

- 1.1 This document introduces the *European Long-Term Investment Funds Regulation (No 2) Instrument 2016* (FCA 2016/34 / FOS 2016/7), which was made by the FCA Board on 21 April 2016. On 27 April 2016, the voluntary jurisdiction rules and standard terms were made by the Board of the Financial Ombudsman Service, subject to the approval of the FCA.

## *European Long-Term Investment Funds Regulation (No 2) Instrument 2016 (FCA 2016/34) (FOS 2016/7)*

- 2.1 Following consultation in CP15/27<sup>1</sup>, the FCA Board has made changes to the FCA Handbook sections listed below:

### **Glossary**

### **SUP 10A and 13A**

### **DISP 1 and 2**

### **COMP 5**

### **FUND 4**

- 2.2 In summary, this instrument makes changes to apply the FCA's redress rules to European Long-Term Investment Funds.
- 2.3 This instrument comes into force on **28 April 2016**.

## *Consultation feedback*

### **Approach to redress for European Long Term Investment Funds**

#### **Background**

- 3.1 In September 2015 we consulted on changes to align our Handbook with the new regulation on European long-term investment funds (the 'ELTIF regulation').<sup>2</sup> The ELTIF regulation is directly applicable under EU law and has applied since 9 December 2015.<sup>3</sup> We also consulted, jointly with the Financial Ombudsman Service, on rules regarding redress arrangements for eligible retail investors in European long-term investment funds (ELTIFs). Overall the response to our proposals was positive, however we considered that the issues raised in relation to our redress proposals required further consideration. This notice provides our joint feedback statement and explanation of how the final rules differ from those which we originally consulted on. Where relevant in the text, "we" refers to both the FCA and the Financial Ombudsman Service.

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<sup>1</sup> CP15/27 *UCITS V implementation and other changes to the Handbook affecting investment funds* (September 2015)  
<http://www.fca.org.uk/your-fca/documents/consultation-papers/cp15-27>

<sup>2</sup> CP15/27 *UCITS V implementation and other changes to the Handbook affecting investment funds* (September 2015)

<sup>3</sup> The ELTIF regulation is Regulation (EU) 2015/760 of the European Parliament and of the Council of 29 April 2015 on European long-term investment funds. These funds will invest in long term projects such as infrastructure.

3.2 On 3 December 2015 the FCA Board approved changes to our Handbook in relation to all proposals on the application of the ELFTIF regulation<sup>4</sup> other than those relating to redress. We are now publishing changes to the Handbook that will apply our redress rules to ELTIFs.

### **Summary of proposals**

3.3 We consulted on bringing all managers and depositaries of UK-domiciled ELTIFs within the scope of the Financial Ombudsman Service (the 'ombudsman service') and the Financial Services Compensation Scheme (FSCS) when these funds are offered to eligible retail investors. This would also have included the activities of:

- incoming EEA alternative investment fund managers (AIFMs) that manage UK-authorized ELTIFs, and
- UK AIFMs managing ELTIFs domiciled elsewhere in the EU from the UK on a services basis

3.4 Our proposals reflected a general continuation of the current regime under the Alternative Investment Fund Managers Directive (AIFMD) (2011/61/EU). ELTIFs are currently categorised as 'unauthorised AIFs' and their managers therefore fall within scope of our redress rules. Our proposed changes to the current regime were:

- A proposal to include depositaries of ELTIFs, which are not covered under existing rules.
- A proposal to include managers and depositaries of ELTIFs set up as closed-ended investment companies. Closed-ended investment companies, commonly known as investment trusts, are not currently within the scope of the redress rules. However, ELTIFs will be authorised by us and eligible investors in all other types of authorised fund receive ombudsman service and FSCS cover. Therefore we were concerned that differences in the regulatory treatment of investors within the ELTIF 'brand' might create confusion for potential retail investors.
- A proposal to amend the definition of an authorised fund to include ELTIFs, for the purposes of the Compensation sourcebook (COMP) and the chapter of the Fees Manual on Financial Services Compensation Scheme Funding (FEES 6).
- Finally, we proposed consequential changes to remove the definitions of 'closed-ended corporate AIF' and 'internally managed corporate AIF' from the Glossary.

