



PUBLIC RESPONSE PAPER

No. 1/2021

PROPOSED AMENDMENTS TO GUIDELINES ON UNIT TRUST FUNDS AND CONSEQUENTIAL AMENDMENTS TO GUIDELINES ON EXCHANGE-TRADED FUNDS AND GUIDELINES ON PRIVATE RETIREMENT SCHEMES

The Securities Commission Malaysia (SC) is issuing this Public Response Paper in response to the feedback received pursuant to the Public Consultation Paper on the proposed amendments to the *Guidelines on Unit Trust Funds* and consequential amendments to the *Guidelines on Exchange-Traded Funds* and *Guidelines on Private Retirement Schemes* dated 11 November 2020.

This Public Response Paper is dated 21 December 2021.

CONTENTS

1	EXECUTIVE SUMMARY	1
2	PROPOSALS RELATING TO THE INVESTMENT UNIVERSE OF A FUND	3
2.1	Transferable Securities and Money Market Instruments.....	3
2.2	Investment in CIS.....	6
2.3	Derivatives and Structured Products	10
2.4	Securities Lending, Repurchase and Reverse Repurchase Transaction	15
2.5	Single Issuer Limit for Investment in Government and Public Transferable Securities or Money Market Instruments	17
2.6	Exception to the Single Financial Institution Limit for Placement in Deposits.....	18
2.7	Exception to the Concentration Limit for Debt Securities.....	18
2.8	Investment Spread Limit for Investment in a Listed REIT	19
2.9	Allowing Investments in Other Type of Securities.....	20
2.10	Investments of a Feeder Fund	22
2.11	Investments of a MMF.....	23
3	FEEDBACK ON PROPOSALS RELATING TO A UTMC	26
3.1	Risk Management Framework Documentation	26
3.2	Holding of a Fund's Units by the UTMC	29
3.3	Oversight Arrangement to Replace Investment Committee	30
3.4	Training Requirements	31
4	FEEDBACK ON PROPOSALS RELATING TO DEALING, VALUATION AND OPERATIONAL MATTERS	33
4.1	Dealing in Units	33
4.2	Revision to the Redemption Payment Period	35
4.3	Basis of Valuation of a Fund's Assets and Incorrect Pricing	36
4.4	Requirements in Relation to Cooling-off Right.....	40
4.5	Enabling a Fund to Pay Distribution out of Capital.....	43
4.6	Removal of the Requirement Restricting the use of any Broker or Dealer for a Fund from Exceeding 50% of a Fund's Dealings	45
4.7	Enhancement to Requirements relating to Soft Commissions	46
4.8	Requirements relating to Termination of a Fund	48
4.9	Requirements on Quorum for Unit Holders' Meeting.....	50

5	OTHER PROPOSED AMENDMENTS	51
5.1	Contents of Annual and Interim Reports (Fund Reports).....	51
5.2	Information on Funds on a UTMC’s Website	53
5.3	Requirement to Disclose a Performance Benchmark.....	55
	GLOSSARY OF TERMS	57

1 EXECUTIVE SUMMARY

- 1.1 On 11 November 2020, the SC published a Consultation Paper inviting public feedback on the proposed amendments to the *Guidelines on Unit Trust Funds* (Unit Trust Guidelines) and the *Prospectus Guidelines for Collective Investment Schemes*, and consequential amendments to the *Guidelines on Exchange-traded Funds* (ETF Guidelines) and *Guidelines on Private Retirement Schemes* (PRS Guidelines).
- 1.2 The proposals seek to promote competitiveness, innovation and other market developments that are balanced with appropriate controls to uphold investor protection.
- 1.3 The Consultation Paper was open for public feedback for two months from 11 November 2020 to 10 January 2021, and we received responses until 10 February 2021.
- 1.4 The SC received written feedback from 32 respondents, comprising UTMCs (some of whom are also ETF management companies and PRS Providers), trustees, fund management companies, financial institutions, Bank Negara Malaysia, FIMM, Association of Trust Companies Malaysia and individuals. Collectively, the respondents represented more than 90% of the unit trust fund industry NAV, 85% of the ETF industry NAV and 86% of PRS industry NAV as at 30 September 2021.
- 1.5 The SC would like to thank all respondents for their valuable and constructive feedback and suggestions. In finalising the amendments, the SC had engaged with the respondents to better understand their feedback and the feedback were given due consideration.
- 1.6 A majority of the respondents supported the proposals, with some proposals receiving full support. Following the feedback received, some proposals have been refined. In relation to the applicability of the proposals to ETF and PRS, a majority of the respondents are of the view that the proposals should apply on the basis of consistency in approach.
- 1.7 Key feedback from the respondents¹ on the proposals, together with the SC's responses are presented in the following sections. This response paper should be read together with the Consultation Paper.

¹ Not all respondents provided feedback to all the proposals. Some respondents opted to reserve their comments on certain proposals citing reasons like lack or absence of exposure or experience in the area discussed. As such, references to all respondents shall refer to respondents that have provided an adequate response to the proposal.

Implementation

- 1.8 The Unit Trust Guidelines will come into effect on 1 March 2022.
- 1.9 Generally, UTMCs are given a 6-month period to comply with revised requirements from the effective date of the Unit Trust Guidelines. However, we note that some of the revisions require UTMCs to make operational and system changes in order to comply. As such, a 12-month transition period from the effective date will be provided for these requirements.

2 PROPOSALS RELATING TO THE INVESTMENT UNIVERSE OF A FUND

2.1 Transferable Securities and Money Market Instruments

PROPOSAL 1

2.1.1 Respondents were asked to give their comments on the following questions:

- Question 1.1 : Do you agree with the proposed definition for “transferable securities”? Please provide specific reasons for your views.
- Question 1.2 : Do you agree with the proposed criteria for “transferable securities”? Please provide specific reasons for your views.
- Question 1.3 : Do you agree for Proposal 1 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

2.1.2 All respondents agreed to the proposals citing views that the proposals provide better clarity, wider scope and alignment with international definition for easier referencing.

2.1.3 Some respondents sought clarification on the following:

- (a) What would be considered liquid;
- (b) The treatment of a transferable security in the event it becomes illiquid subsequent to investment by the fund (liquid being one of the criteria for transferable security), i.e. whether such transferable security would need to be reclassified as other securities, where the investment limit of other securities will then apply;
- (c) How can a UTMC demonstrate or provide evidence of maximum potential loss is indeed limited to amount paid throughout the holding of the transferable securities?; and
- (d) Whether “verifiable valuation” should be “verifiable price” instead;

- 2.1.4 One respondent commented that criteria (b) and (c)², which require investments to be liquid and not impair the fund's ability to satisfy redemption and payment obligations, are very broad and would require the UTMC to undertake liquidity test of its investment universe on a daily basis. This would require extensive increase in manpower and system capabilities. In addition, the requirement may be disruptive to its portfolios as certain bonds or equities may from time to time be temporarily illiquid due to some credit event or adverse market conditions.
- 2.1.5 One respondent suggested to include the word "legal" in "*...but do not include money market instruments or any security the legal title to which can be transferred only with the consent of a third party*" to enhance the definition of "transferable securities". The respondent explained that the current definition is silent on whether both the legal title and beneficial interest is transferred from the transferor to the transferee. The respondent quoted that for sell & buy back agreements, only the legal title is transferred to the transferee. The beneficial interest still resides with the transferor.

The SC's response

- 2.1.6 We would like to reiterate that at the point where the investment is being made, all the criteria for transferable securities must be met. Additionally:
- (a) Guidance has been provided in the Unit Trust Guidelines as to what would be considered as liquid;
 - (b) In the scenario where a transferable security is liquid at the point of investment but eventually become illiquid, the transferable security will not need to be reclassified as other securities. Notwithstanding this, UTMCs are reminded of the importance of effective RMP for a fund, and in this regard the liquidity risk management practices, to ensure that they are able to meet redemption request in an orderly manner and ensure the fair treatment of all investors, including those remaining in the fund;
 - (c) With regards to the clarification on how can a UTMC demonstrate or provide evidence of maximum potential loss is limited to the amount paid throughout the holding of the transferable securities, we would like to clarify that the intention is for the UTMC to ensure they do not commit more than what is paid for the investment of the fund; and

² Referring to paragraph 2.2.5 of the Consultation Paper which requires the transferable securities to also meet the following criteria: (b) The investment is liquid and will not impair the fund's ability to satisfy its redemption and other payment commitments; and (c) The investment is subject to reliable and verifiable valuation on a daily basis.

(d) “Verifiable valuation” means that a third party is able to replicate the valuation based on the process and information documented. “Verifiable prices” can be on the transferable securities’ historical prices. In this respect, “verifiable valuation” is more appropriate.

2.1.7 With regards to the comment under paragraph 2.1.4, in addition to our response in paragraph 2.1.6(b), generally, when a fund has illiquid investments in its portfolio, the UTMC is expected to undertake liquidity tests for the funds on an ongoing basis as part of the UTMC’s RMP.

2.1.8 With regards to the suggestion under paragraph 2.1.5, the inclusion of the word “legal” is not necessary as the exclusion is intended to ensure that any securities that the fund will invest in can be transferred from the fund to another person without the fund having to seek for any consent from a third party. This is to ensure that the fund is not left with any asset which it cannot liquidate. As such, we are maintaining the proposed definition. UTMCs that have any doubt in classifying any specific investments are encouraged to consult the SC.

PROPOSAL 2

2.1.9 Respondents were asked to give their comments on the following questions:

- Question 2.1 : Do you agree with the proposed definition for “eligible market”? Please provide specific reasons for your views.
- Question 2.2 : Do you agree with the proposal for a single definition for “eligible market” whether the market is within or outside Malaysia? Please provide specific reasons for your views.
- Question 2.3 : Do you agree for Proposal 2 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

2.1.10 All respondents agreed to Questions 2.1 to 2.3, with a majority commenting that the revised definition provides transparency, clarity and flexibility.

The SC’s response

2.1.11 We welcome the support for the proposal and will implement it as proposed.

2.2 Investment in CIS

PROPOSAL 3

2.2.1 In the Consultation Paper, the SC **proposed to clarify and liberalise the requirements for investments in other CIS**. Essentially, investments in units or shares of a CIS in the following 4 broad categories would be allowed:

- (A) A CIS authorised or recognised by the SC.
- (B) A CIS that meets all of the following criteria:
 - (i) The CIS is constituted and regulated in a jurisdiction where the laws and practices provide the level of investor protection that is at least equivalent to that offered in Malaysia;
 - (ii) The rules on investments, borrowing and lending are substantially similar to the requirements in the Unit Trust Guidelines; and
Guidance: This would exclude a CIS that aims to achieve a high return through the use of advanced or alternative investment strategies, such as use of long/short exposures, leverage, or hedging and arbitrage techniques (Hedge Funds);
 - (iii) The assets of the CIS are managed by an entity which is approved, authorised, or licensed by a securities regulator to conduct fund management activities; and
 - (iv) The business of the CIS is reported in half-yearly and annual reports to enable an assessment to be made of the assets and liabilities, income and operations over the reporting period.
- (C) A CIS that meets all of the following criteria:
 - (i) Invests in permissible investments, physical gold or real estate;
 - (ii) It meets the criteria imposed on investment in transferable securities;
 - (iii) Its units or shares are listed for quotation and traded on an eligible market; and
 - (iv) It is not an inverse or leveraged product.
- (D) Any other CIS that does not fall under categories (A), (B) or (C) above, except for Hedge Funds.

