



Ref.: CESR/03-378b

**THE ROLE OF CESR
IN THE REGULATION AND SUPERVISION OF UCITS AND
ASSET MANAGEMENT ACTIVITIES IN THE EU**

CONSULTATION PAPER

OCTOBER 2003



Foreword

This consultation paper aims at presenting the views of the Committee of European Securities Regulators (CESR)¹ on the role that the Committee will play in the regulation and supervision of Undertakings for Collective Investment in Transferable Securities (UCITS) and asset management activities in Europe. The paper is structured in three parts: the first provides some background information on the process of involvement of CESR in the regulation and supervision of the asset management industry; the second provides CESR's suggestions on areas of work and related priorities; the third provides indication of the organisation that CESR would like to put in place to address these new issues.

CESR proposals follow an issues-based approach through which market participants, including investors and the European mutual funds and asset management industry, will specify to CESR the areas in which regulators can facilitate an EU based consistent regulation of the "buy side" of the market, which includes: a) traditional and new issues of the regulation of UCITS, b) issues related to the regulation of asset management, c) issues that affect investment management business and that are important for the proper functioning of the internal market for financial services.

The proposals were discussed during an ad-hoc meeting of CESR's experts in the field of collective asset management. The CESR Market Participants Consultative Panel discussed the benefits of an enhanced role given to CESR members on regulation of the UCITS and asset management industry during its last meeting in June. Furthermore, CESR has already conducted informal discussions on the re-organisation of the regulation of UCITS and asset management activities in Europe with representatives of the EU industry.

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In order to give interested parties an opportunity to express their opinions on the consultation paper, CESR will hold an **open hearing on 20 November 2003** at the CESR premises, 11-13 avenue de Friedland, Paris. Please register your interest in participating by e-mail to the secretariat of CESR at secretariat@europefesco.org.

The **deadline for submitting written responses to the consultation paper is 1st of December 2003**. Responses should be addressed to Mr Fabrice Demarigny, Secretary General, CESR, by email at secretariat@europefesco.org.

¹ The Committee was established under the terms of the European Commission's decision of 6 June 2001 (2001/1501/EC). The Committee has set out its own operational arrangements in its Charter. The Commission's decisions and the CESR's Charter are available in the web site www.europefesco.org



1. Background.

- 1.1. In the overall discussion on the extension of the “Lamfalussy procedure” to other financial sectors (namely insurance and banking), UCITS and pension funds were considered to be part of other sectors of financial services, respectively, securities and insurance.

Various arguments can be put forward to consider the collective portfolio management activity to be part of the wider investment securities business, whose regulation and supervision are traditionally attributed to securities regulators:

- the distinction between collective and individual portfolio management activities is not very clear, since they belong to the asset management activity, which is frequently concentrated in one single business unit, performing asset management functions for the entire institution (sometimes for the entire group);
 - the distinction is even less clear at the level of intermediaries: after the amendment to the UCITS Directive (with Directives 2001/107/CE and 2001/108/CE), portfolio management companies may also provide individual portfolio management, subject to the application of the rules established under the ISD. As the same rules will apply to the same business (individual portfolio management), irrespective of the nature of the intermediary, there is a need to ensure a high degree of consistency between regulations applicable to the two areas of portfolio management;
 - the so-called “buy side” (including both individual and collective asset management) should not be separated from the “sell side” in order to have a more complete and coherent regulation of capital markets;
 - securities regulation and supervision normally include collective investment schemes’ activities (even at the level of organisation of securities regulators: e.g. Standing Committee n. 5 of the International Organisation of Securities Commissions, IOSCO). *De facto*, all CESR members are competent authorities in terms of the UCITS Directive.
- 1.2. The Ecofin Council of 3 December 2002 endorsed the final report of the Economic and Financial Committee (EFC) on the extension of the Lamfalussy procedure and subsequent arrangements to the other financial services sectors.

As regards financial regulation, the Council stated that “*sectoral specificities would be best recognised by three separate sectoral committees each at levels 2 and 3: for banking, insurance, including pensions; and securities, including UCITS*”.

As regards financial supervision, the Council emphasised the importance of strengthened supervisory co-operation and better implementation and enforcement of regulation in the EU; CESR has been taken as a model, both in terms of functions and structure, to which the other committees should converge.

- 1.3. Given the decision of the Ecofin Council to incorporate UCITS in the sectoral securities committees, CESR has analysed the possible way forward.

