EFAMA
European Fund and Asset Management Association

CONSULTATION RESPONSE

Brussels, 12 February 2024

EFAMA's RESPONSE TO THE FCA CONSULTATION ON THE OVERSEAS FUND REGIME (OFR)

Introduction

The European Fund and Asset Management Association (EFAMA) represents the views of the European buy-side industry. Our members include EU, UK, and global asset managers, with many having significant operations in the UK and ultimately helping UK investors to meet their investment objectives. As such, we welcome the opportunity to provide input to the Financial Conduct Authority (FCA) consultation paper on operationalising the Overseas Fund Regime (OFR).

Recognising the importance of EEA funds for a thriving UK fund market, we believe that the consultation paper puts forward a broadly compelling vision of how the OFR will operate in practice following the unconditional equivalence determination granted to EEA UCITS funds by the HM Treasury on January 30.[1]

As the gold standard for retail funds, which the UK contributed to create as a former Member of the European Union, it is in the interest of UK customers to retain access to UCITS funds. Among the most significant advantages that these funds offer, we notably count diversification and economies of scale.[2] Through these funds, UK investors would continue to benefit from the investment expertise of a broader pool of European management companies, some of which may not have a sufficient client base to launch UK-domiciled funds. Important as well is that UK investors continued to be served by top-notch expertise in custody, fund administration, and risk management available in other European fund domiciles.

As of the end of December 2022, approximately 8.800 European funds were distributed in the UK, accounting for more than 95% of the overseas funds distributed in the country.[3] Despite these impressive figures, European funds represent however only a fifth of the UK retail fund market (i.e., £228 billion in

[1] UK Parliament, Update on the Overseas Funds Regime: The UK's Equivalence Assessment of the EEA states, 30 January 2024.

[2] According to the EFAMA's 2023 Fact Book, the European investment management industry manages EUR 4.7 billion on behalf of non-EU investors (28 % of the industry's assets under management) (p. 56). Furthermore, according to the 2023 PwC Global Fund Distribution, the top 64 cross-border management groups mainly distribute their investment strategies globally through funds domiciled in Luxembourg and Ireland with some groups also distributing funds domiciled in France, the UK, and Germany (slides 8-10).

[3] PwC, Global Fund Distribution Poster, June 2023.

AuM).[4] This implies that, for many European funds, UK retail investors account only for a limited share of the assets under their management. As a result, an important increase in the cost of access to the UK market may force management companies to reduce their offering to UK retail investors.

We make several recommendations that would ensure that the regime would further reduce market barriers and therefore deliver a better outcome for UK investors. In our opinion, there are indeed multiple provisions in the FCA's proposal that we believe could create barriers to entry into the UK market:

- Additional regulatory or disclosure requirements, some of which do not exist for UK funds, which would result in additional costs for recognised schemes, or simply make these funds more difficult to operate for the management company;

- The supervisory overreach with the FCA granting itself powers that it does not have over UK funds; and

- A potentially burdensome process should all the information that the FCA needs be manually entered into the dedicated online platform. To reduce this risk, the industry's involvement in the design of the platform will be crucial.

Finally, it is crucial that the FCA provide greater clarity on several aspects of the regime, including the definition of certain notions (e.g., 'fund categories', 'ESG focus', and 'negative effects on UK investors') and how it intends to proceed with the transition from the Temporary Marketing Permission Regime (TMPR) to the OFR.

Chapter 2: the wider context

Q1: What, if anything, do you consider to be unintended consequences of our proposed intervention?

Although the framework outlined by the FCA is sensible, certain elements of the OFR, as envisaged in this proposal, would not only result in unnecessary costs for UK investors, but would also create an unlevel playing field creating unnecessary barriers to entry. Over the long-term, this could result in a reduction of competition in the UK market as well as higher costs and reduced choice for UK investors.

First, there are multiple **disclosure requirements** that are either unrealistic (e.g., notifying the FCA 30 days before the suspension of a fund), or would result in excessive costs that UK investors would eventually have to bear (e.g., the disclosure of information such as fees and charges that are readily available in the UCITS KIID). The FCA also proposes new **regulatory obligations** that could require the management company to amend its public disclosure to access the UK market, which would be extremely costly and time-consuming (e.g., the obligation to appoint an 'authorized person' that would be responsible for overseeing the financial promotions of recognised schemes in the UK and the requirement that prospectuses should comply with COLL 4.2.5R). These issues are explored further in our responses to the subsequent questions.