2.2.2 Respondents were asked to give their comments on the following questions:

Question 3.1 : Please provide your feedback on the following categories:

- Category (B)
- Category (C)
- Category (D)

Question 3.2 : Under Category (C), other than Gold ETF, should a unit trust fund be allowed to invest in an ETF where the underlying asset is other precious metal, e.g. silver? Please provide specific reasons for your view.

Question 3.3 : Do you agree for Proposal 3 to apply to ETF and PRS? Please provide specific reasons for your views.

Question 3.1: Category (B)

Public comments

2.2.3 Most of the respondents had no objection to this category. Six respondents suggested that SC provide further clarification on its expectation on criteria (B)(i) and/or (ii).

2.2.4 One respondent each sought clarification on the following:

- (a) Whether item B(iv) refers to the reports on activities of the CIS; and
- (b) Why CIS that uses advanced or alternative investment strategy such as long/short exposures, leverage, or hedging and arbitrage techniques to achieve high return should be prohibited if the risks are adequately disclosed to the investors who are assessed with aggressive investment profiles via suitability assessments. If a CIS uses those advanced techniques for multiple reasons which include hedging, liquidity management and some elements of return enhancement, then would those CIS be allowed.

The SC's response

2.2.5 The SC took note of the need for clarity on SC's expectation on the criteria imposed. In this regard, appropriate guidance has been provided in the Unit Trust Guidelines to assist in interpreting the requirements and their application.

2.2.6 Criteria B(iv) refers to the annual and interim reports of the CIS. The purpose of this requirement is to ensure that UTMCS can expect to receive the CIS's

reports on a regular basis. This is to enable UTMCs to assess if the CIS remains suitable to be invested in.

- 2.2.7 As to the prohibition for a fund to invest in hedge funds, we would like to reiterate that currently, the Unit Trust Guidelines prohibits the establishment of such fund for the retail segment. As such, allowing a fund to invest in hedge funds would not be consistent with this policy. UTMCs are encouraged to consult the SC if they encounter difficulty in assessing a CIS to be a fund's investment under this category.

Question 3.1: Category (C)

Public comments

- 2.2.8 All respondents are agreeable or have no objection with this category.
- 2.2.9 One respondent is of the view that even though REIT's legal form is established as trust, the economic and financial benefits are similar from the listed securities' point of view. As such, listed REIT should be treated as part of transferable securities. In addition, the respondent suggested to include digital assets as permissible investment under criteria C(i) as it opines that digital assets are expected to gain more prominence in coming years as the understanding on this emerging asset class improves and the market infrastructure is working to include it by stages as part of the existing ecosystem of financial market. Having digital assets in this CIS definition would allow market participants to grow alongside the evolution of digital assets globally.

The SC's response

- 2.2.10 The SC agrees that in terms of characteristic, the risks associated with investment in listed REITs are closer to investment in shares and as such, we have proposed to impose the limit that apply to transferable security instead of the CIS limit (through Proposal 10). However, in terms of classification, we are of the view that a REIT can remain as a CIS so to avoid unnecessary disruption, if any.
- 2.2.11 In relation to the suggestion to include a CIS that invests in digital assets, we would like to clarify that the SC is following the development of this asset class closely and encourage UTMCs that propose to invest in this asset class extensively to engage with the SC.

Question 3.1: Category (D)

Public comments

2.2.12 All respondents are agreeable or had no objection. Some respondents commented that there is a need for wider range of products to cater to investors' growing demands.

The SC's response

2.2.13 We welcome the support for the proposal and will implement it as proposed.

2.2.14 We would also like to clarify that leveraged ETFs and inverse ETFs are some of the examples of CIS that fall under Category D.

Question 3.2

Public comments

2.2.15 All respondents welcomed the inclusion of precious metal ETFs as an investible for a unit trust fund, and their views are summarised as follows:

- (a) This would provide diversification and meet investors' demand for wider range of products;
- (b) There is a demand for silver ETFs in the market where the returns for silver ETF have outperformed the broader market, including the FBMKLCI over the past years; and
- (c) This would provide additional source of returns.

The SC's response

2.2.16 We have revised the Unit Trust Guidelines to allow investment in ETF where the underlying asset comprise of other precious metal such as physical silver, platinum or palladium, subject to compliance with requirements that currently apply to investment in gold ETF. The SC agrees that the liberalisation would-

- (a) broaden the types of permissible CIS hence more sources of returns for a fund i.e. from price movement of the precious metal; and
- (b) enable investors to gain exposure to precious metal without having to acquire the metal or directly buying the securities of the ETF from a stock exchange.

2.3 DERIVATIVES AND STRUCTURED PRODUCTS

PROPOSAL 4

2.3.1 Respondents were asked to give their comments on the following questions:

Question 4.1 : Do you agree with the proposal to replace “derivatives” with “financial derivative instruments” and delete specific reference to “structured products”? Please provide specific reasons for your views.

Question 4.2 : Do you agree for Proposal 4 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

2.3.2 All respondents agreed to Questions 4.1 and 4.2. Three respondents commented that the definition of financial derivative instruments is comprehensive and allows wider coverage. One respondent suggested for SC to provide a list of approved financial derivative instruments.

The SC’s response

2.3.3 We welcome the support for the proposal and will implement it as proposed.

2.3.4 The SC is of the view that the definitions together with the proposed criteria for financial derivative instruments as discussed under proposal 5b is sufficient and in this respect, will not be prescribing a list of approved financial derivative instruments for now.

PROPOSAL 5

2.3.5 Respondents were asked to give their comments on the following questions:

Question 5.1 : Do you agree with the proposal to allow exposure to commodity through a financial derivative? Please provide specific reasons for your views.

Question 5.2 : Do you agree with the general criteria on financial derivatives? Please provide specific reasons for your views.

Question 5.3 : Do you agree with the proposal to lower the minimum credit rating requirement for the counterparty of OTC financial derivatives? Please provide specific reasons for your views.

Question 5.4	: Do you agree with the proposal to require the use of commitment approach to calculate a fund's exposure to derivatives? Please provide specific reasons for your views.
Question 5.5	: Do you agree with the introduction of a requirement for embedded derivatives? Please provide specific reasons for your views.
Question 5.6	: Do you agree with the proposal on the calculation of a fund's exposure to counterparty of OTC derivative? Please provide specific reasons for your views.
Question 5.7	: Do you agree with the general requirement to prohibit a fund from assuming any liability which is unlimited? Please provide specific reasons for your views.
Question 5.8	: Do you agree for Proposal 5 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

2.3.6 The respondents generally agreed to all the questions, with a consensus to Questions 5.5, 5.6 and 5.7. Key responses are highlights below:

Question 5.1

Public comments

2.3.7 One respondent commented that a fund should be allowed to invest in physical commodity.

The SC's response

2.3.8 Generally, for investment in physical commodity, factors including storage, liquidity as well as the costs and risks associated with them would need to be considered. For an unlisted retail fund where its features are on transferability as well as the liquid nature of the underlying assets, investments in physical commodity may not be suitable. This is in line with the approach taken by major CIS jurisdictions.

Question 5.2

Public comments

2.3.9 Majority of the respondents agreed with the proposal. Three respondents suggested that the term "liquid" be defined or a guidance on how "liquid" can

be measured be provided. In addition, three respondents highlighted that daily valuation for the OTC financial derivatives may not be available. One respondent proposed that the valuation to be based on counterparty's financial derivative valuation and verified by reasonableness testing, as per the current market practice. Generally, the redemption price will be close to the valuation price provided by counterparty.

The SC's response

- 2.3.10 The SC considered the feedback and has provided a guidance to the term "liquid" under paragraph 6.16(a) of the Unit Trust Guidelines. We have also revised the criteria to provide clarity in relation to valuation of OTC financial derivatives under paragraph 6.17 of the Unit Trust Guidelines.

Question 5.3

Public comments

- 2.3.11 Majority of the respondents agreed with the proposal to lower the credit rating requirement for the counterparty of OTC financial derivatives to investment grade citing the existence of other safeguards, monitoring measures as well as promoting competition for derivative pricing as their reasons. Two respondents disagreed with the proposal citing exposure to settlement risk and high credit rating is required to ensure that there is no counterparty risk at all times as their reasons.
- 2.3.12 One respondent sought clarification on whether they can enter into transaction with a counterparty that is located offshore for better hedging effectiveness or if the onshore counterparty does not have the required risk management solution.

The SC's response

- 2.3.13 We would like to clarify that the Unit Trust Guidelines does not limit the counterparty of OTC financial derivatives to onshore financial institutions only, as long as such counterparty complies with the definition of financial institution. Moreover, the UTMC must perform its due diligence that includes ensuring the relevant risks have been considered and there are controls in place to manage such risks before entering into a transaction with such counterparty. Towards this end, the same consideration is expected to apply to counterparty risk.
- 2.3.14 In addition to the views provided by the majority of the respondents, we are of the view that lowering the credit rating requirement for the counterparty of OTC financial derivatives provides flexibility to the fund manager by widening the pool of financial institutions which they may enter a derivative transaction with.

However, it is the responsibility of the UTMC to ensure the potential counterparties are properly assessed before a fund enter into a transaction with such counterparty.

Question 5.4

Public comments

- 2.3.15 Majority of the respondents agreed with the proposal. Four respondents (including the two respondents that disagreed) suggested that the SC also consider accepting other methods to calculate global exposure to financial derivatives. One respondent suggested that the definition of financial derivatives be further enhanced to cover derivative transactions e.g. FX forward transaction, for clarity. Another respondent suggested that long only option contracts (which have no downside risk) be excluded in the calculation of risk exposure.

The SC's response

- 2.3.16 We would like to clarify that the intention for prescribing commitment approach as a method to calculate global exposure to financial derivatives is to provide clarity to industry participants. It is also prescribed based on the current position of the industry and complexity of financial derivatives employed by retail funds. UTMCs are encouraged to consult the SC if they are of the view that an alternative method is more suitable for the fund that they will be managing.
- 2.3.17 With regards to response relating to derivative transactions, the definition for 'derivative' has been enhance to provide clarity that it also includes derivative transactions.

Question 5.5

Public comments

- 2.3.18 All respondents agreed with the proposal citing consistency with international standards, provision of further guidance to industry, and ensuring consistent treatment. One respondent sought clarity on whether bonds with call or put features are considered transferable securities with embedded derivatives. Another respondent sought clarity on the criteria imposed for embedded derivatives.

The SC's response

- 2.3.19 With regards to criteria for embedded derivatives or whether a bond with call or put features are considered transferable securities with embedded derivatives, UTMCs are encouraged to refer to Malaysian Financial Reporting Standards 9 issued by Malaysian Accounting Standards Board.

Question 5.6

Public comments

- 2.3.20 All respondents agreed with the proposal citing that it provides guidance and consistency in treatment. One respondent sought clarification on whether unsecured credit facility granted by the counterparty without any collateral in favour of the fund for forward currency hedging purposes can be accepted to lower the exposure to the counterparty. Another respondent commented that it may require a clear illustration with an example in calculating exposure to counterparty of OTC financial derivatives.

The SC's response

- 2.3.21 On whether unsecured credit facility without any collateral can be accepted to lower the exposure to the counterparty, we do not see how such arrangement mitigates counterparty risk. As such, we disagree that the unsecured credit facility arrangement can be construed to lower the exposure to the counterparty.
- 2.3.22 Recognising the complexity for investing in financial derivatives, we expect a UTMC to ensure that the human resource with the technical know-how, technology and systems employed are adequately and appropriately resourced at all times and before undertaking such investments. In this regard, UTMCs are welcomed to engage with the SC to demonstrate how the calculation is performed, accordingly.

