



PUBLIC CONSULTATION PAPER

No. 1/2020

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) invites your written comments in this public consultation paper. Comments are due by **10 January 2021** and will only be received when submitted at this link [[Feedback to SC](#)].

Additional copies of this document may be made without seeking permission from the SC or downloaded from its website at www.sc.com.my.

Confidentiality: Your responses may be made public by the SC. If you do not wish for your name to be made public, please state this clearly in the response. Any confidentiality disclaimer that may be generated by your organisation's IT system or included as a general statement in your fax cover sheet will be taken to apply only if you request that the information remain confidential.

The SC agrees to keep your personal data confidential and in full compliance with the applicable principles as laid under the *Personal Data Protection Act 2010*.

This Public Consultation Paper is dated 11 November 2020

CONTENTS

1	INTRODUCTION	4
2	PROPOSALS RELATING TO THE INVESTMENT UNIVERSE OF A FUND	6
2.1	Overview.....	6
2.2	Transferable Securities and Money Market Instruments.....	6
2.3	Investment in CIS.....	9
2.4	Derivatives and Structured Products	11
2.5	Securities Lending, Repurchase and Reverse Repurchase Transaction	17
2.6	Single Issuer Limit for Investment in Government and Public Transferable Securities or Money Market Instruments	20
2.7	Exception to the Single Financial Institution Limit for Placement in Deposits.....	22
2.8	Exception to the Concentration Limit for Debt Securities.....	23
2.9	Investment Spread Limit for Investment in a Listed REIT (i.e. listed REIT under Category C of Proposal 3).....	23
2.10	Allowing Investments in Other Type of Securities.....	24
2.11	Investments of a Feeder Fund	25
2.12	Investments of a MMF.....	26
3	PROPOSALS RELATING TO A UTMC	31
3.1	Risk Management Framework Documentation	31
3.2	Holding of a Fund's Units by the UTMC	33
3.3	Oversight Arrangement to Replace Investment Committee	34
3.4	Training Requirements	35
4	PROPOSALS RELATING TO DEALING, VALUATION AND OPERATIONAL MATTERS.....	37
4.1	Dealing in Units	37
4.2	Revision to the Redemption Payment Period.....	39
4.3	Basis of Valuation of a Fund's Assets and Incorrect Pricing	40
4.4	Requirements in Relation to Cooling-off Right.....	43
4.5	Enabling a Fund to Pay Distribution out of Capital.....	44
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	46
4.7	Enhancement to Requirements relating to Soft Commissions	47
4.8	Requirements relating to Termination of a Fund	48

4.9	Requirements on Quorum for Unit Holders’ Meeting	50
5	OTHER PROPOSED AMENDMENTS	52
5.1	Contents of Annual and Interim Reports (“Fund Reports”)	52
5.2	Information on Funds on a UTMC’s Website	56
5.3	Requirement to Disclose a Performance Benchmark	58
	GLOSSARY OF TERMS	59

1 INTRODUCTION

- 1.1 A unit trust fund allows investors with similar investment objective to pool their monies in a scheme managed by a unit trust management company (UTMC). Unit trust funds are authorised by the SC under section 212(5) of the *Capital Markets and Services Act 2007* (CMSA). The *Guidelines on Unit Trust Funds* (Unit Trust Guidelines) issued pursuant to section 377 of the CMSA aims to provide a regulatory environment that would protect the interests of the investing public and facilitate the orderly development of the unit trust fund industry in Malaysia.
- 1.2 Unit trust funds continue to be the largest component of the Malaysian CIS industry. As at 30 September 2020, there were 39 locally-incorporated management companies approved to offer 693 unit trust funds with a total net asset value (NAV) of RM490.3 billion. Of these, 239 are Islamic funds and 454 are conventional funds.
- 1.3 To further facilitate the development of the unit trust fund industry, the SC is currently undertaking a comprehensive review of the Unit Trust Guidelines. In undertaking this review, the SC has taken into consideration the evolving needs of investors as well as developments and regulatory requirements in the major CIS jurisdictions, including standards issued by IOSCO in areas such as liquidity risk management, money market funds and valuations. In addition, the SC has had discussions with various stakeholders and where appropriate, incorporated their views in developing the proposals in this Public Consultation Paper.
- 1.4 The SC remains committed to a proportionate and facilitative regulatory approach that fosters innovation and competitiveness within a sensible and proactive oversight regime. Towards this end, the proposals under this Public Consultation Paper seeks to ensure that investors protection is not compromised by considering the following:
- (a) New asset classes and activities will be allowed for unit trust funds provided a UTMC ensures that it is equipped with the appropriate systems, capabilities and expertise to manage the risks associated with such asset classes and activities;
 - (b) Prescriptive requirements that are no longer effective in the current environment will be replaced with principles that are supplemented with guidance, where appropriate. This will allow UTMCs greater flexibility in managing the funds in the best interest of the investors; and
 - (c) Greater focus on the risk management process of unit trust funds, as well as the roles and responsibilities of the UTMC and trustee in managing conflict of interest that may exist.

- 1.5 To promote competitiveness both locally and internationally, liberalisations of existing requirements will need to be balanced with appropriate reinforcement to ensure the unit trust industry remains resilient under stressed market conditions, to ensure investor protection is not compromised. Towards this end, lessons from the past global financial crisis that hit the developed economies as well as the measures taken by these economies have formed part of the policy considerations. Where appropriate, transitional provisions to enable full compliance with any new measures will be provided.
- 1.6 The SC is of the view that regular communications between UTMCs and investors is key to investor education and empowerment, ultimately allowing investors to make more informed decisions. Against this backdrop, some of the proposals that deal with practical issues faced by UTMCs should be effected by the UTMC through effective communications with investors to promote good investment experience. Other proposals will be introduced through appropriate disclosure requirements.
- 1.7 Proposals that are relevant and appropriate for exchange-traded funds (ETF) and private retirement schemes (PRS) will be adopted to ensure consistency in policy with unit trust funds.
- 1.8 This Public Consultation Paper seeks feedback on the proposals which will be effected by way of amendments to the following guidelines:
 - (a) Unit Trust Guidelines;
 - (b) ETF Guidelines;
 - (c) PRS Guidelines; and
 - (d) CIS Prospectus Guidelines.

2 **PROPOSALS RELATING TO THE INVESTMENT UNIVERSE OF A FUND**

2.1 **OVERVIEW**

2.1.1 Presently, a fund may invest in the following instruments:

- (a) Transferable securities;
- (b) Money market instruments;
- (c) Units or shares in CIS;
- (d) Deposits with financial institutions;
- (e) Derivatives; and
- (f) Structured products.

2.1.2 We are proposing some changes to the definitions and criteria of the instruments a fund may invest in, to provide funds with greater flexibilities and certainty, particularly when different legal forms are introduced or become available. The proposed approach would be more principle based.

2.2 **TRANSFERABLE SECURITIES AND MONEY MARKET INSTRUMENTS**

2.2.1 Transferable securities are currently defined as equities, debentures and warrants, and based on market practice, includes equity-related securities other than warrants (e.g. participatory notes and depositary receipts).

2.2.2 Transferable securities and money market instruments held by a fund must be traded in or under the rules of an eligible market. Under the Unit Trust Guidelines, an eligible market refers to a market that–

- (a) is regulated by a regulatory authority;
- (b) operates regularly;
- (c) is open to the public; and
- (d) has adequate liquidity for the purposes of the fund in question.

- 2.2.3 Where the transferable securities are not traded in or under the rules of an eligible market, these would be considered unlisted securities¹ and would be subject to an investment limit of 10% of the fund's NAV.
- 2.2.4 For investments in a foreign market, a foreign market is an eligible market where it has satisfactory requirements relating to–
- (a) the regulation of the foreign market;
 - (b) the general carrying on of business in the market with due regard to the interests of the public;
 - (c) corporate governance;
 - (d) disciplining of participants for conduct inconsistent with just and equitable principles in the transaction of business, or for a contravention of, or a failure to comply with the rules of the market; and
 - (e) arrangements for the unimpeded transmission of income and capital from the foreign market².

In addition, the Unit Trust Guidelines limits a fund's investments in foreign markets to markets where the regulatory authority is an ordinary or associate member of the IOSCO³.

- 2.2.5 We **propose to define transferable securities** to mean–

- (a) shares or securities equivalent to shares;
- (b) bonds or other forms of securitised debt; and
- (c) sukuk,

but do not include money market instruments or any security the title to which can be transferred only with the consent of a third party.

"Securities equivalent to shares" would include units or shares in business trusts, depositary receipts, participatory notes, rights and warrants that can be converted into new shares.

Proposal

1

¹ Equities that are not listed and quoted on a stock exchange but have been approved by the relevant regulatory authority for such listing and quotation, and are offered directly to the fund by the issuer, is considered transferable securities.

