



September 29, 2006

Members of the Expert Group on Investment Fund Market Efficiency
European Commission
markt-consult-july-2006expertgroups@ec.europa.eu
Brussels Belgium

Re: Report of the Expert Group on Investment Fund Market Efficiency

Ladies and Gentlemen:

The Financial Services Roundtable (“Roundtable”)¹ appreciates this opportunity to submit written comments on the Report of the Expert Group on Investment Fund Market Efficiency.

The Roundtable supports the Commission’s efforts in the area of Undertakings for the Collective Investment of Transferable Securities (“UCITS”) reform and is pleased to provide the European Commission (“EC”) with these comments as a formal contribution to the ongoing public consultation to facilitate the financial transatlantic dialogue.

In commenting, we hope to share lessons, both good and bad, from the United States (“U.S.”) mutual fund market. More specifically, we provide detailed comments on each of the following five Proposals:

- Reduce Administrative Delays in Getting Investment Funds to Market
- Facilitating UCITS Mergers
- Allowing Pooled Management
- Breathe Life into the Management Company Passport
- Provide More Freedoms for the Depository

Finally, we hope to establish a future dialogue on possible reforms to the European Union (“EU”) framework surrounding UCITS for enhancing the competitive appeal of UCITS on a cross-border basis.

¹ The Financial Services Roundtable represents 100 of the largest integrated financial services companies in the United States providing banking, insurance, investment products and services to the American consumer. Roundtable member companies provide fuel for America’s economic engine accounting directly for \$18.3 trillion in managed assets, \$678 billion in revenue, and 2.1 million jobs. Many of the Roundtable member companies have an international presence.

General Comments

Upon first consideration, the U.S. practitioner might view the current state of UCITS as bearing a considerable resemblance to the U.S. markets prior to Federal preemption and assume that it should be a foregone conclusion that the EU could recognize similar efficiencies *via* cross-border reforms. While the analogy is apt in some respects, upon further review there are significant differences between U.S. and European markets that warrant further discussion.

The U.S. has retained a very strong Federal structure, while the EU framework is more decentralized. To understand the challenges the EU faces with UCITS reform, consider the current U.S. structure, which is based upon Federal preemption of State securities laws. Imagine, for example, that instead of all states or members of a confederation deferring to a federal standard enforced by a central Federal regulator – the Securities and Exchange Commission (“SEC”) – that the U.S. required the State of Texas to accept on good faith that a fund that had met the standards of the State of California was good enough for Texas.

The point is that both the U.S. commentator and the EU practitioner should avoid jumping to the conclusion that the EC should or could mirror U.S. fund market structures too closely. However, the EC can certainly adopt provisions that could have a meaningful and positive competitive impact.

Specific Comments

With the foregoing in mind, the following represents our comments on the five major proposals included in the Report:

1. “Reduce Administrative Delays in Getting Investment Funds to the Market”

In the area of enhancing the current process for authorization of UCITS, we submit that there are valuable lessons to be learned from the U.S. regulatory environment.

- A. Product Approval Deadlines The proposal to limit the time for the home regulator to approve the product, including a review of both the full and summary prospectus, is, from our perspective a good one. Certainty of time allows the product provider and the investor the ability to plan.

However, the proposed timeframes, while admirable, seem ambitious. The general timeframe for adding a new series to an existing investment company in the United States is 75 days. It generally takes the full time to complete the process.

- B. Summary Prospectus Under the proposal, a fund would be able to use the same summary prospectus in all Member States, with any additional information pertaining to an individual state permitted to be added by addendum without triggering additional review either by the home or host state.

The experience in the U.S. with respect to the use of a summary prospectus was not a successful one. In 1998, the SEC permitted the use of a summary prospectus, with the primary goal of reducing confusion for the fund investor. The U.S. “profile prospectus” was meant to be a short-form document, typically running 5-10 pages in contrast to the full prospectus and Statement of Additional Information (“SAI”) that in some instances can run into the hundreds of pages. The profile prospectus was intended to summarize key information, in simplified terms, about the fund in a concise, standardized format to allow the potential investor to evaluate and compare various funds. The information profile included: the fund’s investment objectives and goals; principal investment strategies; principal risks and performance data; fees and expenses; purchase and redemption procedures and other information.

