if they form part of the prospectus; this should be indicated by the notifying UCITS or a third person empowered by written mandate to act on its behalf).

Title of document \_\_\_\_\_

☐ The latest version of the prospectus

Title of document \_\_\_\_\_

☐ The latest version of the key investor information, translated if necessary in accordance with Article 94(1)(b).

☐ The latest published annual report and any subsequent half-yearly report

Title of document \_\_\_\_\_

**Note:**

The latest versions of the required documents listed above must be attached to this letter for onward transmission by the UCITS home State authority, even if copies have previously been provided to that authority. If any of the documents have previously been sent to the host State competent authority and remain valid, the notification letter may refer to that fact.

Indicate where the latest electronic copies of the attachments can be obtained in future:

\_\_\_\_\_



## Part B Non-harmonised part

The following information is provided in conformity with the national laws and regulations of the host State in relation to the marketing of units of UCITS in that Member State.

**UCITS should refer to the website of the competent authority of each Member State for details of which items of information should be provided in this section. A list of relevant website addresses is available at [CESR]**

### Arrangements for distribution

Units in the UCITS / sub-fund(s) will be marketed by (specify names if required):

- ☐ the management company
- ☐ licensed banks \_\_\_\_\_
- ☐ authorised investment firms or advisers \_\_\_\_\_
- ☐ other bodies \_\_\_\_\_

### Arrangements for the provision of facilities to unitholders in accordance with Article 92:

Details of paying agent (name, legal form, registered office, address for correspondence if different)

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Name and address of any other person from whom investors may obtain information and documents \_\_\_\_\_

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Details of where and how unit prices will be published: \_\_\_\_\_

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### Other information and attachments required by the host State authority in accordance with Article 91(3)

Include (where relevant)

- details of any additional information to be disclosed to unitholders or their agents;
- details of the use made of any exemptions from marketing rules and requirements in relation to any UCITS or class of UCITS, or any category of investors;

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If applicable, confirmation of transmission of payment due to the host State competent authority \_\_\_\_\_



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### **Part C Confirmation by the UCITS**

I hereby confirm that the documents attached to this notification letter contain all relevant information as provided for in the Directive. The text of each document is the same as that previously submitted to the home State authority, or is an accurate translation of that text.

\_\_\_\_\_ (signature of the authorised signatory of the UCITS  
or of a third person empowered by a written mandate to act on behalf of the notifying UCITS)

\_\_\_\_\_  
(full name and position of the signatory)

Date and place:\_\_\_\_\_



## ANNEX II

### MODEL ATTESTATION FOR MARKETING OF UNITS OF UCITS IN AN EEA MEMBER STATE

\_\_\_\_\_ is the competent authority  
(name of the UCITS home State competent authority)

in \_\_\_\_\_  
(the UCITS home State)

address:

telephone number:

e-mail address:

fax number:

that carries out the duties provided for in the Directive [2009/65/EC] on the co-ordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)(referred to in this document as “the Directive”) as required by Art. 97(1) of the Directive.

For the purpose of Art. 93(1) of the Directive,

\_\_\_\_\_ certifies that  
(name of competent authority, as above)

\_\_\_\_\_  
(name of UCITS, i.e. the name of the common fund, unit trust or investment company)

is established in \_\_\_\_\_  
(name of its home State)

was set up on \_\_\_\_\_  
(date of approval of the fund rules or instrument of incorporation of the UCITS)

has registry no. (if applicable) \_\_\_\_\_  
(UCITS registry number in its home State)

registered with (if applicable) \_\_\_\_\_  
(name of the authority responsible for the register)

is based at \_\_\_\_\_  
\_\_\_\_\_  
(for investment companies only, address of the UCITS’ head office)



is EITHER ☐ a common fund / unit trust

List of all sub-funds approved in the home State, if applicable	
Serial no.	Name
1	
2	
3	
....	

managed by the management company

\_\_\_\_\_  
*(name and address of the management company)*

OR ☐ an investment company :

List of all sub-funds approved in the home State, if applicable	
Serial no.	Name
1	
2	
3	
....	