² Paragraph 8.07 of the Unit Trust Guidelines

³ Paragraph 8.08 of the Unit Trust Guidelines

Transferable securities must also meet the following criteria:

- (a) The maximum potential loss which the fund may incur as a result of the investment is limited to the amount paid for it;
- (b) The investment is liquid⁴, and will not impair the fund's ability to satisfy its redemption and other payment commitments;
- (c) The investment is subject to reliable and verifiable valuation on a daily basis; and
- (d) There is appropriate information available to the market on the investment.

2.2.6 We believe Proposal 1 provides greater flexibility in terms of the investments of a fund as it allows the transferable securities to be in different legal form but at the same time confined to those that meet the prescribed criteria.

2.2.7 We further **propose to define "eligible market"** to mean an exchange, government securities market or an over-the-counter ("OTC") market–

Proposal
2

- (a) that is regulated by a regulatory authority of that jurisdiction;
- (b) that is open to the public or a substantial number of market participants; and
- (c) on which financial instruments are regularly traded.

The above would apply whether the market is within or outside Malaysia.

2.2.8 We consider the approach taken to defining a market, regardless of whether it is local or foreign, will provide transparency and clarity.

2.2.9 The proposals are in line with requirements in major CIS jurisdictions.

2.2.10 For clarity, the following would be considered transferable securities:

- (a) Equities not listed and quoted on a stock exchange but have been approved by the relevant regulatory authority for such listing and quotation, and are offered directly to the fund by the issuer; and
- (b) Debentures traded on an eligible market.

⁴ Liquid means the ability of a financial instruments to be readily converted into cash at a value close to its fair price under normal market conditions.

Issues for Consultation

Proposal 1

- 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.

Proposal 2

- 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.

2.3 INVESTMENT IN CIS

2.3.1 At present, a fund is permitted to invest in other CIS subject to the following requirements:

- (a) The CIS is regulated by a regulatory authority;
- (b) If the CIS is constituted in Malaysia, the CIS must be authorised or approved by, or lodged with the SC;
- (c) If the CIS is constituted outside Malaysia, the CIS must be registered, authorised or approved by the relevant regulatory authority in its home jurisdiction; and
- (d) Where the CIS is a CIS other than a real estate investment trust or property fund; a gold ETF; or a leveraged or an inverse ETF, the CIS must operate on prudent spread of risk and its investment must not diverge from the general investment principles of the Unit Trust Guidelines.

2.3.2 We **propose 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 who 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 (see paragraph 2.2.5);
 - (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. This would be subject to the investment limits discussed in section 2.10 of this paper.

2.3.3 Retail investors are demanding access to a wider range of products to match their varying profile, risk profile and return expectation.⁵ There is a growing demand for more international options from regional fund registration blocks to be allowed to be distributed locally.⁶ Category (B) intends to provide clarity that target funds, particularly those offered through feeder funds, are not expected to match the Unit Trust Guidelines clause by clause, but must (i) be subject to regulations on diversification of permissible investments, (ii) not use leverage for investments and (iii) undertake securities financing for efficient portfolio management purposes only. Meanwhile, categories (C) and (D) would further widen the types of CIS a UTMC can invest in to cater to investors' growing demands.

Issues for Consultation – Proposal 3

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.

2.4 DERIVATIVES AND STRUCTURED PRODUCTS

2.4.1 We **propose to replace "derivatives" with "financial derivative instruments"** in the list of a fund's permissible investments. In addition, we **propose to delete the specific reference to "structured products"**.

Proposal
4

2.4.2 Notwithstanding the deletion of "structured products", a structured product remains as a permissible investment under the proposals as depending on its features, it may be considered a transferable security (see Proposal 1) or an embedded derivative (see Proposal 5e).

⁵ Institute for Capital Market Research, 'The Evolving Business of Asset Management Malaysia's Perspective', June 2019, p.54

⁶ Institute for Capital Market Research, 'The Evolving Business of Asset Management Malaysia's Perspective', June 2019, p.54

2.4.3 Presently, a fund may invest in derivatives that are traded on an exchange or over-the-counter (OTC), subject to the fund's exposure from the derivative position not exceeding the fund's NAV at all times.

2.4.4 While we note that the majority of existing unit trust funds are using derivatives for hedging purposes, we note that there may be increased interest in employing derivatives for investments as management companies seek to provide such funds to meet investor demands. In anticipation of this, and to ensure that the regulatory framework is comparable with major CIS jurisdictions, we **propose the following requirements for financial derivative instruments** (financial derivatives or derivatives):

*Proposal
5*

(a) Underlying of a financial derivative

*Proposal
5a*

While a fund is not permitted to invest in physical commodity, we propose **to allow exposure to commodity through financial derivatives**. However, when the underlying of a derivative consist of commodities, we **propose that the derivative transaction must be settled in cash at all times**. The trust deed and prospectus of the fund must contain the relevant enabling provisions.

(b) Criteria for investment in financial derivative

*Proposal
5b*

We propose the following enhancements to manage liquidity risk, ensure diversification requirements are met and ensure fair valuation:

- (i) The financial derivative must be liquid and will not impair the fund's ability to satisfy its redemption and other payment commitments;
- (ii) The exposure to the underlying assets of the financial derivative must not exceed the investment restrictions or limitations applicable to such underlying assets and investments as set out in Schedule B of the Unit Trust Guidelines;
- (iii) The financial derivative is subject to reliable and verifiable valuation on a daily basis; and
- (iv) The financial derivative can be sold, liquidated or closed by an offsetting transaction at any time at their fair value.

Accordingly, paragraph 8.19(d) of the Unit Trust Guidelines⁷ will be removed.

(c) Revision to the requirement on the counterparty of the OTC financial derivatives

*Proposal
5c*

With the proposal to introduce numerous enhanced safeguards and to level the playing field for local funds, we propose to revise the requirement on the rating of the financial institution, which is the counterparty of an OTC financial derivative, to “investment grade”.

(d) Method to calculate financial derivative exposure

*Proposal
5d*

Presently, a fund’s exposure from financial derivatives position must not exceed the fund’s NAV at all times.

Global exposure is a measure of the incremental exposure and leverage generated by a fund through the use of financial derivatives. The Unit Trust Guidelines currently do not specify a method for calculating derivatives exposure.

We have considered the different approaches to calculating a fund’s global exposure limits, particularly the commitment approach, the value at risk (VaR) approach and advanced risk measurement methodology. As the VaR approach and advanced risk measurement methodology are generally used when the fund employs complex investment strategies, we believe the commitment approach is a more balanced measurement methodology of a fund’s global exposure to financial derivatives.

In light of this, we propose to prescribe the following in relation to the method of calculation of derivatives exposure:

Commitment approach

1. The fund’s global exposure to derivatives, calculated based on the commitment approach must not exceed 100% of the fund’s NAV.
2. The global exposure of a fund is calculated as the sum of the –
 - (a) absolute value of the exposure of each individual derivative not involved in netting or hedging arrangements; and

⁷ Requirement that for OTC traded derivatives, a transaction may only be entered into where the counterparty must be ready to unwind, buy-back or close out the transaction upon request of the fund manager at a fair value determined on methods or bases which have been verified by the auditor of the fund and approved by the trustee.

- (b) absolute value of the net exposure of each individual derivative after netting or hedging arrangements.

Netting arrangements

- 3. Netting arrangements may be taken into account to reduce a fund's exposure to derivatives.
- 4. A fund may net positions between –
 - (a) derivatives on the same underlying constituents, even if the maturity dates are different; or
 - (b) derivatives and the same corresponding underlying constituents, if those underlying constituents are transferable securities, money market instruments or units/shares in other collective investment schemes.

Hedging arrangements

- 5. Hedging arrangements may be taken into account to reduce a fund's exposure to derivatives.
- 6. The marked-to-market value of transferable securities, money market instruments or units/shares in collective investment schemes involved in hedging arrangements may be taken into account to reduce the exposure of a fund to derivatives.
- 7. The hedging arrangement must –
 - (a) not be aimed at generating a return;
 - (b) result in an overall verifiable reduction of the risk of the fund;
 - (c) offset the general and specific risks linked to the underlying constituent being hedged;
 - (d) relate to the same asset class being hedged; and
 - (e) be able to meet its hedging objective in all market conditions.

(e) Embedded derivatives

For avoidance of doubt, transferable securities and money market instruments with embedded derivatives must be included in the calculation of derivatives exposure. We propose to clarify in the Unit Trust Guidelines that a transferable security or money market instrument is considered to be embedding a financial derivative if it contains a component that fulfils the following criteria:

*Proposal
5e*

1. The component results in some or all of the cash flows that otherwise would be required by the transferable security or money market instrument which functions as host contract to be modified according to a variable including but not limited to a specified interest rate, price of a financial instrument, foreign exchange rate, index of prices or rates, credit rating or credit index, and therefore vary in a way similar to a stand-alone derivative;
2. The component's economic characteristics and risks are not closely related to the economic characteristics and risks of the host contract; and
3. The component has a significant impact on the risk profile and pricing of the transferable security or money market instrument.

