

**MEMO# 18268**

November 30, 2004

# **REPORT OF THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS ON THE INVESTIGATIONS OF THE EUROPEAN FUND INDUSTRY**

[18268] November 30, 2004 TO: INTERNATIONAL OPERATIONS ADVISORY COMMITTEE No. 36-04 RE: REPORT OF THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS ON THE INVESTIGATIONS OF THE EUROPEAN FUND INDUSTRY Attached is a summary report by the Committee of European Securities Regulators (CESR) regarding the investigations of CESR members into abusive practices such as late trading and market timing in the European fund industry. The report covers the methodologies used to investigate possible abuses, the scope of the investigations (including the number of companies approached), the results and findings of the investigations, and the actions taken and the policy implications of the investigations. According to the report, CESR members have not generally found evidence of major abuse such as late trading or market timing in their jurisdictions. The investigations, however, have revealed some issues of regulatory concern, including inadequacies in internal processes of some management companies. The report identifies a list of shortcomings, such as inadequate recordkeeping that prevents verification of compliance with the cut-off times for subscriptions and redemptions and lack of clarity in procedures for issuance and redemptions. The report also discusses the actions taken by European regulators, including regulatory reform to prevent the possibilities of abuse. The report states that, although regulatory tools and approaches differ from jurisdiction to jurisdiction, one of the common features is the requirement concerning the internal control mechanisms of fund management companies and other fund operators. To prevent market timing, regulators are examining carefully the process of fund asset valuation and its relation to the process of subscriptions and redemptions, and many jurisdictions already have or recently have moved to forward pricing of fund shares. Many jurisdictions also are considering allowing and facilitating the use of fair value pricing in valuation to prevent the inclusion of stale prices in the funds' net asset value. The report 2 provides a detailed list of regulatory tools and market practices used in various European jurisdictions to prevent late trading and market timing. Jennifer S. Choi Associate Counsel Attachment (in .pdf format)