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Re: Arrangements for an Asia Region Funds Passport: Feedback Statement and Consultation on  
Draft Rules

Dear Ladies and Gentlemen,

ICI Global<sup>1</sup> welcomes the opportunity to comment to the participating Asia-Pacific Economic Cooperation (APEC) members<sup>2</sup> on the development of the rules and operational arrangements for the Asia Region Funds Passport (ARFP) described in the Arrangements for an Asia Region Funds Passport: Feedback Statement and Consultation on Draft Rules (“Feedback Statement”)<sup>3</sup> and associated annexes (“Second Consultation”).<sup>4</sup> ICI Global commented<sup>5</sup> on the 2014 APEC Consultation Paper: Arrangements for an Asia Region Funds Passport (“First Consultation”).<sup>6</sup>

We appreciate the changes that have been made to the ARFP following the First Consultation. We remain fully supportive of the ARFP which we believe will encourage competition, lower costs and spur fund managers to innovate and find ways to offer superior services and products – all to the benefit of investors.

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<sup>1</sup> The international arm of the Investment Company Institute, ICI Global serves a fund membership that includes regulated funds publicly offered to investors in jurisdictions worldwide, with combined assets of US\$19.6 trillion. We count among our membership 11 Asia headquartered fund managers and many more of our members have significant operations in Asia. ICI Global seeks to advance the common interests and promote public understanding of regulated investment funds, their managers, and investors. Its policy agenda focuses on issues of significance to funds in the areas of financial stability, cross-border regulation, market structure, and pension provision. ICI Global has offices in London, Hong Kong, and Washington, DC

<sup>2</sup> Throughout this letter the term “participant” and “participant economy” refers to an economy that is a party to the ARFP MoU. The term “ARFP Working Group” refers to the group of APEC member economies involved in developing the ARFP framework.

<sup>3</sup> The Feedback Statement is available at <http://fundspassport.apec.org/files/2015/03/ARFP-Feedback-statement-UPDATED-for-release.pdf>

<sup>4</sup> The Consultation Paper is available at <http://fundspassport.apec.org/files/2015/03/ARFP-Annex-1-2-and-3-UPDATED-for-release.pdf>

<sup>5</sup> ICI Global’s comment letter is available at <http://fundspassport.apec.org/files/2015/02/ICI-Global.pdf>

<sup>6</sup> The Consultation Paper is available at <http://fundspassport.apec.org/files/2014/04/20140411-ConsultationPaper-on-the-Passport-Arrangements-FINAL.pdf>

On the more general issues raised in the Feedback Statement and the Second Consultation relating to tax and enlarging the number of Participant economies, we submit the following:

- **Tax and other similar issues** – Tax issues, as we and others have stressed, present crucial challenges for funds distributed cross-border. We strongly support APEC’s continuing commitment to addressing issues, like tax, that could impede the ARFP’s use.<sup>7</sup> We appreciate that at least one country has already begun this work. We stand ready to assist all relevant authorities in minimising, if not eliminating, tax barriers that will erode the benefits of investing in an ARFP fund. We also note that there may be other types of rules in Participant economies, such as capital controls, which could inhibit the regional success of the ARFP. We urge APEC members to continue to devote their efforts to addressing issues that will lessen the attractiveness of the ARFP.
- **Enlargement of number of economies** – We strongly support enlarging the number of Participant economies and making appropriate ARFP changes that would assist in encouraging other economies in the region to join the group. Increasing the number of Participant economies in the ARFP would further support: (i) the development and integration of capital markets across the APEC region; (ii) efforts by Operators<sup>8</sup> to achieve greater regional scale and efficiencies; and (iii) the goal of broadening the base of investors that can benefit from the ARFP.

Our recommendations on substantive requirements, described in more detail below, address the following areas:

- **Delegation** – clarify the process for assessing the effectiveness of regulation in non-Participant economies and the impact of positive (or negative) assessments on the ARFP;
- **Independent Oversight and Compliance Review** – undertake further work to reasonably accommodate the range of fund structures available in the Asia region;
- **Investment in Regulated CIS** – expand the domiciles of regulated CIS available for investment by ARFP funds;
- **Single Entity Exposure Limits** – further calibrate limits to better accommodate cross-border regional and global portfolio management practices (Questions 4-7);
- **Data Protection** – develop procedures for the handling and protection of data on a cross-border basis among regulators and other participants in the ARFP;
- **Funds under Management Threshold** – include separately managed accounts in the assets that can be used to meet the threshold;
- **Financial Resources Requirement** – fix a local currency equivalent exchange rate each year to take account of currency fluctuations, as is adopted in other multi-currency situations (Question 2);
- **Fund Labelling** – evaluate Participant economy rules to enable fund labels, such as MMF and ETF, to comply with home and host rules;
- **Securities Lending Arrangements** – adopt a pragmatic approach for the posting of additional margin collateral by a counterparty to an ARFP fund.