A transferable security or a money market instrument shall not be regarded as embedding a financial derivative where it contains a component which is contractually transferable independently of the transferable security or the money market instrument. Such a component shall be deemed to be a separate financial instrument.

Further, where an instrument is structured as an alternative to an OTC financial derivative or tailor-made to meet the specific needs of a CIS, the instrument should be deemed as embedding a financial derivative.

A structured product would be considered an embedded derivative.

In line with international standards, it is also proposed that all requirements including the limits and restrictions applicable to investment in financial derivatives be applicable to embedded derivatives.

(f) Calculation of exposure to counterparty of OTC financial derivatives

Proposal

5f

In calculating the exposure to counterparty of an OTC derivative, we propose to specify the following:

1. A fund's exposure to a counterparty of an OTC financial derivative be measured based on the maximum potential loss that may be incurred by the unit trust fund if the counterparty defaults and not on the basis of the notional value of the OTC financial derivative.
2. Further, the total exposure to a single counterparty is calculated by summing the exposure arising from all OTC financial derivative transactions entered into with the same counterparty.

3. The exposure to the counterparty of an OTC financial derivative may be lowered if the fund receive collateral, provided that the collateral meet the proposed requirements under Proposal 6 below.

(g) Unlimited liability

*Proposal
5g*

We further propose that a fund may not acquire any asset or engage in any transaction which involves the assumption of any liability which is unlimited. Consequently, paragraphs 8.21⁸ and 8.22⁹ of the Unit Trust Guidelines will be removed, accordingly.

Issues for Consultation	
<i>Proposal 4</i>	
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.
<i>Proposal 5</i>	
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.

⁸ 8.21 The writing of option derivatives and short position of futures contracts by the fund are strictly prohibited.

⁹ 8.22 Notwithstanding paragraph 8.21, short position of futures contract for hedging purposes is allowed.

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.

2.5 SECURITIES LENDING, REPURCHASE AND REVERSE REPURCHASE TRANSACTION

2.5.1 Presently, the Unit Trust Guidelines permits a fund to participate in securities lending activity but only confined to lending of securities within the meaning of the *Securities Borrowing and Lending Guidelines*. This means that the pool of securities which a fund may lend is limited to securities under the *SBL Eligible Securities* as provided by Bursa Malaysia and published on its website.

2.5.2 Globally, there has been an increasing trend where CIS are entering into securities lending as well as repurchase and reverse repurchase transactions (collectively referred to herein as "repurchase transactions") to enhance return.

2.5.3 To ensure that the Unit Trust Guidelines is able to cater for the present needs of the industry, we propose to liberalise our requirements **to allow unit trust funds to lend foreign securities and participate in repurchase transactions**, provided that the participation in these transactions will be in the best interest of the fund and its unit holders. Details of the proposals are as follows:

*Proposal
6a*

- (a) A fund is permitted to undertake securities lending and repurchase transactions for the sole purpose of efficient portfolio management (EPM).
- (b) For the purpose of securities lending, a fund may lend its transferable securities either–
 - (i) directly;

- (ii) through a standardised lending system facilitated by a clearing house which performs a central counterparty role; or
 - (iii) through securities lending agents, who are recognised as specialists in securities lending.
- (c) Securities lending and repurchase transactions should be effected in accordance with good market practice.
- (d) The counterparty to the securities lending and repurchase transactions is a financial institution that has a minimum top three long-term rating provided by any domestic or global rating agency. Where the counterparty to the transaction is a party related to the UTMC or the fund manager of the fund, adequate arrangements must be in place to manage potential conflicts of interest.
- (e) The agreement between the fund and the counterparty, either directly or through its agent, should require the counterparty to provide additional collateral to the fund or its agent no later than the close of the next business day if the current value of the eligible collateral tendered is insufficient.
- (f) The collateral provided to the fund may only consist of cash, debt securities and other forms of securitised debt instruments, or money market instruments that comply with the following requirements:
 - (i) **Liquidity:** The collateral must be sufficiently liquid and tradable in order that it can be sold quickly at a robust price that is close to pre-sale valuation. Collateral should normally trade in a deep and liquid marketplace with transparent pricing;
 - (ii) **Valuation:** The collateral must be marked-to-market daily by using independent pricing source;
 - (iii) **Issuer credit quality:** The collateral must be of high credit quality and should be replaced immediately as soon as the credit quality of the collateral or the issuer of the asset being used as collateral has deteriorated to such a degree that it would undermine the effectiveness of the collateral;
 - (iv) **Haircut:** The collateral should be subject to prudent haircut policy;
 - (v) **Diversification:** The collateral must be appropriately diversified so as to avoid concentrated exposure to any single entity and/or entities within the same group. The fund's exposure to the

issuer(s) of the collateral should be taken into account in compliance with investment restrictions and limits prescribed under Schedule B of the Unit Trust Guidelines;

- (vi) **Correlation:** The value of the collateral must not have any significant correlation with the creditworthiness of the counterparty in such a way that would undermine the effectiveness of the collateral. As such, securities issued by the counterparty or any of its related entities must not be used as collateral;
 - (vii) **Management of operational and legal risks:** The UTMC and/or fund manager of the fund must have appropriate systems, operational capabilities and legal expertise for proper collateral management;
 - (viii) **Independent custodian:** The collateral must be held by the trustee of the fund;
 - (ix) **Enforceability:** The collateral must be readily accessible/enforceable by the trustee of the fund without further recourse to the issuer of the derivatives, or the counterparty of the securities lending and repurchase transactions;
 - (x) **Reinvestment of collateral:** Cash collateral received may only be reinvested in short-term deposits, high quality money market instruments, and subject to corresponding investment restrictions or limitations applicable to such investments as set out in Schedule B of the Unit Trust Guidelines. Non-cash collateral received may not be sold, reinvested or pledged; and
 - (xi) Debt securities and other forms of securitised debt instruments as well as money market instruments with embedded derivatives are not eligible as collateral.
- (g) Information on the collateral policy must be disclosed in the fund's prospectus.
 - (h) The description of collateral holdings must be disclosed in the interim and annual reports of the fund (see Proposal 28).
 - (i) The fund manager must ensure that the volume of securities lending or repurchase transactions is kept at an appropriate level.

- (j) The fund manager must ensure at least 100% collateralisation in respect of the securities lending and repurchase transaction(s) into which it enters and ensure there is no uncollateralised counterparty risk exposure arising from these transaction(s).

2.5.4 We are also proposing to require **all revenues arising 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, be returned to the fund**, the rationale being that the assets which are the subject of the transactions belong to the fund and the purpose for undertaking such transactions is for the benefit of the fund.

*Proposal
6b*

Issues for Consultation – Proposal 6

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) above? 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.

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

2.6.1 Presently, the investment spread and concentration limits do not apply to securities or instruments issued or guaranteed by the Malaysian government or Bank Negara Malaysia.

2.6.2 The SC notes that in most other major fund jurisdictions, higher limits are generally allowed for securities issued or guaranteed by governments:

- (a) Hong Kong: Up to 30% of a CIS' NAV may be invested in government and other public securities of the same issue¹⁰;
- (b) UCITS: Up to 35% of a CIS' NAV in transferable securities or money market instruments that are issued or guaranteed by a member state, by its local authorities, by a third country or by public international bodies of which one or more member states are members^{11,12}; and
- (c) Singapore: Up to 35% of a CIS' NAV in a single entity, provided that the issuing entity or trust is, or the issue is guaranteed by, either a government, government agency or supranational, that has a minimum long-term rating of BBB by Fitch, Baa by Moody's or BBB by Standard and Poor's (including such sub-categories or gradations therein)¹³.

2.6.3 To provide Malaysian funds with more flexibility, and recognising the lower risks posed by such issuers, we are **proposing that** where a transferable security or money market instrument is issued by, or the issue is guaranteed by, either a government, government agency, central bank or supranational, that has a minimum long-term rating of investment grade by an international rating agency ("Govvies") -

Proposal
7

- (a) The 15% single issuer limit may be raised to 35% of the fund's NAV;
- (b) The 25% aggregate value of a fund's investment with any single issuer may be raised to 35% of the fund's NAV;
- (c) The 20% Group limit may be raised to 35% of the fund's NAV; and
- (d) Accordingly, the relevant limits applicable to a bond/fixed income fund or a money market fund may be raised to 35% of the fund's NAV.

2.6.4 For avoidance of doubt, there will be no change to securities or instruments issued or guaranteed by the Malaysian government or Bank Negara Malaysia, i.e. the investment spread and concentration limits do not apply.