Question 5.7

Public comments

- 2.3.23 All respondents agreed with the proposal citing that a fund's liability should be limited and it is a prudent measure from risk management perspectives as unlimited liability poses disproportionate risk to investors.

The SC's response

- 2.3.24 We welcome the support for the proposal and will implement it as proposed.

2.4 SECURITIES LENDING, REPURCHASE AND REVERSE REPURCHASE TRANSACTION

PROPOSAL 6

2.4.1 Respondents were asked to give their comments on the following questions:

- Question 6.1 : Do you agree with the proposal to allow a unit trust fund to undertake securities lending and repurchase transactions for the sole purpose of EPM? Please provide specific reasons for your views.
- Question 6.2 : Do you agree with the proposed criteria for securities lending and repurchase transactions as outlined in paragraphs 2.5.3(a) to (j) of the Consultation Paper? Please provide specific reasons for your views.
- Question 6.3 : Do you agree with the proposal to impose a requirement that all revenues from the securities lending and repurchase transactions, net of direct and indirect expenses as reasonable for the services rendered in the context of securities lending and repurchase transactions, to be returned to the fund? Please provide specific reasons for your views.
- Question 6.4 : Do you agree for Proposal 6 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

2.4.2 The respondents generally agreed to Questions 6.1 to 6.4.

2.4.3 One respondent was initially of the view that there should be flexibility accorded to the respective funds to negotiate commercial terms with their counterparties (e.g. issuer credit quality, haircut, diversification of collateral, correlation, reinvestment of collateral, types of collateral and sufficiency of collateral) as there are many variables at play, expressing concern that the criteria proposed introduced rigidity which will discourage the growth and vibrancy of the securities and borrowing lending market. Nevertheless, the respondent subsequently acknowledged that the requirements are introduced to provide safeguards as well as consistency in practice for the industry given that the scope of securities lending will be expanded to securities not limited to those on Bursa Malaysia (and rules relating to this are prescribed by Bursa Malaysia), and the introduction of new activities i.e. repurchase transactions. The

respondent noted that these requirements are introduced after a benchmarking exercise against major CIS jurisdictions.

2.4.4 In relation to holding of collateral, one respondent proposed to expand the requirement to allow the collateral to be held by borrowing/lending agent instead of the trustee, as the agent is normally the party contracted to hold the securities/collateral on behalf of the lender or borrower.

2.4.5 The respondents also sought clarifications on the following:

- (a) With regards to the requirement on the counterparty, one respondent sought clarity on what “domestic rating agency” refers to.
- (b) Two respondents also sought clarity on whether debt securities with embedded derivatives are eligible as collateral.
- (c) One respondent sought clarification on whether a UTMC is able to charge a management fee or a haircut on the net revenues for rendering the facility or trades.

The SC’s response

2.4.6 In relation to holding of collateral, the SC noted the feedback and we have revised the requirements to allow borrowing/lending agent to hold collateral in addition to the trustee as long as the collateral is legally secured from the consequences of the failure of the trustee, counterparty or agent.

2.4.7 We would like to provide a response to the clarification sought:

- (a) In relation to the clarification sought on the reference to domestic rating agency, we are referring to a Malaysian rating agency.
- (b) Debt securities (as well as money market instruments) with embedded derivatives are not eligible to be posted as collateral.
- (c) A UTMC is not allowed to charge a management fee. However, the UTMC is allowed to charge for the direct and indirect expenses as reasonable for the services rendered for securities lending and repurchase transactions.

2.4.8 We also noted that under the current framework, e.g. equities approved by Bursa Malaysia can be accepted as collateral. In this respect, we have also revised the criteria for collateral to provide clarity that the current requirement is maintained with some enhancement, i.e. equity securities³ can be accepted

³ Equities securities as approved or prescribed by the clearing house to be accepted as collateral subject to the compliance with the criteria for a collateral.

as collateral for securities lending is made through a standardised lending system (e.g. Bursa Malaysia).

2.5 **SINGLE ISSUER LIMIT FOR INVESTMENT IN GOVERNMENT AND PUBLIC TRANSFERABLE SECURITIES OR MONEY MARKET INSTRUMENTS**

PROPOSAL 7

2.5.1 Respondents were asked to give their comments on the following questions:

Question 7.1 : Do you agree with the proposal to allow an increase of exposure to Govvies? Please provide specific reasons for your views.

Question 7.2 : Do you agree for Proposal 7 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

2.5.2 The respondents generally agreed to all proposals. However, two respondents commented that there are difficulties in identifying whether the transferable securities or money market instruments are guaranteed by such Govvies as the information on the guarantor is not readily available to the trustees. As such, it was suggested that UTMC is responsible to provide the information to the trustee.

The SC's response

2.5.3 The UTMC and trustee of a fund have a fiduciary duty to their unit holders, one of which is for both parties to act in the best interests of unit holders. As such, due consideration should be given for every investment decision of the fund. In addition, the trustee of a fund, in performing its role, should request for the relevant information to be provided to them as it deems fit.

2.6 **EXCEPTION TO THE SINGLE FINANCIAL INSTITUTION LIMIT FOR PLACEMENT IN DEPOSITS**

PROPOSAL 8

2.6.1 Respondents were asked to give their comments on the following questions:

Question 8.1 : Do you agree with the proposal to provide exception to the single financial institution limit for placement in deposits?
Please provide specific reasons for your views.

Question 8.2 : Do you agree for Proposal 8 to apply to ETF and PRS?
Please provide specific reasons for your views.

Public comments

2.6.2 All respondents agreed with the proposal.

2.6.3 Three respondents sought clarification on whether the exception could be applied to a fund in which the size is small. Two other respondents suggested the SC to provide clarity on the exception "At any point where the fund receives the subscription monies prior to the commencement of investment by the fund".

The SC's response

2.6.4 We would like to clarify that the intention of the proposal is to address the occurrence of passive breaches under the circumstances mentioned in proposal 8 and as such, the exceptions are meant to be temporary in nature. In addition, the existing limit for placement in deposits with any single financial institution is meant for diversification purposes. In this regard, UTMCs may want to consider the viability of a fund with small size as well as other available option e.g. fund seeding which is now allowed. We have also provided the necessary guidance in the Unit Trust Guidelines for clarity as requested.

2.7 **EXCEPTION TO THE CONCENTRATION LIMIT FOR DEBT SECURITIES**

PROPOSAL 9

2.7.1 Respondents were asked to give their comments on the following questions:

Question 9.1 : Do you agree with the proposal not to impose the concentration limit on debt securities that do not have a

pre-determined issue size? Please provide specific reasons for your views.

Question 9.2 : Do you agree for Proposal 9 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

2.7.2 The respondents generally agreed with the proposal, but two respondents expressed concern on concentration risk and suggested that the exception should only be temporary. Four respondents sought clarification on whether the concentration limit is determined at the issue or tranche level or at the issuer level.

The SC's response

2.7.3 We have considered the feedback received and agree that the exception should be temporary and the concentration limit must be complied with when the gross amount is determined. For avoidance of doubt, the concentration limit is to be determined at the issuer level based on the debt securities issued. UTMCs are encouraged to engage the SC if they have specific concerns.

2.8 INVESTMENT SPREAD LIMIT FOR INVESTMENT IN A LISTED REIT

PROPOSAL 10

2.8.1 Respondents were asked to give their comments on the following questions:

Question 10.1 : Do you agree with the new limit for investment in listed REIT? Please provide specific reasons for your views.

Question 10.2 : Do you agree for Proposal 10 to apply to PRS? Please provide specific reasons for your views.

Public comments

2.8.2 Majority agreed with the proposal and shared the view that in terms of characteristic, the risks of a listed REIT are closer to an investment in shares than investment in mutual funds. Another respondent added that listed REITs are not as diversified as a typical CIS and another added that investment of more than 15% in one listed REIT is considered too risky and as such is agreeable to the new limit.

2.8.3 A few respondents disagreed. Reasons cited included the following:

- (a) There is a limited number of listed REITs available for investments in Asia;
- (b) Listed REITs share characteristic of a bond/fixed income instrument. Listed REITs derive rental income from its underlying investments which are real properties, which is then distributed to its unit holders. As this income stream is somewhat fixed compared to equities, which is volatile and dependent on the performance of a company, amendment to the limit is not necessary; and
- (c) REITs are CIS in nature and should still be categorised as a CIS.

The SC's response

2.8.4 Although a listed REIT distributes regular income like a bond or fixed income instrument, the income streams are mainly from rental income and the performance of a REIT is likened to a company e.g. property investment companies. As such, consistent with the views of the majority, the proposal to apply a single issuer limit of 15% of a fund's NAV on listed REITs is maintained. In terms of categorisation, we agree that it is generally structured as CIS and as such, this has been reflected in the Unit Trust Guidelines.

2.9 ALLOWING INVESTMENTS IN OTHER TYPE OF SECURITIES

PROPOSAL 11

2.9.1 Respondents were asked to give their comments on the following questions:

- Question 11.1 : Do you agree with the proposed expansion of "unlisted securities" to "other securities"? Please provide specific reasons for your views.
- Question 11.2 : Do you agree with the proposed limits for other securities? i.e.
- (i) investment in other securities must not exceed an aggregate limit of 15% of the fund's NAV; and
 - (ii) investment in other securities is subject to a limit of 10% of the fund's NAV per single issuer.
- Please provide specific reasons for your views.
- Question 11.3 : Do you agree for Proposal 11 to apply to PRS? Please provide specific reasons for your views.

Public comments

- 2.9.2 All respondents agreed with the proposal with key feedback as follows:
- (a) SC to provide clarity as to what constitutes of "other securities" and whether the single issuer limit is a separate limit from the general single issuer limit;
 - (b) UTMCs must have the knowledge on "other securities";
 - (c) One respondent enquired whether digital assets would be included as "transferable securities". Another respondent was of the view that as cryptocurrency are mostly event driven with no fundamental analysis or research that can be done on it, the SC is to consider introducing requirements to address concerns on UTMC's expertise, investor protection, liquidity risk, concentration risk and volatility; and
 - (d) One respondent suggested that Investment Accounts⁴ are included as "Other Securities" which would be subject to the limit.

The SC's response

- 2.9.3 The SC noted respondents' feedback on the need for clarity on what constitute as "other securities". In this regard, appropriate guidance have been included accordingly in the Unit Trust Guidelines.
- 2.9.4 For avoidance of doubt, the 10% single issuer limit is an aggregate limit for a fund e.g. if a fund has invested 5% of its NAV in the ordinary shares of Company A and has no other investment in Company A. The fund is allowed to invest up to 5% of its NAV in the "other securities" of Company A.
- 2.9.5 As digital assets investment is still a developing area, it will be subject to the single issuer limit of 10% of the fund's NAV and the aggregate limit of 15% of the fund's NAV (Other Securities Limit). We would also like to reiterate that RMP is an important component in managing a fund. Specifically, UTMCs are expected to ensure adequate RMP is in place before undertaking any investment activities.
- 2.9.6 The SC may consider higher limits for digital assets in the future, and UTMCs that wish to manage such a fund are encouraged to consult the SC. In considering proposals in this area, additional conditions may be specified by the SC.

⁴ has the meaning assigned to it in the *Islamic Financial Services Act 2013*.

