



There is a strong agreement among industry stakeholders on the added value of the proposals made for reviewing the UCITS Directive (UCITS IV) ie streamlining of the notification process, fund mergers, pooling / master feeder techniques, Key

Investor Document and supervisory cooperation. On the other hand the Management Company Passport (MCP) concept has remained controversial particularly for contractual funds which are not legal entities (eg FCPs). The concept of the MCP already exists in the current UCITS III framework but is limited to corporate funds (eg SICAV which have a legal personality).

In July 2008 CESR was requested by the Commission to provide advice on remaining technical questions that need to be addressed when introducing a MCP.

Eurofi and a working group composed of industry representatives from all parts of the value chain, ie asset managers, depositaries and administrative agents operating in different EU financial centers¹, assessed during the first semester of 2008 the practical conditions for UCITS funds to receive services from a remote management company (MC) based in a foreign EU member state. Our evaluation has particularly focused on the administrative activities performed by the MC² which are at the heart of the current debate evolving around investor protection and economic issues.

Our overall conclusion at this stage is that implementing a MCP is a feasible and economically attractive objective to improve the efficiency of the EU funds industry but should be implemented with a staged approach.

We consider that conditions for Management Companies (MC) to operate cross-border could be significantly optimized in the short run with an adequate framework of responsibilities defined at Level I. MCs should in particular no longer be required to maintain a capitalized legal entity in the fund domicile to perform their activity which would lead to significant potential savings.

Three main conditions indeed need to be fulfilled for a MC to manage UCITS funds on a remote basis:

- UCITS funds receiving services from a MC based abroad must continue to be managed and administered by the MC in compliance with the relevant rules of the UCITS domicile
- A clear definition of the respective responsibilities of the Fund regulator and of the MC regulator must be possible as well as cooperation mechanisms between regulators and interfaces between regulators, the MC and the depositary
- The conditions required for passporting MC collective portfolio services should generate sufficient economic benefits and not lead to regressions in Member States (MSs) where administrative activities can be widely outsourced on a cross-border basis

The assessments conducted by the Eurofi working group show that there are no major technical obstacles at present for MCs to fulfill these conditions on a remote basis with modern communication means. Most administrative activities involve data processing that can be operationally conducted cross-border. In addition initial proposals were made to define a framework of responsibilities ensuring that investor protection is safeguarded in this context. These principles could be defined at Level I of the Directive and further detailed at Level II:

- The current responsibilities of the Management Company and the Depositary should remain unchanged
- Supervisory responsibilities should be allocated between the Fund regulator and the Management Company regulator with leadership given to the Fund regulator for matters regarding the Fund
- A framework should be defined for cooperation, arbitration and escalation mechanisms between supervisors, applicable to the authorization process and to the on-going monitoring of the fund³.

But a detailed operational analysis of the way administrative activities are conducted on a day-to-day basis shows that the current differences in local laws across EU countries and specific local requirements that impact administrative activities of the fund – eg NAV calculation or fund accounting with differing splits of responsibilities between the MC and the depositary, differing methods, delegation rules etc... - make the remote performance of some services and the maintenance of expertise more complex in a cross-border environment.

¹ AFG, BNP Paribas Investment Partners and Securities Services, The Bank of New York Mellon, CA-CEIS and Crédit Agricole Asset Management, Citi, Deutsche Bank, JPMorgan Asset Management, Schroders, Société Générale Securities Services, Union Investment

² Administrative activities cover: eg fund accounting, NAV calculation, shareholder register maintenance... The other activities conducted by MCs ie investment management and marketing activities are already frequently conducted on a cross-border basis

³ This should be facilitated by the rules for supervisory cooperation described in the UCITS IV proposal

MCs in particular have to have sufficient knowledge of differing and evolving local rules and be able to respond quickly to changing demands on administrative activities and provide possible recourse in case of difficulty.

This is why the Eurofi working group has suggested a staged approach with a transitional period - until sufficient convergence of administrative rules governing administrative activities related to the fund has been achieved – during which the MC would maintain a local representation in the Fund domicile. This local representation would not need to be capitalized and would have the following responsibilities:

- Interface with the counterparts of the MC in the fund domicile: depositary, fund regulator, fund auditor
- Take responsibility for the MC in the fund domicile, in particular that administrative activities relating to the fund are performed and controlled according to fund domicile rules.

Provided MCs can assume these responsibilities they should be free to organize the way they perform administrative activities related to the fund. In particular the local representation should not be required in the directive to perform specific operational activities in the fund domicile.

This proposal applicable in UCITS IV should allow to generate significant savings – at an estimated 250 to 300 Mio € per year corresponding to 30 to 50% of total gains accessible with an effective MCP⁴ - while maintaining effective supervision and investor protection.

Present safeguards for investors provided by the oversight responsibilities of the depositary and compliance with fund domicile rules will indeed be maintained in this context. The local representation will ensure - until legal frameworks are further streamlined - that expertise of fund domicile rules is maintained by the MC. Additionally the depositary and Fund regulator will have an adequate counterpart and possible recourse in the fund domicile.

This will be a significant step towards an effective Management Company Passport (MCP), though further convergence of legal rules governing administrative activities related to the fund – to be initiated in the context of UCITS IV - is needed to:

- Facilitate the oversight of UCITS funds in a cross-border environment with similar fund rules and therefore make the local representation redundant over time.
- Facilitate further economies of scale and concentration of know-how in the longer term which are necessary for exploiting the full potential efficiency gains of the MCP.

A certain number of key issues need to be further assessed, identifying the legal rules on which convergence should apply in priority, detailing the different cooperation and escalation mechanisms between regulators and clarifying the statute of the local representation that could be put in place and the enforceability of the actions conducted by the fund supervisor and the way breaches will be dealt with. Some of these issues should be covered in the advice given by CESR.

⁴ Based on the evaluations of the impact assessment of the EU Commission and on additional data provided by Eurofi group participants: Total potential savings from a MCP should amount to ~500 to 750 Mio € / year. Around 30 to 50% of this amount could be potentially saved in the first stage proposed ie 250 to 300 Mio € / year (corresponding to the cost of capital and cost of managing the legal entity, board of directors, ...). The remaining costs relate to operational activities of the local representation that can be optimized in a second stage once sufficient convergence has been achieved.