¹⁰ Paragraph 7.4 of SFC's *Code on Unit Trusts and Mutual Funds*

¹¹ Regulation 70(4) of CBI's *European Communities (Undertakings for Collective Investment in Transferable Securities) Regulations 2011*

¹² Article 43(3) of CSSF's *Law of 17 December 2010 relating to undertakings for collective investment*

¹³ Paragraph 2.5 of MAS' *Code on Collective Investment Schemes*

Issues for Consultation – Proposal 7

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.

2.7 EXCEPTION TO THE SINGLE FINANCIAL INSTITUTION LIMIT FOR PLACEMENT IN DEPOSITS

2.7.1 Presently, the Unit Trust Guidelines provides that the value of a fund's placement in deposits with any single financial institution must not be more than 20% of the fund's NAV.

2.7.2 The SC notes that there may be circumstances where it may not be in the best interest of the fund to comply with the 20% limit and **proposes that the limit does not apply in these circumstances**, i.e. the following:

Proposal
8

- (a) At any point where the fund receives the subscription monies prior to the commencement of investment by the fund;
- (b) During liquidation of investments prior to the termination or maturity of the fund, where the placement of deposits with various financial institutions would not be in the best interests of unit holders; or
- (c) Monies held for the settlement of redemption or other payment obligations, where the placement of deposits with various financial institutions would not be in the best interests of unit holders.

Issues for Consultation - Proposal 8

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.

2.8 EXCEPTION TO THE CONCENTRATION LIMIT FOR DEBT SECURITIES

2.8.1 Paragraph 23, Schedule B of the Unit Trust Guidelines states that a fund's investments in debentures must not exceed 20% of the debentures issued by any single issuer. However, we are cognisant that like money market instruments, debt securities too may not have a pre-determined issue size. As such, we are **proposing to introduce the same exception** on the concentration limit in paragraph 24, Schedule B of the Unit Trust Guidelines to paragraph 23, Schedule B of the Unit Trust Guidelines.

Proposal
9

Issues for Consultation - Proposal 9

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.

2.9 INVESTMENT SPREAD LIMIT FOR INVESTMENT IN A LISTED REIT (I.E. LISTED REIT UNDER CATEGORY C OF PROPOSAL 3)

2.9.1 For the purpose of investment limits, a REIT is currently categorised as a CIS. In terms of characteristic, the risks of an investment in an equity REIT is closer to an investment in shares than investments in a mutual fund, and hence it would be more appropriate to apply the transferable security limit instead of a CIS limit. As such, we **propose to apply the 15% Single Issuer Limit** for a fund's investment in a listed REIT.

Proposal
10

Issues for Consultation– Proposal 10

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.

2.10 ALLOWING INVESTMENTS IN OTHER TYPE OF SECURITIES

2.10.1 The Unit Trust Guidelines currently prescribes that investments in unlisted securities must not exceed 10% of the fund’s NAV.

2.10.2 From time to time, there have been requests to allow a fund to invest in securities that do not meet the criteria for transferable securities or CIS such as leveraged and inverse ETFs¹⁴, and digital assets¹⁵.

2.10.3 We note that UCITS is permitted to invest no more that 10% of its NAV in transferable securities or money market instruments other than those listed under the list of permitted investments (commonly referred to as the “trash ratio”).

2.10.4 We **propose to expand “unlisted securities” to “other securities”** to allow a fund to invest in securities that do not meet the requirement applicable to transferable securities or CIS, subject to an aggregate limit of 15% of a fund’s NAV, and subject to a limit of 10% of the fund’s NAV per single issuer.

Proposal
11

2.10.5 For avoidance of doubt, a fund’s investments in CIS under Category D (under Proposal 3), would fall within the investment limit for other securities.

¹⁴ On 13 March 2020, SC informed UTMCs that unit trust funds are allowed to invest in leveraged and inverse ETFs subject to a limit of 10% of the fund’s NAV (in aggregate with other unlisted securities)

¹⁵ The *Capital Markets and Services (Prescription of Securities) (Digital Currency and Digital Token) Order 2019* (“Order”) came into force on 15 January 2019. Pursuant to the Order, all digital currencies and digital tokens that satisfy the requirements in the Order are prescribed as securities for purposes of securities laws (referred to as “digital assets”).

Issues for Consultation - Proposal 11

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.

2.11 INVESTMENTS OF A FEEDER FUND

2.11.1 Paragraph 2, Schedule B – Appendix III of the Unit Trust Guidelines states that a feeder fund’s assets should only consist of units or shares in a single CIS. In practice, a feeder fund will invest in other assets for liquidity purposes. To address the discrepancy, and to be in line with the international standards, **we propose to require a feeder fund to invest at least 85% of its NAV in a single CIS.**

*Proposal
12a*

2.11.2 For clarity, **we further propose** to prescribe that a feeder fund may invest up to 15% of its NAV in one or more of the following permitted investments:

*Proposal
12b*

- (a) Money market instruments dealt in or under the rules of an eligible market, and whose residual maturity does not exceed 12 months;
- (b) Short-term deposits; and
- (c) Derivatives for the sole purpose of hedging arrangement.

Issues for Consultation - Proposal 12

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.

2.12 INVESTMENTS OF A MMF

2.12.1 The Financial Stability Board and IOSCO have undertaken initiatives intended to mitigate MMFs' susceptibility to runs and other systemic risks, following the run on some MMFs globally in 2008. As a result, IOSCO had published the IOSCO's Policy Recommendations for Money Market Funds (IOSCO MMF Recommendations) in October 2012. To date, the recommendations have been implemented by jurisdictions such as Hong Kong, Singapore, the European Union and the United States of America.

2.12.2 We have considered the IOSCO MMF Recommendations and based on the feedback provided by various stakeholders as well as the current market environment in relation to the assets of a MMF, we propose a phased approach to implementing some of the IOSCO MMF Recommendations.

2.12.3 Where appropriate, we propose to issue a document that serves to provide guidance in managing MMFs. We believe this approach would enable a smoother transition in adopting the recommendations for managing MMFs.

2.12.4 At the same time, proposed amendments are made to the requirements on MMFs to provide clarity to the industry.

2.12.5 Under this section, proposals to be incorporated under the guidance will be marked as "MMF Guidance".

Permitted investments of a MMF

2.12.6 Presently, the Unit Trust Guidelines states a MMF is a fund that invests primarily in short-term debentures, short-term money market instruments and placement in short-term deposits, subject to the prescribed exposure limits.

2.12.7 We propose to provide clarity that a **MMF is allowed to invest in the following:**

*Proposal
13a*

- (a) Units or shares of other MMFs; and
- (b) Derivatives for the sole purpose of hedging arrangement¹⁶.

2.12.8 We further **propose to revise the criteria** for the short-term debt securities and short-term money market instruments that a MMF can invest in, and the criteria are summarised as follows:

*Proposal
13b*

- (a) It must meet either one of the following requirements:
 - (i) It has a legal maturity at issuance of 397 calendar days or less;
 - (ii) It has a remaining term to maturity of not more than 397 calendar days; or
 - (iii) Where a debt security or a money market instrument is issued by, or the issue is guaranteed by, either a government, government agency, central bank or supranational, not more than 2 years;
- (b) It must be dealt in on an eligible market; and
- (c) It must not contain an embedded derivative.

Investment limits

2.12.9 We **propose to revise the exposure limits** as follows:

*Proposal
13c*

- (a) A MMF must invest at least 90% of its NAV in–
 - (i) short-term debt securities and short-term money market instruments; and
 - (ii) placement in short-term deposits.
- (b) The value of investments in units or shares of other MMFs and derivatives for hedging purposes must not exceed 10% of the MMF's NAV.

¹⁶ Notwithstanding the list of permitted investments in paragraph (4), Schedule B – Appendix I, a MMF is currently permitted to invest in derivatives, subject to the derivatives complying with the core requirements for non-specialised funds. The UTF Guidelines will be amended to explicitly allow MMF to use derivatives for hedging purpose.

Consequently, paragraph 7 of Schedule B – Appendix I of the Unit Trust Guidelines will be removed¹⁷.

Repurchase transactions

2.12.10 Where a MMF is undertaking repurchase transactions for EPM purposes, we **propose to introduce the following additional requirements:**

*Proposal
13d*

- (a) The amount of cash received by the MMF must not in aggregate exceed 10% of NAV;
- (b) The aggregate amount of cash provided to the same counterparty in reverse repurchase agreements may not exceed 15% of NAV;
- (c) Collateral received may only be cash, high quality money market instruments and may also include, in the case of reverse repurchase transactions, government securities receiving a favourable assessment on credit quality; and
- (d) The holding of collateral, together with other investments of the MMF, must not contravene the proposed requirements of Schedule B – Appendix I of the Unit Trust Guidelines.