2.9.7 The SC will also provide clarity on investments in Investment Accounts (IA). Generally, there are 2 types of IA, Unrestricted IA (UIA) and Restricted IA (RIA). Currently, investment in UIA that have features that are similar to money market instruments, e.g. General Investment Accounts and Term Investment Accounts, are allowed and the investment spread limit applicable to money market instruments applies. As for other UIA and RIA, the Other Securities Limit will apply. In this respect, guidance has been provided in the Unit Trust Guidelines for clarity.

2.10 INVESTMENTS OF A FEEDER FUND

PROPOSAL 12

2.10.1 Respondents were asked to give their comments on the following questions:

Question 12.1	: Do you agree with the proposed investment limits for a feeder fund? Please provide specific reasons for your views.
Question 12.2	: Do you agree with the proposed permitted investments for a feeder fund? Please provide specific reasons for your views.
Question 12.3	: Do you agree for the proposed permitted investments to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

2.10.2 Majority of the respondents agreed with the proposals as well as the rationale provided.

2.10.3 One respondent is of the view that the fund strategy should mimic the target fund. The remaining investment not invested in the target fund should remain for liquidity purposes to meet redemption requirements only, for the feeder fund to be considered true-to-label.

The SC's response

2.10.4 We agree that a feeder fund should invest substantially in a target fund to be true-to-label. However, we recognise that some feeder funds need to use financial derivatives, typically to hedge its exposure to foreign exchange risk. Proposal 12b is meant to provide flexibility to UTMC for such purpose. Consistent with the feedback of the majority of the respondents, the proposal is maintained.

2.11 INVESTMENTS OF A MMF

PROPOSAL 13

2.11.1 Respondents were asked to give their comments on the following questions:

- Question 13.1 : Do you agree with the proposals relating to MMF? Please provide specific reasons for your views.
- Question 13.2 : Do you agree with the phase approach in implementing some of the IOSCO MMF Recommendations via the MMF Guidance? If you do not agree, should the MMF Guidance be issued as requirements under the Unit Trust Guidelines? Please provide specific reasons for your views.
- Question 13.3 : Do you agree for Proposal 13 to apply to PRS? Please provide specific reasons for your views.

Public comments

2.11.1 The respondents generally agreed with the proposals.

2.11.2 The key feedback to highlight is on proposal 13c, whereby two respondents proposed that the existing requirement i.e. paragraph 7 of Schedule B – Appendix I of the Unit Trust Guidelines (Existing Requirement) be maintained, due to the current low interest rate environment.

2.11.3 One of the respondents that proposed for the Existing Requirement to be retained also disagreed with the following proposals:

- (a) Proposals 13a and 13c: Do not agree because a MMF is a “lowest risk asset class” with good liquidity. Further, the respondent is of the view that there is no need for hedging arrangement for costs purpose coupled with the maturity of the instruments which are generally short term in nature. With regards to the proposed limit, the respondent views that MMFs are meant for low risk investments with high assurance of principal to be returned upon redemption.
- (b) Proposal 13d: The respondent is of the view that it is not necessary to allow a MMF to participate in any repurchase arrangements as this would increase the risk profile and return of the of the MMF, thus leaving other MMFs at a disadvantage.
- (c) Proposal 13e: The respondent disagreed with the proposed guidance for the WAM of a Standard MMF to be not more than 6 months citing that

such period is too short and provide investors with lower return particularly in an ultra low rate environment. In relation to the proposed guidance for MMFs to maintain minimum amount of liquid assets to strengthen their ability to face redemptions and prevent fire sales, the respondent is of the view that the minimum daily liquidity is too restrictive as it would affect returns in a scenario of a prolonged low interest rate environment. Further, such limit is not a one size fits all and varies among UTMCs.

2.11.4 All respondents agreed with the phase approach in implementing some of the IOSCO MMF recommendation through a Guidance Note for Money Market Funds.

The SC's response

2.11.5 In relation to proposal 13a, we would like to reiterate that the proposal is made to provide flexibility to UTMC as these instruments can be employed where necessary after considering the risk profile of the MMF. The proposal is **not intended to mandate** all MMF to invest in other MMF or enter into financial derivatives, for hedging purposes.

2.11.6 In relation to proposal 13c, the SC noted the feedback and has retained the requirement in the Unit Trust Guidelines but subject to the following:

- a) The debt securities are of 'high quality'; and
- b) The limit will be aggregated with investment in other MMFs and financial derivatives for hedging purposes i.e. 10% of the fund's NAV.

2.11.7 In relation to proposal 13d, it was introduced to enable MMF to undertake repurchase transactions for the sole purpose of EPM. Recognising the risk profile of a MMF, additional requirements have been proposed. However, the respondent argued that MMFs that undertake repurchase transactions will alter the MMFs risk profile. In this regard, we would like to reiterate that a MMF is only allowed to undertake repurchase transactions for the sole purpose of EPM. **It is not mandatory for a MMF to undertake repurchase transactions.** With regards to custodian having their reservations, we did not receive any feedback from the relevant parties on this matter. Industry participants are encouraged to engage the SC, if necessary.

2.11.8 In relation to proposal 13e, we would like to reiterate that the proposal is to outline a set of guidance in which UTMCS are encouraged to adopt in managing MMFs. The effectiveness of the set of guidance are meant to be reviewed after an appropriate period of time, before they are given due consideration on whether they are necessary to be codified in the Unit Trust Guidelines. Towards this end, as all respondents agreed with the proposal to implement the IOSCO MMF Recommendations on a phase approach, the MMF Guidance will be issued in due course.

3 FEEDBACK ON PROPOSALS RELATING TO A UTMC

3.1 RISK MANAGEMENT FRAMEWORK DOCUMENTATION

PROPOSAL 14

3.1.1 In the Consultation Paper, the SC proposed to require UTMCs to file with the SC, risk management process (RMP) documentation⁵ for all funds managed by a UTMC, both existing and new funds, including any subsequent amendments to the RMP.⁶

3.1.2 Respondents were asked to give their comments on the following questions:

Question 14.1 : (i) Do you agree with the proposal to require a filing of the RMP documentation with the SC for all funds managed by a UTMC? Please provide specific reasons for your views.

(ii) What are your views as to how long the transition period should be for existing funds to fully comply with the proposed filing of RMP documentation with the SC? Please provide specific reasons for your views.

Question 14.2 : Do you agree for Proposal 14 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

3.1.3 Majority of the respondents supported the proposals.

3.1.4 Some respondents, including two respondents that disagreed with the proposal, envisaged that a master copy of the RMP documentation can be submitted to SC and supplemental documentation can be submitted for different types of fund, where applicable. In addition, another respondent that disagreed with the proposal views that risk management should be managed at the UTMC level and not at fund level.

3.1.5 One respondent who agreed with the proposal, commented that the RMP documentation contributes to increasing best practices across the industry and enhances investor protection by increasing the transparency on the risk

⁵ The SC does not prescribe the format of the RMP documentation. A UTMC can design a format that enables the documentation to be updated via supplemental or appendix from time to time. Where possible, a master RMP documentation for all funds managed by the UTMC is also acceptable.

⁶ Presently, the RMP documentation is required as part of the feeder fund authorisation process.

management methods and tools used. The respondent also welcomed the proposal to allow flexibility and discretion on the format and content of the RMP documentation as it will enable each UTMC to tailor the document to the scale and complexity of their business. However, clarity is required on (i) the frequency at which the RMP documentation should be updated and submitted and (ii) the events which would trigger an update of the RMP documentation.

3.1.6 Another respondent highlighted that the risk management (processes and controls) provides oversight via monitoring and reporting of key risk indicators, with escalation of breaches or exceptions both at fund and entity level. This is governed by the risk management framework complemented by financial and non-financial risk policies and procedures. In addition, risk monitoring tools and systems are also utilised. The various risk management processes are incorporated across various policies, procedures and manuals and not contained within a single documentation. It is recommended that the SC share a sample template/questions of the RMP prior to finalisation/issuance for better understanding on the granularity of details required.

3.1.7 Another respondent shared that ensuring a proper risk management is in place is vital, what is more crucial is the monitoring of the risk management mechanisms in place. Having a standard filing requirement of the mechanisms for different fund types may be more effective in ensuring checks and balances of RMP. Hence, the respondent opined that more risk management guidelines and requirements including methodologies to be adopted would provide clarity to UTMCs in their risk adoptions. The respondent also reiterated the point that there is no one size fits all for risk management and it may also differ from fund to fund depending on its asset class and investment objectives/strategies, etc. Imposing a standard requirement on all the funds may sometimes be too restrictive and may not entirely benefit the unitholders. The respondent also suggested that perhaps a requirement to have a risk management officer would enable UTMCs to have a more focused role in ensuring adherence to these risk management requirements.

3.1.8 The respondents that disagreed have cited the following:

(a) UTMCs already have in place their respective internal RMP which has gone through internal governance and process. The proposal poses administrative challenges to prepare RMP documentation at fund level; and

(b) There is no guidance as to how to prepare the RMP documentation.

3.1.9 Feedback was also received with regards to the transitional period that ranges between six months to two years considering some UTMCs are managing many funds. Majority of the respondents requested a one-year transitional period.

The SC's response

- 3.1.10 The RMP documentation is intended to document the policy and procedures in place to manage the risks of a particular fund. We take cognizance that the RMP may be incorporated in various policies and procedures within the entity but without a proper documentation, it will be a challenge to assess the UTMCs' RMP as there is an expectation that all UTMCs must have RMP that is appropriate and proportionate to the nature and complexity of the funds being managed. The RMP documentation is meant to provide the needed check and balance. Towards this end, with proper guidance, we believe the implementation of this proposal will increase the best practices across the industry for the orderly development of the industry.
- 3.1.11 In terms of the format of the RMP documentation, we would like to clarify that UTMCs may prepare a single RMP document for the funds they manage as long as all associated risks are identified and the corresponding risk management policy and procedures are clearly documented. With regards to the frequency or triggering event that requires an update to the RMP documentation, UTMCs may supplement the RMP documentation with additional information as and when new funds are being established or as and when new risks or material changes in the RMP have occurred.
- 3.1.12 After due consideration, the SC has revised the proposal as follows:
- (a) Where a fund intends to invest in new or higher risk investments including investing extensively in financial derivatives, digital assets or undertaking securities lending and repurchase transactions, the RMP documentation must be submitted as part of the fund application or in the case of existing fund, before any changes are to be effected to the fund documentation.
 - (b) As for the other funds (including existing funds) that are not mentioned in paragraph (a) above, we have revised the proposal by not requiring a UTMC to submit the RMP documentation to the SC. However, UTMCs are still required to prepare the RMP documentation for the reasons mentioned above. A transitional period of 1.5 years will be provided for UTMCs to prepare the RMP documentation. Thereafter, the SC will rely on the risk-based regulatory approach to assess and where necessary, request for the RMP documentation from a UTMC.
 - (c) A RMP guidance document (RMP Guidance) has been issued to provide clarity on what should be covered in the RMP and this RMP Guidance will be updated from time to time, where necessary. Generally, the RMP documentation must be a stand-alone document that include all relevant information that are clear and understandable.

3.2 **HOLDING OF A FUND'S UNITS BY THE UTMC**

PROPOSAL 15

3.2.1 Respondents were asked to give their comments on the following questions:

- Question 15.1 : Do you agree with the proposal to allow a UTMC to contribute seed money in a fund? Please provide specific reasons for your views.
- Question 15.2 : Do you agree with the proposal to remove the Maximum Units in the Manager's box? Please provide specific reasons for your views.
- Question 15.3 : Do you agree for Proposal 15 to apply to PRS? Please provide specific reasons for your views.

