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Report

drawn up on behalf of the Legal Affairs Committee

on the proposal from the Commission of the European Communities to the Council (Doc. 114/76) for a directive for the coordination of laws, regulations and administrative provisions regarding collective investment undertakings for transferable securities

Rapporteur: Lord ARDWICK

PE 46.460/fin.

By letter of 13 May 1976, the President of the Council of the European Communities requested the European Parliament, pursuant to Article 54 of the EEC Treaty, to deliver an opinion on the proposal from the Commission of the European Communities to the Council for a directive for the coordination of laws, regulations and administrative provisions regarding collective investment undertakings for transferable securities.

On 25 May 1976 the President of the European Parliament referred this proposal to the Legal Affairs Committee as the committee responsible and to the Committee on Economic and Monetary Affairs for its opinion.

On 31 May 1976 the Legal Affairs Committee appointed Lord Ardwick rapporteur.

It considered this proposal at its meetings of 20 September 1976, 25 November 1976 and 20 January 1977.

At its meeting of 20 January 1977 the committee adopted the motion for a resolution and explanatory statement with twelve votes in favour and one abstention.

Present : Sir Derek Walker-Smith, chairman; Lord Ardwick, rapporteur; Mr Berkhouwer (deputizing for Mr Pianta); Mr Broeksz, Mr De Keersmaeker, Mr Lautenschlager, Lord Murray of Gravesend, Mr Mursch (deputizing for Mr Poher); Sir Brandon Rhys Williams, Mr Riz, Mr Scelba, Mr Shaw and Mr Walkhoff.

The opinion of the Committee on Economic and Monetary Affairs is attached.

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The Legal Affairs Committee hereby submits to the European Parliament the following motion for a resolution together with explanatory statement :

MOTION FOR A RESOLUTION

embodying the opinion of the European Parliament on the proposal from the Commission of the European Communities to the Council for a directive coordinating the laws, regulations and administrative provisions regarding collective investment undertakings for transferable securities

The European Parliament,

- having regard to the proposal from the Commission of the European Communities to the Council¹,
 - having been consulted by the Council pursuant to Article 54 of the EEC Treaty (Doc. 114/76),
 - having regard to the report of the Legal Affairs Committee and the opinion of the Committee on Economic and Monetary Affairs (Doc. 532/76),
1. Welcomes the proposed directive as a necessary preliminary to the establishment of the free movement of units of CIUTS within the Community;
 2. Looks forward to being consulted upon the proposal on which the Commission is currently working for a directive specifically providing for increased freedom of movement of such units;
 3. Notes, however, that the co-ordination measures contained in the proposed directive are incomplete, as each Member State will continue to apply its own marketing regulations to units of CIUTS marketed on its territory;

¹ OJ No. C171, 26.7.76, p.1

4. Notes that no provision has been made for the harmonization of administrative procedures;
5. Asks the Commission to take steps to study the practices adopted in regard to fees and charges, which are not generally dealt with in the proposal;
6. Calls upon the Commission, pursuant to the second paragraph of Article 149 of the EEC Treaty, to incorporate the following amendments in its proposal :

Proposal for a Council directive
for the coordination of
laws, regulations and administrative provisions
regarding collective investment undertakings
for transferable securities of the open-ended type

Preamble and recitals unchanged

Article 1

1. Member States shall apply the provisions of this directive to collective investment undertakings for transferable securities (CIUTS) situated within their territories.
2. Subject to provisions relating to the movement of capital and to Articles 55(1) and 61(2) of this directive, a Member State shall not apply any provisions whatsoever to CIUTS situated in another Member State or to the units issued by such CIUTS.
3. Member States may apply to CIUTS situated within their territories requirements which are stricter than or additional to those provided in Article 5 et seq of this directive, provided that they are of general application and do not conflict with the provisions of this directive.

Article 1

1. unchanged
2. Subject to its national provisions relating to the movement of capital and to Articles 55(1) and 61(2) of this directive Member State 'A' shall not apply any provisions to CIUTS situated in Member State 'B' which market their units in Member State 'A', or to the units issued by such CIUTS.

3. Unchanged

Articles 2-4 unchanged

Article 5

1. A CIUTS shall not carry on activities unless it has been authorized by the competent authorities. Such authorization shall be valid for all Member States.

Article 5

1. A CIUTS shall not carry on activities unless it has been authorized by the competent authorities. A CIUTS once authorized may operate in all the Member States without further authorization.

¹For full text, see OJ No. C 171, 26.7.1976, p. 1

2. A unit trust shall only be authorised if the competent authorities have approved the management company, the fund rules and the choice of depositary company. An investment company shall only be authorised if the competent authorities have approved both the memorandum and articles of association and the choice of depositary company.

2. unchanged

3. The competent authorities shall not authorise a CIUTS if the directors of the management company, the investment company or the depositary company are not of good repute or are not competent to carry out their duties. To this end, the names of the directors of the management company and of the investment company and of every person succeeding them in the office shall be notified immediately to the competent authorities. The same shall apply to the directors of the depositary company, unless such notification has already been given to other authorities of the Member States in which the CIUTS is situated.

