

MEMO# 21042

April 5, 2007

IOSCO Publishes Final Report on the Role of Independent Review and Oversight in Fund Governance

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TO: INTERNATIONAL INVESTING SUBCOMMITTEE No. 4-07
INTERNATIONAL MEMBERS No. 8-07 RE: IOSCO PUBLISHES FINAL REPORT ON THE ROLE OF INDEPENDENT REVIEW AND OVERSIGHT IN FUND GOVERNANCE

The Technical Committee of the International Organization of Securities Commissions (IOSCO) has published its final report on the role of independent review and oversight in the governance of collective investment schemes (CIS). [\[1\]](#) The broad principles developed in the report concerning the concept of independence and the powers and specific functions of independent oversight entities (IOEs) are the same as those discussed in the IOSCO consultation report published in June 2006 and summarized in an earlier Institute memorandum. [\[2\]](#) The explanations elaborating the report's broad principles have been modified in some cases to reflect additional deliberation at IOSCO in response to comments on the report, including those submitted by the Institute. [\[3\]](#)

The Institute's comment letter strongly supported the consultation report's clear recognition of both the importance of independent oversight and the need for significant flexibility to adapt regulatory requirements on independent oversight to different CIS models. Despite that general support, however, the Institute's letter expressed three main concerns with the consultation report. First, the letter discussed a recommendation in the report that IOEs should have a duty of reporting material compliance failures or irregularities to the regulatory authorities or CIS shareholders. The letter recommended that IOSCO revise the principle so that IOEs have the flexibility to determine when and how to publicly disclose such breaches or irregularities. Second, the letter expressed concern

that the report in some respects did not fully recognize the important role played by internal CIS compliance mechanisms, such as the use of compliance officers and written compliance programs. And third, the letter expressed concern that the report in certain respects set forth unrealistic standards or was overly prescriptive, and offered several suggestions for technical corrections.

We are pleased to inform you that the revisions adopted by IOSCO in the final report largely address each of the three concerns highlighted in the Institute's comment letter. First, the final report clarifies that there may not be a duty to report material compliance failures or irregularities when an IOE has no direct or indirect material relationships with the CIS operator or its affiliates (a category that includes independent directors in the United States). [4] This modification recognizes the existing fund governance structure in the United States, where independent directors are empowered to oversee and resolve compliance matters. Second, the final report specifically acknowledges that certain oversight functions may be performed by a compliance officer or other staff, experts, or service providers, so long as the IOE retains supervisory responsibility. [5] And third, the final report adopts changes clarifying the concept of independence and the powers and functions of IOEs.

If you would like to discuss the IOSCO report, please contact me at 202-326-5837 or gguymon@ici.org.

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endnotes

[1] Examination of Governance for Collective Investment Schemes, Part II, Final Report of the Technical Committee of IOSCO (Feb. 2007), available at www.iosco.org/library/pubdocs/pdf/IOSCOPD237.pdf.

[2] See [Memorandum](#) to International Investing Subcommittee 15-06, International Members 12-06, International Operations Advisory Committee 17-06, Investment Company Directors 13-06 [20158], dated July 7, 2006.

[3] See Letter from Robert C. Grohowski, Senior Counsel, Investment Company Institute, to Ms. Pamela Vulpes, IOSCO General Secretariat, dated October 12, 2006, available at http://www.ici.org/policy/regulation/compliance/06_iosco_governance_com. The final report includes a feedback statement that summarizes comments submitted on the report and how or whether those issues were addressed by IOSCO in the final report.

[4] See the revised explanation of Principle IV.3 on p. 13 and footnote 4 on p. 4 of the final report.

[5] See footnotes 12 and 13 on p. 12 of the final report.

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