MMF Guidance

2.12.11 The IOSCO MMF Recommendations include introducing requirements that restrict the type of assets that are permitted to be held by a MMF, i.e. MMF's assets to comprise mainly of high quality money market instruments and other low-duration fixed income instruments. In addition, as the assessment of credit worthiness lies with the management company, mechanistic reliance on external ratings should be avoided in order to reduce herding and the risk of fire sales.

*Proposal
13e*

MMF Guidance

- (a) When investing in short-term debt securities and short-term money market instruments, a MMF should invests in high quality debt securities and high quality money market instruments.
- (b) In assessing whether a debt security or money market instrument is high quality, the fund manager should satisfy the trustee that the quality of such instrument is equivalent to the following:

¹⁷ The value of a fund's investments in permitted investments which have a remaining maturity period of more than 365 days but fewer than 732 days must not exceed 10% of the fund's NAV

- (i) In the case of short-term credit rating, one (1) of the two (2) highest credit ratings; and
- (ii) In the case of long-term credit rating, one (1) of the three (3) highest credit ratings,
as rated by any domestic or global rating agency.
- (c) Fund manager should assess the credit quality of the instrument based on a prudent internal credit quality assessment practices and avoid any mechanistic reliance on external ratings.

2.12.12 Based on IOSCO MMF Recommendations, in order to limit asset-liability mismatches, limits should be imposed regarding the remaining maturity until the legal redemption date of the instruments held in the portfolios. In addition, limits on the average weighted term to maturity (WAM)¹⁸ and weighted average life (WAL)¹⁹ of the portfolio should also be defined and more conservative MMFs should generally have a WAM of not more than 60 calendar days and WAL of not more than 120 calendar days.

MMF Guidance

- (a) A Standard MMF is a fund where-
 - (i) the non-deposit investments have a remaining term to maturity of not more than two (2) years;
 - (ii) the WAM is not more than 6 months; and
 - (iii) WAL is not more than 12 months

¹⁸ Weighted term to maturity is a measure of the average length of time to maturity of all of the underlying securities in the fund weighted to reflect the relative holdings in each instrument. It is used to measure the sensitivity of a money market fund to changing money market interest rates.

¹⁹ Weighted average life is the weighted average of the remaining life (maturity) of each security held in a fund. It is used to measure the credit risk, as well as the liquidity risk.

- (b) A Short-term MMF is a fund where-
 - (i) the non-deposit investments have a remaining term to maturity of not more than 397 calendar days;
 - (ii) the WAM is not more than 60 calendar days; and
 - (iii) the WAL is not more than 120 calendar days.
- (c) Where the MMF adopts (a) or (b), the fund report should contain additional disclosure on the WAM and WAL of the MMF.

2.12.13 The IOSCO MMF Recommendations also cover liquidity requirements whereby:

- (a) MMFs should establish sound policies and procedures to know their investors;
- (b) MMFs should hold a minimum amount of liquid assets to strengthen their ability to face redemptions and prevent fire sales;
- (c) MMFs should periodically conduct appropriate stress testing; and
- (d) MMFs should have tools in place to deal with exceptional market conditions and substantial redemption pressures.

In this regard, the LRM Guidance Notes (see section 3, paragraph 3.1.2 below) sets out the good practices and recommendations covering item (a), (c) and (d). As for item (b), fund manager can be guided by the following:

MMF Guidance

To strengthen its ability to face redemptions and prevent fire sales, a MMF should invest at least 7.5% of its NAV in daily maturing liquid assets, and at least 15% of its NAV in weekly maturing liquid assets. Accordingly, the fund report should also contain additional disclosure on the amounts of daily liquid assets and as a percentage of the MMF's total net asset value.

Issues for Consultation - Proposal 13

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.

3 PROPOSALS RELATING TO A UTMC

3.1 RISK MANAGEMENT FRAMEWORK DOCUMENTATION

3.1.1 The Unit Trust Guidelines requires a UTMC to establish a risk management process in managing the risks associated with the management and operations of a fund. As such, a UTMC is required to have in place proper risk management and control systems to effectively monitor, measure and manage, on an ongoing basis, all relevant risks in relation to the fund. The said risk management and control systems must commensurate with the nature and scale of the transactions and investment activities that are undertaken for the fund, and be able to deal with normal and exceptional circumstances.

3.1.2 Following the issuance of Recommendations for Liquidity Risk Management for Collective Investment Schemes in 2018 by IOSCO, the SC has issued a *Guidance Notes on Liquidity Risk Management for Fund Management and Unit Trust Management Companies* in 2019 (LRM Guidance Notes). The purpose of the LRM Guidance Notes is to provide guidance on sound liquidity risk management (LRM) practices in managing open-ended funds. As such, a UTMC is expected to take into account the LRM Guidance Notes and enhance its existing LRM process, where appropriate. The extent of the adoption and application of the LRM Guidance Notes lies with the UTMC after having considered the size, scale and complexity of its business models and the profile of the funds managed.

3.1.3 With regard to credit risk, a UTMC will be expected to maintain and implement effective policies and procedures in assessing the credit risk of instruments invested by the fund. Going forward, a UTMC should avoid mechanistic reliance and over-reliance on ratings issued by rating agencies. The use of such ratings

should only be one of the factors to take into consideration in assessing the credit quality of an instrument.

- 3.1.4 If a UTMC undertakes securities lending and repurchase transactions activities, or investment in financial derivatives or digital assets, for a fund, the risk management process for the fund must commensurate with the nature and scale of the transactions and investment activities that are undertaken. In addition, it is the duty and responsibility of a UTMC to ensure there are sufficient human and technical resources and experience to undertake such investment activities.
- 3.1.5 Toward this end, **we propose to require UTMCs to file with the SC, risk management process (RMP) documentation²⁰ for all funds managed by a UTMC**, both existing and new funds, including any subsequent amendments to the RMP.²¹ We are cognisant that the industry would need time to comply with this requirement, therefore, adequate transition period will be provided for the industry to prepare the RMP documentation for existing funds.
- 3.1.6 We will not prescribe the minimum contents of the RMP as we are of the view that there is no "one-size-fits-all" RMP. It is the UTMC's duty to ensure the RMP for a fund is appropriate and proportionate to the nature and complexity of the fund. Consideration should also be given to the investment policy and strategy formulated for the investment objective of the fund. In addition, each UTMC has its own organisational and operational structure as well as risk management controls and monitoring systems established based on the nature of its business activities. Notwithstanding this, we may issue guidance or clarifications from time to time to express our expectations on the RMP.

Proposal
14

Issues for Consultation - Proposal 14

- 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.

²⁰ 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.

²¹ Presently, the RMP documentation is required as part of the feeder fund authorisation process.

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

3.2 HOLDING OF A FUND'S UNITS BY THE UTMC

3.2.1 Paragraph 3.10 of the Unit Trust Guidelines states that a UTMC may only hold units in its fund for the purpose of complying with repurchase requests or in creating new units to meet anticipated requests for units by investors. However, the number of units held is subject to a maximum limit of 3 million units or 10% of the units in circulation, whichever is lower ("Maximum Units").

3.2.2 Based on the requirement, a UTMC is prohibited from contributing seed money²² in a unit trust fund. Whilst the intention for the requirement is to mitigate conflict of interest, we take note of feedback from UTMCs on the importance of seed money in a fund to build a viable fund size to make meaningful investments and to establish performance track record for the fund.

3.2.3 In addition, our research shows that there is no prohibition in other jurisdictions for a UTMC to contribute seed money in a fund nor any requirements in relation to Manager's box.

3.2.4 In light of the above, and that there are currently requirements in the Unit Trust Guidelines for a UTMC to act in the best interest of unit holders and, if there is a conflict between unit holders' interest and its own interest, give priority to unit holders' interests²³, **we are proposing to allow a UTMC to contribute seed money in a fund, provided that -**

- (a) the fund's trustee prior approval on the transaction [i.e. investment (including subsequent investment) and redemption of units] has been obtained. With regard to redemption of units, the trustee must ensure that such transaction will not be detrimental to unit holders' interest; and
- (b) any potential conflict that may arise is addressed.

In relation to managing potential conflict of interest, the UTMC and its board of directors must ensure that there are adequate policies, procedures and controls

²² Referred to as NAV contributed by a UTMC in the unit trust fund managed by the same UTMC.

²³ Paragraph 3.05(b). Also, section 297(3) of the CMSA states that a management company shall not make improper use of its position in managing the unit trust scheme to gain, directly or indirectly, an advantage for itself or any other person or to cause detriment to the unit holders of such unit trust scheme.

established and maintained for the UTMC, in respect of any seed money, including but not limited to investments and redemptions by the UTMC.