Public comments

- 3.2.2 All respondents agreed with the proposals. Some notable comments include seed money places more emphasis to UTMC to believe in their own products, build track record and allows a fund with small fund size to be managed more effectively.
- 3.2.3 One respondent suggested that the proposed condition that trustee approval be obtained prior to any transaction by the UTMC be removed to be consistent with international practices and avoid creating another layer of compliance.

The SC's response

- 3.2.4 The SC noted the suggestion and revised the proposal to emphasise that holding of a fund's units by a UTMC is allowed provided that any potential conflict of interest that may arise is addressed. In this respect, the UTMC and its board of directors must ensure that there are adequate policies, procedures and controls established to manage any potential conflict that may arise.
- 3.2.5 Recognising that there are other ways to mitigate potential conflict of interest from an operational perspective, it may be onerous and unnecessary to require trustee's approval for each transaction. Toward this end, the revised proposal will no longer require trustee's approval on every seed money transactions. Instead, the policies, procedures and controls on conflict of interest may include a process to obtain the trustee of the fund's approval based on certain materiality thresholds.

3.2.6 Furthermore, the scope of the revised proposal is also extended to corporations related to the UTMC that contribute seed money to a fund. This is to ensure any potential conflict that may arise as a result of providing the seed money is addressed.

3.3 **OVERSIGHT ARRANGEMENT TO REPLACE INVESTMENT COMMITTEE**

PROPOSAL 16

3.3.1 Respondents were asked to give their comments on the following questions:

Question 16.1 : Do you agree with the proposal to remove the requirement to appoint an investment committee as well as the requirements on the structure and composition of the investment committee? Please provide specific reasons for your views.

Question 16.2 : Do you agree with the proposal to, in place of an investment committee, require the UTMC to establish an oversight arrangement to undertake the existing roles and responsibilities of an investment committee for its fund? Please provide specific reasons for your views.

Question 16.3 : Do you agree for Proposal 16 to apply to PRS? Please provide specific reasons for your views.

Public comments

3.3.2 Majority of the respondents agreed with proposal with key feedback as follows:

- (a) Some of the roles and responsibilities of an investment committee are more appropriate when they are undertaken by internal functions.
- (b) An oversight arrangement would be able to replace the function of the investment committee. A UTMC should have some flexibility in appointing suitable members for the oversight function.
- (c) SC to provide more clarity and guidance to ensure that the oversight arrangement of the UTMC remains independent and ensure clear segregation of duties.

3.3.3 One respondent that disagreed with the proposal cited the removal of the requirement to appoint an investment committee would erode the effectiveness

of the check and balance controls, that are necessary to ensure proper supervision over the funds' investment activities.

The SC's response

- 3.3.4 We would like to clarify that the proposal is to remove prescription for an investment committee e.g. *minimum 2 independent members while maintaining a minimum ratio of at least one-third independent members*. The existing roles and responsibilities of an investment committee will now be required to be undertaken by the oversight arrangement.
- 3.3.5 Taking into consideration the respondent's feedback whereby clarity is required to ensure the persons undertaking the oversight arrangement remain independent, we have included a requirement to require the persons undertaking the oversight function to be independent from the functions where the oversight arrangements are on to enable such persons to undertake its role effectively. In addition, a guidance is also included to provide clarity to the industry.
- 3.3.6 For avoidance of doubt, UTMCs that wish to maintain an investment committee may continue to do so as long as the arrangement complies with the revised Unit Trust Guidelines.

3.4 TRAINING REQUIREMENTS

PROPOSAL 17

- 3.4.1 In the Consultation Paper, the SC **proposed to replace the Training Requirements** with the following:
- (d) A UTMC must ensure that its executive directors and employees, including compliance officer and personnel involved in operations are adequately trained and kept abreast of industry developments; and
 - (e) Details of all training provided are to be properly maintain by the UTMC.
- 3.4.2 Respondents were asked to give their comments on the following questions:

Question 17.1 : Do you agree with the proposal to replace the Training Requirements with a broader obligation for UTMC to provide adequate training to its executive directors and employees? Please provide specific reasons for your view.
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Question 17.2 : Do you agree for Proposal 17 to apply to PRS? Please provide specific reasons for your view.

Public comments

3.4.3 The respondents generally agreed with the proposal. Two respondents highlighted that more clarity is required as to what would be considered "adequate". One respondent suggested that the requirement to be redrafted to state that all employees under the payroll of the UTMC, whether on a permanent or contractual basis but excluding interns and temporary staff, are adequately trained and kept abreast of industry developments.

The SC's response

3.4.4 The SC noted the feedback and has included a guidance to assist the industry to ascertain what is considered "adequate". With regards to the suggested redraft of the requirement, we disagree with the proposal as the term "interns" or "temporary staff" may be subject to different interpretation. Based on the principle of the requirements, UTMCs are given the liberty to assess who should be adequately trained.

4 FEEDBACK ON PROPOSALS RELATING TO DEALING, VALUATION AND OPERATIONAL MATTERS

4.1 DEALING IN UNITS

PROPOSAL 18

4.1.1 Respondents were asked to give their comments on the following questions:

Question 18.1	: Do you agree with the proposal on frequency of valuation and dealing in units of a Variable Price Fund? Please provide specific reasons for your views.
Question 18.2	: Do you agree with the proposal on suspension of dealing in units? Please provide specific reasons for your views.
Question 18.3	: Do you agree with the proposal of having an expressed prohibition on the use of redemptions in-kind and side pockets? Please provide specific reasons for your views.
Question 18.4	: Do you agree for Proposal 18 to apply to ETF and PRS? Please provide specific reasons for your views.

Question 18.1

Public comments

4.1.2 All respondents supported the proposals.

The SC's response

4.1.3 We welcome the support for the proposal and will implement it as proposed.

Question 18.2

Public comments

4.1.4 All respondents supported the proposals.

4.1.5 Three respondents sought clarification on what constitutes "material portion" and one of them further suggested that SC provide examples of what would constitute "exceptional circumstances" where a UTMC may suspend dealing. Another respondent sought clarification on whether a situation where the market value or fair value of a material portion of the fund's assets "cannot be determined" refers to a situation where the market price or fair value of the fund's assets cannot be correctly or accurately determined. The respondent is

of the view that “cannot be determined” may imply that the data or information may not be available due to e.g. system error or connectivity issue.

- 4.1.6 Another respondent commented that the ability to suspend is important as suspension is a mechanism for the fund to act in the best interest of investors under certain circumstances to avoid a fire-sale of assets, such as in instances where the market is not functioning normally.

The SC’s response

- 4.1.7 We would like to clarify that one of the examples in which dealings can be suspended is where the market value or fair value of a material portion of the fund’s assets cannot be determined e.g. the market prices are not quoted or limited information to enable fair valuation assessment on the instruments. However, this should only be due to exceptional circumstances including a situation where the market the fund is exposed to is not functioning normally.
- 4.1.8 For avoidance of doubt, difficulties in realising the fund’s assets or temporary shortfalls in liquidity may not on their own be sufficient justification for suspension. A guidance has been provided for the Unit Trust Guidelines to provide clarity to the industry.

Question 18.3

Public comments

- 4.1.9 The majority of respondents supported the proposals. The respondents that agreed generally shared the view that redemptions in-kind and side pockets are not suitable LRM tools when dealing with retail investors. One respondent added that for redemption in-kind:
- (a) Not all asset classes can be split.
 - (b) Distributing of the underlying assets to investors does not alleviate liquidity issues as it transfers the problem to investors.
 - (c) Transfer of securities to investors who will sell them on the market may adversely impact the value for the remaining investors if such a sale had significant market impact consequences.
 - (d) Large-scale operational impacts in processing the delivery of physical assets to investors.

On the other hand, for side-pockets:

- (e) There is potential for abuse e.g. illiquid assets being segregated into

side-pockets accounts to protect the fund manager's fees.

- (f) Potential issues arising from the extent of fund managers' discretion to designate investments into a side pocket.

4.1.10 Three respondents disagreed with the proposal and were of the view that redemptions in-kind and side pockets should be allowed as LRM tools to facilitate instances of illiquid assets owned by a fund.

4.1.11 Two respondents highlighted the prohibition to use redemption in-kind should not be applicable to ETFs.

The SC's response

4.1.12 The SC will take the approach of prohibiting the use of redemption in-kind and side pockets as LRM tools for retail funds. UTMCs that wish to use these tools will need to satisfy the SC that the use is suitable for retail investors, including providing details of the mechanism and ensuring proper safeguards are in place.

4.1.13 With regards to whether prohibition of the use of redemption in-kind should be applicable to ETFs, we would like to clarify that the proposal is in relation to liquidity risk management tools exercised at the discretion of the UTMC. For ETFs, in-kind redemption is a feature of the ETF product and is a primary market transaction whereby a basket size is predetermined.

4.2 REVISION TO THE REDEMPTION PAYMENT PERIOD

PROPOSAL 19

4.2.1 Respondents were asked to give their comments on the following questions:

Question 19.1 : Do you agree with the proposed amendments to requirements in relation to the payment period of proceeds of repurchase of units? Please provide specific reasons for your views.

Question 19.2 : (i) Consequent to Proposal 19, should paragraphs 10.04⁷ and 10.05⁸ of the Unit Trust Guidelines be amended?
(ii) If the answer to (i) is "No", please provide specific reasons for your views.

⁷ A UTMC must pay the trustee the value of units created within 10 days of giving instructions to the trustee to create units.

⁸ A trustee must pay the UTMC the value of units cancelled within 10 days of receiving instructions from the UTMC to cancel units.

(iii) If the answer to (i) is "Yes", would 7 business days be appropriate? Please provide specific reasons for your views.

Question 19.3 : Do you agree for Proposal 19 to apply to PRS? Please provide specific reasons for your views.

Public comments

4.2.2 All respondents agreed with the proposals.

4.2.3 One respondent sought information on the transitional arrangement for existing funds. Two respondents suggested SC to reconsider allowing a UTMC to satisfy the requirement by paying the IUTA or CUTA that operates under a nominee system.

The SC's response

4.2.4 We would like to clarify that the expectation to satisfy the requirement for the payment of redemption proceeds has always been to the end beneficiary of the units. In this regard, the UTMC and the respective IUTA and CUTA are expected to comply with the said requirement for the benefit of the end beneficiary of the units. As to the transitional arrangement, please refer to the Frequently Asked Questions (FAQ) as published on SC's website.

4.3 **BASIS OF VALUATION OF A FUND'S ASSETS AND INCORRECT PRICING**

PROPOSAL 20

4.3.1 Respondents were asked to give their comments on the following questions:

Question 20.1 : Do you agree with the proposals in relation to the valuation of a fund's assets? Please provide specific reasons for your views.

Question 20.2 : Do you agree for Proposal 20 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

4.3.2 The respondents generally agreed with the proposals. Three respondents provided the following comments:

(a) On valuation of bonds

With regards to valuation of foreign bonds, one respondent proposed that foreign bonds that are cleared through clearing platforms (whether quoted on an exchange or otherwise) be valued based on prices provided by pricing providers such as Refinitiv and Bloomberg.

The SC also received 3 feedback regarding valuation of bonds using prices quoted by Bond Pricing Agency Malaysia (BPAM) whereby one of them recommended the use of prices provided by other pricing providers, such as Markit, while the remaining two sought clarification on whether UTMCs may use prices provided by providers other than BPAM.