### **Feedback**

4.1 We received five responses, including four from trade associations, touching on our redress proposals.

4.2 Two respondents were satisfied with our proposals. Two others supported the proposal to bring managers and depositaries of ELTIFs marketed to retail investors within the scope of the ombudsman service and the FSCS, but suggested a clearer distinction should be made between ELTIFs that will be marketed to retail investors and those that will not. Finally, one respondent said managers and depositaries of ELTIFs set up as investment trusts should not fall within the scope of the ombudsman service and the FSCS.

4.3 This respondent raised several concerns:

- Our policy could create a possibility that more investment trusts are brought into scope of the ombudsman service in the future, which the respondent considered unacceptable.

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<sup>4</sup> HN28/15 Handbook Notice No.28 (December 2015)  
<http://www.fca.org.uk/static/documents/handbook/fca-handbook-notice-28.pdf>

- The ombudsman service might make a financial award where the eligible complainant is an individual shareholder in a self-managed ELTIF. Complainants would be compensated out of the assets attributable to other shareholders in the self-managed ELTIF, and no mechanism is available to compensate such complainants without compromising the interests of other holders of the same class of security.
- Shareholders in investment trusts are already protected by tailored governance and legal mechanisms under established principles of company law, which may conflict with our proposals.

4.4 This respondent sent further specific questions on the practical application of the rules to assist us in our analysis.

### ***Our response***

4.5 We intend to implement our proposal for ELTIFs as consulted on, with the exception of ELTIFs set up as investment trusts.

4.6 A general distinction between retail and non-retail ELTIFs is already in place for firms. As set out in DISP 1.1.12R, firms can benefit from an exemption from the rules by notifying us in writing that they will have no dealings with eligible complainants. Similarly, FEES 6.2 sets out how firms can claim exemptions from FSCS levies. These exemptions will also be available to managers and depositaries of ELTIFs that are not marketed to retail investors, so a specific distinction is not required.

4.7 We have considered the arguments regarding consistency of treatment for all investment trusts against the desire to provide consistency within the ELTIF brand. We have also taken into account the risks associated with bringing ELTIFs that are investment trusts, particularly those that are self-managed, within the scope of the ombudsman service and the FSCS.

4.8 We have also considered the specific concerns raised and take the view that:

- Our position on bringing established investment trusts within the scope of the ombudsman service and the FSCS was set out in our policy statement on implementing AIFMD.<sup>5</sup> Our latest proposal does not reopen the debate on their treatment.
- In the case of a self-managed investment trust, the assets of the company are indirectly those of the investors and as such, any compensation awarded by the ombudsman service might affect the assets and returns of all investors in the company. However, not all complainants are awarded financial compensation – the ombudsman service may require a firm to resolve a complaint by other means. In reality, the risks of a successful complaint affecting the assets of all investors can be mitigated: the ombudsman service has the power to dismiss a complaint if evidence leads it to believe the complaint would be better suited for the courts.
- As such, and after further engagement, we do not think our proposal to bring ELTIFs that are investment trusts within the scope of the ombudsman service and the FSCS would create a misalignment with company law. The ELTIF regulation makes the manager of an ELTIF liable for any infringement of the regulation and for losses or damages resulting from non-compliance with the regulation.<sup>6</sup> The ombudsman service would offer an alternative for eligible retail investors, who might not have the means to go to court to seek redress.