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<sup>7</sup> Paragraph 16, Feedback Statement

<sup>8</sup> Throughout this letter the term “Operator” refers to the operator of the ARFP fund as defined in Section 56 of Annex 3

## Comments on Substantive ARFP Requirements

### Delegation

We believe that it would be helpful to provide further clarity in three areas:

- *The process for assessing eligible non-Participant economies.*<sup>9</sup> The Working Group should better describe the standards used to ensure consistency in the assessments of Home Regulators. In addition, the Working Group should provide clarity as to whether a non-Participant economy that is not an IOSCO Appendix A signatory but, in the opinion of a Home Regulator has a regulatory framework that is “*broadly similar in effectiveness*” to the Home Economy, could pass the delegation assessment.
- *The effect of positive (or negative) assessments of non-Participant economies on other Member Economies and the ARFP.* The Working Group should provide clarity as to how the positive (or negative) assessment of a non-Participant economy as “*broadly similar in effectiveness*” by one Home Regulator impacts Operators and ARFP funds in other Participant economies. For example, would other Passport Regulators need to undertake their own assessment of the non-Participant economy or “endorse” the assessment before their local Operators could delegate to the non-Participant economy?<sup>10</sup>
- *The eligibility of delegates.* The Working Group should provide further guidance on the conditions that must be met to permit the delegation of up to 20% of an ARFP fund’s portfolio. The Feedback Statement permits delegation to an entity which “*is subject to a regulatory regime that provides broadly similar outcomes*”.<sup>11</sup> On the other hand, the rules in the Second Consultation require the investment officers of the delegate to have a certain level of experience.<sup>12</sup> The Feedback Statement requirement for the delegate to be subject to a regulatory framework that is “*broadly similar in effectiveness*” only appears to be applicable if more than 20% of an ARFP Fund’s assets are delegated.<sup>13</sup>

### Independent Oversight

We support the concept of independent oversight but emphasise that it must accommodate different fund structures to be workable and successful, as IOSCO has sought to in its work in this area.<sup>14</sup> We remain concerned about the workability of the proposal in a trust structure. We recommend that further work be undertaken to accommodate the full range of permissible fund structures regionally, taking account of oversight arrangements in other economies. Such work will strengthen the ARFP and take account of future innovations.

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<sup>9</sup> Paragraph 11(3) requires that “the delegate must be regulated in a Participant or in an economy that has a regulatory framework applying to financial asset CIS that is broadly similar in effectiveness to that of the Home Economy in the opinion of the Home Regulator, having regard where relevant to the IOSCO principles and IOSCO assessment methodology relating to CIS”.

<sup>10</sup> i.e. if the Home Regulator in Participant A deemed Country X’s regulatory framework to be “broadly similar in effectiveness” to its own regulatory framework, could a Fund Operator in another Participant B delegate to Country X on the basis of the assessment undertaken by Participant A’s Home Regulator?

<sup>11</sup> Page 13, Feedback Statement

<sup>12</sup> Paragraph 11(4), page 22, Annex 3

<sup>13</sup> Paragraph 11(2), page 22, Annex 3

<sup>14</sup> IOSCO, Examination of governance for collective investment schemes, Final Report, available from

<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD219.pdf>, describes several fund organisation types and arrangements for independent oversight.

We believe this work will also be very important in efforts to enlarge the group of Participant economies.

### Compliance Review

We support the goals of a compliance review. To limit cost, and the possibility of duplication and complexity from multiple compliance reviews, we recommend that further consideration should be given to other ways to accomplish it. For example, considering a role for the independent oversight entity in a compliance review with the Operator's compliance staff. In addition, there may be Participant economy oversight arrangements that also involve compliance reviews.

### Investment in Regulated CIS

We recommend expanding the domiciles of regulated CIS available for investment by ARFP funds. There are substantively regulated funds that are sold to retail investors in other parts of the world, including in Asia, which are highly similar to UCITS. We do not believe the ARFP should discriminate among regulated funds in one jurisdiction over another and are concerned this could raise issues, for example under Member Economy trade agreements with "national treatment" commitments. We also do not see a rationale for only allowing a single type of regulated fund from one region.