3. The competent authorities shall not authorise a CIUTS if the directors of the management company, the investment company or the depositary company are not of good repute or are not competent to carry out their duties. To this end, the names of the directors of the management company and of the investment company and of every person succeeding them in the office shall be notified immediately to the competent authorities. The same shall apply to the directors of the depositary company (20 words deleted).

Articles 6 - 14 unchanged

Article 15

The assets of a unit trust may not be the subject of any claim whatsoever by persons other than the management company and the unit holders.

Article 15

Only the management company and the unit holders may make a claim against the assets of a unit trust.

In all cases claims by the management company or the unit holders may only be satisfied from the assets of the unit trust where there are charges expressly attaching to these assets under the law or the fund rules.

Unchanged

Articles 16 - 26 unchanged

Article 27

1. A CIUTS shall not invest more than 10% of its assets in units issued by other CIUTS.
2. Without prejudice to paragraph 1 a unit trust shall not invest more than 5% of its assets in the units of other unit trusts managed by the same management company as its own, and in such cases charging of further costs shall be prohibited.

Article 27

1. unchanged
2. Notwithstanding paragraph 1 a unit trust shall not invest more than 15% of its assets in the units of other unit trusts managed by the same management company as its own, and in such cases charging of further costs shall be prohibited.

3. Subject to paragraph 2, whenever a CIUTS invests part of its assets in the units of another CIUTS, any charging of further costs shall be shown in the periodical reports referred to in Article 31.

Articles 28 - 29 unchanged

Article 30

1. The limits provided for in Articles 25(2), 26(1) and (2) and 27(1) and (2) may be exceeded on condition that any such excess stems from price variations in the assets of the CIUTS, the exercise by the CIUTS of subscription rights relating to securities making up its assets, or from a contraction in size by the CIUTS, and on condition that the total value of the excess is not more than 10% of the value of the assets of the CIUTS

Article 30

1. unchanged

2. Should the total value of the excess amount at any time to more than 10% of the value of the assets of the CIUTS, it shall be reduced to 10% within the following six months.

Article 31

1. The CIUTS shall publish:
- a prospectus and, each financial year,
- an annual report
- and two half-yearly reports.
2. The annual and half-yearly reports shall be published within the following limits from the end of the period to which they refer:
- 4 months for the annual report
- 2 months for the half-yearly reports.
3. By way of derogation from paragraph 1, the CIUTS shall not be obliged to publish the half-yearly reports relating to the second six-month period of the financial year if the annual report for that financial year is published during the two month period.

Article 31

1. unchanged

2. unchanged

3. By way of derogation from paragraph 1, the CIUTS shall not be obliged to publish the half-yearly reports relating to the second six-month period of the financial year if the annual report for that financial year is published during the two month period which is prescribed for the publication of the second half-yearly report.

Articles 32-35 unchanged

Article 36

1. Member States shall specify the independent persons or the bodies whose duty it is to verify the financial data contained in the annual reports.
2. Each annual report shall indicate precisely the person or body whose duty it is to verify the financial data.

Article 36

1. Member States shall specify the independent persons or the bodies whose duty it is to inspect and check the financial data contained in the annual reports.

2. Unchanged

Articles 37 - 40 unchanged

Article 41

1. A CIUTS shall not borrow
2. Paragraph 1 notwithstanding, Member States may provide that the competent authorities may permit:
 - a) CIUTS to borrow funds up to 10% of the value of their assets for the repurchase or redemption of their units or for the exercise of subscription rights, on condition that the funds borrowed are repaid within a short period and are not secured by a charge on the assets of the CIUTS
 - b) investment companies to borrow funds to acquire buildings which are necessary in order to carry on their business.

Article 41

1. unchanged
2. Paragraph 1 notwithstanding, Member States may provide that the competent authorities may permit:
 - a) CIUTS to borrow funds up to 10% of the value of their assets for the repurchase or redemption of their units or for the exercise of subscription rights, or for the purchase of foreign currency in order to purchase foreign securities, on condition that the funds borrowed are repaid within a short period and are not secured by a charge on the assets of the CIUTS
 - b) investment companies to borrow funds to acquire such buildings as are strictly necessary for them in order to carry on their business.

Articles 42-49 unchanged

Article 50

The following persons:

- the management company and the depositary company;
- the directors and staff of these companies or of the investment company;
- subsidiaries of the management company or depositary company;
- the investment advisers of the management company, the investment company, or the depositary company;
- any persons holding more than 10% of the voting rights in the management company, investment company or depositary company,

shall not act as a party to transactions effected on behalf of a CIUTS unless such transactions concern transferable securities and are carried out:

a) at a price which is equal to or more advantageous for the unit-holders than the price of the official quotation of a stock exchange, if the transferable securities involved have been admitted to its quotation;

b) at a price which is equal to or more advantageous for the unit-holders than that observed on any other regulated market which operates regularly and is recognised and open to the public, if the transferable securities involved have been traded on this market;

c) at the price calculated in accordance with regulations laid down by the fund rules or the memorandum and articles of association of the investment company in the case of transferable securities other than those referred to in subparagraphs a) and b);

d) at the issue price to the public in the case of new issues in respect of which the depositary company acts as an intermediary.