The regulation did not mandate the use of the profile and its use was very limited, largely due to caution from legal experts regarding the potential increased legal liability. There is some sentiment within the U.S. regulatory authority in reviving its use and addressing the liability issue, particularly because the SEC is looking to simplify investor disclosures. Another reason for this is that the SEC, working closely with the U.S. mutual fund industry, has solicited the input of mutual fund investors, most of whom overwhelmingly approve of the simplified prospectus.

Increasingly, U.S. regulators are seeking the input of actual investors when crafting new or enhanced disclosure documents. In addition to its standard comment period, whereby interested parties can comment on proposed rules, the SEC recently conducted its own survey with investors on what constituted “good, plain-English disclosure.” What the SEC learned was that their own simplified proposed forms were still too complicated for the average investor.

- C. Access to Information The hallmark of the U.S. regulatory scheme is “full and fair” disclosure to fund investors. Information regarding any mutual fund is readily available to the press and investors. The U.S. regulators are constantly looking for ways to improve the availability of information.

The disclosure regime in the United States includes information regarding the costs of investing in mutual funds, including a prescribed format for

discussion of fees and performance so that an investor can compare not only these items regarding a particular fund from year to year, but also to allow comparison of one fund to another. The authorization or registration process in the United States also requires detailed disclosure about the fund adviser, including any disciplinary history of the principals of the adviser, to allow the investor to make an informed choice. Distributors of funds also are required to make detailed disclosures and to engage in on-going continuing education to ensure that they are well-versed in the changes in the industry.

Funds and their advisers are required to have dedicated chief compliance officers whose role is to ensure compliance with the entire mutual fund regulatory regime. This recent requirement has focused increased attention and resources on the critical issue of compliance. One way to make the UCITS' market more transparent to investors is to incorporate the chief compliance officer requirement in the EU provisions.

The notion of full and fair disclosure goes hand-in-hand with investor education. The U.S. regulatory authority spends much time providing meaningful tools for investors in funds so that they can make informed investment decisions. Some of these tools include investor alerts, the mutual fund fee calculator and educational forums, some aimed at youngsters to start their financial educations early. We encourage those interested to visit the SEC's website at <http://sec.gov/investor.shtml> for a quick preview of the types of investor education materials available. The SEC also encourages the mutual funds themselves to provide educational tools for investors.

On a related note, in the United States, there is much transparency regarding the positions of the regulatory authorities (such as the published positions of the SEC, including no-action letters). The EC might consider whether there is a way to make regulatory thinking more transparent to the industry.

Along the lines of increasing information transparency, one initiative that could substantially benefit efforts to reduce administrative delays and the expense of bringing funds to market is to consider adoption of an online disclosure warehouse. The U.S. markets have done so for approximately ten years. The U.S. system is called EDGAR (Electronic Data Gathering, Analysis and Retrieval system), and contains most filings (registration statements, periodic reports, and other forms) submitted to the SEC by public companies, including funds. Anyone can access and download this information for free. In addition to enhancing disclosure, this enables rapid assessment of industry practice. The service can be found at <http://www.sec.gov/edgar.shtml>.

D. Additional Disclosure/Information Issues As noted above, the U.S. regulators are constantly striving to find new and innovative ways to make information available to investors. The most recent proposed innovations are the “Point of Sale” and “Profile Plus” currently under consideration by the SEC and NASD. The most interesting aspect of these reforms is that at their heart is a call for the SEC to adopt an “access equals delivery” standard that would allow firms to satisfy their disclosure requirements by posting the relevant information on the internet. The U.S. regulators’ view of electronic delivery has evolved substantially over the years, but allowing access in lieu of actual “delivery” *per se* is a relatively recent step.

Although the NASD’s Mutual Fund Task Force endorsed the “access equals delivery” approach, the SEC has not been inclined to adopt this approach in its totality. It has, however, been amenable to certain aspects. The revised proposals would permit certain types of disclosures to be provided online, including information regarding revenue sharing, certain payments from issuer assets, other distribution related information and broker-dealer compensation. The SEC has also stressed that the new requirements are not to be considered a safe harbor from the broad antifraud provisions of the securities laws. Rather, they are a minimum standard which must be observed. The new disclosures also require that firms disclose certain information regarding their conflicts of interest.

2. “Facilitating UCITS Mergers”

There is currently no provision for UCITS to merge with each other on a cross-border basis.

