

# **Expert Working Group on investment fund market efficiency: Terms of Reference**

## **1. Background**

The European market for UCITS<sup>1</sup> has grown rapidly in the last decade. Since 1994, assets under management have experienced a nearly four-fold increase and the number of funds has multiplied by nearly three. In June 2005, asset managed by UCITS amounted to €4.7 trillion or some 75-80% of the assets under management by the whole European investment fund industry.

Integration of the UCITS market has also progressed in recent years. The number of cross-border funds has more than doubled since 1998. Today, 17 % of UCITS are true cross-border funds and are attracting an increasing share of new sales.

However, viewed from the perspective of overall market efficiency, the sector's potential is not yet fully exploited. The landscape remains dominated by funds of sub-optimal size. European funds are on average 5 times smaller than their average US counterpart. As a result, the fund industry is not able to benefit fully from scale economies. This translates into relatively higher Total Expense Ratios (TERs) which lead, at the end of the day, to lower net returns to end-investors.

The Commission Green Paper on the enhancement of the EU framework for investment funds has identified some avenues towards a cost-efficient fund industry including: cross-border fund mergers; pooling; management company passport; greater freedom to choose a depositary; and standardisation of fund units processing. The role of the expert group will be to move forward the on-going debate on these (and possibly other) avenues to promote a more efficient and competitive European fund industry.

## **2. Mandate for the expert group**

### **2.1 Objective**

The expert group's objective is to advise the Commission on cost-effective ways to support a more efficient organisation of different stages in the European fund value-chain. The Group's assessment could consider options other than those mentioned above.

The Group will provide technical, commercial and market analysis that could serve as a basis for debate with Member States and other stakeholders. The Group's work will also provide qualitative and, where possible, quantitative input to guide reflections on:

- How proposed EU level action(s) would assist in the realisation of efficiency-enhancing commercial freedoms for fund managers or other actors in the fund value-chain, having regards to any possible implications for the levels of investor protection;
- Form and focus of such actions;
- Consequences and potential costs associated with these actions.

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<sup>1</sup> Undertakings for Collective Investments in Transferable Securities

## 2.2 Output

The expert group shall produce a report advising the European Commission which will be made public as a basis for discussion with Member State authorities, EU bodies and other stakeholders, in particular consumers/investors associations. The report shall reflect the consensus view of members of the group. The report shall not be considered as reflecting the views of the Commission services nor be binding on those.

## 2.3 Indicative analytical framework

### *a. Problem identification and prioritisation of possible solutions*

The Group will identify those features of the industry landscape or value-chain (fund design, management, administration, oversight, distribution) which cannot be organised/rationalised on a cross-border basis. It shall explore the extent to which the absence of such possibilities translates into higher costs for market participants, clients and/or investors.

In a first instance, the group shall provide a broad-brush indication of the commercial freedoms which they wish to investigate. The Group shall indicate clearly (and supported by documentary evidence) how the absence of these single market freedoms gives rise to extra cost/inefficiency (benchmarks to be defined) having regards to any possible implications for the levels of investor protection.

The experts will then agree on a prioritisation of the identified efficiency channels, indicating which ones require greater attention and why. This shall include an assessment of the likely take-up of envisaged freedoms, and a reasoned description of potential implications for business models and the organisation of the European investment fund industry. On this basis, the Group would work in the form of sub-groups focussing on higher priority solutions.

### *b. In-depth analysis of each alternative*

Working at sub-group level, experts will:

- Further refine or specify the alternative that is envisaged in clear commercial, legal and technical terms;
- identify the main hurdles preventing the identified solution to be successfully implemented. They will indicate the type of obstacles (tax, legal, organisational...) and give an indication of the relative importance of each of those;
- Identify options for addressing the identified problems and the actors who are best placed to give effect to them (national/EU authorities; industry), taking account also of impacts on other stakeholders including investors
- Exploring the merits and demerits of various options (where options have been identified) or possible solutions. Does it effectively solve the problems identified? How it will do so? A key consideration will be to assess the cost-effectiveness of envisaged solutions and to examine whether it represents a superior outcome to 'do nothing' option.

### *c. Policy recommendations*

On the basis of the above analysis, the Group will advise on possible cost-effective ways to improve materially the efficiency of the EU market for investment funds, while maintaining a

high level of investor protection. In line with those conclusions, the Group will put forward policy recommendations to the Commission.

These will be reflected in the Group's final report. The report will be made public. The Group's conclusions/recommendations will not necessarily reflect the views of the Commission or its services.

### **3. Practical modalities for composition and operation**

#### **3.1 Composition**

The Group will comprise a maximum of 25 experts. It will be composed on the basis of proposals received from representative trade associations of the EU investment fund industry, particularly those having particular expertise in respect of the issues covered by these terms of reference.