Second, although we recognise that the FCA should have the **supervisory power** to prevent the distribution of overseas funds in the case it determines that these schemes would be harmful to UK investors, we strongly encourage the FCA to ensure that it follows a transparent and pragmatic approach

[4] The IA, Investment Management in the UK 2022-2023, October 2023, pp. 91-92.

that recognises that these funds have already been authorised in another jurisdiction whose regulatory framework is deemed equivalent. There are two important considerations to make in this regard:

- **The FCA should ensure that it sufficiently explains any decision to reject the application of an overseas fund:** At this stage, the FCA does not foresee sufficient transparency on the criteria that it will use when evaluating overseas funds, nor sufficient guarantees that asset managers will receive a thorough justification should their funds be rejected. For instance, the FCA states that it will *"not consider it appropriate to recognise a scheme with an inappropriate or misleading name."* Unfortunately, nowhere does the FCA provide any details on how it would determine whether the fund name is 'inappropriate' or 'misleading' within the OFR context, nor the reassurance that it could motivate its decision; and

- **The FCA should not have supervisory powers over overseas funds that exceed those that it has over UK funds:** It is our understanding that, under the proposed regime, the FCA would be able to refuse a recognition on grounds that the fees charged by the fund are deemed excessive, even if currently, the FCA does not have an equivalent power over UK funds.

Moreover, it is important to underscore that the OFR should not grant the FCA additional supervisory powers than those strictly necessary to screen the access of overseas funds into the UK market. Should it require any additional information in this regard, it should work with its European peers by leveraging the 2019 Multilateral Memorandum of Understanding (MMoU) concerning consultation, cooperation and the exchange of information relating to market surveillance, investment services and asset management activities.[5]

The MMoU, for instance, states in Article 4 (Exchange of Information) that *"[t]he Requested Authority intends to provide the Requesting Authority, upon written request, with assistance in obtaining information not otherwise available to the Requesting Authority, and, where needed, interpreting such information so as to enable the Requesting Authority to discharge its responsibilities and assess compliance with its Laws and Regulations. The information covered by this Article includes, without limitation: a) Information and documents held in the files of the Requested Authority regarding the matters set forth in the request for assistance; b) Findings from regulatory and/or supervisory reports prepared by the Requested Authority."* Equally, the MMoU states in Article 9 (Unsolicited assistance) that *"[e]ach Authority will make all reasonable efforts to provide the other Authority, in as much detail as possible, without prior request and in advance to the extent practicable, with any information likely to be of assistance to the other Authority for the purposes of carrying out its responsibilities under the Laws and Regulations, including information concerning: a) Any known material event that could have a significant effect on the operation of a Covered Entity or could otherwise adversely impact investor protection, financial stability or the integrity and orderly functioning of the markets in the jurisdiction of the other Authority; […] c) Any known material event that could have a significant effect on the operation of a Covered Entity or could otherwise adversely impact investor protection, financial stability or the integrity and orderly functioning of the markets in the jurisdiction of the other Authority."* Based on this MMoU, the FCA can also expect the cooperation of EEA NCAs on enforcement matters. Article 11 (Cooperation on enforcement) states that *"[t]he Requested Authority should, as far as its applicable legislation permits, assist the Requesting Authority where it is necessary to enforce the Laws and Regulations breached or*

[5] FCA-EEA NCAs, Multilateral Memorandum of Understanding concerning consultation, cooperation and the exchange of information relating to market surveillance, investment services and asset management activities, February 2019.

suspected to have been breached by a Covered Entity established in the jurisdiction of the Requested Authority."

Finally, EFAMA welcomes the FCA's intention to enhance its online system for the collection of information under the OFR. When developing this online platform, the FCA should involve the industry to **ensure that the administrative burden associated with the application and subsequent notification process is minimal**. In particular, to avoid that the application process, or the notification of changes, becomes an overly manual process, we would welcome the possibility for management companies to upload the necessary information to the platform using either CSV, XML, or Excel files. This possibility would be appreciated by large management companies that may have to apply for the recognition of dozens, if not hundreds, of overseas funds. This would be particularly helpful should these companies have to report the fees and charges at scheme and share class level, which are not always easy to collect and can change regularly.

Chapter 3: Applying for recognition

Q4: Do you agree with the proposed set of data to be required from overseas schemes at the OFR recognition stage? If not, please explain why not and indicate what alternative approach you would suggest.

These mandatory pre-approval disclosures in some areas exceed the information that EU asset managers provide to their own national competent authority under the UCITS/AIFMD frameworks.