1.3.1. The current legislation



The UCITS Contact Committee has been set up by the European Commission on the basis of Article 53 of the UCITS Directive (85/611/EC). Its original functions were:

- to facilitate the harmonised implementation of the Directive;
- to facilitate consultation between Member States on more rigorous requirements;
- to advise the Commission on additions or amendments to the Directive.

The Committee has been recently empowered with new “regulatory” powers (Article 53a), introduced by the Directive 2001/108/EEC². Comitology is sought to assist the Commission “in regard to technical modifications” to be made to the Directive in the following areas:

- clarification of the definitions;
- alignment of terminology.

In accordance with Article 53a(3), the rules of procedure (the same for the European Securities Committee, ESC) for the exercise of implementing powers conferred on the Commission have been approved by the Committee.

From the above, it is clear that the functions attributed to the UCITS Contact Committee do not differ from those foreseen under the Lamfalussy procedures without, however, a clear distinction between Level 2 and Level 3.

1.3.2. Next steps for adapting the EU institutional framework

Having considered the scope and the nature of the functions attributed to the UCITS Contact Committee, three different aspects should then be considered: i) how the functions of the UCITS Contact Committee will be re-allocated from the UCITS Contact Committee to ESC/CESR, ii) the uncertainties of this process and iii) how CESR intends to address the intermediate stage.

- i) The re-allocation of functions given at present to the UCITS Contact Committee will take the form of a directive amending the current (revised) text of the UCITS Directive. The EU Commission’s services have taken the view that for both level 2 and 3 it is necessary to amend the UCITS Directive, in order to abolish existing powers of the UCITS Contact Committee and create new ones for the ESC and CESR. Therefore, the Commission intends to adopt a proposal for amending the UCITS Directive, as well as the directives in the banking and insurance fields. Furthermore, the Commission intends to

² Article 53a inserted in Directive 85/611 by Article 1, paragraph 22, of Directive 2001/108 of 21 January 2002 reads as follows:

“ 1. In addition to its functions provided for in Article 53(1), the Contact Committee may also meet as a Regulatory Committee within the meaning of Article 5 of Decision 1999/468/EC to assist the Commission in regard to the technical modifications to be made to this Directive in the following areas:

- clarification of the definitions in order to ensure uniform application of this Directive throughout the Community,
- alignment of terminology and the framing of definitions in accordance with subsequent acts on UCITS and related matters.

2. Where reference is made to this paragraph, Articles 5 and 7 of Decision 1999/468/EC shall apply, having regard to the provisions of Article 8 thereof.

The period provided for in Article 5(6) of Decision 1999/468/EC shall be set at three months.

3. The Committee shall adopt its rules of procedure.”



amend the two decisions establishing CESR and the ESC, to expand their respective competences to the UCITS sector; these decisions will also enter into force most probably at the same time when the amended directive will also enter into force.

- ii) Nonetheless, the timing of implementation of the Ecofin decision is still uncertain. A comprehensive package covering the banking, insurance and UCITS sectors will be presented for adoption by the Commission most probably in October 2003. This package consists, on the one hand, in a draft Directive, modifying, among other issues, the Directive which created the UCITS Contact Committee. This Directive will then be submitted to co-legislators; however, final adoption and entry into force is uncertain, given the calendar of events in 2004, notably the election for the European Parliament, the appointment of the new European Commission.
- iii) In the meantime, CESR has been invited to attend, and already attends as observer, the meetings of the UCITS Contact Committee. In this context, the role of CESR is to provide input to the current UCITS Contact Committee, and in future to the ESC. The objective being that, when the legal transfer will become effective, CESR is able to ensure full continuity on issues currently discussed within the UCITS Contact Committee (and in the future with the ESC) and to answer the request by the “buy side” industry to be properly represented within CESR. Given the uncertainties on the timing for the adoption of the legal changes, CESR considers it appropriate to start working in the area of UCITS and asset management, in order to provide a coherent response to regulation and supervision across Europe, including providing input to the UCITS Contact Committee.

- *Do market participants share the views of CESR on the need for its future involvement in the areas of UCITS and asset management?*
- *Do market participants agree with the proposed role of CESR in facilitating convergence of the regulation and supervision on the “buy side”?*

2. Areas of work by CESR in the asset management activities.

Following a fruitful discussion during an ad-hoc meeting of CESR experts on UCITS and asset management, taking into consideration the list of issues presented by representatives of the EU industry to CESR, CESR has identified the following general principles and priorities as to the future role of CESR in the area of UCITS and asset management activities.