A possible approach could be to limit investment to regulated funds subject to regulatory regimes that are consistent with IOSCO standards, in a similar vein to the approach proposed for the delegation of investment management functions. We also believe that permitting the ARFP funds to invest in more regulated funds would align the requirements with those in the ASEAN CIS Framework (as well as global approaches for regulated funds).<sup>15</sup> We are supportive of investment into such funds as such investments support portfolio diversification and efficiencies – objectives of the ARFP.

### Single Entity Exposure Limits (Questions 4-7)

We support the graduated approach for single entity exposure limits proposed in Option 1 in the Second Consultation with some modifications.<sup>16</sup> We recommend the following changes to help Operators reduce costs and the operational complexities of managing passport and non-passport funds with the same or similar investment objectives and strategies, *e.g.*, "mirror" funds.

- We respectfully recommend that the obligations on an Operator to assess the default risk of an assessed CCP, given that such CCPs are authorised and subject to ongoing regulatory supervision, be removed.<sup>17</sup>
- We recommend including an explicit statement in the final rules that assessed CCPs are exempt from the single entity exposure limits.<sup>18</sup>

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<sup>15</sup> Paragraph 4, section 2, Standard of Qualifying CIS, ASEAN CIS Framework, available from [http://www.theacmf.org/ACMF/upload/standards\\_of\\_qualifying\\_cis.pdf](http://www.theacmf.org/ACMF/upload/standards_of_qualifying_cis.pdf)

<sup>16</sup> Section 30, p41-44, Annex 3

<sup>17</sup> Paragraph 27(3)(b), second "(g)" states "*the Operator of the Passport Fund believes on reasonable grounds, having regard to independent sources of information, that there is very low risk of the central clearing counterparty defaulting in any of its obligations over the subsequent 5 year period*"

<sup>18</sup> The first consultation provided an exception for CCPs, subject to certain conditions (page 27) but the second consultation does not appear to contain a similar exception.

- We recommend that further consideration be given to increasing the single entity exposure limits for government securities, including risk-assessed government securities. For instance, in many markets around the world, including in the Asia region, investors that are approaching retirement make use of funds with exposure to government securities higher than that accommodated under the proposed limits (e.g. certain life-cycle or target-date funds).<sup>19</sup> Recent ICI Global research shows the beneficial role fund flows play in providing stability and diversity to securities markets, particularly in emerging economies.<sup>20</sup>
- We recommend that further guidance should be provided on the interaction of home rules and the passport rules concerning limits on investments conferring significant management influence.<sup>21</sup> Various obligations and thresholds exist in Participants' home rules which may permit exposures higher or lower than those accommodated under the proposed limits.<sup>22</sup> We recommend that the various home rules are evaluated to identify potential areas of interaction with the passport rules.

### Data Protection

The ARFP will necessarily involve the use and transfer of data on a cross-border basis among regulators, operators, delegates, distributors, investors and other participants. Appropriate handling and protection of this data is essential for public and investor confidence in the ARFP.

We recommend that consideration be given to the development of policies and procedures for the transmission, storage and use of data<sup>23</sup>, including drawing on existing frameworks in other parts of the world.<sup>24</sup> Many fund management organisations with a presence in multiple countries have developed global programs to accommodate data protection requirements around the world. We also recommend that the regulatory rules that are applicable to data protection and data privacy for the ARFP be addressed (e.g. Home, Host, Passport or some combination), including how conflicts will be resolved.

Consideration should also be given to developing Passport Rules for a single disclosure framework for ARFP investors on the use of their personal data.<sup>25</sup> Disclosure on the use and protection of data could be made at the point of investment. These disclosures would serve to enhance awareness among investors and provide an efficient mechanism through which Operators could satisfy any data protection and data privacy requirements.

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<sup>19</sup> The EU UCITS Directive permits Member States to allow funds to invest in accordance with the principle of risk spreading up to 100 % of their assets in different transferable securities and money market instruments issued or guaranteed by a Member State, one or more of its local authorities, a third country, or a public international body to which one or more Member States belong (Article 54(1), DIRECTIVE 2009/65/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS))

<sup>20</sup> Plantier, L. Christopher. 2015. 'Regulated Funds, Emerging Markets, and Financial Stability.' ICI Global Research Perspective 2, no. 1 (April). Available at [www.iciglobal.org/pdf/icig\\_per02-01.pdf](http://www.iciglobal.org/pdf/icig_per02-01.pdf)

<sup>21</sup> Paragraph 36, page 47, Annex 3

<sup>22</sup> For example, limits on the holding of outstanding shares, general offer obligations, and notification of substantial shareholding.

