Principles on suspensions of redemptions in Collective Investment Schemes. March 2012.

IOSCO Technical Committee has published, on the 19 of January 2012, its final report on the principles on suspensions of redemptions for open-ended Collective Investment Schemes (CIS). The principles, which are based on the CIS´s responsible entities basic duty to manage CIS liquidity on an on-going basis so as to avoid suspensions to the extent possible, generally cover all types of open-ended CIS which offer a continuous redemption right, and apply irrespective of whether they are offered to institutional or retail investors. They are addressed to those entities responsible for the overall operation of the CIS and in particular its compliance with the legal/regulatory framework in the respective jurisdiction and thus for the implementation of the principles. The delegation of activities may not be used to circumvent the principles and there should be compliance with the principles, whether activities are performed directly or through a third party. The principles reflect a common level of approach and provide standards against which both regulators and the industry can assess the quality of regulation and industry practices concerning suspensions of redemptions. The principles are divided into six sections:

Management of liquidity risk.

Principle 1: The responsible entity should ensure that the degree of liquidity of the open-ended CIS it manages allow it in general to meet redemption obligations and other liabilities. Some jurisdictions address this by setting requirements on the amount of liquidity (for example, as percentage of NAV) to be held in the portfolio of a CIS to deal with redemptions and other payments such as margin calls or collateral requirements for derivative positions. The routine use of borrowing is not and appropriate way to manage CIS liquidity risk.

Principle 2: Before and during any investment, the responsible entity should consider the liquidity of the types of instruments and assets and its consistency with the overall liquidity profile of the open-ended CIS. For this purpose, the responsible entity should establish, implement and maintain an appropriate liquidity management policy and process. Some jurisdictions deal with this issue by implementing eligibility criteria with regard to the liquidity of financial instruments/assets. The liquidity risk management policy and process will be part of the overall risk management arrangements.

Ex ante disclosure to investors.

Principle 3: The responsible entity should clearly disclose the ability to suspend redemptions in exceptional circumstances to investors prior to their investment into the CIS. The CIS constitutional documents and/or prospectus should clearly disclose this information; it is recommended not to define in the CIS documentation the terms “exceptional circumstances” but to use non-exhaustive examples of what might constitute “exceptional circumstances”.

Criteria/Reasons for the suspension.

Principle 4: Suspension of redemptions by the responsible entity may be justified only a)if permitted by law and in exceptional circumstances provided such suspension is exclusively in the best interest of unit-holders within the CIS, or b) if the suspension is required by law, regulation or regulators. The decision to suspend, therefore, requires exceptional circumstances and best interest of unit-holders. Regarding the exceptional circumstances, these should be temporary and rare (such as where fair an robust valuation of the assets is not possible). The report indicates possible reasons for suspension that are not meant to define an exhaustive list and that should be tested exceptional by the responsible entity: market failures, exchanges closures by unexpected events, unpredictable operational problems and technical failures, unforeseeable lack of liquidity when it is necessary to stop redemptions that could cause a spiral (vicious circle scenario) that sharpen lack of liquidity, and other events such as natural disasters or catastrophes. Poor liquidity management is not considered reason enough to suspend redemptions. Regarding best interest of investors, fair and equal treatment of incoming, ongoing and outgoing

investors should be maintained.

Decision to suspend.

Principle 5: The responsible entity should have operational capacity to suspend redemptions in an orderly and efficient manner. The responsible entity should implement a decision-making process and draw up plans/processes for potential suspension events and an emergency plan for the immediately reaction of personnel involved in the decision to suspend and their roles, potential avenues that probably can avoid a suspension and the notification procedure to the competent authority and investors. When the entity responsible arrives at the point to consider a suspension, it should analyse the situation even with external legal counsel, will require the prior agreement/approval of the depositary and of the competent authority will consider any other alternatives and should take into account the investor profile.

Principle 6: The decision by the responsible entity to suspend redemptions, in particular, the reasons for the suspension and the planned actions should be appropriately: documented, communicated to competent authorities and other relevant parties and communicated to unit-holders. Documentation should also define objective criteria, the meeting of which will trigger the resumption of normal operations or the liquidations of the CIS. The communication to the competent authority should also be done to the authorities of those jurisdictions where the CIS is authorised to be marketed publicly. If the information filed with the competent authority indicates that the suspension is a result of poor management rather than external unpredictable factors, the competent authority could take measures and consider exercising sanction Powers against the persons responsible. In particular, the immediate cessation of active distribution of the CIS should be ensured. The communication to unit-holders should be done in a timely manner and to all unit-holders in a way that it does not involve a heavy loss of confidence and reputation and therefore also spillover effects in the market.

During the suspension.

Principle 7: During the suspension of the redemptions, the responsible entity should not accept new subscriptions. However, in cases where subscriptions are allowed by national law, any prospective subscriber should be informed about the suspension in a clear and comprehensive manner prior to the subscription and given a chance to cancel de order before it is accepted.

Principle 8: The suspension should be regularly reviewed by the responsible entity. The responsible entity should take all necessary steps in order to resume normal operations as soon as possible having regard to the best interest of unit-holders. The review decision implies monitor the market and the liquidity, stay in close contact with relevant investors (without prejudice to the principle of equal treatment of unit-holders) and should take in account the expectation of redemption requests. The responsible entity should consider the length the suspension is in place and how long it may continue depending on the circumstances, jurisdiction and the way the CIS was marketed to investors. It is unacceptable that suspensions remain in force for a long time and, in this case, the responsible entity should consider alternatives such as liquidations, changing of the CIS structure or the setting-up of side pockets (separated illiquid assets portfolio).

Principle 9: The responsible entity should keep the competent authority and unit-holders informed throughout the period of suspension. The decision to resume normal operations should also be communicated as soon as practical. The communication strategy of the responsible entity should not end with the disclosure of the decision to suspend but the unit-holds should be kept updated throughout the suspension, and the same the competent authorities that should also be informed of the proposed date for the resumption of normal operations.

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