To ensure consistency in the information that management companies provide the FCA in their applications, the FCA should strive for greater clarity around the terminology it uses and, to the extent possible, align it with the terminology used by the EU industry:

- **Fund category/asset classes:** The FCA should provide more clarity on the way management companies should describe their overseas funds. Different classifications could indeed be taken as a reference to describe these funds: the type of financial instrument (shares, bonds, money market instruments), the geographical focus of the invested assets (Europe, US, Asia), or the types of issuers (corporate, financial institutions, government entities). Moreover, management companies may use different naming conventions from one jurisdiction to the other. For instance, the FCA requires funds that include 'UK Equities' in their name to be restricted to companies that are headquartered, or conduct the majority of their business, in the UK, instead of just having a UK listing. However, this naming convention does not apply in other jurisdictions;

- **Dealing frequency:** The FCA should clarify whether this information request only concerns subscription operations, or whether it also concerns other types of operations concerning the fund shares (e.g. redemption operations and switches); and

- **ESG focus:** The FCA should use another terminology than 'ESG focus' to collect information about the funds' 'sustainability objectives' or 'characteristics'. As the application of the UK's Sustainability Disclosure Requirements (SDR) and labelling regime on recognised schemes will be subject to further consultation, it is unclear what the term 'focus' would stand for in the OFR's context. Considering that this term is not currently defined in EU law either, applicant firms would probably not know which information to provide the FCA. Using SFDR-aligned terminology such as 'sustainability objectives' and/or 'characteristics' would create more consistency in the way management companies will respond to this information request.

EFAMA disagrees with the proposal for the FCA to require the disclosure, as part of the application process, of information that is irrelevant, or already available in a machine-readable format in the fund's prospectus and marketing materials. UCITS funds already disclose a significant amount of information to the public through their prospectuses and other disclosures (e.g., fees and charges, availability of liquidity management tools, and use of derivatives). Providing this information to the FCA would be largely redundant. Concerning annual management fees, we consider that this information would be irrelevant because a) there is no inducement in the UK; b) this requirement would be extremely burdensome; and c) UK funds are not subject to similar requirements.

Finally, as regards fund names, the FCA should not refuse recognition for funds that have the same name as a UK fund for the reason that the former are usually not distributed through the same distribution channel as the latter. A review of the register conducted by the Investment Association confirms that there are indeed a number of funds currently recognised under the TMPR which have the same names as UK authorised funds. To the best of our knowledge, these have not resulted in confusion, or investors accidentally investing in the recognised scheme rather than the UK fund, or vice versa. This is because, in practice, it is unusual for both a recognised scheme and a UK fund with the same names and investment strategies to be distributed through the same channel. In any case, on the rare occasions that both funds might be made available, no investor will ever be presented with the fund names alone. The funds can readily be differentiated through other information that is provided pre-investment, such as its unique identifier and country of domicile.

Q5: Is there any data that you do not think would be appropriate for ETFs to submit as part of the OFR recognition process? If so, please provide examples and explain your answer.

The application disclosures should be adapted to the ETFs' specificities. There are several data points that appear irrelevant for this fund structure:

- **Target investors**
- **UK representatives**
- **Dealing frequency**
- **Minimum investment amount**
- **Other fees and charges:** ETFs do not support any other fee/charge retained by the fund operator/fund service provider;
- **Sponsor or other person influencing the scheme's design or management:** Only the fund operator and the index sponsor may influence/design the scheme or management, and these two actors are already presented/defined otherwise in the prospectus; and
- **Details of any promotional payments to entities associated with marketing or distributing the scheme:** Not relevant for ETFs as they are listed.

Q6: Do you have any comments on our approach to setting fee rates?

EFAMA welcomes the FCA's decision to align the application and periodic fees of recognised schemes with those of UK funds, thereby guaranteeing that there is a level playing field among these funds.

Chapter 4: proposed notification of changes

Q7: Do you agree with our proposal to be notified of ad-hoc changes to OFR recognised schemes, including ETFs? If not, please explain your reason.

While EFAMA understands the necessity for the FCA to be informed of certain *ad hoc* changes regarding recognised schemes, greater clarity would be welcome on how the FCA intends to use these notifications. It is indeed crucial that these mandatory notifications do not result in a *de facto* dual supervision. As outlined by IOSCO, equivalence regimes have as an objective the reduction of market fragmentation by reducing regulatory overlaps.[6]

The FCA should also ensure that these notification requirements do not exceed those that apply to UK funds. For instance, to the best of our knowledge, the FCA does not require UK funds to notify changes related to their Legal Entity Identifiers (LEIs) or investor targets, while it does for recognised schemes. Likewise, there is no requirement for UK funds to pre-notify changes related to comparator benchmarks. The only exception is for UK funds with a target or constraining benchmark, which are in this case required to request the FCA's authorisation for a change of benchmark, where such a change would equate to a modification of the investment objective and/or policy.

