THE
INVESTMENT
ASSOCIATION
INVESTMENT MATTERS

Joint Committee of the European Supervisory Authorities

The Investment Association
65 Kingsway, London, WC2B 6TD

T +44 20 7831 0898
W theinvestmentassociation.org
Twitter @InvAssoc

Submitted via electronic submission

Date: 2 October 2015

Dear Sirs

RE: Draft Joint Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector

The Investment Association welcomes the opportunity to respond to the Joint Committee of the European Supervisory Authority's consultation.

The Investment Association represents the UK asset management industry. Our members manage over €7.5 trillion of assets on behalf of UK, European and international clients, both retail and institutional. Collectively, our members make up the second-largest asset management industry in the world.

We fully support the objectives of the proposed Guidelines to provide the necessary legal certainty, clarity and predictability with regard to the assessment processes contemplated in the sectoral Directives and Regulations. In doing so we note the objectives of the Directive which state that the requirements for prudential assessments 'should not prevent market participants from operating effectively in the securities market', and that the 'information required for assessing a proposed acquisition… should be proportionate to the involvement of the proposed acquirer in the management of the entity' being acquired.

Key issues:
Asset managers acquire positions on behalf of a diverse range of their underlying clients. In transacting deals on behalf of these underlying and unconnected clients, asset managers are not seeking to acquire control, regardless of whether the aggregation of their total positions held in an investment firm may amount to a controlling position.

The Investment Association is a company limited by guarantee registered in England and Wales. Registered number 04343737. Registered office as above.

Given the asset management model of ownership for investment return, rather than control, and the recitals noted above, we strongly argue for changes to the Guidelines to provide proportionate relief for asset managers, by delivering a regime which is suitably tailored to reflect the nature of, and reasons for, an asset manager’s ownership.

Yours

Adrian Hood
Regulatory and Financial Crime Expert

Chapter 3: Background and rationale

Q1: Do you have any general comments on the draft Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector?

"Decision to acquire"
The business model of an asset manager means that it will manage significant assets across many funds and multiple segregated mandates, quite possibly across a number of asset management entities with multiple portfolio managers in different locations making independent investment decisions.

As a result of this business model, asset management firms' systems are unable to track intended acquisitions in advance. In particular, parent entities within the group structure would not normally be informed of, or otherwise privy to, any intended investment decisions by asset management firms within their group. Entities within an asset management group, regardless of their position within the organisational structure, may only become aware of their aggregated indirect holdings after the thresholds have been reached. At no point in time are any of these entities capable of determining intended group-wide holdings in any particular issuer, as they are not acquiring them with the intent to control, but merely as investments on behalf of their customers. Consequentially, capturing the decision to acquire/moment of intent to reach or cross a relevant threshold is practically impossible for the notifying entities higher up in groups.

The concept of a 'decision to acquire' should not be applicable to situations where the asset management acquirer crossed a threshold without taking the deliberate decision to do so. This would include the situation of asset managers increasing their holding for one client, which results in their aggregated position passing through a threshold. The asset manager did not, by increasing their holding for that one client, intend to acquire control of the firm.

In practice, the only way that an asset management firm can apply the point of 'the decision to acquire' is to put in the notification when the firm comes close to the threshold. However, even then there may be a change of business appetite so that the asset manager does not, subsequently, wish to cross the threshold. This would mean that an asset management firm would frequently have to withdraw notifications. Or after finally obtaining the permission to cross the threshold (and the time and effort that this required) sell down and fall back below and then have to restart the whole notification period again. We, therefore, request that the Guidelines introduce a notification regime, similar to that which operates in the UK presently under the FCA's Section 178 notice, as it allows permission for an extended period of time and allows asset management firms to move up and down around the 10% threshold.

"Assessment Period"
Given that the Directive states that the prudential assessment 'should not prevent market participants from operating effectively in the securities market', and that 'the information required for assessing a proposed acquisition' should be 'proportionate to the involvement of the proposed acquirer in the management of the entity being acquired' we consider that the requirements of the draft Guidelines on assessment periods are inconsistent with these recitals of the Directive for asset management firms.

Asset management firms rely on their ability to react to market conditions in real time and in order to act in the long-term best interests of their clients. The extended assessment period limits the ability of asset manager to react in real time to market conditions where they are close to a threshold for which a prudential assessment may be required. This constitutes a *de facto* prohibition on such investments, to the disadvantage of the underlying investors.