The European funds market has only two-thirds as many assets as the U.S. market, yet it has over three times as many funds. This is presumably at least in part because of the difficulty in effecting fund mergers for UCITS, whereas in the U.S., fund mergers are common industry practice. In fact, last year alone 222 mutual funds were absorbed into other funds in the U.S., a trend which is expected to continue. It is accepted within the U.S. markets that mergers create economies of scale, and enable funds to trim operating costs, including those relating to fund audits and prospectuses, among others. For example, last year, Bank of America’s Columbia Management unit combined its Tax Managed Growth Fund I, which had an expense ratio of 1.31 percent, with its Tax managed Growth Fund II, with expenses of 1.49 percent, to create a combined fund with a lower expense ratio of 1.22 percent.

Creating a structure for cross-border UCITS mergers would certainly be beneficial not only to the industry but also to investors. One avenue the EC may wish to consider is having a uniform standard for determining voting rights, valuation

issues, appropriate performance measurement, and exchange ratios, as this could make enacting fund merger provisions easier and help eliminate the tendency of the industry to “shop” for the jurisdiction permitting, for example, the perceived best performance for the surviving fund.

Adopting uniform standards does not eliminate complexity, however. In the U.S. fund managers must keep a keen eye to pending mergers, in some cases even “managing to the merger.” For example, if one fund merger party has embedded taxable gains, and the other does not, the investors of the latter fund could get stuck with embedded taxable gains of the survivor from which they never benefited. Additionally, fund mergers can depress the performance of an acquiring fund. Mergers of funds with dissimilar investment strategies can also throw off shareholder investment objectives. All of these issues should be taken into consideration when contemplating fund mergers. While complex to achieve, allowing for rapid and efficient merger of funds would be key to helping UCITS become more competitive. However, one’s perception of what is “rapid and efficient” should be tempered. Even the most experienced large complexes in the United States, where mergers are fairly common, typically take a full year to effect fund mergers.

In the U.S., fund mergers require the approval of the acquired fund’s shareholders, as well as the directors of both funds. The shareholders of the acquiring fund, however, are not entitled to vote.

3. “Allowing Pooled Management”

The lack of a provision for master–feeder types of structures within the UCITS directive is a potential barrier to entry for providers within, as well as outside of, the EU. Such a provision could greatly increase European investors’ access to additional investment choices, would foster competition with U.S. funds and otherwise increase UCITS investor satisfaction, without the expense of setting up mirror funds.

Master-feeder structures offer many benefits to both investors and managers, including elimination of trade allocation issues among feeder funds, providing “critical mass” at the master level to reduce both startup and ongoing costs for feeders (as well as increasing access to credit lines), and facilitating creation of new feeders to accommodate demand within specific market segments (e.g., adding an institutional feeder or even a “private label” feeder).

There are several cautionary notes regarding master-feeder structures as well. For example, for an existing fund to become a feeder, its portfolio of securities would typically either be liquidated, or contributed in kind to the master. This can have tax consequences.

From the U.S. experience, the trickiest issue in managing a master-feeder structure is determining which fees and services go to which level. Additionally, overall fee levels must be reasonable – that is, a fund must be careful not to overload both levels with fees. Generally, it may be more workable to assess certain fees at the feeder level to avoid inequities that can result if the fees are charged at the master level. The EC would be well advised to make critical decisions around permitted fee structures in advance of adopting this reform.

4. “Breathe Life Into the Management Company Passport”

Due to the centralized market within the U.S., we have no basis for comment.

5. “Provide More Freedoms for the Depositary”

Under the UCITS structure, the depositary institution is roughly analogous to the custodian within the U.S. fund structure. The depositary, however, serves a more robust governance function than a U.S. custodian, including certain fiduciary functions more typically falling to the fund board in the U.S. (including oversight of net asset value of the fund, among other items).

This topic, as well, is one with little analogy to the U.S. market, because of the major differences between the depositary and a U.S. custodian. Therefore, it is hard to offer any parallels in the U.S. structure, or suggest best practices.

Conclusion:

Although all of the proposed UCITS reforms would increase business opportunities for U.S. firms in the EU, more importantly, they would increase business opportunities for EU firms within Europe and enhance their competitiveness with U.S. funds. To the extent that the proposed reforms make EU funds more readily available to investors and increase investors’ understanding of the products, the world marketplace benefits.

The Financial Services Roundtable applauds the efforts of the EC and the Expert Group in taking on this significant effort in such a thorough and transparent manner. We thank you for the opportunity to contribute to this important dialogue. Please feel free to contact us if we can provide further assistance.

Sincerely,

Richard M. Whiting

Richard M. Whiting
Executive Director and General Counsel