Finally, the FCA should specify a number of notions that remain unclear to our members: 'supervisory sanctions', 'fundamental change', 'negative effects on UK investors', and 'connected parties'. As regards the notification of 'supervisory sanctions', we would recommend that the FCA clarify that management companies should only disclose sanctions that are related to fund management activities.

Q8: Do you agree with our proposal for the timing of notifications? If not, please explain your reason.

The requirement to notify the FCA 30 days before certain pre-defined changes enter into force would result in longer notification periods than those prescribed under the law of the fund's home jurisdiction. Indeed, management companies already have to notify their home national competent authority and their investor base of many of the changes identified by the FCA (e.g. changes to a scheme's name, a scheme's legal structure, a scheme's investment objective, policy or strategy, a material increase in fees, or a change in redemption terms). The timing of these notifications may however vary from one EU Member State to the other. For instance, a change to a scheme's name would require an investor notice with a length of 30 days in Luxembourg and 15 days in Ireland. To reduce complexity, the timing of these notifications should be aligned with the applicable timeline in the home jurisdiction.

In the case of the suspension of redemptions, a strict timeline is difficult to understand considering that a similar requirement does not exist for UK funds, which are required to notify the FCA immediately but not before the management company suspends the fund. Furthermore, in a number of situations, management companies would be unable to comply with the requirement to notify the FCA 30 days in advance. Management companies regularly have to deal with unforeseen developments that require that they rapidly, if not immediately, react to a market situation (e.g. in the case of large redemptions).

As a result, in table 8, the FCA should shift several events from the category of changes that requires 'notification at least 30 days before the change could take effect in the UK' to the category of changes that requires 'notification as soon as is reasonably possible'. The changes that would need to be moved

[6] IOSCO, Report on Market Fragmentation and Cross-border Regulation, June 2019.

from the first category to the second include the introduction of supervisory sanctions, the suspension of dealing, the liquidation of a fund, matters leading to negative effects on UK investors, and changes related to connected parties. In addition, for the termination of a fund, the FCA will also have to clarify in COLL 9.5.9G that the notification should be done 'as soon as is reasonably possible' rather than 'immediately when the management company becomes aware that the scheme will be terminated'. There is always a latency period during which management companies take the necessary administrative steps for the liquidation of the fund (e.g., preparation of the relevant legal documents, shareholder communication, and depositary consultation) before it informs its home NCA. An 'immediate' notification to the FCA would therefore result in a situation where the management company would notify the FCA before its home supervisor, which is not appropriate.

Finally, the FCA should clarify what are the 'other changes' that would require management companies to notify the FCA 30 days in advance. In paragraph 4.13 of the consultation, the FCA states that *"[f]or other changes, we propose to require operators to notify us within 30 days of those changes, and to confirm on an annual basis on our system that all the data we hold is up to date."* Should these relate to changes to the information provided during the application process, the FCA should make it explicit.

Chapter 5: Enhanced disclosures regarding lack of access to FSCS and FOS

Q9: Do you agree that our rules for financial promotions for OFR recognized schemes should require a statement about the scope of the FOS and FSCS in relation to the scheme? If so, does the proposed disclosure contain the right information for investors? Please explain any alternative disclosure proposal.

Yes.

Q10: Do you agree that the prospectus of an OFR recognized scheme should include statements about the scope of the FOS and FSCS in relation to the scheme, and the possible availability of alternative redress options? If so, does the proposed disclosure contain the right information for investors? Please explain any alternative disclosure proposal.

No, any change to the prospectus would require a revision by the home NCA, which would add legal uncertainty, uncontrolled delays, and additional costs. Such a requirement is moreover difficult to understand considering that retail investors prefer digital disclosures to prospectuses.

Instead, we would recommend that such statements are included in marketing documents provided to investors at the point of sale, or directly on the management company or distributor's website. Management companies should also have the possibility to develop an integrated version of the UCITS KIID that incorporates this additional information.