Article 50

The following persons:

- the management company and the depositary company;
- the directors and staff of these companies or of the investment company;
- subsidiaries of the management company or depositary company;
- the investment advisers of the management company, the investment company, or the depositary company;
- any persons holding more than 10% of the voting rights in the management company, investment company or depositary company,

shall not directly or indirectly act as a party to transactions effected on behalf of a CIUTS unless such transactions concern transferable securities and are carried out:

a) unchanged

b) unchanged

c) unchanged

d) unchanged

Article 54

1. If a CIUTS intends to market its units in a Member State other than that in which it is situated, it shall notify such intention to the competent authorities as well as the authorities of the other Member State.
2. In the case referred to in paragraph 1, the CIUTS must possess financial facilities in the other Member State through which the unit-holders may exercise their rights.

Article 54

1. By way of derogation from Article 1(2), a Member State may apply its own marketing regulations to CIUTS situated in other Member States and marketing or intending to market their units in its territory.
2. For the purposes of paragraph 1, the term "marketing regulations" shall cover mainly:
 - a) the rules relating to entries in trade registers;
 - b) the rules relating to sales promotion;
 - c) the rules relating to unfair competition;
 - d) the rules relating to canvassing or other marketing techniques;
 - e) the rules governing the various forms of savings plan.
3. The marketing regulations referred to in paragraph 1 shall be applied in a non-discriminatory manner and must not have the effect of imposing on CIUTS situated in other Member States stricter conditions than those envisaged in this directive.

Article 55

1. By way of derogation from Article 1(2), a Member State may apply its own marketing regulations to CIUTS situated in other Member States and marketing or intending to market their units in its territory.
2. For the purposes of paragraph 1, the term "marketing regulations" shall cover mainly:
 - a) the rules relating to entries in trade registers;
 - b) the rules relating to sales promotion;
 - c) the rules relating to unfair competition;
 - d) the rules relating to canvassing or other marketing techniques;
 - e) the rules governing the various forms of savings plan.

Article 55

1. If a CIUTS intends to market its units in a Member State other than that in which it is situated, it shall notify such intention to the competent authorities as well as the authorities of the other Member State.
2. In the case referred to in paragraph 1, the CIUTS must possess financial facilities in the other Member State through which the unit-holders may exercise their rights.

3. The marketing regulations referred to in paragraph 1 shall be applied in a non-discriminatory manner and must not have the effect of imposing on CIUTS situated in other Member States stricter conditions than those envisaged in this directive.
3. deleted

Articles 56-71, unchanged

Article 72

Member States shall ensure that the Commission is notified of the text of essential provisions subsequently adopted under national law in the fields covered by this directive.

Article 72

Member States shall ensure that the Commission is notified of the text of essential provisions which they intend to adopt or adopt under national law in the fields covered by this directive.

Article 73 unchanged

EXPLANATORY STATEMENTI. BACKGROUND TO THE PROPOSAL

1. During the past ten years, mutual Funds in Europe and the United States have become an important factor in long-term investment markets. The structure of the Funds differs from one country to another, but all have a variable capital structure, with capital waxing as sales increase and waning as redemptions increase. These collective investment undertakings (CIUTS) gather the funds of as many savers as possible by issuing units. The funds thus obtained are invested in securities or other assets on the principle of risk spreading. The unit price, usually calculated each day, is obtained by dividing the net asset value of the portfolio by the number of units in issue. The dividends on the investments of the Fund are distributed to holders in accordance with the size of their holdings.

2. These institutions offer savers the advantages of a wide spread of investments made after experts have carried out careful comparisons, which would often be difficult for the individual saver to make, particularly comparisons of the opportunities presented in foreign markets. Units are marketed by means of offers to the public, often directed at small inexperienced savers who therefore require a high degree of protection. Many countries have accordingly adopted special rules for the control of collective investment undertakings.

3. These Funds are usually operated by a management company and a depositary company, on the basis of a contract between the two. The contract may, as in the United Kingdom, constitute a trust deed whereby the depositary company is a trustee. France is an exception here, as its mutual Funds are joint stock companies with variable capital and there are no management companies. Generally the management company is a joint stock company whose shares are owned by the sponsors, a bank, a life assurance company or perhaps a syndicate of financial institutions. The role of the management company is to supervise the selection of the portfolio, the advertizing, buying and selling of units and the payment of dividends to subscribers. The role of the depositary company is to inspect the advertisements, see that the portfolio is safely kept and generally to act as watchdog for the subscribers.

4. Although in most Member States, the legal requirements for the operation of Funds are clearly defined, they are far from uniform. The Commission wishes to coordinate Member States' legislation in this field on the basis of common rules:

- (a) to bring about more uniform and effective safeguards for savers.
- (b) to ensure more uniform conditions of competition.

Your committee agrees with these reasons.

The Community must be concerned to give the small saver both the protection he needs and the best opportunities for saving. A legislative framework possessing some uniformity that leaves open the possibilities of innovation is therefore needed. For mutual funds are no longer the modest yielding goldmine they once appeared to be to the small investor. Sad experience has destroyed the faith that once existed in equities as a hedge against inflation, whilst the bond market has suffered severe fluctuations. The failure of I.O.S. involved a million German investors, owing to the liberality of German laws at the time, and led to a loss of confidence in funds in that country.

- (c) to promote at Community level more thorough penetration of markets in transferable securities.

