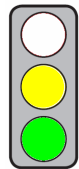


MAIN ISSUES

Objectives of the Directive: Investor information on EU-wide harmonised investment funds ("UCITS") are to be presented more concisely and their cross-border marketing procedure is to be facilitated. UCITS are to become entitled to merge with other UCITS and to invest more assets in other funds than to date.

Groups Affected: Investment funds and investment companies, supervisory authorities, investors.



Pros: (1) The shortening of mandatory investor information to key information facilitates the comparison of investment products and thus boosts competition.
(2) It is reasonable to simplify cross-border marketing of UCITS without entirely waiving the supervision by competent authorities in the host Member States.
(3) Simplified mergers between UCITS might lead to administrative cost savings by exploiting economies of scale.

Cons: It is not comprehensible why the authorization procedure for the cross-border marketing of UCITS already approved in a Member State should last 30 days.

CONTENT

Title

Proposal COM(2008) 458 of 16 July 2008 for a **Directive** of the European Parliament and the Council on the coordination of laws, regulations and administrative provisions relating to **undertakings for collective investment in transferable securities (UCITS)** [Recast]

Abstract

► Object of the Directive

- "undertakings for collective investment in transferable securities" (UCITS) are undertakings
 - the sole object of which is the collective investment in transferable securities and/or in other liquid financial assets of capital raised from the public and
 - the units of which are, at the request of holders, re-purchased or redeemed at any time (Art. 1 (2)).
- According to the Council Directive 85/611/EEC, UCITS are subject to EU-wide harmonised provisions. In particular, this Directive, which shall be revised by the Proposal, contains the following:
 - provisions on the organization, management and supervision of UCITS;
 - provisions on UCITS' investment strategies and on the diversification and liquidity of its investments.
- UCITS manage € 5,600 billion, or 10 % of the financial assets of European households.
- UCITS usually take the legal form of investment funds, yet may also be established in the form of investment companies or unit trusts (Art. 1 (3)).

► Information to Investors

- UCITS shall be obliged to provide their investors with the following documents:
 - "key investor information" (Art. 70),
 - the prospectus and the latest published annual report and half-yearly reports (Art. 73).
- "Key investor information" (KII) has to be kept short (maximum two pages), enabling investors to take investment decisions on an informed basis. It has to be clear and comprehensive and made available to investors before contract conclusion. Liability shall arise only where information is "misleading, inaccurate or inconsistent with the relevant parts of the prospectus". KII have to describe investment objectives and investment policy, costs and associated charges, past performances of the fund and the risk profile of the investment (Art. 73 (1), (3) and (5), Art. 74).

► Cross-Border Marketing of UCITS

- As for UCITS wishing to market its units in another EU Member State, the Directive proposes a streamlined notification procedure. Under the new rules, UCITS will submit the following documents to its home competent authorities (Art. 88 (3), (7)):
 - a notification letter describing the arrangements made for marketing the units of UCITS;
 - the "key investor information", which has to be translated into one of the official languages of the UCITS host Member State, unless exceptions are provided for by the competent authority;
 - contract terms, prospectus and the latest annual report and subsequent half-yearly report translated into the same official language, or into a language "customary in the sphere of international finance".

- The competent authorities of the UCITS home Member State shall verify whether the documentation submitted is complete no later than one month after the date of receipt, and shall electronically transmit it to the competent authorities of the host Member State. UCITS may market its units in the host Member State as of that date (Art. 88 (3)).
- The competent authorities of the host Member State may not request any additional documents from UCITS (Art. 88 (6)).
- However, if the competent authorities of the UCITS host Member State “have clear and demonstrable grounds” for believing that a UCITS is in breach of the Directive’s provisions, they shall give notice hereof to the competent authorities of the home Member State. If the latter fails to remedy such a breach adequately, the competent authorities of the host Member State may take “appropriate measures” and even impose a marketing ban on the UCITS concerned on their territory (Art. 103 (3), (4)).