EFAMA objects to the proposed COLL 9.5.5R(2)(a) change, which requires management companies to ensure that prospectuses contain information required in COL 4.2.5R. This may include information that is not required in prospectuses in other jurisdictions (e.g., eligible markets, benchmarks, 'total return'). In our view, the national competent authority of one jurisdiction should not determine the contents required for a prospectus regulated in another jurisdiction. There is moreover a risk that the home national competent authority may object to the inclusion of certain contents in a prospectus considering that some of the requirements in COLL 4.2.5R may not fit into a prospectus drafted according to a different regulatory framework. Since the HM Treasury deemed the EEA UCITS regime equivalent, the FCA should not impose detailed requirements on the prospectuses of funds that were drafted according to that framework.

Q11: Do you agree that the supplementary UCITS information provided to retail investors at point of sale should provide the same information as the prospectus, concerning complaints and compensation rights? Please explain any alternative disclosure proposal.

Yes.

A central element of the OFR should be the possibility for recognised schemes to have access to the UK market without having to make significant changes to their marketing material (incl. the UCITS KIID). It would be highly costly for these funds to develop marketing materials tailored only for the UK. From this perspective, supplementary disclosures represent an appropriate balance between this objective and the objective to ensure that UK investors can easily compare recognised schemes and UK funds.

We would nevertheless challenge the two proposals below:

- **Application of the UK Retail Disclosure Framework to recognised schemes:** It is our understanding that the HM Treasury has decided that the up-coming UK Retail Disclosure Framework would apply to both UK and recognised funds.[7] Under the *status quo*, recognised schemes would already incur additional costs as they would have to either develop or update their UCITS KIID in addition to the PRIIPs KID currently used for marketing in the rest of the EEA. Having to comply with new rules would only further increase the costs to market overseas funds in the UK. Although this issue is not part of the scope of this consultation, we recommend that the FCA coordinate with the HM Treasury to ensure that recognised schemes remain out of scope; and

- **Appointment of 'authorised persons' responsible for overseeing the financial promotions of recognised schemes in the UK:** The FCA proposes that management companies marketing recognised schemes should appoint a firm with a Part 4A permission to carry out regulated activities in the UK for communicating or approving their marketing communications. Such a requirement would result in additional costs that funds in the TMPR do not currently face and may moreover result in management companies having to develop communication materials specific to the UK market. The FCA should therefore lift this requirement.

Chapter 7: Other matters

Q16: Do you have any comments on our proposals for maintaining UK facilities for investors in OFR recognised schemes under the OFR? Do you agree that we should review the rules on providing UK facilities for schemes recognised under s.272?

While the FCA allows for the possibility to use remote facilities in the UK, it would be in practice difficult for management companies to meet the conditions outlined by the FCA (e.g., the need to obtain consent from existing or potential investors to rely exclusively on remote facilities).

[7] HM Treasury, UK Retail Disclosure Framework: Policy Note, pp. 11-12.

Q17: Do you agree that it should continue to be possible for a UK UCITS scheme to be merged with an EEA UCITS recognised under the OFR (if this is permitted) and under section 272?

Yes.

Other feedback

The FCA should seek an orderly transition from the Temporary Marketing Permission Regime (TMPR) to the OFR. In particular, it should consult on how the 'landing slots' will be allocated (e.g., fund vs. company-level). While all the sub-funds should fall within a single landing slot for umbrella funds, the FCA should also consider a staggered approach for firms that have several (umbrella) funds in the TMPR. The FCA should however also consider the fact that certain umbrella funds may contain Money Market Funds for which the TMPR has been extended to 2027 due to the on-going review of the MMFR. In such a case, these funds should receive a different landing slot than the one for the rest of the UCITS umbrella.

Lastly, we would strongly recommend that, following this consultative work, the FCA contact its relevant EU peers to explore ways their mutual collaboration can reduce burdens on recognised schemes (e.g., by ensure an exchange of information that would make certain disclosures to the FCA unnecessary) and thereby ensure a smooth transition from the TMPR to the OFR.

ABOUT EFAMA

EFAMA is the voice of the European investment management industry, which manages EUR 28.5 trillion of assets on behalf of its clients in Europe and around the world. We advocate for a regulatory environment that supports our industry's crucial role in steering capital towards investments for a sustainable future and providing long-term value for investors.

Besides fostering a Capital Markets Union, consumer empowerment and sustainable finance in Europe, we also support open and well-functioning global capital markets and engage with international standard setters and relevant third-country authorities. EFAMA is a primary source of industry statistical data and issues regular publications, including Market Insights and the EFAMA Fact Book.

More information is available at www.efama.org

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