2.1. General principles

- A. Any future work done by CESR regarding UCITS would have to be conducted in full coherence with the EU institutional framework.



- B. CESR should take in a global vision of the so-called “buy side”, and not limit its activities to investment funds.
- C. CESR should not start to work on matters where the UCITS Contact Committee is about to finish its work (e.g. simplified prospectus, derivatives).
- D. Account should be taken of the outcome of work already done by IOSCO.

2.2. Priorities and possible input by CESR in the area of UCITS and Asset Management activities

CESR proposes four areas of possible intervention and priority work streams and sets out what each of these streams of work might include, as follows:

- A. Areas where supervisory convergence should be achieved, such as:
 - Elaboration of common supervisory techniques by exchanging experiences and developing standards regarding, in particular, risk management, marketing policy, fee structures, and conflicts of interest
 - Co-operation between competent authorities concerning Asset Management companies being active in several Member States
 - New activities in the UCITS sector (e.g. distribution techniques)
 - Collection of data by supervisors
- B. Areas where input to ensure the harmonized implementation of the UCITS Directive could be provided to the UCITS Contact Committee, ideally on its request. In relation for example to:
 - Depositories
 - Outsourcing/delegation of functions
 - Scope of the passport of asset management companies
 - Use of indexes
 - Money-market instruments (in conjunction with the STEP Task Force)
- C. Areas not harmonised at EU level but where a common approach by regulators is necessary (“Autonomous Level 3”):
 - Non-harmonised Collective Investment Schemes (such as real-estate funds, and possibly private-equity funds)
 - Hedge funds
- D. Areas where consistency with other EU Directives are needed:
 - ISD – passport issues, conduct of business rules (regarding, for example, best execution and conflicts of interest)
 - IAS – concerning, especially, listed UCITS, consolidation and scope of application
 - Distance Marketing Directive
 - E-Commerce Directive

- *Do market participants agree with the list of general points and the definition of priorities and possible input by CESR as set out above?*



- *Are there any areas on which CESR should concentrate?*
- *Which areas of work do you consider to be a priority?*

3. Organisation of CESR work.

The decision of CESR to start working on UCITS and asset management activities raise the question of how CESR envisages incorporating these new areas in its internal organisation to perform these functions.

The objective is to present at the end of the year 2003 a concrete proposal to set up a provisional Expert Group on UCITS and Asset Management Activities with a specific mandate. A two-step approach can be envisaged at present:

- a) First, on the basis of the list of issues abovementioned, and in light of the comments received during the consultation process CESR starts working with a provisional Expert Group, with appropriate consultation mechanisms, and, if relevant, channels some of these issues to other existing Expert Groups;
- b) Secondly, depending on the timing of the final adoption and entry into force of the legal texts transferring competences to CESR, CESR can set up a permanent group.

In terms of impact for the CESR forces, this prospect will imply the allocation of a permanent member of the Secretariat to this specific task (with the recruitment of an expert with a strong background in the area of asset management from the network of CESR members).

In terms of consultation, CESR will follow the same standards of openness and transparency in conducting work in the area of UCITS and asset management. The Public Statement on Consultation Practices (Ref. CESR/01-007c) (annex 1) should therefore be applicable when CESR elaborates standards or provides technical expertise.

In addition, in order to take account of the specificities of the “buy side” activities, CESR would like to set up a Consultative Working Group of market participants of the sector (including practitioners, consumers and end-users). The role of this Consultative Group will be to provide technical expertise to the provisional Expert Group at an early stage and provide an opinion on priorities. The Consultative Group would include no more than 12 members, appointed on a personal capacity, with the following areas of expertise: portfolio management techniques (shares, bonds, money markets, derivatives, ...), index management, valuation techniques, back-office matters, conduct of business rules, buy side analysts, marketing and distribution techniques, risk management, specialised funds. The members of CESR would be asked to indicate candidates to the Panel. The final decision on the composition of the Panel would be taken by CESR.