The proposed coordination here is also a step on the way towards removing restrictions on the free movement within the Community of units of CIUTS. Because of differences in the rules of Member States, there has been reluctance to allow these units to be traded freely across borders. This obstacle to the opening up of frontiers must be removed before free movement of capital can be established in this sector. The Commission intends to present a proposal to the Council for an additional directive to ensure, when it becomes feasible, the necessary freedom of movement for units of CIUTS in order that the present directive may have the maximum effect.

If a European capital market is ever to be realized it will be essential to have something like a uniform supervision of the investing institutions. At this point your committee must stress that the proposed directive prepares largely for a future eventuality on what no date can as yet be put; the day when free movement of capital between Member States can be permitted.

II. SUMMARY OF THE PROPOSAL

a. Scope of the proposal

5. The proposed rules cover the structure, operations, functions and limitations of mutual funds. Most importantly they also cover their investment policy and what the public must be told about them.

There are two groups of collective investment undertakings for transferable securities:

- (1) closed end
- (2) open end

The proposal applies only to the latter as the former are less numerous and in general are subject to company law. Open ended CIUTS are of two types:

- (a) having a corporate structure (investment companies)
- (b) having a non-corporate structure, i.e. contractual or trust (unit trusts)

Unit trusts are institutions without legal personality.

The Commission's proposal covers only investment companies or unit trusts:

- (i) which invest in transferable securities or retain as liquid assets at least 80% of the capital they collect
- (ii) which accumulate this capital by means of offers to the public
- (iii) which operate on the principle of risk spreading
- (iv) whose units are or have been issued continuously or in blocks at short intervals and/or are directly or indirectly repurchased or redeemed at the request of the holder using the assets of these undertakings (Article 2)

b. Principles of coordination

6. The proposal requires the Member States to apply a number of minimum rules to CIUTS situated¹ on their territory, regardless of whether they

¹ CIUTS are situated, for the purposes of the proposal, in the Member State in which their management is effectively carried on (Article 3)

operate in one or more Member States. Stricter and/or additional requirements, if of general application and not in conflict with the provisions of the directive, may also be applied to such CIUTS, but not to those situated in another Member State (Article 1). CIUTS will therefore, as a general rule, be governed exclusively by the legislation of the Member State in which they are situated. This legislation must comply with the minimum rules laid down in the proposal.

A CIUTS must seek authorisation to trade from the competent body in the Member State in which it is situated and, once it has obtained this, it will be able to market its units in any Member State without further authorisation. The body granting the authorization must supervise the activities throughout the territory of the Community of CIUTS situated on their national territory (Article 58). There are two exceptions to this general principle. They concern:

- (a) provisions governing capital movements.
- (b) marketing of units.

The proposal provides that when units of a CIUTS based in Member State A are marketed in Member State B, the latter may apply its own marketing regulations. The competent body in the Member State where the units are marketed will supervise the application of marketing regulations. Such regulations must, however, be applied in a non-discriminatory manner and may not impose on CIUTS based in another Member State stricter conditions than those envisaged in Article 55 of the proposal.

c. Contents of the proposal

7. The proposal contains rules relating to:

A) Structure of unit trusts and investment companies

Some examples are:

- (i) activities of the management company to be confined to the management of the unit trusts (Article 8)
- (ii) supervision by the depositary company of certain activities of the management company or investment company (Article 10)
- (iii) depositary company to have its registered office in the same Member State as that where the CIUTS is situated, or be established in, or have a centre of activity in, that Member State if it has its registered office in another Member State

(iv) depositary company to be responsible for the custody of the transferable securities and liquid assets constituting the assets of the CIUTS (Article 10). (It is to be noted that the depositary company has less extensive responsibilities than the depositary company of the unit trust).

- B) Composition of the assets of the CIUTS
- C) The investment policy of CIUTS (Articles 25-30)
- D) Information to be disclosed by CIUTS (Articles 31-40)
- E) General obligations to be fulfilled by CIUTS (Articles 41-53)
- F) CIUTS which market their units in a Member State other than that in which they are situated (Articles 54-57)
- G) The duties of the body responsible for authorising and supervising the CIUTS (Articles 58-62)
- H) The setting up of a liaison committee to be composed of representatives of the Member States and the Commission (Article 66). The task of the committee will be to facilitate consultation between Member States relating in particular to practical problems encountered in implementing the directive and to the stricter or additional requirements of the marketing rules which Member States may apply under the directive. The committee will also advise the Commission as necessary on additions or amendments to the directive.

III. OBSERVATIONS ON THE PROPOSAL

a. General Principles

8. Your committee suggests that any criticism of the proposal should be made with a certain amount of modesty. When account is taken of the differences in the operation of CIUTS in the Member States one realises that expert experience is necessary to evaluate fully the wisdom of the Commission's proposal. Parliament has in fact come in at a late stage in a very complex debate which national and international organisations representing CIUTS have been engaged in with officials in Member States and with the Commission.

9. It would be preferable for the words "of the open ended type" to be added to the title of the proposal as it in fact deals only with undertakings of this sort.

10. On page 8 of the explanatory memorandum the Commission has set out a number of objectives which the proposal is designed to achieve. It appears that all these objectives are regarded as being of equal importance.

11. The Commission considers that if the proposal were not sufficiently strict so that savers in the Community were not sufficiently protected, the directive would fail to achieve its purpose.