► UCITS’ Mergers

- Member States must allow for mergers between UCITS, irrespective of their legal form, if the requirements of the Directive are fully complied with (Art. 35).
- The “merging” UCITS has to file an application for the merger with the “receiving” fund at the competent authorities of the home Member State (Art. 36 (1)). The application must include:
 - the common draft terms of the proposed merger of the UCITS involved, including the type of merger and the rationale behind it, as well as the expected impact of the proposed merger on the unit-holders (Art. 36 (2) lit. a, Art. 37);
 - the validation by an independent auditor of criteria and methods adopted for the valuation of assets and liabilities as well as of the method of calculation of the exchange ratio (Art. 36 (4) lit. a and Art. 39);
 - “satisfying” information on the proposed merger, which the UCITS involved plan to provide their unit-holders with (Art. 36 (4) lit. b and c, Art. 40).
- The competent authorities shall decide upon the application within a period of 30 days. In particular, they shall assess the potential impacts of the merger on unit-holders and may require that the information provided to unit-holders of the merging UCITS be “clarified”. If they expect a “substantial impact” on the receiving UCITS, they may require that “appropriate and accurate information” on the proposed merger be made available to unit-holders of the receiving UCITS (Art. 36 Abs. 3 and 5).
- A merger is subject to the approval of unit-holders of UCITS only where required by the national laws of Member States. Such approval may not require more than 75% of the votes (Art. 41).
- In the case of mergers, unit-holders have the right to request the redemption of their units without charge. Alternatively, they may request converting them into units in another UCITS with investment policies similar to the original UCITS (Art. 42).

► “Master-Feeder Structures”

- In the future, UCITS will be entitled to invest *at least* 85% of their assets in units of *another* UCITS (Art. 53 (1), Art. 54). The feeding UCITS (“Feeder”) may invest in one single other UCITS (“Master”) only. A Master may not act as Feeder at the same time (Art. 53 (3)).
- Investments of Feeders in Masters are subject to prior approval by the competent authorities of the Feeder’s home Member State (Art. 53 and Art. 54 (1)).
- Said approval requires a legally binding agreement between Master and Feeder, especially on the Master’s investment objective and policy as well as on the rules governing a possible modification of these (Art. 55 (1) and Art. 56 (1)). The Feeder is obliged to “effectively” monitor the Master’s investment activities in the best interest of its unit-holders (Art. 60 (2)).
- The Feeder has to declare that it is a Feeder in its prospectus. Moreover, it has to describe the Master and briefly describe the agreement entered into by Master and Feeder. The prospectus of the Master UCITS has to be attached to the Feeder UCITS’ prospectus (Art. 58).

Changes Compared to the Status Quo

- In the future, UCITS will have to provide their unit-holders with “key investor information” in a short and simple form of not more than two pages, instead of a previously often extensive “simplified prospectus”.
- In the future, cross-border marketing of UCITS will be approved by the competent authorities in the home Member State, instead of in the host Member State. The delay of the verification procedure will be reduced from two months to one month.
- To date, EU rules on cross-border mergers do not exist. In the past, this led to issues whenever the legal form of a UCITS involved in a merger was not approved by all Member States. In the future, differences in the legal form may no longer impede mergers.
- To date, UCITS are only allowed to invest a maximum of 20% of their assets in one and the same fund. Now, “Master-Feeder Structures” are being introduced into EU law.

Statement on Subsidiarity

According to the Commission, only the EU is able to establish harmonised cross-border provisions.

Political Background

In November 2006 the Commission published a White Paper on the EU legal framework for investment funds. It was preceded by extensive consultations, often calling for an EU passport for fund management companies. Such an EU passport would enable management companies to become established in any Member State of the EU and to manage investment funds based and approved in another Member State from there.

Luxemburg and Ireland are sceptical about an EU passport. These countries have become centres of the European fund management industry, managing 40% of all UCITS assets. They fear that an EU passport might lead to a movement of fund management companies to financial centres in other Member States. Other Member States argue that a divergence between the Member State where the UCITS is authorised and the one where it is managed is acceptable only once financial supervision in the EU is enhanced.

The Commission did not integrate the EU passport into its Proposal so as to not endanger the passing of other reforms. However, the Commission will draw up a proposal on the EU passport based on advice to be submitted by the Committee of European Securities Regulators (CESR) by 1 November 2008; said proposal shall be passed by the European Parliament and the Council before November 2009.

The Economic and Monetary Affairs Committee of the European Parliament intends to submit a report on the proposed Directive to the plenum by the beginning of December. The plenum wants to vote on it by mid-January 2009.

Status of Legislation

16.07.08 Adoption by Commission

Open Adoption by the European Parliament and the Council, publication in the Official Journal of the European Union and entry into force

Options for Influencing the Political Process

Leading Directorate General:	DG Internal Market and Services
Committees of the European Parliament:	Economic and Monetary Affairs (in charge), rapporteur: Wolf Klinz (ALDE-group, D); Legal Affairs
Committees of the German Bundestag:	Finance (in charge); Affairs of the European Union
Decision Mode in the Council:	Qualified majority (approval by a majority of Member States and at least 255 out of 345 votes; Germany: 29 votes)

Formalities

Legal competence:	Article 47 (2) TEC (Freedom of Establishment)
Form of legislative competence:	Concurrent legislative competence
Legislative procedure:	Article 251 TEC (Codecision)

ASSESSMENT

Economic Impact

Ordoliberal Assessment

Although the Commission holds the view that the EU market for investment funds is currently too fragmented, statutory rules should not be applied in order to reach a specific organisation of the market. Therefore, it can be seen as a positive approach that the proposed measures allow for a reorganisation of the EU internal market for investment funds yet do not enforce them. Whether or not these will actually entail greater and more cost-efficient funds as a result will depend upon competition and investors' preferences, and not upon the Commission's view.

