ICI Comments on Efforts to Improve Cross-Border Fund Market in Europe, November 2005

November 15, 2005

European Commission
Brussels, Belgium

Re: Response to the Commission's Consultation on the Enhancement of the EU Framework for Investment Funds (COM (2005) 314)

Dear Sirs:

The Investment Company Institute[1] is writing in response to the Commission's Green Paper on the Enhancement of the EU Framework for Investment Funds, which reviews areas for improvement in the UCITS Directive. Many of our members actively participate in the UCITS market, and our comments reflect their experiences in organizing, advising, and distributing investment funds in Europe.

We applaud the efforts of the Commission to foster an integrated and efficient market for investment funds in Europe. As the Green Paper recognizes, collective investment funds are, and likely will remain, the very best vehicle for average investors to participate in the securities markets, accumulate wealth, and achieve their most important long-term financial goals. At their best, investment funds offer unparalleled advantages – professional management, broad diversification, liquidity, abundant information, a wide array of choice, and a high degree of convenience and investor service – all at relatively low cost. Improvements in the structure of the market for investment funds in Europe will lead to greater availability and choice of investment funds to the benefit of European investors.

The UCITS Directive has the potential to establish a framework for a pan-European fund market by providing a convenient passport that allows funds to be sold throughout the EU. Unfortunately, as the Commission clearly recognizes, the cross-border ideal inherent in UCITS has yet to become a reality. In practice, the cross-border sale of funds is difficult and expensive, and distribution of funds along national lines still predominates.

In response to the Green Paper, we suggest five ways in which the cross-border market for funds in Europe could be improved:

- Streamline and simplify the notification procedure for passporting funds;
- Enhance the usefulness of disclosure available at the point of sale, particularly by allowing funds and intermediaries to rely principally on the Internet for purposes of communicating the required information to investors;
- Enhance the usefulness and comparability of fund advertising materials through the establishment of standardized performance methodologies;
- Streamline the process by which Member States approve marketing plans; and
- Improve the European infrastructure for processing subscription and redemption orders.

We also recommend that the Commission establish a working group to consider adopting a common understanding or definition of “private placement” across the EU. Our reasons for these recommendations and our responses to some of the specific questions in the Green Paper are included below.

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Section 2.1 – Priority Actions

The Commission lists four priority areas in Section 2.1 of the Green Paper. In our view, the second priority – simplifying the notification procedure for passporting funds – remains the most important. Member states continue to administer the provisions of the UCITS Directive differently, resulting in substantial delays in completing the notification procedure for passporting funds. For example, in Italy, registering a non-Italian UCITS fund for sale routinely takes six months, rather than the maximum of sixty days contemplated in the Directive. CESR’s work to build up convergence in this area is crucial to the realization of a true EU passport for funds.[2] We urge the Commission to fully support CESR’s efforts with respect to the convergence of notification procedures.

Section 2.2.2 – Distribution, sales, and promotion of funds

The Commission asks whether greater transparency, comparability, and attention to investor needs in fund distribution materials will enhance the functioning of European investment fund markets and the level of investor protection. The answer clearly is “yes.” We fully support enhanced disclosure to be available at the point of sale to help investors assess and evaluate a recommendation to purchase fund shares.[3]

In evaluating possible approaches to point of sale disclosure, the Commission should consider expressly recognizing the use of the Internet. We have urged our own Securities and Exchange Commission to craft disclosure rules that recognize the growing use of the Internet by investors and allow funds and intermediaries to rely principally on the Internet for purposes of communicating the required information to investors. We encourage the Commission to do the same. The Internet is an effective way to provide investors with timely and convenient access to the required information without imposing inappropriate costs and burdens on the sale of fund shares.

Two other issues relating to the distribution, sale, and promotion of funds warrant attention by the Commission. The first is the comparability of performance advertising in the EU. We agree with the Commission that investors and intermediaries increasingly need meaningful performance information. Standardized performance methodologies will provide comparable performance information, which we believe will promote a pan-European market for investment funds. [4] We therefore urge the Commission to standardize the methodology for computing fund performance across the European Union and require funds that advertise performance to include standardized performance figures.[5]

Second, the Commission should examine the practice by member states of approving marketing plans and consider limiting the time that member states have to grant the necessary approvals. Host countries have the jurisdiction to set marketing requirements. This has meant, in practice, that funds are subject to varied and conflicting requirements relating to advertising and disclosure. The result is an overlapping, duplicative, and inconsistent set of requirements that effectively creates a barrier to passporting funds in the EU.

Section 3.1 – Towards a cost-efficient industry

The Commission notes that the European infrastructure for processing subscription and redemption orders is fragmented. As highlighted by the EU Asset Management Expert Group, cross-border processing of fund units is a key issue for the asset management industry. [6] In 2001, the Institute formed the International Operations Advisory Committee (“IOAC”) to provide a forum for our members to work with the providers of clearing and settlement services and the distributors of investment funds on our common goal of achieving standardization and automation of clearance and settlement procedures for investment fund capital shares in the pan-European marketplace. The IOAC has a continuing dialog with EFAMA, which, as the Commission recognizes, is working to develop pan-European standards relevant to order processing for investment funds.

The Institute appreciates the Commission’s support for industry efforts to develop efficient and safe clearing and settlement systems for investment fund capital shares. We agree with the Commission’s instinct that industry should continue to take the lead and that EU policy makers should only become involved in the event of manifest coordination problems or insurmountable regulatory or policy barriers.

Section 3.4 – Europe's alternative investment market

The Commission suggests that it may establish a working group to consider, inter alia, the extent to which a common understanding of "private placement" could facilitate the cross-border offer of funds to qualified investors. We support the concept of a common understanding or standardization of private placement exceptions in Europe because we believe that it could significantly streamline the sale of cross-border investment funds (both UCITS and non-UCITS) to pension plans. Accordingly, we encourage the Commission to establish a working group in this area, but also to ensure that the mandate of that working group is broad enough to consider the benefits of standardized private placement rules to European pension managers.

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The Institute appreciates the opportunity to comment on the Commission's Green Paper. If you have any questions about our comments, please contact me at +1-202-371-5430 or rcg@ici.org.

Sincerely,

Robert C. Grohowski
Senior Counsel – International Affairs

ENDNOTES

[1] The Investment Company Institute is the national association of the United States investment company industry. The Investment Company Institute's membership includes 8,518 open-end investment companies (mutual funds), 663 closed-end investment companies, 148 exchange-traded funds, and 5 sponsors of unit investment trusts. Mutual fund members of the ICI have total assets of approximately $8.5 trillion (representing more than 95 percent of all assets of US mutual funds); these funds serve approximately 86.7 million shareholders in more than 51 million households.

[2] CESR recently issued a consultation paper on this topic. See CESR/05-484 (Oct. 27, 2005).

[3] We have expressed concern, however, that point of sale disclosure could have the undesirable effect of creating a disincentive for intermediaries to sell retail investment funds, as compared to other products that are not subject to similar requirements. We would encourage the European Commission to consider the potential effect that its disclosure requirements might have on the sale of retail investment funds as compared to other investment products.

[4] For a detailed explanation of our reasons, see ICI's letter to Niall Bohan, dated May 25, 2005.

[5] We do not believe that requiring standardized performance figures to be included in advertisements will disturb the home state-host state balance in the current UCITS Directive. Host member states will retain the authority to regulate the marketing of UCITS funds in their jurisdiction. Host states simply will have to require an additional performance figure in fund advertisements that include performance information.

[6] See "Financial Services Action Plan: Progress and Prospects," Final Report of the Asset Management Expert Group on the Financial Services Action Plan (May 2004).