We would also like to raise the issue of the burdensome amount of information that is required for each and every notification. It is not uncommon for holdings of an asset management firm to hover around thresholds, resulting in multiple notifications, each of which takes a significant amount of work and time to complete. Due to the complexity of an asset management group's structure the amount of detail required about every entity in the chain of control can create an onerous administrative burden. Combined with the lack of harmonisation on the actual information and documentation required in each Member State, and it makes it very difficult to produce a notification that would be considered complete. This may require so much man-power and time that asset management firms may seek not to cross any such thresholds. This can, again, constitute a *de facto* deterrent to such investments, to the disadvantage of the underlying investor.

"Acting in Concert"
The current broad description of 'acting in concert' in the Guidelines means that various jurisdictions have taken different approaches to what would be considered to be 'acting in concert'. This causes serious legal uncertainty for asset management firms, among others, trying to comply with their obligations under the Directive. By way of example, it is not always clear if staff of an asset management firm could be considered to be acting in concert with the asset management firm, which would require the firm to aggregate its holdings with the personal holdings of all its staff. While we do not think that staff should be considered to be acting in concert with their asset management employer, we would appreciate it if the ESAs could provide clear guidance within the proposed Guidelines on this definition such that a harmonised regime operates across the EU.

Q2: Do you consider the level of detail used in the draft Guidelines to be appropriate?

We consider that the Guidelines impose an undue burden on asset management firms due to their not reflecting the nature of an asset management firm's business. We recommend that the Guidelines be amended to make the requirements imposed on asset management firms proportionate.

Asset management firms acquire positions on behalf of clients, as long-term investors, not in order to gain, or exercise, control over them. As an asset management firm may hold positions in an investment firm on behalf of numerous clients, its aggregated position could unintentionally breach thresholds set out in the Directive. The asset management firm is not, thus, seeking to acquire "control" of the firm. The aggregated position which an asset management firm holds can regularly change, such that it may repeatedly cross thresholds, necessitating continual submission of notifications to the national competent authority.

We, therefore, request that the Guidelines recognise the business model of an asset management firm by introducing a simplified, proportionate, notification regime, similar to that which operates in the UK presently under the FCA's Section 178 notice. Such a regime, operating across the EU, would reduce the administrative burden imposed on asset management firms, deliver the required proportionality, and ensure participants within the securities markets could continue to operate effectively for the benefit of both the market and the asset management firm's investors.

Chapter 4: Joint Committee Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector

Q3: Which approach identified above do you consider to be the most appropriate, Option A or Option B? Please explain your answer.

Given that the Directive defines a 'qualifying holding' as including direct and indirect holdings in an investment firm, we would rather Option B, as the multiplication will always give a more realistic indication of the true level of control.

However, there are serious problems with this in practice. There is no legal obligation for an acquired firm to disclose its underlying holdings to the asset management firm. There is, thus, no certainty that the asset management firm can obtain the data on indirect holdings which would enable it to comply with this obligation. Chains of ownership can be long, and if the detail of investment firms partially owned or controlled further down the chain is not disclosed at any point, then firms higher up the chain will have no knowledge of any investment firms which may exist. As a result an asset management firm may invest in a non-investment firm, e.g. holding 50%, but be entirely unaware that this firm itself has a qualifying holding in an investment firm. Without this knowledge the asset management firm risks inadvertently failing to make the appropriate notifications.

We disagree with the premise that a firm could have control solely through an indirect holding. We understand that the Directive currently states that indirect holdings can make up a qualifying holding, and that the ESAs cannot change the law at the moment. We do, however, want to encourage the ESAs to engage on this issue.

We would, ideally, ask for a relief to be applied to asset management firms, in light of their holdings being for the purposes of investment, rather than control, resulting in their not having the ability to 'look-through' to underlying holdings.

Further, we would propose that, for asset management firms, the ESAs' Guidelines should make it clear that 'control' would be considered to exist only in a situation where the holding in another firm reached the Take-Over mandatory bid level relevant to that jurisdiction (as this could at least be managed by an asset management firm).

We also propose, in keeping with a proportionate application, that the assessment of indirect holdings for asset management firms should apply only in relation to the first layer of indirect holdings – as not doing so could impose obligations across a, potentially, infinite chain of underlying holdings. Finally, we recommend that the guidelines give recognition to the fact that a qualifying holding could not solely be comprised of indirect holdings.

Q4: Would you propose a different test for assessing whether a qualifying holding is being acquired indirectly? Please explain your answer.

Please see our comments to Q3.

We would propose that the ESAs grant asset management firms a relief so that they do not have to attribute indirect holdings, where these cannot be ascertained, towards a qualifying holding. The ESAs should grant this relief on the basis that asset management firms are passive investors and do not seek to have control. If a relief could not be granted then we would stress that indirect holdings should only be included if the ESAs' guidance specified that an asset management firm would only be considered to have control of an issuer if it obtained the mandatory bid level relevant to that jurisdiction.