- *Do Market participants agree with this approach?*
- *Do Market participants agree with the approach to consultation?*
- *Do Market participants agree to create a specific Consultative Working Group in order to reflect the specificity of the “buy side”?*
- *Do Market participants see other areas of expertise that the Consultative Working Group should benefit from?*



Annex 1

Date: December 2001

Ref.: CESR/01-007c

Public Statement of Consultation Practices

Having regard to the decision of the EU Commission establishing the Committee (2001/1501/EC) and, in particular, its article 5;

Having regard to the Charter of the Committee of European Securities Regulators (“the Charter”), which commits the Committee to make a Public Statement of its consultation practices;

Considering the Final Report of the Committee of Wise Men on the Regulation of European Securities Markets (15 February 2001) (“the Report”) and its recommendations on the consultation procedures and transparency for the Committee;

Considering Article 5.7 of the Charter, which commits the Committee and its expert groups to working in an open and transparent manner;

Considering Article 5.10 and 5.11 of the Charter, which commits the Committee to using appropriate processes to consult (both *ex ante* and *ex post*) market participants, market operators, consumers and end-users;

The Committee of European Securities Regulators has approved the following statement for all its work including levels two and three as set out in the Report:

1. **The aim of consultation** is to build consensus where possible between all interested and affected parties on what legislation or regulation is appropriate and to improve the decision making process of the Committee by:
 - a) Benefiting from the expertise of market participants and operators, consumers and end-users, notably in assessing and analysing regulatory issues and possible solutions;
 - b) Assisting determination of whether a problem exists which requires a regulatory action, and if so, what form of regulatory actions is appropriate;
 - c) Providing opportunities for alternative approaches to a given issue to be considered;
 - d) Obtaining information and views on the potential impact of proposals;
 - e) Obtaining feedback on the Committee’s work;
 - f) Promoting understanding of the work of the Committee and its role.
2. **To deliver this aim, the Committee emphasises,**
 - (i) **the need for all involved to “play a co-operative game”** (page 42 of the Report). This places mutual obligations on the Committee and those consulted to work in a manner that promotes the success of the process. This has particular significance at Level Two, where the scope and timetable of the Committee’s work will be determined by mandates from the European Commission.
 - (ii) **the need for a flexible and proportionate approach to consultation** that can be adapted according to the significance of an issue.



3. **Notwithstanding the need for flexibility, the Committee will be guided by the following principles:**
- a) On **who** it consults, the Committee will:
 - i) Target the full range of interested parties, including market participants, consumers and end-users;
 - ii) Make consultation proposals widely known and available through all appropriate means, in particular the Internet;
 - iii) Consult at national, european and international levels.
 - b) On **when** it consults, the Committee will:
 - i) Publish an anticipated annual work programme so that all interested parties know when to expect output from the Committee;
 - ii) Publish any mandate received from the European Commission as soon as practical after receipt;
 - iii) Organise upon request informal discussions at an early stage with those most likely to be directly affected;
 - iv) Consult at a sufficiently early stage to enable the Committee to take the responses into account;
 - v) Allow those consulted adequate time to respond, given the complexity of the issue and the time available. For significant issues, the Committee will aim to allow a three month consultation period.
 - c) On **how it consults**, the Committee will:
 - i) Provide an opportunity for interested parties to make submissions on receipt and publication by the Committee of a mandate from the European Commission;
 - ii) When necessary, release its thinking at various stages, including via concept releases;
 - iii) Produce reasoned consultative proposals, based on thorough analysis of the issues and objectives of the proposal and, where possible, on statistical information, expressed in concise and clear language, and, if possible, include in proposals preliminary information on their impact;
 - iv) Establish working consultative groups of experts where appropriate;
 - v) Consult using a variety of media, including public hearings/roundtables, written and Internet consultations. In the interests of efficiency, use of the Internet will be encouraged and facilitated;
 - vi) Use appropriate processes when necessary to target consultations better to particular affected parties (such as face to face meetings).
 - d) On **how it responds** to consultation, the Committee will:
 - i) Give due consideration to responses received;
 - ii) Make public all responses to formal European consultations, unless the respondent requests otherwise, or make public a summary of the responses received;
 - iii) Publish a reasoned explanation addressing all major points raised;
 - iv) Consult for a second time if the response to the first consultation reveals significant problems, or where revised proposals are radically different from the original proposals on which consultation was based.



- v) Publish all formal proposals and advice, including advice to the European Commission given under Level Two.
4. If it is not possible for the Committee to follow the principles described above, the Committee will publish its reasons.
5. When necessary, the Committee will review this statement of consultation practices.