In particular, **the Commission's approach to apply the principle of mutual recognition of authorisation to cross-border marketing of UCITS** – as is already the case in the internal market for goods – **is to be appreciated**. UCITS that have already been authorised in their home Member State and wish to market their units on another territory should not be verified a second time by the competent authorities of the host Member State. After all, UCITS still remain under the control of local supervision authorities, although the domestic authorities' competences to intervene prevail over those of the host authorities.

Impact on Efficiency and Individual Freedom of Choice

The Directive reduces barriers on the internal market for UCITS and helps to improve the efficiency of investment markets.

The obligation to present "key investor information" on two pages reduces red tape. It facilitates the comparison of different investment products and thus strengthens competition leading to higher efficiency.

The simplification of the rules governing cross-border marketing of UCITS provide for a more efficient EU-wide marketing of centrally managed funds. Master-Feeder structures allow for a decentralised marketing of Feeders, the assets of which are administered by the Master in a centralised and thus cost-efficient way. However, **greater efficiency could be reached if the authorization procedure regarding cross-**

border marketing was reduced to less than 30 days. Given that the competent authorities of the home Member State have to verify solely the completeness of the application filed, **a few days should suffice.**

Cross-border mergers enable UCITS to organise their structures more efficiently. Hence, scale economies can be realised, helping to reduce the administrative costs of funds. As European funds are usually characterised by relatively small-sized investment volumes, their average administrative costs are approximately twice as high as those of their US American counterparts. However, the proposal does not address the tax issues arising in connection with cross-border mergers.

However, **the Commission should introduce an EU passport for UCITS**, since it would help investment companies to further cut administrative costs.

Currently, most of UCITS assets are authorised in Luxemburg or Ireland. For these funds, investment companies have to appoint management companies domiciled there too. However, in most cases the actual administration of funds is accomplished in other financial centres due to their vicinity to investors. The EU passport would remove such inefficiency by way of enabling investment companies to manage units that are authorised in other Member States in a centralised form. The Commission estimates efficiency gains through the EU passport at € 762 million per year (Commission Staff Working Document SEC(2006) 1451).

To ensure effective financial supervision, it is necessary that the supervising authorities improve and better coordinate their cooperation. Only such close cooperation can guarantee that competition does not negatively affect the quality of supervision.

Impact on Growth and Employment

Even though efficient investment markets provide investors with cost-efficient capital, the Directive's positive impact on growth and employment is likely to be marginal.

Impact on Europe as a Business Location

Higher investments into the EU as a result of reduced administrative for fund management are not expected.

Legal Assessment

Legal Competence

Competences are laid down in Art. 47 (2) TEC.

Subsidiarity

Unproblematic.

Proportionality

Unproblematic.

Compatibility with EU Law

Unproblematic.

Compatibility with German Law

Mainly the German Investment Law (*Investmentgesetz – InvG*) has to be modified. The provisions on a simplified prospectus, in particular Art. 42 *InvG*, have to be substituted by provisions on “key investor information”. The provision on liability in Art. 127 *InvG* has to be modified, too, since liability arises only where “key investor information” are “misleading, inaccurate or inconsistent with the relevant parts of the prospectus”. The provisions on mergers (Art. 40 *InvG*) as well as on cross-border marketing (Art. 128 et sqq. *InvG*) have to be modified. New rules on Master-Feeder structures have to be stipulated.

Alternative Policy Options

The period of delay for approving cross-border marketing of UCITS, already approved, should be reduced to a few days.

Possible Future EU Options

It can be assumed that as of November 2008 and upon consultation with the Committee of European Securities Regulators (CESR), the Commission will propose to introduce an EU passport for UCITS as well as a procedure for an improved cooperation of competent supervisory authorities. It is still open whether the Commission will initiate a clarification of tax issues related to fund mergers.

Conclusion

The obligation to present “key investor information” in a short and simple manner helps investors to better compare investment products and boosts competition. Furthermore, it is reasonable to simplify the cross-border marketing of UCITS units, the more so as the competent authorities of the host Member State remain in control of legal supervision. The period of delay for the authorization of cross-border marketing of already approved UCITS should be reduced. The admission of mergers and the establishment of Master-Feeder structures enables UCITS to save costs by exploiting economies of scale.