12. The Liaison Committee is provided for in Article 66 of the proposal. Its task is to facilitate the implementation of the directive through consultation between Member States, particularly where practical problems arise ; to facilitate consultation as regards the stricter or supplementary requirements and the marketing rules which Member States may impose ; to advise the Commission, if necessary, on additions or amendments to the directive. The Committee is to be composed of representatives of the Member States and the Commission and to be presided over by a representative of the Commission, which will also supply the Secretariat.

This Committee should make a very valuable contribution to the smooth implementation of the directive, in view of the considerable differences between the legislation of Member States which will remain in existence. It therefore has important work to do. The details given in relation to the Committee in Article 66 are somewhat incomplete, as Annex C to the proposal shows. The Commission, however,

envisages that once the members have been appointed, further details will be settled at the first, or subsequent, meetings. Your committee hopes that the Committee's first meeting will be held as soon as possible after the directive comes into force and that members of professional bodies will be able to participate in all meetings of the Committee.

13. The objection has been raised that the fact that a Member State may apply its own marketing regulations to undertakings situated in other Member States means that two systems of law will be applied to undertakings marketing their shares or units in a country other than that in which they are situated. This is an important derogation from the principle of the directive whereby a single set of legal provisions will apply to undertakings located in any Member State.

Nevertheless, your committee accepts the Commission's explanation that this is inevitable in view of the existing divergencies between marketing regulations in the Member States.

The Liaison Committee should be most useful here and Member States are also directed to cooperate with each other in the application of the directive.

The Commission also considers that this problem should be dealt with more extensively so that marketing regulations concerning transferable securities as a whole may be coordinated (see first paragraph, page 11 of the explanatory memorandum).

The Commission is working on its further directive concerning transferable securities generally and your committee hopes that the further proposal will not be too long delayed.

14. The committee suggests that a proposal similar to the present one for the coordination of laws, etc. relating to property funds should be drawn up as soon as possible.

15. The Economic and Monetary Affairs Committee has also commented in its opinion that the scope for harmonization is too limited, partly because of the important derogation from the general principle already mentioned, and partly because of numerous further derogations, e.g. Article 67 (1) and (2).

b. Individual Articles

16. Article 1 (2) : This seems to be badly worded. The provisions relating to the movement of capital to which reference is made, are provisions of national legislation. This should be made clear. Secondly, the phrase 'a Member State shall not apply any provisions whatsoever to CIUTS situated in another Member State or to the units issued by such CIUTS' reads rather oddly. There can be no question of a State's applying its national legislation to a CIUTS or its units situated in another Member State unless that CIUTS is operating in the first Member State. The Article might be reworded as follows so as to make the meaning clear : 'Subject to its national provisions relating to the movement of capital and to Articles 55(1) and 61(2) of this directive, Member State A shall not apply any provisions to CIUTS situated in Member State B which market their units in Member State A or to the units issued by such CIUTS'.
17. Article 5 (1) : The wording 'such authorization shall be valid for all the Member States' seems unsuitable. It would be preferable to say 'a CIUTS once authorized may operate in all the Member States without further authorization'.
18. Article 5 (3) : Your committee wonders why the rule set out here should not apply in all cases to the Depository Company. Even if notification is given to other authorities, they might not necessarily pass it on to the competent authorities referred to here whose information would thus be incomplete.
19. Article 15 : The wording of the first part is rather strange and might perhaps read better as follows : 'only the Management Company and the unit holders may make a claim against the assets of a unit trust'.
20. Article 19 : The Economic and Monetary Affairs Committee has raised the question of the lesser duties assigned to the Depository Company of an Investment Company by comparison with the Depository Company of a unit trust. The Commission has said (page 17 of the explanatory memorandum) that this is because
- (a) unit holders in Investment Companies are able to exert direct influence and control over the management of such a company by taking part in meetings.

(b) there is no danger of a clash of interests as the unit holders and the shareholders of the Investment Company are the same people.

Your committee is inclined to accept what is said by the Commission here, but the point has been made that the opportunities to exercise direct influence and control by taking part in meetings are of a theoretical nature.

21. Article 25 (2) : The Commission should perhaps consider going into detail concerning the application of the percentages laid down in this Article.
22. Article 29 (3)b : These provisions are apparently very complicated and it is worth noting that they are, in fact, designed to cover a specific case : that of investments in Brazil.
23. Articles 27 to 30 inclusive : As regards these articles it should be pointed out that the various figures concerning the assets of CIUTS have been based either on general practice in the Member States, e.g. Article 26(1), or on a compromise, e.g. Article 27. Page 19 of the explanatory memorandum has an important explanation on the links in the matter of figures between Articles 2 and 25 of the proposal.
24. Articles 27 (2) : The figure given here appears somewhat low. The main risk here for investors is that of double charging of costs but this is in any event prohibited by paragraph 2. There may be cases where it is very useful for a fund to be able to invest in another Fund managed by the same management or company, in order to take advantage of particular expertise and specialisation. Your committee, therefore, considers that the figure might safely be raised to 15% here.
25. Article 30 : So that managers are not compelled to dispose immediately of securities causing an excess above the 10% permitted by this Article, which might not necessarily be in the interest of investors, it would be preferable to allow a period of time, for example, six months, during which this might be done.
26. Article 31 : The publication of so many reports will be expensive for CIUTS and your committee wonders whether an annual one only would not be sufficient.