Consequently, the requirement on Maximum Units in the Manager's box will be removed.

Issues for Consultation - Proposal 15	
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.

3.3 **OVERSIGHT ARRANGEMENT TO REPLACE INVESTMENT COMMITTEE**

3.3.1 The Unit Trust Guidelines requires a UTMC to appoint an investment committee for each of its funds. This requirement was introduced in the 1990s when the industry in Malaysia was still in its infancy, and intends to provide oversight over the UTMCs in managing a fund.

3.3.2 Since then and over the years, the SC has reinforced its supervisory oversight on the industry intermediaries with the introduction of, among others, the licensing framework, conduct requirements for fund managers, and in 2018, the registration framework for trustees as capital market services providers. Based on our observations and feedback from the industry, some of the roles and responsibilities of an investment committee are more appropriate when they are undertaken by internal functions.

3.3.3 Against this backdrop, and in addition to the proposed enhancement to a UTMC's RMP, we are **proposing to remove the requirement to appoint an investment committee**²⁴. This will be replaced by a requirement for a UTMC to have oversight arrangements within the UTMC to undertake the following existing roles and responsibilities of an investment committee. These are—

Proposal
16

²⁴ Paragraph 6.02(a), 6.03, 6.04 and 6.05 of the Unit Trust Guidelines

- (a) Ensuring that the fund is managed in accordance with its deed (including in accordance with the fund’s investment objective), prospectus, internal investment restrictions and policies and requirements in the Unit Trust Guidelines;
- (b) Ensuring that the strategies selected are properly and efficiently implemented by the management company or the fund manager;
- (c) Actively monitor, measure and evaluate the fund management performance of the management company or the fund manager; and
- (d) Approving the appointment of a broker or a dealer and ensuring that there is a good spread of brokers and dealers for the fund.

Issues for Consultation - Proposal 16	
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.

3.4 TRAINING REQUIREMENTS

3.4.1 Paragraphs 11.64 and 11.65 of the Unit Trust Guidelines require a UTMC to provide training to its officers to improve and upgrade their skills and expertise, specifying that at least 3% per annum of gross salary expense must be spent by management companies on training its officers (“Training Requirements”).

3.4.2 In addition to the Unit Trust Guidelines, the SC also prescribes training requirements in the following:

- (a) *Licensing Handbook*;²⁵

²⁵ Sub-paragraphs 7.02(12)(b) and (c) which states that a CMSL holder must ensure that its licensed representatives are sufficiently trained for those duties before acting as a

- (b) FM Guidelines;²⁶ and
- (c) *Guidelines on the Registration and Conduct of Capital Market Services Providers.*²⁷

3.4.3 To streamline the requirements on training, we **propose to replace the Training Requirements** with the following:

Proposal
17

- (a) 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
- (b) Details of all training provided are to be properly maintain by the UTMC.

Issues for Consultation - Proposal 17

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.

Question 17.2 : Do you agree for Proposal 17 to apply to PRS? Please provide specific reasons for your view.

representative, and kept abreast of developments by means of continuing training programmes.

²⁶ Paragraph 5.13 which states that a fund management company must ensure that its executive directors and employees, including the compliance officer and personnel involved in operations are adequately trained and kept abreast of industry developments.

²⁷ Paragraph 7.10 which states that a registered trustee must provide training to its officers to ensure that they continuously improve and upgrade their skills and expertise.

4 PROPOSALS RELATING TO DEALING, VALUATION AND OPERATIONAL MATTERS

4.1 DEALING IN UNITS

4.1.1 The Unit Trust Guidelines requires a UTMC to value the fund's assets and to deal in units of a fund on every business day. The only exception to this requirement is when the fund is a close-ended fund with limited repurchase arrangements.

4.1.2 With regard to suspension of dealing in units, the Unit Trust Guidelines only permits the trustee of the fund, as opposed to the UTMC, to suspend the dealing in units–

- (a) if the request to cancel units to satisfy a repurchase request is considered not to be in the best interests of unit holders to permit the fund's assets to be sold or that the fund's assets cannot be liquidated at an appropriate price or on adequate terms; or
- (b) due to exceptional circumstances, where there is good and sufficient reason to do so, considering the interests of unit holders.

The suspension due to exceptional circumstances must not exceed 21 calendar days from the commencement of the suspension.

4.1.3 Consistent with the LRM Guidance Notes and to facilitate UTMCs to employ appropriate LRM tools e.g. redemption gates, swing pricing and suspensions in managing a fund, we **propose to revise the requirements** as follows:

Frequency of valuation and dealing in units of a Variable Price Fund

- (a) A UTMC must ensure that the assets of a Variable Price Fund are valued on a regular basis and in accordance with the deed and the prospectus. In any event, the valuation must be conducted on the days that the units of the Variable Price Fund are offered or redeemed (**dealing day**) and there must at least be one dealing day in a month. Where a Variable Price Fund's dealing day is not daily, there must be sufficient disclosure as to the reason why in the fund's prospectus.

*Proposal
18a*

Suspension of dealings in units

- (a) A UTMC may, in consultation with the trustee and having considered the interests of unit holders, suspend dealing in units of a fund –
 - (i) where the market value or fair value of a material portion of the fund's assets cannot be determined; or

*Proposal
18b*

(ii) due to exceptional circumstances, where there is good and sufficient reason to do so, considering the interests of unit holders.

(b) Where the suspension of dealings is due to exceptional circumstances, the suspension should cease as soon as practicable after the exceptional circumstances have ceased, and in any event, within 21 calendar days of the commencement of the suspension. The period of suspension may be extended if the UTMC satisfies the trustee that it is in the best interest of unit holders for the dealing in units to remain suspended. Such extension should be subject to weekly review by the trustee.

4.1.4 Our research shows there are LRM tools that may not be suitable for a fund offered to retail investors, i.e. redemptions in-kind²⁸ and side pockets²⁹. As such, we intend to **prohibit the use of such tools** by unit trust funds.

*Proposal
18c*

Issues for Consultation - Proposal 18

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.

²⁸ Sometimes referred to as "in specie redemptions" and are a mechanism by which funds can distribute the underlying assets generally on a pro-rata basis to investors as opposed to paying cash to honour redemptions.

²⁹ Generally, side pockets are a mechanism by which a fund manager establishes a separate account for the sole purpose of segregating specific assets from the fund's overall portfolio. Side pockets are often used to hold illiquid securities and used in times of uncertainty where fair valuation of an asset is temporarily very difficult or impossible.

4.2 REVISION TO THE REDEMPTION PAYMENT PERIOD

4.2.1 The Unit Trust Guidelines requires a UTMC to pay the unit holder in cash the proceeds of the repurchase of units (Redemption Payment) as soon as possible, within 10 calendar days of receiving the repurchase request. In a situation where there are extended public holidays and weekends, fulfilling the Redemption Payment within 10 calendar days can be a challenge. In addition, we also note the challenges faced by certain types of funds in making Redemption Payment within 10 calendar days. These are funds where the base currency or classes of units that are denominated in a currency other than RM, and feeder funds particularly when their target funds utilise redemption gates and suspensions. Based on feedback from the industry players and evidenced from the applications for variation to the requirement that the SC has granted in the past, these are the funds where remittance involving non-RM currencies requires a longer time.

4.2.2 In light of the above, we **propose the following:**

Proposal
19

- (a) A UTMC must pay the unit holder³⁰ in cash the proceeds of the repurchase of units as soon as practicable, within 7 business days³¹ of receiving repurchase request, i.e. T + 7 business days.
- (b) The 7 business days in (a) may be extended in the following circumstances:
 - (i) In relation to a feeder fund, the Redemption Payment must be made within 5 business days from the receipt of redemption proceeds from the target fund and provided that adequate disclosures are made in the prospectus on the target fund's redemption policy;
 - (ii) A fund that faces currency conversion issues, including a fund that invests in markets outside Malaysia, or a fund with multi-currency classes, that renders the Redemption Payment within 7 business days not practicable, provided that adequate disclosures are made in the prospectus; or
 - (iii) A fund that utilises liquidity risk management tools, provided that adequate disclosures are made in the prospectus.

³⁰ Includes the end beneficiary of the units i.e. a person that invested in a fund through an IUTA or a CUTA that operates under a nominee system.

³¹ Refers to the fund's dealing day as defined in the fund's deed and prospectus.

4.2.3 In any case, the UTMC has a duty to act in the best interest of unit holders in ensuring the Redemption Payment is paid to unit holders as soon as practicable.

Issues for Consultation - Proposal 19

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 10.04³² and 10.05³³ of the Unit Trust Guidelines be amended?

(ii) If the answer to (i) is "No", please provide specific reasons for your views.

(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.

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

4.3.1 The Unit Trust Guidelines requires all the assets of a fund to be fairly and accurately valued, and that the NAV and the NAV per unit of a fund are correctly calculated or priced. Accurate valuation and correct pricing are critical in ensuring investors' confidence.

