



18 May 2005

Mr. Philippe Richard
IOSCO Secretary General
Oquendo 12
28006 Madrid
Spain

Dear Mr. Richard

**Best Practice Standards on Anti-Market Timing and Associated Issues for
Collective Investment Schemes**

The Depository and Trustee Association (DATA) represents the depositaries and trustees of authorised unit trusts and investment companies with variable capital (ICVCs). At the end of March 2005, the members of DATA were responsible for the safeguarding of £280 billion of funds under management.

DATA is pleased to comment on your Consultation Document on Best Practice Standards on Anti-Market Timing and Associated Issues for Collective Investment Schemes.

The IOSCO report proposes three best practice Standards:

- CIS operators should act in the best interest of CIS investors
- CIS operators should ensure that their operations and disclosure in respect of market timing and late trading are consistent with the first Standard
- The regulatory regime should allow operators appropriate flexibility in addressing the risk of detriment to investors arising from market timing

DATA agrees with the above standards at a general level, but is not comfortable with all the detailed supporting proposals, some of which, so far as the UK is concerned, go beyond what is necessary or proportionate to meet the Standards. DATA's concerns are described below.

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1 CIS operators should act in the best interest of CIS investors

In general DATA is comfortable that this standard is addressed by the FSA's "Principles" and "Senior Management Systems and Controls" rules. However, we have some observations on the more detailed proposals in the paper.

Clause 4

The paper proposes that a CIS operator should disclose to investors its policies for dealing with conflicts of interest in connection with market timing. We understand that in some jurisdictions inclusion of such policies within scheme documentation will enable a CIS operator to deter, discourage or penalise investors involved, or suspected of being involved with, market timing. Clearly, in such circumstances, disclosure is an appropriate course.

In the UK, however, such powers are already contained within the FSA regulations and CIS operators do not need to take any additional steps, e.g. disclosure, to utilise these powers. Whilst a number of CIS operators do refer to market timing within their scheme Prospectus, there is general reluctance to give overly specific details of policies, trigger levels etc, as this can give potential market timers information to enable them to circumvent the CIS operator's controls. For example, disclosing the threshold at which a fund might swing its price could lead to market timers designing trading strategies that undercut that threshold.

2 CIS operators should ensure that their operations and disclosure in respect of market timing and late trading are consistent with Standard One

Once again, DATA is comfortable that, in general, this Standard is already addressed by the FSA's collective investment scheme rules. However, there are a number of detailed points with which DATA disagrees.

Clause 6

This clause proposes that CIS operators should be required to disclose their policies and procedures relating to market timing and late trading, fair valuation and disclosure of portfolio holdings. UK regulations already require disclosure of fair valuation policies and a recent recommendation from a review of CIS Governance by the Investment Management Association (the UK investment management industry trade body), in which DATA participated, has recommended that CIS operators' policies in relation to portfolio disclosure should be stated in each fund Prospectus (a copy of this review is attached to this letter). However, as noted under clause 4 above, DATA believes that there is more potential detriment than benefit in detailed disclosure of CIS operators' policies and procedures relating to market timing and late trading.

Clause 8

Whilst DATA supports the proposition in Clause 8 (iv) that CIS operators should monitor valuation methodologies to ensure that the CIS's NAV is accurate, it would be helpful if this clause were expanded to cater for the principles of fair value pricing. There is clearly no "accurate" fair value price and the key word in this definition is "estimate". Clause 8 (iv) could usefully be expanded to propose that CIS operators should follow robust and consistent fair value processes that are regularly reviewed.

Clauses 11 to 13

Clauses 11 to 13 relate to late trading, an activity, which in the UK, is barred by regulation and to which depositaries and trustees of UK collective investment schemes give particular attention during their monitoring reviews. UK regulations give no additional latitude to intermediary trades, which must be received by the CIS operator at the same cut-off point as trades received from direct investors.

Clause 22

This clause proposes that external auditors and the depository or the trustee (where it exists) of CIS operators should review as part of their regular audit the systems and controls established by the operator and comment on their effectiveness. Whilst in the UK there is not a specific regulatory requirement in this regard, in practical terms depositaries/trustees already have an oversight responsibility for virtually all rules applicable to CIS. In one respect (the CIS operator's decision as to whether or not to apply a dilution levy to individual holder transactions) the IMA report on CIS Governance referred to above, has recommended that the depository/trustee oversight be extended to cover this aspect. The FSA is currently considering this recommendation, along with a number of other governance recommendations.

Clause 24

Please refer to our response to Clause 6 above.

3 The regulatory regime should allow operators appropriate flexibility in addressing the risk of detriment to investors arising from market timing

Clause 25

DATA's view is that the FSA regulations applicable to UK collective investment schemes, together with the FSA Principles, provide CIS operators with a comprehensive regulatory toolkit, which can be applied to protect CIS investors' interests.

Clause 27

This clause proposes that where market timing and associated issues cause CIS investors or a group of CIS investors to suffer loss, or the CIS suffers dilution, the CIS operator's duty should be to put them back in the position they would have been had there not been a failure to meet Standard 1, i.e. had the transaction that caused the dilution or loss not taken place. This may mean compensating investors direct and /or the CIS itself.

Whilst supporting this stance in principle, DATA suggests that the paper takes into account that no matter how robust the CIS operator's processes, detection of market timing cannot be guaranteed, especially when business is transacted through a number of different aggregators. Consequently, DATA believes that an absolute requirement for the CIS operator to compensate investors or the fund in every instance may be unreasonably harsh and that the CIS operator should only bear liability where it has been in breach of its obligations, either in not having policies and procedures consistent with its regulator's requirements, or indeed where it has not been adhering to such policies and procedures.

Clause 29

Please refer to our comments on disclosure under Clause 4.

We would be very happy to discuss the points raised above if you would find this helpful.

Yours sincerely

Tim Gandy
Chairman, Depositary and Trustee Association

cc: Dan Waters, Asset Management Sector Leader, UK Financial Services Authority.
Ashley Kovas, Collective Investment Scheme Policy Unit, UK Financial Services Authority.