If the half-yearly reports are to be retained, paragraph 3 is rather badly worded. Reference to 'a two month period' suggests that that is the period specified in paragraph 2 for the annual report, but a delay of four months is allowed for publication of the annual report so the reference must be to the two month period for the second half-yearly report. This is not clear. The paragraph should therefore be reworded as follows : '... if the annual report for that financial year is published during the two month period which is prescribed for publication of the second half-yearly report'.

27. Article 36 : Your committee suggests that the persons or bodies appointed should 'inspect and check' the financial data, as this phrase more accurately defines the work which they would normally be expected to do.

28. Article 37 : A question has been raised as to the time at which the CIUTS is to take the comments of the competent authorities into account.

The Commission envisages that this might be the following report if the comments refer to matters of presentation or the information to be given, etc. If errors have been noted by the competent authorities, these should be rectified by the issue of a corrigendum. This seems reasonable.

29. Article 41(1) : The committee proposes the insertion of a provision allowing 'back-to-back' loans for the purpose of borrowing foreign currency in order to purchase foreign securities, as the explanatory memorandum states that such loans are permitted.

30. Article 41(2)b: It appears that the Commission envisages here a wide interpretation of the word "business" to cover all operations of the CIUTS. The occasions for such borrowing would, the Commission suggests, be of themselves limited.

However, it would be preferable in the interest of investors to restrict this borrowing to that which is needed for the acquisition of only those buildings which the CIUTS must have in order to operate. If any latitude were allowed there could be some danger of buildings being acquired as an investment which would change the character of the fund. Your

committee, therefore, proposes that the Article should be amended in this sense.

31. Article 50 : Your committee proposes that it should be provided that the persons specified in this Article should not act as parties to transactions effected on behalf of a CIUTS either directly or indirectly.
32. Articles 54 and 55: It would seem more logical if the order of these Articles were inverted.
33. Article 61(2) : Your committee wonders what the measures which are referred to here might be and against whom they would be taken as the CIUTS in question would not be situated in the Member State which would have to take the measures. Certainly, the CIUTS in such circumstances would be providing a financial service in that Member State in order to comply with the provisions of the directive. But it would not necessarily be established there as the financial service may be provided for example through an office in a bank.

The Commission foresees that as a last resort the Member State might stop the CIUTS from marketing its units. Where the question of enforcement is concerned, it is envisaged that resort might be had to bilateral agreements between Member States.

34. Articles 63 and 64 : On the question of the derogations provided in these Articles for investment companies which market their units exclusively through one or more official Stock Exchanges, the committee considered whether they were dangerous precedents detracting from the harmonization which the directive is designed to ensure but decided this was not the case.

35. Article 67 : The Economic and Monetary Affairs Committee in its opinion has proposed an amendment to Article 67 (2). That committee considers that managements of CIUTS which also carry on business as, or in conjunction with, credit institutions or insurance companies may not be given access to information about any company which might influence policy in regard to investment in that company and which would not be available to all shareholders in that company.

It seems to your committee that it is inevitable that such information should be acquired, but in the absence of any evidence that this is likely to lead to abuses, and in view of the difficulty of providing adequate safeguards as to the nature of which the Economic and Monetary Affairs Committee has made no suggestion, your committee does not feel inclined to support the proposed amendment.

36. Article 72 : So that the Commission is kept fully informed, this Article should be amended to read : "Member States shall ensure that the Commission is notified of the text of essential provisions which they intend to adopt or adopt under national law in the fields covered by this directive".

37. The Schedules : As these are of a highly technical nature, the Legal Affairs Committee does not propose to deal with them. It does, however, ask the Commission to take account of the comments which have been or will be made upon them by interested organizations.

IV. OMISSIONS IN THE PRESENT PROPOSAL

38. Some of these omissions have been noted following a study of the Standard Rules for the Operations of Institutions for Collective Investment in Securities, prepared by the Committee on Financial Markets of the OECD (Paris, 1972).

39. No provision has been made for the harmonization of administrative procedures. If it is the case that these procedures vary considerably from one Member State to another, this might cause problems for the CIUTS marketing their units abroad.

40. Nothing is said about the amount of fees and charges save in Schedule A, under which some information about these is to be given in the prospectus. The Commission might consider whether some attempt should not be made in the directive to ensure that these do not vary too greatly from one Member State to another. The fourth rule of OECD provides that an investor must be able to find out exactly how much he is paying and for what.

41. The 23rd rule of OECD contains a prohibition on various persons from doing business with the fund. Article 50 of the proposal contains similar provisions but they do not go so far, in that the spouses and children of the directors and staff of the CIUTS are not included in the scope of the Article. The OECD rule also applies to all persons who through affiliation, are liable to come directly or indirectly under the influence of any person or body, to whom reference has already been made in the rule. It should also be noted that Article 50 provides for exceptions to the general rule which the OECD rule does not.

V. CONCLUSION

42. Taking into account the proposed amendments and comments set out above, your committee recommends the adoption by Parliament of this report.