#### **3.2 Call for expressions of interest from trade associations:**

Upon adoption of the Commission decision to create the Group, the Commission services will publish a call for expressions of interest from interested trade associations which can mobilise relevant expertise in respect of the issues governed by these terms of reference. Associations wishing to propose experts to the Group shall express their interest in the form of a written correspondence, to be posted to the Commission not later than 30 December 2005. The expression of interest must be accompanied by the list of prospective experts which the association wishes to put forward for consideration as possible members. The submission must therefore include relevant information to allow the Commission to assess the suitability/expertise of the proposed individual expert having reference to the criteria set out below.

Trade associations must represent the interests of all or part of the EU investment fund industry. These associations should have a pan-European scope or at least cover a representative number of Member States. Priority will be given to experts proposed by trade associations having such a pan-European dimension. However, national associations representing the interest of a particular function/actor (administration, management, custody, distribution...) within the fund industry value-chain could be invited to designate an expert if such a function/actor is not adequately represented at a pan-European level. The Commission shall also have to ensure that the interests and situation of small, locally-oriented operators are reflected in the composition of the expert groups.

Each tendering association or representative body is free to propose the number and of experts that it considers appropriate in view of its scope of activities, membership, and the number functions within the industry value-chain covered.

#### ***Criteria governing the selection of experts:***

- The experts proposed by each association must have recent, direct professional expertise in respect of the issues covered by these terms of reference. In particular, proposed experts should have relevant direct experience— from an earnings-generating and/or cost-management capacity – in business projects or matters which equip them with commercial or technical insights needed to develop solutions to the issues raised by this terms of reference.

- Proposed experts should also play a key role in shaping the views of their parent organisation or the trade association in respect of these matters.

Individual proposals should therefore be accompanied by material demonstrating that the expert put forward meets the above conditions.

Individual experts shall also be proficient in a language which is customary in the sphere of finance, at a level which allows them to contribute to discussions and report drafting in that language.

### **3.3 Final determination of group composition**

The Commission shall decide upon the final composition of the group on the basis of eligible proposals submitted by trade associations which respond to the call for the expressions of interest.

The Commission shall select the proposed experts who best embody the required commercial and technical expertise in respect of the matters covered by the mandate for the expert group, as evidenced by prior experience in proposing or implementing solutions to these problems within their parent organisation or sponsoring association.

The Commission will also seek to ensure that the group composition spans the range of relevant functions within the industry value-chain given the issues raised by these terms of reference. The Commission will also wish to ensure an appropriate multi-disciplinary mix within the group.

In making the final selection of group members based on the basis of submitted proposals, the Commission shall be guided by the need to ensure that, in addition to covering all main areas of expertise, the Group has, to the greatest extent possible, a balanced geographical and gender composition. Geographical representation shall mean ensuring a fair spread of experts, taking account of the distribution of the relevant activities, and relevant commercial experience, across the single market.

However, the over-riding criterion will always be the extent to which individual experts have a track-record in dealing with commercial projects or problems of the type arising from the mandate.

Once the Commission services have arrived at a definitive selection of group members, they shall advise all sponsoring associations of their decision. The list of expert group members shall be made public on DG Internal Market and Services website prior to the commencement of its work.

### **3.4 Duration and location**

The Group's activities will begin in early 2006. The Group is established for 6 months. The Commission may extend this period if considered necessary to complete the Group's work.

Four to five plenary meetings will take place in Brussels on the Commission premises in accordance with the procedures and schedule established by it.

Sub-groups' meetings/discussions may be held at other locations or via other communication means such as conference calls and/or e-mail exchanges.

### **3.5 Operation**

The Commission shall Chair the group. The Commission provides secretarial services. The group shall adopt its rules of procedure on the basis of the standard rules of procedure adopted by the Commission.

In agreement with the Commission, sub-groups may be set up to examine specific questions under these terms of reference; they shall be disbanded as soon as these have been fulfilled. Sub-groups will appoint a “facilitator” that will, in collaboration with the Commission representative(s), chair the sub-group’s debates.

The Commission may ask experts or observers with specific competence on a subject on the agenda to participate in the group’s or sub-group’s deliberations if this is useful and/or necessary. The Commission will, in particular, invite observer(s) from consumers/investors associations. Other Commission officials with an interest in the proceedings may attend these meetings.

Members of the Group will remain in office until such time as they are replaced or their mandate is renewed. Members who are or are deemed to be no longer able to contribute effectively to the Group’s deliberations may be replaced for the remaining period of their mandate. The above mentioned selection criteria should be respected when nominating new members.

Information obtained by participating in the group’s or sub-group’s deliberations may not be divulged where the Commission lays down that this relates to confidential matters.

The Commission may publish on the DG Internal Market and Services website, after consultation with the group, in the original language of the document concerned, any résumé, conclusion, or partial conclusion or working document of the group.

### **3.6 Expenses of group members**

The Commission shall reimburse travel and subsistence expenses for its members in connection with the group’s activities in accordance with the provisions in force at the Commission. The members shall not be paid for their duties.