



Mark Glibbery  
Retail Policy Division  
Financial Services Authority  
25 The North Colonnade  
Canary Wharf  
London E14 5HS

6<sup>th</sup> December 2006

Dear Mark,

**Response to CP06/18: Quarterly Consultation No. 10**

The Depository and Trustee Association (DATA) represents all depositaries and trustees of UK-based authorised unit trusts and open-ended investment companies (OEICs). At the end of September 2006, the members of DATA were responsible for safeguarding £385.9 billion of funds under management.

We welcome the opportunity to comment on the proposals outlined in CP06/18. Our responses to your specific questions are detailed in the attached document. In particular, I would like to draw your attention to our comments in response to question 9 and our request for further consideration of the issues identified in relation to the proposed treatment of stocklending income.

We would welcome further clarification as requested on these points and would be happy to discuss with you, in further detail, any comments we have made.

Yours sincerely,

David England  
Chairman of DATA

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**CP 06/18: Quarterly Consultation No 10 – Chapter 6 Proposed amendments to COLL**

DATA's detailed response

Q4: Do you agree that we should permit the issue of hedged currency class units?

**DATA support the FSA's proposal to introduce the flexibility to offer hedged currency class units. The additional flexibility should allow AFM's to further protect the interests of their investors and brings UK UCITS in line with their Dublin and Luxembourg counterparts. We would however ask you to remove the reference to consulting with the depositary from the proposed Guidance in COLL 3.3.5G 1b. We believe the correct reference should be to the fund's auditors only.**

Q5: Do you think our proposals for hedging of currency class of units appropriately protect the interests of all investors in a fund?

**DATA believes the current controls and processes required by the derivative risk management process should be sufficient, when combined with the proposed disclosure requirements, to protect the interests of all investors. We agree that the alternative proposition of requiring the AFM to seek indemnities to cover any cross unit class contagion would result in additional unnecessary costs and would likely deter AFMs from using this provision.**

Q6: Should the proposed rules and guidance address any other issues?

**DATA believes that there may be benefit from including in either COLL 5.3.3 or COLL 5.3.4 G a statement to clarify that any assets required as cover for a hedged unit class should be considered prior to establishing the available cover for the fund in general.**

Q7: Do you agree these proposals for allowing aggregation of unit classes provide a suitable balance between operational flexibility and investor protection?

**DATA supports the proposals for allowing unit classes to be aggregated in certain circumstances. FSA's proposals are in line with DATA's response to CP 06/7 (Single and dual pricing for authorised CIS). The control mechanisms proposed relating to the circumstances where aggregating unit classes will be possible combined with the requirement for prior approval from a depositary should prove sufficient. Having reviewed the draft rules we would welcome the amendment of COLL 6.2.6 A R1 to read "with the prior agreement of the depositary..." as we believe this reflects, more closely, the sentiment of paragraph 6.27.**

Q8: Do you agree that these proposals will facilitate stock lending by authorised funds without a significant increase in risk?

**DATA supports the proposals to provide additional flexibility for AFMs when entering into stock lending arrangements. However, we would ask the FSA to consider the following two points;**

- 1. Clarify that when commercial paper is taken as collateral that it is “plain vanilla” commercial paper with no embedded derivative content. We would also ask the FSA to consider including a glossary term for commercial paper to avoid ambiguity.**
- 2. Develop standards by which other stock lending programmes may be deemed acceptable alongside the specific example of Euroclear’s SLBP. There may well be other providers that offer equivalent services and appropriate protection through guarantees. This would seem to be more in-keeping with the FSA’s drive for principle based regulation.**

Q9: Do you agree with our proposed treatment of income from stock lending?

**DATA welcomes FSA’s review of stock lending income. We do not object to the attempt to add clarity to the treatment of stocklending income and the circumstances where payments may be made out of this income. We would, however, welcome further clarification on the following points and would ask the FSA to consider closely the impact the proposals will have on the established market practices of stock lending agents.**

- 1. Where income sharing arrangements are currently in place, what transitional periods will AFMs have to bring those arrangements in line with the new rules?**
- 2. Based on our interpretation of the proposed rules and the existing requirements of COLL 4.3 we believe that any payment out of the stock lending income, for the first time, would be considered a new type of payment and therefore a fundamental change, requiring unitholder approval. If you are in agreement with this we would welcome this example being added to the guidance in COLL 4.3.5 G. We have also considered that there may be cause to give separate consideration between payments made to the stock lending agent or the AFM to come to the appropriate conclusion.**
- 3. Given that market practice as far as stock lending income is concerned is usually based on the stocklending agent taking a fixed percentage of the income, how do the FSA see this fitting into the proposed list of eligible payments that would seem to be transaction orientated? We are also concerned that the content of para 6.37 would suggest more flexibility in what may be charged to the scheme than the proposed bullet points might allow. To avoid any ambiguity we would welcome further clarification from the FSA on this point, specifically the use of the word “counterparty” in the context of COLL 5.4.3 R 3a and that this means the lending agent.**

4. Where reference is made to the disclosure of the payments that may be made out of the stock lending income (COLL 5.4.3 R4) we would welcome confirmation that the FSA believe the current disclosure requirements within the prospectus (COLL 4.2.5R 13) are sufficient.

In our comments above we have not raised the issue of the possible need for the distinction between the recovery of expenses and the payment of remuneration and any consideration of materiality. This is an issue that we believe may be worthy of further discussion.

Q10: Do you agree the proposed guidance on the reinvestment of cash collateral is appropriate? Should there be a transitional period following its introduction?

DATA supports the inclusion of the additional Guidance relating to the reinvestment of cash collateral taken on behalf of the fund. However, the primary concern should be that any reinvestment is restricted to the asset types that are set out in COLL 5.4.6 R 1, any further restriction is, in our opinion unnecessary. We would therefore ask that the first point (COLL 5.4.8 G 1) of the proposed guidance be removed. The FSA do not require any other form of collateral taken to be in line with the scheme's objectives, only that it meets the requirements of COLL 5.4.6. We do not believe there is a need for a formal transitional provision given the flexibility offered by the proposal being introduced as Guidance.

Q11: Do you agree with the proposed amendment to the Glossary definition of "income property"?

DATA supports the additional flexibility that the revised Glossary definition will permit. We would welcome confirmation from the FSA in their policy statement over the attached change event considerations attached to the impact of effective yield and the subsequent impact on distributions.

Q12: Do you agree with our assessment of the costs and benefits of our proposals?

DATA has no specific comments to make on the FSA's cost benefit analysis of these proposals.