<sup>23</sup> We acknowledge that arrangements for cross-border supervisory arrangements for regulators will comprise "Annex 4" of the MoU. Annex 4 was not released as part of the consultation.

<sup>24</sup> The EU has a well-established framework through which regulators share information (see, for example, Article 50 and 52 of DIRECTIVE 2011/61/EU OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010, available from <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:174:0001:0073:EN:PDF>)

<sup>25</sup> The EU has a well-established framework for the protection of personal data which is currently being reformed (Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data, available from <http://eur-lex.europa.eu/legal-content/en/ALL/?uri=CELEX:31995L0046>) and ongoing reforms ([http://ec.europa.eu/justice/newsroom/data-protection/news/120125\\_en.htm](http://ec.europa.eu/justice/newsroom/data-protection/news/120125_en.htm)).

### Funds under Management Threshold

The Second Consultation allows investment funds that predominantly hold permitted investments<sup>26</sup> to count towards the USD 500 million threshold.<sup>27</sup> It is not uncommon for Operators to manage assets that are Permitted Investments in other ways such as through separate accounts (e.g., assets under delegation arrangements, pension mandates). We submit that under those circumstances it should be appropriate for such accounts to be counted towards the funds under management threshold as the purpose is to demonstrate experience managing such assets.

### Financial Resources (Question 2)

We recognise that a specific currency is technically needed when setting the financial resources requirement for an Operator.<sup>28</sup> One approach adopted in other multi-currency situations is to fix the local currency equivalent exchange rate for a particular period (e.g., a year) for calculating the financial resources requirement. For instance, the EU base capital resources requirements for insurers in the UK are determined each year on 31 December using the local exchange rate on the last [business] day of the preceding October.<sup>29</sup>

### Fund Labelling

We remain concerned about possible incompatible requirements between home and host countries, particularly for Money Market Funds (MMFs). One method through which this issue may be resolved is by avoiding the usage of terms such as “money market fund,” although this may not be possible if required to use such a label in some situations.<sup>30</sup> In addition, labels can be important to an investor’s understanding of a fund, including facilitating the comparison of funds. Rather than avoiding the use of labels, we recommend that local Participant rules be evaluated to identify how labels can be used in a manner which complies with home and host rules.

### Securities Lending Arrangements

We recommend adopting a pragmatic approach to determining the time period over which additional margin collateral should be posted to an ARFP fund to cover securities lending arrangements. Funds in the Asia region often enter into arrangements with counterparties based in other parts of the world, including in the US and Europe. Geographic and timezone differences may raise practical challenges for counterparties to post collateral by the close of their next local business day, for instance if they need to instruct another party to effect a collateral transfer. A possible approach to take account of these challenges could be to require a counterparty to post collateral as soon as practicable, taking account of geographic and timezone considerations.

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<sup>26</sup> As defined in Division 6.2 of Annex 3 (page 35)

<sup>27</sup> Paragraph 3(4)(a) of Annex 2 (page 7)

<sup>28</sup> Section 7, p19, Annex 3

<sup>29</sup> UK Prudential Regulatory Authority GENPRU 2.1.33R rule “In the case of an *insurer* and for the purposes of the *base capital resources requirement*, the exchange rate from the Euro to the pound sterling for each year beginning on 31 December is the rate applicable on the last day of the preceding October for which the exchange rates for the currencies of all the European Union member states were published in the Official Journal of the European Union”, available from <http://fshandbook.info/FS/html/handbook/GENPRU/2/1>

<sup>30</sup> p7, Feedback Statement

## **Conclusion**

The ARFP continues to hold great potential benefit to investors and regulated fund managers in the participating countries. We appreciate the substantial efforts that have been undertaken to date on the ARFP and welcome the opportunity to provide input for the Second Consultation. We also strongly support efforts to increase the number of economies participating in the ARFP. We believe a larger number of participants will strengthen the ARFP and further the goals of APEC. We look forward to working with you in further developing the ARFP and encourage your efforts to have other countries in the region join this initiative.

If you have any questions about our comments or would like additional information please contact Qiumei Yang, CEO, Asia Pacific ([qiumei.yang@iciglobal.org](mailto:qiumei.yang@iciglobal.org)), Susan Olson, Chief Counsel ([susan.olson@iciglobal.org](mailto:susan.olson@iciglobal.org)), or Giles Swan, Director of Global Funds Policy ([giles.swan@iciglobal.org](mailto:giles.swan@iciglobal.org)).

Yours faithfully,

/s/

Dan Waters  
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