(b) On use of amortised cost accounting for valuation of unlisted investment instruments

One respondent suggested that for prudent valuation basis, the lower of fair value and amortised cost should prevail, while another respondent suggested that the use of amortised cost accounting should be limited to valuation of money market instruments.

(c) On requiring trustee's approval on methods or bases for determining fair value

One of the respondents sought clarification on whether the requirement for technical consultation prior to the trustee's approval on basis to determine the fair value is meant to necessitate the trustee to seek the necessary consultation at their end rather than the UTMC's end.

Two respondents proposed for the fund's auditor to verify the valuation method used by the UTMC to ensure that it is consistent with accounting standards. The respondents suggested that the SC consider including the need for the fund's auditor to verify the basis for determining the fair value before providing it to the trustee for approval.

(d) On valuation of OTC financial derivative

One respondent commented that OTC financial derivatives are not very liquid and there may not be a meaningful quote of the value other than the quote from the counterparty. As such it may be counterproductive to require the UTMC to value OTC financial derivatives at market value (which in most instances are not available) other than the value predominantly provided by the counterparty. In addition, the respondent is not aware of independent service providers in the market which specialises in valuation of OTC financial derivatives beside the financial

institution. Even if there is, there will be additional costs involved and lack of available market data for such financial derivatives.

On the other hand, another respondent highlighted that a UTMC must ensure operational readiness of its infrastructure or capacity to value complex OTC or listed derivatives fairly, prior to trading it. The fair value provided by the counterparty should be independently assessed on a periodic basis, to ascertain whether it is fair or not.

On the point on capacity to value OTC financial derivatives, another respondent commented that it may rely on external source e.g. external appointed fund administrator who performs fund accounting services for the fund.

The SC's response

- 4.3.3 On valuation of bonds, the SC will require the bonds to be valued based on fair value. This can be achieved by valuing bonds, regardless whether the bonds are denominated in RM or otherwise, using price quoted by reputable pricing service providers. In this regard, the use of prices by BPAM for RM-denominated bonds will no longer be made mandatory. This method of determining fair value also applies to bonds that are listed but the price is not quoted on the exchange. The SC wishes to clarify that for bonds that are listed and quoted on an exchange, the official closing price or last known transacted price must be used to determine the value of such bonds. However, if the price is not representative or not available to the market, the investments should be valued at fair value.
- 4.3.4 On item (b), we would also like to clarify that the use of amortised cost accounting is allowed but restricted to what is proposed under proposal 20 and the use of amortised cost accounting is not mandatory.
- 4.3.5 On item (c), we confirm that the understanding is correct as long as the fair value is determined in accordance with the requirements. In relation to getting technical consultation on the basis of determining the fair value, both the UTMC and the trustee have the discretion to decide whether this is necessary. For example, in the case where the basis of determining the fair value is well established, it may not be necessary to incur the additional expense to the fund. With regards to the proposal to get the fund's auditor to verify the basis of determining the fair value, we are of the view that this does not need to be imposed as a mandatory requirement as it is already covered under technical consultation, when required.
- 4.3.6 On item (d), the SC has revised the criteria such that in the case of OTC financial derivatives, "reliable and verifiable valuation on a daily basis" refers to (i) a valuation made by the UTMC based on a current market value; or (ii)

where such value is not available, a fair value based on an appropriate valuation method which is checked at an appropriate frequency by an independent party (as mentioned under paragraph 2.3.10 above). This is reflected as paragraph 6.17 of the Unit Trust Guidelines and the intention is to ensure that the UTMC has in place the process to enable for independent verification of the valuation. The proposed requirement does not require the valuation for the OTC financial derivative to be provided by an independent party. Instead, the valuation must be made by the UTMC based on the current market value, or where such value is not available, a fair value based on an appropriate valuation method which is checked at an appropriate frequency by an independent party. The independent party being envisaged is either the fund's auditor or fund's accountant.

PROPOSAL 21

4.3.7 Respondents were asked to give their comments on the following questions:

Question 21.1 : Do you agree with the proposals in relation to the incorrect pricing of the units of a fund? Please provide specific reasons for your views.

Question 21.2 : Do you agree for Proposal 21 to apply to PRS? Please provide specific reasons for your views.

Public comments

4.3.8 The respondents generally agreed with the proposals. One of the respondents provided the following feedback:

- (a) To clarify whether the guidance in regard to cumulative effect of unit pricing errors and disclosure requirement regarding pricing error threshold that are provided for in FIMM's Investment Management Standards will be included in the Unit Trust Guidelines.
- (b) Proposed not to remove paragraph 10.41(b) of the Unit Trust Guidelines⁹ because should there be any valuation or pricing errors which will result in the UTMC having to reimburse the investor, the UTMC will also be able to recover the valuation or pricing difference for the creation or cancellation of units executed from the fund, accordingly. The rectification of creating and cancellation is to be treated consistently

⁹ Requirements state that the UTMC must take immediate remedial action to rectify any incorrect valuation or pricing. Rectification must be extended to the reimbursement of money from the fund to the UTMC.

based on the correct fund price. Two other respondents also disagreed to remove paragraph 10.41(b).

- 4.3.9 Two other respondents disagreed with the proposal that trustee’s approval would be required on the manner of compensation to unit holders, given that UTMC is given the ability to choose.

The SC’s response

- 4.3.10 The SC noted the feedback provided and have revised the proposal as follows:

- (a) A guidance has been included in the Unit Trust Guidelines to provide clarity on cumulative effect of unit pricing errors and a disclosure requirement regarding pricing errors has been included in the CIS Prospectus Guidelines.
- (b) Paragraph 10.41(b) of the Unit Trust Guidelines is retained. A guidance is also included to provide clarity on when a UTMC should reimburse the fund as a result of a valuation or pricing error.
- (c) The intention for requiring the trustee’s approval on the manner to reimburse unit holders is to avoid affected unit holders to be disadvantaged. However, we have reconsidered the proposal and have since revised the requirement whereby trustee’s approval is no longer required provided that reimbursement to former unit holders (i.e. unit holders that no longer have any investments in the fund) must only be made by way of cash.

- 4.3.11 In addition to the above, we have also introduced a new requirement for the trustee to notify the SC when the UTMC has completed the reimbursement satisfactorily.

4.4 REQUIREMENTS IN RELATION TO COOLING-OFF RIGHT

PROPOSAL 22

- 4.4.1 Respondents were asked to give their comments on the following questions:

Question 22.1	: Do you agree with the proposed revision to the cooling-off right? Please provide specific reasons for your views.
Question 22.2	: Do you agree for Proposal 22 to apply to PRS? Please provide specific reasons for your views.

Public comments

4.4.2 The respondents generally agreed with the proposal with some expressing that the approach is fairer for the UTMC, does not place unreasonable burden on the UTMC and prevents any potential abuse of the cooling-off rights. Other feedback are summarised as follows:

- (a) One respondent suggested to shorten the cooling-off right from 6 business days to 3 business days in order to minimise the impact to the investors. Another respondent suggested that the payment period be revised to be consistent with the revised redemption payment period i.e. from 10 calendar days to 7 business days.
- (b) One respondent suggested that the SC reconsider the proposal as investors may not have adequate knowledge nor experience in investment and should be given ample time to consider their decision within the cooling-off period. While it was noted that the intention here is to mitigate the risk of investor taking advantage of this cooling off right, there could also be circumstances where the investor decides to pull off from the investment due to other genuine reasons.
- (c) Two respondents sought clarification on whether the fund or the UTMC would be able to retain the excess following the cooling-off where it is required to refund the investor the original price when the market price is higher than the original price of a unit. One of the respondents added that given the new proposal, perhaps it is better to remove cooling-off rights as this would eliminate any unfair circumstances.
- (d) One respondent sought clarification on the proposal that “where the market price is higher than the original price paid by investor, the UTMC may agree to pay the investor the excess amount, provided that such amount is not paid out of the fund or assets of the fund” as it felt that the phrase “provided that such amount is not paid out of the fund or assets of the fund” was redundant. The respondent further commented that if there is foreign currency conversion involved, the prevailing market rate at the point of cooling-off should be applied. The respondent concluded that the existing cooling-off requirement should be maintained i.e. the refund is the same amount as the subscription amount.
- (e) One respondent noted that based on its low cooling-off request records, it will be costlier to enhance the system than to provide a cooling off in accordance with the existing requirements.

The SC's response

4.4.3 The SC's response to the public comments highlighted above are as follows:

- (a) We do not share the view where shortening the deadline to exercise cooling-off right will minimize the impact to the investors. In our view, an investor may not be able to act accordingly if the deadline is shortened. However, we do agree with the proposal to revise the payment period to 7 business day for consistency and have reflected this in the Unit Trust Guidelines, accordingly.
- (b) We would like to reiterate that under the proposal, when an eligible investor exercise the cooling-off right, the sales charge imposed must be refunded together with the proceeds. This is based on the rationale that the investor is not likely to exercise the cooling-off right in the event the investor understood the investment at the point of deciding to invest. Generally, liquidity is one of the main features of a retail fund whereby it is a requirement to deal in the redemption of units at least once a month. Unlike an investment product with lock-in period, investors of a retail fund are able to divest their investment with ease. In addition, maintaining the existing cooling-off rights may not be in the best interest of the fund (and other unit holders of the fund) as monies received from investors will be invested and the fund may be forced to liquidate its investments to honour the payment, which may be at a higher amount than the prevailing NAV per unit.
- (c) With regards to the excess proceeds following a cooling-off, we would like to clarify that the excess must be retained by the fund as the assets of the fund is being liquidated for the cooling-off payment. We do not agree with the proposal to remove the cooling-off right as this will effectively remove the need to refund the sales charges imposed.
- (d) We would also like to clarify that the proposal that "where the market price is higher than the original price paid by investor, the UTMC may agree to pay the investor the excess amount, provided that such amount is not paid out of the fund or assets of the fund" simply means that a UTMC, on their own expense, may decide to refund the difference in amount between market price at the point where an investor exercise the cooling-off right which is higher than the original price paid by the investor, hence the proviso that the amount is not paid out from the fund or assets of the fund. Where foreign currency is involved, the treatment should be consistently applied when ascertaining the NAV per unit of the fund, regardless of whether the purpose is for cooling-off or a redemption of units.

- (e) Lastly, we would like to clarify that a UTMC is allowed to adopt the current cooling-off provisions as long as it does not breach the minimum requirements of the revised cooling-off right as outlined in the Unit Trust Guidelines.

4.5 **ENABLING A FUND TO PAY DISTRIBUTION OUT OF CAPITAL**

PROPOSAL 23

- 4.5.1 Respondents were asked to give their comments on the following questions:

- Question 23.1 : Do you agree with the proposal to allow distribution out of capital and the disclosures to be made in the prospectus and fund report of a Variable Price Fund? Please provide specific reasons for your views.
- Question 23.2 : Do you agree for Proposal 23 to apply to ETF, PRS and wholesale fund? Please provide specific reasons for your views.