*either:* ☐ that has designated as its management company

\_\_\_\_\_  
*(name and address of the designated management company)*

*or:* ☐ that is self-managed

Date\_\_\_\_\_

\_\_\_\_\_  
*(signature of the representative of the UCITS home State authority)*

\_\_\_\_\_  
*(full name and capacity of the representative of the UCITS home State authority)*

## ANNEX III

### LIQUIDATION, MERGER OR DIVISION OF MASTER UCITS

The following scenarios illustrate possible timelines for the procedures set out in Boxes 5 and 6 (section 2.3)

#### Scenario 1:

##### **Liquidation of master UCITS, feeder UCITS to invest in another master**

- 31/8** master UCITS gives all investors (inc. feeder UCITS) three months' notice that it intends to liquidate on **30/11** (Art. 60(4))
- 30/10** feeder applies to its competent authority (CA) for approval to invest in another master
- 20/11** CA grants approval after 15 working days as allowed for by Art. 59
- 23/11** feeder confirms to master how liquidation proceeds are to be paid to it
- 27/11** feeder notifies its unitholders with information required by Art. 64(1) and (2)
- 30/11** liquidation of master commences; feeder suspends subscriptions
- 7/12** feeder receives proceeds of (initial)<sup>6</sup> liquidation payment
- 27/12** end of 30 days' disinvestment period for unitholders allowed by Art. 64(1)(d)
- 28/12** feeder begins investing in new master and re-opens for subscriptions

#### Scenario 2:

##### **Merger of master UCITS, feeder UCITS to continue investing in it**

- 31/8** master UCITS gives all investors (inc. feeder UCITS) two months' notice that it intends to be the receiving UCITS in a merger to take effect on **30/10** (Art. 60(5))
- 30/9** feeder confirms to its CA that it intends to continue investing in the master
- 20/10** CA grants approval after 15 working days
- 21/10** feeder confirms to master that it will continue to invest
- 30/10** merger takes effect, no impact on unitholders of feeder

#### Scenario 3:

##### **Division of master UCITS, feeder UCITS to invest in new UCITS resulting from division**

- 31/8** master UCITS gives all investors (inc. feeder UCITS) two months' notice that it intends to sub-divide into two UCITS, one of which will have a new investment objective and policy, effective from **30/10** (Art. 60(5))
- 30/9** feeder UCITS applies to its CA for approval to invest in the new UCITS resulting from the sub-division
- 21/10** CA grants approval after 15 working days

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<sup>6</sup> Payment of the full proceeds may take place some time after the liquidation has commenced; for the sake of simplicity it is assumed in these examples that the greater part of the master UCITS' assets are paid out initially, with a final payment much later on.





- 22/10 feeder gives instruction to master to redeem its units, and suspends subscriptions in its own units
- 28/10 feeder notifies its unitholders with information required by Art. 64(1) and (2)
- 29/10 feeder receives settlement of redemption proceeds from master
- 30/10 division takes effect
- 27/11 end of 30 days' disinvestment period for unitholders allowed by Art. 64(1)(d)
- 30/11 feeder begins investing in new master and re-opens for subscriptions

#### **Scenario 4:**

##### **Merger of master UCITS with extended notice, feeder to invest in UCITS resulting from merger**

- 31/8 master UCITS gives all investors (inc. feeder UCITS) three months' notice that it intends to be the merging UCITS in a merger to take effect on 30/11 (Art. 60(5))
- 30/9 feeder applies to its CA to invest in the receiving UCITS following the merger
- 20/10 CA grants approval after 15 working days
- 21/10 feeder confirms to master that it will continue investing under the terms of the merger
- 27/10 feeder notifies its unitholders with information required (Box 4 paragraph 6)
- 26/11 end of 30 days' disinvestment period for unitholders
- 30/11 merger takes effect, feeder is issued with units in receiving UCITS, no impact on unitholders of feeder

#### **Scenario 5:**

##### **Liquidation of master UCITS with extended notice, feeder to convert to non-feeder UCITS**

- 31/8 master UCITS gives all investors (inc. feeder UCITS) five months' notice that it intends to liquidate on 29/1/2010 (Art. 60(4))
- 26/11 feeder applies to its CA for approval to become a non-feeder UCITS
- 17/12 CA grants approval after 15 working days
- 18/12 feeder confirms to master how liquidation proceeds are to be paid to it
- 24/12 feeder notifies its unitholders with information required by Art. 64(1) and (2)
- 23/1/10 end of 30 days' disinvestment period for unitholders allowed by Art. 64(1)(d)
- 29/1/10 liquidation of master commences; feeder suspends subscriptions
- 5/2/10 feeder receives proceeds of (initial) liquidation payment, begins investing in accordance with new objective and policy, and reopens for subscriptions