OPINION OF THE COMMITTEE ON ECONOMIC AND MONETARY AFFAIRS

Draftsman : Sir Brandon Rhys Williams

On 24 June 1976 the Committee on Economic and Monetary Affairs appointed Sir Brandon Rhys Williams draftsman.

It considered the draft opinion at its meetings of 18 October 1976 and 22 November 1976 and adopted it unanimously on 3 December 1976.

Present : Mr Van Der Hek, chairman; Sir Brandon Rhys Williams, draftsman; Lord Ardwick, Mr Artzinger, Mr Delmotte, Mr Hansen (deputizing for Mr Knud Nielsen), Mrs Kellett-Bowman (deputizing for Mr Dykes), Mr Krall (deputizing for Mr Achenbach), Mr Lange, Mr Leonardi, Lord Murray of Gravesend (deputizing for Mr Thornley), Mr Normanton, Mr Nyborg, Mr Springorum (deputizing for Mr Burgbacher) and Mr Suck.

I OBJECT OF THE PROPOSAL

The aim of collective investment undertakings is to gather together the funds of as many savers as possible by issuing units and to invest these funds, using the principle of risk spreading in securities or other assets.

These institutions offer savers the advantage of a wide spread of investments, which is often difficult for the individual saver, in particular as regards foreign markets.

To safeguard the savings of small, often inexperienced savers, many countries have evolved special rules relating to the activities pursued by, and the controls to be laid down in respect of, these undertakings. There is a clear need to coordinate the differing laws in this field. This is important to protect savers, especially small savers, in the Community and also, insofar as competition will be stimulated, to afford them more advantageous conditions for placing their savings. The proposed directive would represent some progress towards a unified capital market, in that it would help to foster the interpenetration of markets in transferable securities. The Commission's work in this field can be seen in some way as a counterpart to its work in the fields of credit institutions and stock exchanges¹, and the Committee welcome this development. They note, however, the continuing lack of any overall Community policy for savings and hope that the Commission will soon remedy this deficiency.

The Committee have paid particular attention to the Commission statement that "Coordination is thus a prior condition for establishing the free movement of capital in this sector".² The Commission goes on to point out that for the envisaged coordination to be really effective "the necessary measures must be taken in respect of movements in parallel with the implementation of the present directive".² The Committee look forward therefore with especial interest to the directive which the Commission is preparing, which aims at the removal of restrictions on the free movement of units of collective investment undertakings, and hope that the European Parliament will be consulted on this before the end of 1976.

¹ For the Committee's views on the Commission proposals in these fields see the Scholten Report (Doc.66/75), their opinions attached to the Armengaud Report (Doc.186/73) and the Bangemann Report (Doc.236/76). The Committee generally speaking welcomed the proposals but felt they did not go far enough, and regretted that they dealt with very limited areas.

² Doc.114/76, page 7

(a) Scope of the proposal

The proposed directive is concerned only with collective investment undertakings for transferable securities (CIUTS) which are open-ended. These are for the most part the undertakings normally known as unit trusts. It does not extend to investment trusts, which are closed-ended. The latter are much less numerous and by their nature normally fall within the scope of company law.

There are included among the CIUTS other than of the closed-end type those undertakings with a corporate structure - that is, investment companies which are similar in form to public limited companies- as well as the collective investment undertakings other than with a corporate structure, i.e. unit trusts proper.

To be even more precise, this directive only concerns CIUTS

- whose object is collective investment in transferable securities and liquid assets of at least 80% of the capital they collect;
- which accumulate this capital by means of offers to the public;
- which operates on the principle of risk spreading;
- whose units are or have been issued continuously or in blocks at short intervals and/or directly or indirectly repurchased or redeemed at the request of the holder using the assets of these undertakings.

Consequently the following are specifically excluded:

- collective investment undertakings more than 20% of whose funds are invested in assets other than transferable securities or kept liquid (i.e. property funds, holiday funds, property development funds, etc.);
- holding companies;
- investment clubs, etc.

(b) The case for coordination

There are several objectives which this coordination directive is designed to meet. By coordinating the national legislation applying to CIUTS, it should be possible to render the protection offered to savers more effective at Community level and provide more uniform safeguards for all savers.

Furthermore, coordinating the legislation in question should also enable the conditions of competition in which the CIUTS operate to be improved.

Finally, this coordination aims at removing restrictions on the free movement within the Community of units of CIUTS. It is thus a prior condition for establishing the free movement of capital in this sector.

With this in mind, the present directive requires Member States to apply a number of minimum rules to CIUTS located in their territory.

II. ANALYSIS OF THE MINIMUM COORDINATION RULES CONTAINED IN THE PROPOSAL FOR A DIRECTIVE

(a) General principles underlying coordination

The proposed directive is designed to make CIUTS located in any Member State subject to a single set of legal provisions, regardless of whether they operate in only one country or throughout the Community. Thus, according to this directive, CIUTS in Member States will be subject solely to the legislation of the Member State in which their management is effectively carried on. The Member State concerned must comply with the minimum rules laid down in the proposed directive (Article 1).

The required authorisation (Article 4h), which will be granted only by the competent authorities of the Member State in which the CIUTS is situated, will be valid for all the Member States.