Valuation of fund's assets

4.3.2 Presently, the valuation basis for the investments of a fund is prescribed by the Unit Trust Guidelines. This can pose challenges where there are more appropriate valuation approaches to achieve fair value, particularly during unusual market conditions. Considering this, we **propose to revise the requirements to reflect a more principle based approach**, replacing Schedule C of the Unit Trust Guidelines with the following:

Proposal
20

³² A UTMC must pay the trustee the value of units created within 10 days of giving instructions to the trustee to create units.

³³ A trustee must pay the UTMC the value of units cancelled within 10 days of receiving instructions from the UTMC to cancel units.

Investment instruments	Valuation basis
Listed investment instruments	<p>The official closing price or last known transacted price on the eligible market on which the investment is quoted.</p> <p>However, if the price is not representative or not available to the market, the investments should be valued at fair value.</p>
Unlisted investment instruments	<p>(A) Fair value</p> <p>(B) Amortised cost accounting may be used subject to the following:</p> <ul style="list-style-type: none"> (i) Only permitted to be used by Variable Price Funds to value money market instruments with remaining term to maturity of not more than 90 calendar days at the time of acquisition; and (ii) The UTMC must have in place adequate measures and safeguards to properly address relevant risks associated with the use of amortised cost accounting. <p><i>Guidance on (ii)</i></p> <p>Measures and safeguards include monitoring the difference between the amortised cost of a money market instrument and its value on an ongoing basis; and ensuring appropriate actions are taken promptly where such difference exceeds a threshold determined by the UTMC for the fund.</p>
<p>Fair value refers to the price that the fund would reasonably expect to receive upon the current sale of the investment. Fair value should be determined with due care and in good faith, and the UTMC should ensure that the basis for determining the fair value of the investment is approved by the trustee (after appropriate technical consultation), and is documented.</p>	

4.3.3 Presently, in the case of OTC financial derivatives, the counterparty of the OTC financial derivative transaction must provide a reliable and verifiable valuation on a regular basis. With the introduction of Proposal 5b(iii) above and consistent with our proposal in relation to valuation, paragraph 8.19(c) of the Unit Trust Guidelines will be streamlined to require the valuation of the OTC financial derivative to be carried out by the UTMC based on a current market value; or where such value is not available, a fair value. The valuation by the UTMC should not be based solely on a valuation provided by the counterparty to the

transaction. Accordingly, paragraph 8.19(b) of the Unit Trust Guidelines will be removed.

Incorrect pricing of units

- 4.3.4 Presently, where there is incorrect pricing or valuation of units, the Unit Trust Guidelines requires the UTMC to take immediate remedial action unless the trustee considers the incorrect pricing or valuation to be of minimal significance (Incorrect Pricing Requirement).
- 4.3.5 Meanwhile, FIMM's Investment Management Standards provides that significant threshold is considered to be 0.5% of the NAV of the unit, unless the total impact on an individual account is less than RM10.00 in absolute amount (Significant Threshold).
- 4.3.6 As the Incorrect Pricing Requirement resides within the Unit Trust Guidelines, we propose to include the requirements outlined in paragraph 4.3.5 above in the Unit Trust Guidelines.
- 4.3.7 In addition, we propose to allow a UTMC to determine the manner in which investors who have subscribed or purchased overvalued units in a fund may be compensated, i.e. in the form of cash or additional units in the fund.
- 4.3.8 The **proposed requirements are summarised as follows:**
- (a) **Threshold for compensation:** 0.5% of the fund's NAV per unit after adjustment for the error.
 - (b) **Compensation to investors:** Required where total amount (either purchasing or redeeming) due to pricing error exceeding 10.00 denominated in respective currency denomination of class of units, or such lower amount as the UTMC may decide.
 - (c) **Compensation to fund:** Required where any losses incurred in all circumstances where the valuation error represents 0.5% or more of the fund's NAV per unit.
 - (d) **No compensation to UTMC:** The UTMC should not pay or cause to be paid from the fund any expenses incurred as a result of effecting compensation for a valuation error. Accordingly, paragraph 10.41(b) of the Unit Trust Guidelines will be removed.
 - (e) **Manner of compensation to unit holders:** the UTMC may decide the manner to compensate a unit holder, either by way of cash or additional units of the fund, subject to the approval of the trustee of the fund.

Issues for Consultation	
<i>Proposal 20</i>	
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.
<i>Proposal 21</i>	
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.

4.4 REQUIREMENTS IN RELATION TO COOLING-OFF RIGHT

4.4.1 The Unit Trust Guidelines requires a cooling-off right to be given to an eligible individual investor who is investing in any fund managed by a particular UTMC for the first time.

4.4.2 When an eligible individual investor exercise the cooling-off right, the UTMC must refund the investor the sum of-

- (a) the price of a unit on the day the units were purchased (referred to as "Original Amount"); and
- (b) the charges imposed on the day the units were purchased.

4.4.3 The cooling-off right allows eligible investors to exit within a reasonable time if they decide that the investment made was not an appropriate investment decision. However, refunding the investor the Original Amount may pose an unreasonable burden to the UTMC. In addition, the cooling-off right may be used to take advantage of an adverse market movement immediately after investment. This is not the intention of the cooling-off right. Towards this end, we **propose to revise the requirements under paragraph 11.05 of the Unit Trust Guidelines as follows:**

- (a) A UTMC is required to refund the investor as follows:

- (i) If the original price of a unit is higher than the price of a unit at the point of exercising the cooling-off right (market price), the market price at point of cooling-off; or
- (ii) If the market price is higher than the original price of a unit, the original price at point of cooling-off.

In addition to (i) or (ii), the management company must also refund the charges imposed on the day the units were purchased.

- (b) 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.

Issues for Consultation - Proposal 22	
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.

4.5 ENABLING A FUND TO PAY DISTRIBUTION OUT OF CAPITAL

4.5.1 Presently, distribution of income by a unit trust fund can only be made from realised gains or realised income, after taking into consideration of the following:

- (a) Total return for the period;
- (b) Income for the period;
- (c) Cash flow for distribution;
- (d) Stability and sustainability of distribution of income; and
- (e) The investment objective and distribution policy of the fund

(Paragraph 11.07 of the Unit Trust Guidelines).

4.5.2 Jurisdictional benchmarking

Our research shows that there is no similar requirements in relation to income distributions in jurisdictions such as Singapore and Hong Kong as well as the

UCITS Directive. In addition, we note that in Ireland and Hong Kong, where there is distribution out of capital, the following additional requirements apply:

- (a) The Central Bank of Ireland requires a responsible person to ensure the constitutional document of a UCITS permit any distribution from capital before making such distribution from the UCITS. In addition, additional disclosures in relation to the risks and effects from making distribution from capital in the prospectus of the UCITS are required; and
- (b) The SFC requires the investment manager to ensure that the offering documents include a prominent risk warning that the fund may pay dividend out of capital and disclose the associated risks and impact on investors. The compositions of the distributions, i.e. the relative amounts paid out of net distributable income and/or capital, for the last 12 months are made available by the investment manager/Hong Kong representative on request and also on the fund's website. The compositions of distribution payments may be presented by way of dollar amount and/or in percentage terms.

4.5.3 Having considered the above, the SC **proposes the following:**

- (a) To permit a Variable Price Fund to distribute from capital, provided it is permitted in the deed and disclosed in the prospectus of the fund.
- (b) Where distribution out of capital of the Variable Price Fund is made, the fund report must disclose the compositions of distribution payments in value and in percentage terms, i.e. the percentage sourced from income and capital, respectively.
- (c) Where distribution of capital is permitted, there must be additional disclosure in the prospectus of the Variable Price Fund on—
 - (i) the rationale for the policy to distribute out of capital;
 - (ii) the effects of making distribution from capital;
 - (iii) a statement indicating the greater risk of capital erosion that exists and the likelihood that, due to capital erosion, the value of future returns would also be diminished; and
 - (iv) a warning statement in a prominent position of the inside cover page to the effect that capital will be eroded, the distribution is achieved by forgoing the potential for future capital growth and this cycle may continue until all capital is depleted.

Issues for Consultation - Proposal 23

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.

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

4.6.1 Paragraph 11.23 of the Unit Trust Guidelines restricts the use of any broker or dealer for a fund to not more than 50% of the fund's dealings in value in any one financial year of the fund.

4.6.2 The purpose of this requirement is to ensure dealings of a fund is not concentrated to any single broker or dealer. We are **proposing to remove the restriction**, having considered the following:

- (a) Paragraph 11.21 requires the dealings in the fund's assets be effected by the broker and dealer on terms which are most favourable for the fund; and
- (b) The FM Guidelines sets out requirements on best execution that includes, among others, requirements for a fund management company to (i) establish, maintain and implement written policies and procedures to ensure best execution of trades for its clients, and (ii) ensure that the use of any dealer or financial institution for the execution of its trades must not exceed 50% of the total dealings in value in any one financial year.