Public comments

- 4.5.2 The respondents generally agreed with the proposal. The key responses are as follows:
- (a) Such features are already common in overseas funds and helps to meet the needs of certain investors who require a steady stream of distributions, even if these distributions have to come from capital. Proper disclosure requirements however must be prescribed to ensure that investors are aware that the distributions are not from the income of the fund.
 - (b) One respondent agreed as long as it is in line with the fund's objective and in accordance to the disclosure in the prospectus of the fund.
 - (c) One respondent commented that distribution out of capital would allow UTMC to better manage the distribution policy of funds.
 - (d) Two respondents highlighted that investors must be made aware of such policy before investing in a fund that allows distribution out of capital and awareness to the investing community should also be made. The proposal should only be targeted to specific age group via a dedicated fund e.g. close-ended fund.

- (e) One respondent suggested that the format of tax vouchers (i.e. percentage of distribution out of income and capital) should be standardised as uniform disclosure across the industry will ease investors' understanding on the source of income distribution.

4.5.3 A few respondents disagreed with key reasons as follows:

- (a) Enabling a Variable Price Fund to distribute out of capital, will erode capital and is detrimental to investors.
- (b) The investors in Malaysia are not advanced in financial knowledge as compared to Singapore and Hong Kong, which may lead to misinterpretation of the fund account by potential investors.
- (c) The proposal may not be in the best interest of investors.
- (d) Two respondents disagreed to apply the proposal to PRS as they viewed PRS as a form of savings for retirement. One of the respondents added that if PRS is to distribute out of capital, it will defeat the purpose of retirement savings. Also, if there is distribution for PRS, it must be in the form of reinvestment as there may be tax implication if it is paid out in cash to unit holder (i.e. withdrawal). Such payout may also be to the detriment to those who have reached retirement age and are eligible to withdraw, where they would have been paid monies they have invested earlier prior to retirement. Whereas, those who have yet to retire or eligible for withdrawal will still have sufficient time to recoup their investment.

The SC's response

4.5.4 We are of the view that the proposal will provide flexibility for UTMCs to introduce funds that meet the investment objective of investors that need regular income and are fully aware that such income may be paid out from the capital of the fund. Depriving such investors to funds with such features is not desirable and would restrict product innovation to meet investors' need.

4.5.5 We also understand that the flexibility may allow a UTMC to more optimally manage the portfolio of such funds.

4.5.6 In our Consultation Paper, we have emphasised that effective communications between UTMCs and investors is key to investor education and empowerment, ultimately allowing investors to make informed decisions. Towards this end, we would like to reiterate that suitability assessments (as opposed to targeting a specific age group) and adequate disclosure to investors is key to promoting good investment experiences.

- 4.5.7 The above comments apply to PRS. The SC is mindful of the members' profile, in which a member that has reached the retirement age may opt for a decumulation PRS that provide regular income that suit the member's need.
- 4.5.8 With regards to standardisation of disclosure in tax vouchers, the SC agrees that it will ease investors' understanding. In this regard, we will engage FIMM in due course to look into the suggestion.
- 4.6 **REMOVAL OF THE REQUIREMENT RESTRICTING THE USE OF ANY BROKER OR DEALER FOR A FUND FROM EXCEEDING 50% OF A FUND'S DEALINGS**

PROPOSAL 24

- 4.6.1 Respondents were asked to give their comments on the following questions:

Question 24.1	: Do you agree with the proposal to remove the restriction on the use of any broker or dealer for the fund's dealings? Please provide specific reasons for your views.
Question 24.2	: Do you agree for Proposal 24 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

- 4.6.2 The respondents generally agreed with the proposals. Generally, the respondents were of the view that the removal of the restriction will provide flexibility to UTMCs in managing their broker allocation and trades can be allocated to brokers which are most favourable to the fund.
- 4.6.3 One respondent disagreed citing that the limit should be retained so that no single broker is "monopolizing" the business and it is good to have a diversified pool of brokers and dealers to ensure the best pricing for the execution of trades.

The SC's response

- 4.6.4 The issue with lack of diversification should not arise as at the entity level, a fund manager must already adhere to the current 50% single broker limit imposed in the SC's FM Guidelines. In addition, we do not share the view that a single broker can monopolise the trades for a fund as the decision to trade with any brokers, in the best interest of a fund, lies with the UTMC.

4.7 ENHANCEMENT TO REQUIREMENTS RELATING TO SOFT COMMISSIONS

PROPOSAL 25

4.7.1 Respondents were asked to give their comments on the following questions:

Question 25.1 : Do you agree with the proposal to enhance the requirements on soft commissions? Please provide specific reasons for your views.

Question 25.2 : Do you have any feedback on the following expenses that would not be considered as part of soft commissions:

(i) systems or services relating to performance measurement of portfolios; and

(ii) subscription fees for fund's benchmark indices.

Please provide specific reasons for your views.

Question 25.2 : Do you agree for Proposal 25 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

4.7.2 The respondents generally agreed with the proposal stating that it will provide greater transparency, clarity and it helps to mitigate conflict of interest. It also broadens the scope of soft commissions. One respondent suggested that the SC clarify its expectation on "In situation where a soft commission may benefit the fund and others, the UTMC must disclose the arrangements in such a way that unit holders are able to assess the scope of the arrangements and how the soft commissions will benefit others".

4.7.3 Two respondents disagreed citing the following reasons:

(a) The enhancement will add additional administrative layer and potentially cost to the unit holders (as soft commission are channelled back to the fund); and

(b) There is no need for further disclosure as the definition of soft commission is already restrictive in nature.

4.7.4 Feedback was also sought on whether the following should not be considered as part of soft commission:

- (a) Systems or services relating to performance measurement of portfolios;
and
- (b) Subscription fees for fund's benchmark indices.

Generally, the respondents are of the view that (a) and (b) should be allowed as soft commission because these tools are used as part of fund management processes and they benefit the unit holders as they provide pertinent information that enable investors to assess their investment returns.

The SC's response

- 4.7.5 The SC is of the view that the enhancements are necessary to ensure that potential conflict of interests are mitigated and soft commission may only be accepted if the UTMC can demonstrate that such acceptance will bring benefit to the fund. We would like to clarify that a UTMC is expected to know who benefits from the soft commissions received which may include the UTMC's clients other than the funds it manages (e.g. other investment portfolios). In this regard, adequate disclosure on the scope of the arrangement must be disclosed to enable investors to make an informed decision. The industry is welcomed to approach the SC if they encounter difficulty in providing disclosure on a specific arrangement.
- 4.7.6 After considering the feedback from the respondents, we will allow items (a) and (b) in 4.7.4 above to be considered as soft commission on the basis that these tools bring a direct benefit to the management of the fund. Among others, these tools provide pertinent information to assist in identifying performance drivers for the portfolio, aid in portfolio risk analysis and for tracking the portfolio performance of peers which assist UTMC to make better investment decisions for the fund.

4.8 REQUIREMENTS RELATING TO TERMINATION OF A FUND

PROPOSAL 26

4.8.1 Respondents were asked to give their comments on the following questions:

- Question 26.1 : Do you agree with Proposal 26? Please provide specific reasons for your views.
- Question 26.2 : Do you agree for Proposal 26 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

4.8.2 The respondents generally agreed with the proposal. Key feedback are summarised as follows:

- (a) The proposal provides a more detailed and standardised process in the industry for fund termination and this would also promote investors' understanding of their rights and obligations pertaining to fund termination. It will also protect any potential investor from subscribing a fund that is undergoing a termination process. However, clarity is required on whether "number of unit holders" include the end beneficiaries that invest through an IUTA or a CUTA that operates under a nominee system. It is also proposed that a similar process be applicable for termination of a share class under similar situation i.e. where the fund size is no longer viable to maintain such share class.
- (b) Suggest for SC to define "commencement date" and "completion date".
- (c) One respondent requested that SC provide clarity on whether SC can provide a list of termination circumstances or the UTMC (with consent of trustee) is to specify the termination circumstances in the fund's deed and prospectus. Another respondent suggested that SC provide criteria for clarity purposes (e.g. for retail funds with AUM below a certain threshold for example RM20 million and/or number of unit holders below (for example below 25) and in instances of feeder fund, upon notice of closure of target fund). If such criteria is met, the termination of such retail fund should be allowed automatically without the need to go through the lengthy process of calling unit holders meetings which resulted additional costs to the fund/unit holders.
- (d) In some circumstances, it is impossible to determine the "date of expected completion" because there are various factors that may affect the completion timeline. For example, illiquid asset, dependencies,

foreign jurisdiction, tax declaration requirement, audit, withholding tax, etc.

- (e) The proposal is practical and will allow UTMC to act swiftly to terminate funds that are no longer viable. Any delay in the process e.g. unit holders' meeting may have an impact on the fund's performance. It is proposed that the UTMC should not be required to disclose the cost of termination where the termination cost is borne by the UTMC.

4.8.3 Two respondents disagreed with the proposal that it is the trustee obligation to notify the SC at the completion of fund termination. The respondents commented that the trustee will dispose the assets upon the UTMC's instruction. The trustee does not distribute the money directly to the unit holders. Instead, the trustee will transfer the money to the UTMC for the UTMC's onward transmission to the unit holders. Hence, upon completion of the termination of a fund, the UTMC (as opposed to trustee) should notify the SC and the trustee.

4.8.4 One respondent disagreed with the proposal that fund termination circumstances apply to PRS. Under the proposal, a PRS scheme can be terminated by merely notifying unitholders. However, as their retirement savings are in question, they should at least have a say in the termination, perhaps by way of a members' meeting, regardless of the circumstances behind the termination.

The SC's response

4.8.5 The SC's response to the feedback are as follows:

- (a) We would like to clarify "number of unit holders" include the end beneficiaries. We also note the feedback to apply the termination process to termination of a share class of a fund. We agree and have reflected the requirement in the revised Unit Trust Guidelines.
- (b) We note the feedback and are of the view that the revised Unit Trust Guidelines is clear.
- (c) We are of the view that is it not practical for the SC to prescribe or provide a list of circumstances for fund termination. It is the UTMC's responsibility to ensure the circumstances of termination is in the best interest of unit holders.
- (d) The industry is welcomed to approach the SC if they encounter such circumstances that leads to the difficulty in providing an expected date of completion.

4.8.6 With regards to the respondents view in paragraph 4.8.3, we do not share the same view as the trustee being as an independent party with fiduciary duty to unit holders, provides a check-and-balance to the UTMC when providing the notification to the SC.

4.8.7 In relation to the feedback on PRS, the *Capital Markets and Services (Private Retirement Scheme Industry) Regulation 2012* states that termination of a PRS scheme cannot take place without approval of the SC. Therefore, at the underlying fund level, there could be circumstances where the fund can be terminated upon the triggering of certain circumstances if provided for under the PRS Guidelines.

4.9 **REQUIREMENTS ON QUORUM FOR UNIT HOLDERS' MEETING**

PROPOSAL 27

4.9.1 Respondents were asked to give their comments on the following questions:

Question 27.1 : Do you agree with Proposal 27? Please provide specific reasons for your views.

Question 27.2 : Do you agree for Proposal 27 ETF and PRS? Please provide specific reasons for your views.

Public comments

4.9.2 All respondents agreed with the proposal as the reduction in the number required for quorum improves the chances to convene unit holders' meeting especially for funds with less than five unit holders.

4.9.3 One respondent highlighted the possibility that the fund may only have one unit holder and suggested that in this case, any changes may be effected upon receipt of written approval from that unit holder.

The SC's response

4.9.4 We note the feedback and agree that it is possible for a fund to be left with one unit holder. As such, a requirement has been included in the revised Unit Trust Guidelines to cater for the situation where there is only one unit holder remaining in the fund (or class of units), such unit holder, whether present in person or by proxy, at the meeting shall constitute as quorum.