However, by way of derogation from the principle of a single set of legal provisions, Article 55 provides that the regulations for governing the marketing of CIUTS units and the supervision of the application of these regulations will remain the responsibility of the authorities of the Member State in which the units are marketed. This derogation is, in the opinion of the Commission¹, 'important'. To justify this important limitation of the principle of a single set of legal provisions, the Commission points to the 'marked differences' between the Member States in this field and the need to resolve these problems.

Among the general principles already mentioned, the proposal for a directive lays down a number of regulations concerning the structure, the obligations and the supervision of CIUTS.

¹Doc. COM (76) 152 final, page 10.

(b) Consideration of other provisions contained in the directive

1. The structure of unit trusts and investment companies

The proposal for a directive stipulates (Article 8) that the activities of unit trust management companies must be limited to the management of these trusts.

However, there are two derogations from this decision: the first (Article 67(1) to allow Belgian management companies to retain the right to issue bearer certificates representing registered securities of other companies; the second (Article 67 (2) to allow Irish, British and Dutch management companies, which may at the moment be involved in other activities such as banking or insurance, to continue these activities.

In this respect the committee is of the opinion that there must also be adequate safeguards to ensure that opportunities are not afforded to the managements of CIUTS which also carry on business as or in conjunction with credit institutions or insurance companies to gain access to information about any company which might influence this policy in regard to investment in that company, other than information simultaneously available to all shareholders in that company.

Bearing in mind the important role (Articles 10 and 19) which the depositary company must play in protecting the saver (safekeeping of securities, day-to-day administration, supervision of the management company's or the investment company's activities) the proposal for a directive similarly stipulates that the depositary company must have its registered office (or place of business) in the Member State where the CIUTS is located, i.e. in the Member State where the business of management is actually carried on. This rule on location is intended to ensure efficient and practicable supervision of management activities by the depositary company.

However, it should be noted that Article 19 does not assign to the depositary company of an investment company all the duties of the depositary company of a unit trust (i.e. Article 19 does not repeat the duties referred to in Article 10(2) (c) and (d)) because the unitholders in an investment company are protected by company law.

2. The obligations of CIUTS

The proposal for a directive contains a number of provisions relating to the obligations of CIUTS as regards the composition of their assets, their investment policy, borrowing policy and the information they must provide.

¹Doc. COM (76) 152 final, page 17.

- Composition of the assets of CIUTS

Article 25(1) lists the conditions which CIUTS must fulfil in building up their assets, subject to the exceptions listed in Article 25(2) (a maximum of 10% in transferable securities other than those referred to in (1) and a maximum of 5% in such items as gold and property).

These maximum limits represent guarantees against excessive risks for unitholders.

- Investment policy of CIUTS

To protect savers, Article 26(1) stipulates, for example, that a CIUTS may not invest more than 5% of its assets in transferable securities of the same issuer (principle of risk spreading).

Article 27(1) further lays down that a CIUTS may not invest in all more than 10% of its assets in units issued by other CIUTS. Similarly, so as to prevent a CIUTS from pursuing a policy of gaining control over companies in which it invests, Article 29 provides that a CIUTS may not hold more than 5% of the securities of the same category of an issuer or have more than 5% of the total votes attaching to the securities of this issuer.

- Borrowing policy

The proposal for a directive forbids CIUTS (Articles 41 and 70) from borrowing, except for the repurchase or redemption of units or for the exercise of subscription rights. However, this ban on borrowing does not apply (Article 70) to CIUTS whose fund rules included on 1 January 1976 provisions enabling loans to be contracted for investment.

Moreover, Article 48 of the proposal prohibits CIUTS from carrying out particularly speculative transactions (uncovered dealings in transferable securities).

- Information a CIUTS must provide

Articles 34 and 57 of the proposal stipulate those particulars which CIUTS must publish:

- a prospectus relating to the structure of the CIUTS, its objectives, procedures for issuing and repurchasing shares, an annual report and two half-yearly reports.

The prospectus will be subject to prior checking by the competent authorities while the reports may be checked at a later date by these authorities.

Finally, a Liaison Committee is to be set up (Article 66), to facilitate consultation between the Member States on the implementation of this directive.

CONCLUSIONS

Consideration of this proposal for a directive leads to the following conclusions:

1. The Committee welcome the proposed directive as a further step towards the achievement of a unified Community capital market, but stress the importance of its being followed as soon as possible by a directive to enable units of collective investment undertakings to circulate without restriction;
2. The proposal for a directive certainly contains a number of useful and necessary provisions relating to the protection of savers both in terms of the structure and obligations of CIUTS;
3. However, the scope of the harmonisation is limited since it does not cover the rules for marketing units of CIUTS;
4. Moreover, among other derogations the derogation (Article 67) which permits unit trust managements to be associated with merchant banks permits the misapplication of confidential information to the disadvantage of other shareholders. This danger may be averted through strict adherence to investment and banking traditions in the principal capital markets, but the occasion should not be lost to ensure that abuses should not be allowed to arise.
5. The Commission should initiate a study of the whole problem of insider trading, including professional independence, with particular reference to the objective of establishing a united Community capital market;
6. Finally, despite the number and detail of the provisions of this proposal, it can only be described as limited in scope;
7. This opportunity should also be taken to emphasise the considerable delay in introducing real freedom of movement in the capital market (inadequacies stemming from the limits of the text of the present proposal) and even more, in establishing a Community savings policy.