

**H.M. TREASURY**

**FINANCIAL SERVICES AND MARKETS ACT**

**TWO YEAR REVIEW: CHANGES TO SECONDARY LEGISLATION**

**RESPONSE FROM EVERSHEDES LLP**

1. **INTRODUCTION**

1.1 Eversheds welcomes the opportunity to comment on H.M. Treasury's proposals in respect of secondary legislation arising out of the Financial Services and Markets Act 2000 (the "Proposals").

1.2 We have not commented on all questions: only where the Proposals are relevant to Eversheds' financial services funds' practice.

## **SECTION 10: OPEN-ENDED INVESTMENT COMPANIES**

### **Requirement for an Annual General Meeting, preparing documentation and organising meeting venues**

#### **Q. 51 Do you agree that the costs of requiring OEICS to have an AGM outweigh the benefits?**

In our experience, as advisers to a large number of fund managers operating open-ended investment companies, we have found that authorised corporate directors do find AGM's expensive both in terms of time, money and resource. Many OEICS have hundreds of thousands of investors and to prepare AGM documentation and despatch it with the relevant report and accounts can incur high printing and postage costs

Considerable manpower is also involved in drafting the relevant documents and submitting them to the Financial Services Authority for Regulation 21 FSMA approval (which has a one month approval period), as well as in organising and staffing the meeting itself.

Fund managers will be able to provide precise figures but our experience suggest that the majority of fund managers receive a very limited response to AGM meetings and in our experience it is rare that shareholders attend the AGMs in person.

#### **Q. 52 Do you agree that OEICS should be able to elect to dispense with the holding of AGMs?**

When OEICS were first consulted on by H.M. Treasury in the mid 1990s, AGMs were suggested as a way of making an ICVC accountable to its shareholders in much the same way as a company is accountable to its shareholders under the Companies Act through its AGM.

In practice, the AGM has not been used by shareholders as a mechanism for challenging the ACD on its management of the OEIC and is merely an administrative inconvenience for most ACDs.

In addition, there is a further argument against the use of AGMs. The Financial Services Authority ("FSA") have over the last few years been seeking to put unit trusts and OEICS on a level playing field.<sup>1</sup> We have seen the culmination of this in April 2004 with the advent of a new Sourcebook for Collective Investment Schemes (COLL) in which the FSA have sought to eliminate the remaining differences which remained between authorised unit trusts and OEICS. The requirement for an OEIC to hold a meeting is one of the few remaining differences. Unit trusts are not obliged to hold an AGM and the FSA did not seek to

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<sup>1</sup> Paragraph 2.4 of Consultation Paper 185, "The CIS Sourcebook - a new approach", Financial Services Authority, May 2003.

introduce such a mechanism for authorised unit trusts in its recent review of the CIS Sourcebook.

For these reasons we would argue that AGMs for OEICS are not fulfilling the purpose for which they were introduced and the ACD should at least have the option of electing to dispense with them.

**Q. 53 Do you agree that there will be adequate safeguards to protect shareholders if the requirement for OEICS to have an AGM is changed to an elective requirement?**

The structure of the AGM as currently provided does not in practice afford the shareholders much opportunity to affect the running of the OEIC or to bring about changes to protect their own interests. For example, shareholders are asked to approve the appointment or re-appointment of the auditor but are not equipped with information (such as the fee rates) to allow them to make an informed decision on the auditor and the value for money they provide to the Fund. As mentioned above, shareholders rarely attend AGMs and we are not aware of any instances of shareholders requisitioning resolutions at AGMs to air their concerns.

In addition, the system put in place by the FSA rules does afford holders a number of protections. For example, a shareholder meeting is required to introduce a new category of remuneration or a change to the investment and borrowing powers or other fundamental changes to the Fund. The Depositary has its role of oversight of the Fund and is required to act in the sole interests of shareholders (see CIS 7.4.1R(3)). The Depositary has obligations to notify the FSA of infringements of the rules in certain circumstances. The shareholders also have the ultimate safeguard if they were unhappy with their investment - the ability to redeem at NAV at any time.

**Q. 54 Is the requirement that all shareholders agree to an elective resolution too onerous a requirement for OEICS to meet? Should the threshold be lower e.g. 95% of shareholders?**

Experience has shown that typically shareholder response to a notice of meeting and a request to vote by proxy is low. Fund managers will be able to provide the statistics but we understand that response level is typically less than 50%.

We believe it is impractical to require a 100% response rate. Many investors will not respond to such a mailing. This raises the question as to whether non-respondents will need to be chased and on how many occasions? This will add to the expense and administrative burden of such an exercise.

In addition, many fund managers have a percentage of “gone away” holders on their register. Would these holders need to be included or would they be disregarded for the purposes of the vote?

We would advocate that a threshold is set which is no higher than the requirements of the FSA Rules on shareholder meetings. In such cases 75% of holders who vote need to be in favour for a resolution to be passed. This threshold is set in respect of resolutions which it could be argued are more fundamental to a fund than removing the AGM provisions, a change to investment objective for example.

Under the new FSA rule book (COLL) the FSA permits fund managers to decide whether or not the change they are proposing is “fundamental” and so requires a shareholder meeting or is significant and therefore requires 60 days’ prior notification to holders. A significant change includes a change which:

- (a) affects a unitholder’s ability to exercise his rights in relation to his investment; or
- (b) would reasonable be expected to cause the unitholder to reconsider his participation in the scheme.

Were the proposed change in respect of AGMs governed by this regime, there are strong arguments that the change would only be classified as significant and accordingly holders would only need to be notified 60 days in advance of the change.

**Q. 55 Should an ordinary resolution be sufficient to revoke the elective resolution?**

Given that re-introducing AGMs would be a direct cost to the OEIC concerned, we believe that an extraordinary resolution would be more appropriate.

**Q. 56 Regarding the proposing amendments to regulation 34 outlined in paragraph 10.18, do you agree that appointments should not have effect for longer than twelve months starting on the date of the appointment?**

This would seem to be a sensible approach.

**Q. 57 Do you have any comments on our proposed amendment for regulation 36 outlined in paragraph 10.19?**

We disagree with this approach. This will incur further expense for fund managers and it is unlikely that most holders will read the information. An alternative approach would be to simply highlight to investors, perhaps in the next report and accounts and in the Prospectus, that the information set out in regulation 36 can be inspected at the offices of the ACD. This

is the approach taken in respect of, for example, the instrument of incorporation and material contracts, such as the agreement with the Depositary.