5 OTHER PROPOSED AMENDMENTS

PROPOSAL 28

5.1 CONTENTS OF ANNUAL AND INTERIM REPORTS (FUND REPORTS)

5.1.1 Respondents were asked to give their comments on the following questions:

Question 28.1 : Do you agree with our proposal to prescribe requirement to disclose information on exposure to derivatives, securities financing transactions and collateral? Please provide specific reasons for your views.

Question 28.2 : Do you agree with our proposal to prescribe the basis of performance calculation? Please provide specific reasons for your views.

Question 28.3 : Do you agree with our proposal to prescribe the additional disclosure on expense ratio for fund with performance fee? Please provide specific reasons for your views.

Question 28.4 : Do you agree with our proposal to prescribe new disclosure relating to transactions with parties related to the UTMC? Please provide specific reasons for your views.

Question 28.5 : With regard to Proposal 28e, do you agree with the exception to the disclosure required? Please provide specific reasons for your views.

Question 28.6 : Do you agree for Proposal 28 to apply to ETF and PRS? Please provide specific reasons for your views.

Public comments

5.1.2 Generally, the respondents agreed with all the proposals, save for proposals 28a (requirement to disclose detailed information on derivative investments) and 28d (disclosures on related party transactions) where for each proposal, two respondents had disagreed with the proposal.

5.1.3 For proposal 28a, the responses received are as follows:

- (a) One respondent disagreed on the basis that information on the underlying asset of the derivative is a proprietary information; and
- (b) Concerns relating to increased cost to operate as major system enhancement will be needed to meet the disclosure requirements.

- 5.1.4 For proposal 28d, the reasons for the disagreement was the issue with obtaining the relevant internal confirmation in time for the issuance of fund reports, and the said proposal is pertaining to the UTMC, which is out of scope of the fund reports.
- 5.1.5 Respondents that agreed with the proposals have also provided the following constructive feedback:
- (a) On disclosure item in proposal 28a, -
 - (i) specifically *"The lowest, highest and average exposure arising from the use of derivative ..."*, one respondent expressed reservations on whether investors would find this additional standalone disclosure useful as it should be viewed together with the underlying holdings from a comprehensive perspective. Further, it will be onerous in terms of monitoring and tracking by the UTMC too; and
 - (ii) another respondent suggested that the information should only be required when it is not done for hedging purposes.
 - (b) On proposal 28e (additional disclosures for feeder funds), key feedback were as follows:
 - (i) The feeder fund and the target fund have different reporting period. As such, UTMC should be allowed to use the information on the target fund as set out in the target fund's latest available fund report;
 - (ii) Although the information on the target fund's top 10 holdings should be readily available, in any case that the information is not available then the guideline needs to be flexible to allow non-disclosure of the information, subject to a reasonable justification; and
 - (iii) The issue is when the information is extracted and published in the annual report. The target fund manager will not provide the latest holdings, as there are concern that the feeder fund manager may replicate the same. There is normally a 1 to 3 months lead time in the data provided by the target fund manager.

The SC's response

- 5.1.6 In relation to proposal 28a, the SC sees the merit in the responses received and as such, the requirement to disclose detailed information on derivative

investments will only apply to funds that had invested in derivatives (i.e. not for hedging purposes) during the period under review.

- 5.1.7 In addition to the above, the SC will not be implementing the requirement in item (d) under “Information on exposure arising from derivatives”. Instead, the UTMC will only be required to disclose details on the global exposure arising from derivatives for the period under review (e.g. the method of calculating the global exposure as well as the fund’s global exposure at the reporting date).
- 5.1.8 In relation to proposal 28d, the SC agrees with the response and will not be implementing proposal 28d, specifically the introduction of new disclosure requirements. Notwithstanding this, the removal of existing requirements mentioned in this proposal will be effected because any disclosure relating to related party transactions must comply with *Malaysian Financial Reporting Standard 124: Related Party Disclosures*.
- 5.1.9 In relation to proposal 28e, the SC will proceed to implement the proposal. With regards to the concern highlighted we wish to reiterate that the disclosure is only required if the information on the top 10 holdings by the target fund is available. Where such information is available, the SC acknowledges that the date of the information may not be the same as the reporting date of the feeder fund. For transparency, the UTMC should disclose the date of the information.

5.2 **INFORMATION ON FUNDS ON A UTMC’S WEBSITE**

PROPOSAL 29

- 5.2.1 Respondents were asked to give their comments on the following questions:

Question 29.1 : Do you agree with the proposal for UTMC to make available to the public the following information (offering document including product highlights sheet; circulars, notices, and announcements; fund reports; latest available NAV of funds; and distributions declared) without charge or requiring a person to be registered with the UTMC? Please provide specific reasons for your views.

Question 29.2 : With regard to announcement of distribution by a fund, do you agree with the proposal to also publish the composition of income and capital to be distributed in percentage terms? Please provide specific reasons for your views.

Question 29.3 : Do you agree for Proposal 29 to apply to ETF and PRS?
Please provide specific reasons for your views.

Public comments

- 5.2.2 All respondents agreed with the proposal citing that it serves as a “one-stop centre” and information to be provided are basic and relevant information that an investor would require to make appropriate assessment of a fund and some of the respondents added that they are currently doing so. In addition, one respondent suggests that similar expectations be imposed on IUTAs. Two respondents suggest SC to clarify when should the information be made available and that the information published should be on the latest position of a fund report and distribution information available. Two respondents propose the SC to consider the need to apply for approval from the SC to publish information such as the prospectus on the UTMC’s website.
- 5.2.3 One respondent disagreed to the requirement to publish fund reports on the website citing the publication of fund reports on the UTMC’s website will allow the public and competitor UTMCs to have full access to the funds' entire portfolio holdings which was deemed to be highly confidential, as the reason. The respondent suggests that only the selected pages of the annual reports that are similar to that of interim reports are published. The annual reports of funds (with the funds' entire portfolio holdings) should only be made available to existing unit holders via existing channels.

The SC’s response

- 5.2.4 We take note on the feedback to impose similar requirements on IUTAs. In this regard, CUTAs should also be considered for consistency in policy. We will engage FIMM in due course to look into the suggestion. Meanwhile, with the implementation of the proposal, investors will at least be able to access to the information through the respective UTMC’s website.
- 5.2.5 We would like to clarify that UTMCs should make available the required information on its website as soon as practicable. The SC expects the information published to be the latest information that is available.
- 5.2.6 We do not share the same view on the reason why publication of fund reports should not be made. In addition, publication of fund reports that contains the fund’s entire portfolio holdings is being practised by UTMCs in major CIS jurisdictions around the world. Also, the portfolio holdings in the report is a snapshot of the fund’s position which will be two-months old when it is published. Further, from a competitor’s perspective, it is not difficult to gain access to such reports i.e. becoming a unit holder.

5.2.7 After considering the feedback from the respondents, the SC will also exempt UTMCs from having to apply for SC's approval under Parts 1 & 3 of the *Guidelines on Online Transactions and Activities in relation to Unit Trusts* (Online Guidelines). However, such UTMCs are required to submit a notification to the SC, which is to be accompanied by the following:

- (a) Relevant declarations; and
- (b) Checklist on compliance with the Online Guidelines.

For avoidance of doubt, existing UTMCs that have obtained the relevant approvals under the Online Guidelines are not required to submit the notification to the SC but these UTMCs are expected to comply with the Online Guidelines at all times.

5.3 **REQUIREMENT TO DISCLOSE A PERFORMANCE BENCHMARK**

PROPOSAL 30

5.3.1 Respondents were asked to give their comments on the following questions:

- Question 30.1 : Should disclosure of a unit trust fund's performance benchmark in its prospectus be made optional? Please provide specific reasons for your views.
- Question 30.2 : Do you have the same opinion for PRS? Please provide specific reasons for your views.

Public comments

5.3.2 Majority of those that responded opined that such disclosure should be optional, based on the reasons summarised as follows:

- (a) Not every fund is managed to be similar to a benchmark and such performance comparison may not be fair. Some funds are benchmark unconstrained;
- (b) Performance of the fund can be measured against its peers, deposit rates or target return objectives; and
- (c) The benchmark itself could have issues on appropriateness and by itself does not safeguard investors' interest.

These respondents agreed that benchmark should only be required when a fund's principle objective is to track or replicate, or outperform an index.

5.3.3 On the other hand, a few respondents are of the view that disclosure of a benchmark should be mandatory, citing the following reasons:

- (a) It is beneficial for the investors to have a basis to compare.
- (b) Good to have performance benchmark, which is reflective of the fund's investment objective. Allows investors to assess whether the fund is performing well or not, relative to the benchmark and also competitor funds. For better investor decision making.
- (c) Benchmark should be used to make comparison with the fund. Without benchmark, there is no comparison to be made which may lead to misinterpretation by the investors.
- (d) It is very important for investors especially for those who is a first timer investor to analyse the performance of each fund.
- (e) Performance benchmark is one of the key indicator and fundamental information that investor must be made aware of upfront via offering document and arrive at an informed decision to gauge on the expected return.

The SC's response

5.3.4 The SC has considered the feedback provided and share the view that benchmark must be disclosed if the fund's objective is to track or outperform an index. In this regard, it forms an appropriate basis to compare. However, mandating the disclosure of a benchmark that results in comparing the performance of a fund with a benchmark that is not reflective of the investment objective or strategy of the fund is not appropriate and may mislead investors. Furthermore, a benchmark or its past performance should not be used as an indicator to gauge future returns of a fund.

5.3.5 As such, the SC agrees that disclosure of a benchmark should be made optional save for a fund where its objective is to track or outperform an index. In addition, to assist investors to make an informed decisions, where a fund has no benchmark, disclosure must include an explanation on why the fund has no benchmark. In the event there is a change in benchmark or the benchmark is being removed, disclosure must include an explanation on why the change or the removal, as the case may be.

GLOSSARY OF TERMS

CIS	collective investment scheme
CIS Prospectus Guidelines	<i>Prospectus Guidelines for Collective Investment Schemes</i>
CUTA	corporate adviser registered with FIMM
EPM	<p>efficient portfolio management. A transaction is deemed to be for the purpose of EPM if it meets the following criteria:</p> <p>(a) It is economically appropriate in that it is realised in a cost-effective way;</p> <p>(b) It is entered into for one or more of the following specific aims:</p> <ul style="list-style-type: none"> (i) reduction of risk; (ii) reduction of cost; or (iii) generation of additional capital or income for the fund with a level of risk which is consistent with the risk profile of the fund and the risk diversification of requirements as prescribed in the Unit Trust Guidelines; <p>(c) The exposure is fully covered to meet any obligation to pay or deliver; and</p> <p>(d) The risks are adequately captured by the risk management process of the fund.</p>
ETF	exchange-traded fund
FIMM	Federation of Investment Managers Malaysia
FM Guidelines	<i>Guidelines on Compliance Function for Fund Management Companies</i>
financial derivative/derivative	financial derivative
fund	unit trust fund
Govvie	a government, government agency, or supranational
IOSCO	International Organization of Securities Commissions
IUTA	institutional adviser registered with FIMM

MMF	money market fund
NAV	net asset value
OTC	over-the-counter
PRS	private retirement scheme
REIT	real estate investment trust or property fund
RMP	risk management policy and procedures
Unit Trust Guidelines	<i>Guidelines on Unit Trust Funds</i>
UTMC	unit trust management company
Variable Price Fund	unit trust fund in which the price of a unit is the NAV per unit of the fund