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<sup>5</sup> PS13/5 *Implementation of the Alternative Investment Fund Managers Directive* (June 2013)  
<https://www.fca.org.uk/your-fca/documents/ps13-5-implementation-of-the-aifmd>

<sup>6</sup> Article 8(3) of the ELTIF regulation

- 4.9 However, notwithstanding the above we have decided to postpone applying our proposals to ELTIFs set up as investment trusts, at least until we have a better overview of the ELTIF market, for a number of reasons. Investment trusts, unlike some other types of legal structures for investment, provide additional ways for investors to influence the actions of their board. This means the range of issues that might give rise to an unresolved complaint being referred to the ombudsman service is likely, in practice, to be limited. Therefore, the costs associated with setting-up internal procedures and paying on-going levies might not currently be proportionate.
- 4.10 This is not to say that investors in investment trusts are less likely to have cause for complaint, but the mechanisms available to them under company law should be sufficient to mitigate our concerns for the time being. Other investment trusts are not currently subject to the ombudsman service or the FSCS. In addition, we do not have evidence to suggest that the lack of such cover has been a cause of consumer detriment since the rules were amended in 2003 to strengthen the governance of investment companies.<sup>7</sup>
- 4.11 As no market for ELTIFs has yet developed, we have therefore proposed to treat ELTIFs set up as investment trusts like other such companies under the redress rules, at least for the time being.
- 4.12 We nevertheless expect all firms to act in line with FCA Principles for Business as applicable<sup>8</sup> and with our Treating Consumers Fairly principles.<sup>9</sup> This includes providing consumers with clear information about what they are investing in and ensuring there are no unnecessary barriers to complaining when something goes wrong.
- 4.13 ELTIFs available to retail investors will be required to produce a key information document (KID) in line with the regulation on packaged retail and insurance-based investment products (PRIIPs).<sup>10</sup> The KID will require a brief description of whether the ELTIF is covered by an investor compensation scheme and if so, which risks are covered and which are not.<sup>11</sup> It will also give information about how and to whom an investor can make a complaint about the product and/or the conduct of the manager (and/or the person advising or selling the product).<sup>12</sup>
- 4.14 While the PRIIPs regulation will not be applicable until 31 December 2016, we would consider it good practice for managers of ELTIFs marketable to retail investors to comply with disclosures as set out in PRIIPS prior to its entry into force, wherever possible. This includes disclosing to their potential investors whether or not they are within the scope of the ombudsman service and the FSCS in the intervening period.
- 4.15 We will consider, through our authorisation and supervision powers, whether the provisions within company law and the Listing Rules are in practice proving to be sufficient to meet the requirements of the ELTIF regulation and our standards of investor protection.
- 4.16 As the retail ELTIF market develops, we will review our position. If evidence shows a need to apply consistency of treatment under the redress rules for ELTIF investors, we may consult again on bringing ELTIFs set up as closed-ended investment companies within the scope of the ombudsman service and the FSCS.

### **Cost benefit analysis and compatibility statement**

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<sup>7</sup> PS164 *Investment companies (including investment trusts), Changes to the Listing Rules and the Conduct of Business Rules; Changes to the Model Code, Feedback on CP164 and made text* (October 2003) <http://www.fsa.gov.uk/pubs/policy/ps164.pdf>

<sup>8</sup> <https://www.handbook.fca.org.uk/handbook/PRIN/2/?view=chapter>

<sup>9</sup> *Treating customers fairly – towards fair outcomes for consumers* (July 2006) <http://www.fca.org.uk/static/fca/documents/fsa-tcf-towards.pdf>

<sup>10</sup> The PRIIPs regulation is Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs). See also Article 23(1) of the ELTIF regulation.

<sup>11</sup> Article 8(3)(e) of the PRIIPs regulation

<sup>12</sup> Article 8(3)(h) of the PRIIPs regulation

4.17 Our cost benefit analysis (CBA) set out the costs we expected for firms that are not currently covered by the ombudsman service and the FSCS. We have not received any information which contradicts our analysis. As fewer firms will be impacted by our new rules, our CBA now overestimates the costs to firms of setting up new procedures.

**Equality and diversity issues**

4.18 Our proposals do not pose any equality or diversity issues for protected groups.

4.19 The changes made by this instrument are listed at the beginning of this Supplement.