Proposal
24

Issues for Consultation – Proposal 24

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.

4.7 **ENHANCEMENT TO REQUIREMENTS RELATING TO SOFT COMMISSIONS**

4.7.1 Paragraph 11.24 of the Unit Trust Guidelines prohibits a UTMC, fund manager, trustee or trustee's delegate from retaining any rebate from, or otherwise share in any commission with, any broker or dealer in consideration for directing dealings in a fund's assets. Accordingly, any rebate or shared commission should be directed to the account of the fund concerned.

4.7.2 However, paragraph 11.25 of the Unit Trust Guidelines allows goods and services (soft commissions) provided by any broker or dealer to be retained by the UTMC or the fund manager if–

- (a) the goods and services are of demonstrable benefit to unit holders and in the form of research and advisory services that assist in the decision making process relating to the fund's investments;
- (b) any dealing with the broker or dealer is executed on terms which are the most favourable for the fund; and
- (c) the practice of the UTMC or the fund manager in relation to soft commissions is adequately disclosed in the prospectus and fund reports, including a description of the goods and services received by the UTMC or the fund manager.

4.7.3 The intention of the requirements is to mitigate potential conflict of interest that may arise by allowing a UTMC or fund manager to retain soft commissions. As such, after considering the recommended good practices provided by IOSCO in the Good Practice for Fees and Expenses of Collective Investment Schemes issued in August 2018, we **propose to enhance the requirements** as follows:

Proposal
25

A UTMC or fund manager may retain goods and service (soft commissions) provided by any broker or dealer if the following conditions are met:

- (a) The soft commissions bring a direct benefit or advantage to the management of the fund and may include research and advisory related services;
- (b) Any dealings with broker or dealer is executed on terms which are most favourable for the fund;
- (c) The availability of soft commissions is not the sole or primary purpose to perform or arrange transactions with such broker or dealer, and the UTMC or fund manager must not enter into unnecessary trades in order to achieve a sufficient volume of transactions to qualify for soft commissions;

- (d) The practice of the UTMC or the fund manager in relation to soft commissions is adequately disclosed in the prospectus and fund reports, including a description of the goods and services received by the UTMC or the fund manager. 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;
- (e) In relation to fund reports, the UTMC must disclose the following:
 - (i) a statement to the effect that the broker and/or dealer had also executed trades for other CIS³⁴ managed by the UTMC or fund manager, and disclose the arrangements in such a way that unit holders of the fund are able to assess the scope of the arrangements and how the soft commissions will benefit other CIS;
 - (ii) confirmation that the goods and services received were for the benefit of the fund; and
 - (iii) that there was no churning of trades.

Issues for Consultation – Proposal 25

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.

4.8 REQUIREMENTS RELATING TO TERMINATION OF A FUND

4.8.1 Paragraph 11.28 of the Unit Trust Guidelines outlines the events where a fund must be terminated. Notwithstanding paragraph 11.28, a fund may also be

³⁴ CIS in this context refers to other unit trust funds, wholesale funds and/or ETFs managed by the same UTMC.

terminated upon the occurrence of specific termination circumstances (e.g. when the fund is at a size that is no longer viable) provided these circumstances have been provided for in the deed and disclosed in the fund's prospectus. As this is not expressly provided in the Unit Trust Guidelines, some UTMCs are not aware that this is allowed.

4.8.2 In addition, the Unit Trust Guidelines does not have any provisions in relation to the process for fund termination. As such, the fund termination practice may differ between UTMCs.

4.8.3 In view of the above, we **propose the following:**

Proposal
26

Fund termination circumstances

(A) We propose to include a provision in the Unit Trust Guidelines that a fund can also be terminated without obtaining unit holders' approval in the event of an occurrence of specific termination circumstances which have been provided for in the deed and disclosed in the prospectus of the fund, provided that such circumstances are in the best interest of unit holders.

Fund termination process

(B) Where a fund is to be terminated-

- (i) a notice to unit holders (Termination Notice) must be sent at least 1 month before the commencement date of fund termination (Commencement Date);
- (ii) within the period from the date of the Termination Notice until the Commencement Date, the fund must not accept application for subscription of units;
- (iii) a notice to SC (Termination Notice to SC) must be sent at least 2 weeks before the Commencement Date;
- (iv) within the period from the Commencement Date until the date of completion of termination (Completion Date), the fund must not accept application for redemption of units; and
- (v) at the Completion Date, the trustee of the fund must notify the SC by confirming the following:
 - (a) The assets of the fund has been realised and distributed to unit holders; and

- (b) The UTMC has managed the fund as per the deed and relevant laws.
- (C) The contents of the Termination Notice must include the following:
 - (i) Commencement Date;
 - (ii) Rationale for termination;
 - (iii) Options available to unit holders;
 - (iv) Date of expected completion;
 - (v) Estimated cost of termination; and
 - (vi) Termination cost borne by the UTMC or the fund.
- (D) The contents of the Termination Notice to SC must include the items outlined in paragraph (C) above and the following:
 - (i) Size of the fund;
 - (ii) Number of unit holders; and
 - (iii) Last date of sale of units.

Issues for Consultation – Proposal 26

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.

4.9 REQUIREMENTS ON QUORUM FOR UNIT HOLDERS’ MEETING

4.9.1 Paragraph 11.46 of the Unit Trust Guidelines states that the quorum required for a meeting is five (5) unit holders, whether present in person or by proxy. Further, the quorum for a meeting which requires a special resolution is five (5) unit holders holding in aggregate at least 25% of the units in issue at the time of the meeting.

4.9.2 We note that there is a need to provide for a scenario where there are five (5) or less unit holders in the register of unit holders. Without the additional provisions, a meeting will need to be held and adjourned before an adjourned meeting can be held to achieve the quorum. This will result in additional cost and time.

4.9.3 We would like to **propose the following**:

- (a) If a fund has five (5) or less unit holders, the quorum required for a meeting of the unit holders of the fund shall be two (2) unit holders, whether present in person or by proxy. If the meeting requires a special resolution, the quorum of the meeting is two (2) unit holders holding in aggregate at least 25% of the units in issue at the time of the meeting.
- (b) The provision in (a) will also apply to a meeting of unit holders of a class of units.

Issues for Consultation – Proposal 27

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.

5 OTHER PROPOSED AMENDMENTS

5.1 CONTENTS OF ANNUAL AND INTERIM REPORTS ("FUND REPORTS")

- 5.1.1 In light of the proposals on the use of derivatives (proposal 5) and securities lending and repurchase transactions (securities financing transactions) (proposal 6), we **propose to introduce new disclosure requirements in the fund reports as follows:**

*Proposal
28a*

Information on exposure arising from derivatives

The Fund Reports must contain disclosure on a fund's exposure to derivatives, specifically the following:

- (a) The market value of derivatives and as a percentage of the fund's NAV as at the end of the period under review;
- (b) The net gains or losses on derivatives realised during the period under review;
- (c) The net gains or losses on outstanding derivatives marked to market as at the end of the period under review;
- (d) The lowest, highest and average exposure arising from the use of derivative during the period in respect of the following:
 - (i) Gross exposure arising from the use of derivatives for any purposes, with reference to equivalent market value of the underlying assets of the derivative instruments, as a proportion to the fund's total NAV; and
 - (ii) Net derivative exposure as a proportion to the fund's NAV;
- (e) The underlying assets of derivatives instruments; and
- (f) The name of the issuer(s)/counterparty(ies) of the derivative instruments.

Information on securities financing transactions

(A) Commitments

Details of any contingent liabilities and commitments of the fund;

(B) *Securities financing transactions*

- (a) Details of the securities involved in each type of securities financing transactions;
- (b) The amount of securities on loan as a proportion of the fund's total lendable assets and of the fund's total NAV;
- (c) The respective absolute amounts of each type of securities financing transactions and as a proportion of the fund's total NAV;
- (d) The top 10 largest collateral issuers across all securities financing transactions with details on the amounts of collateral received by the fund; and
- (e) The top 10 counterparties of each type of securities financing transactions, including name of counterparty and gross amounts of outstanding transactions;
- (f) The aggregate transaction data for each type of securities financing transactions:
 - (i) The amount (including the currency denomination);
 - (ii) Maturity tenor, including open transactions;
 - (iii) Identity and country of the counterparty(ies);
 - (iv) Settlement and clearing means (e.g. tri-party, central counterparty, bilateral); and
 - (v) Collateral received by the fund to limit counterparty exposure with details required under items (a) and (e) of the *Holding of collateral*;
- (g) The amount of revenue, and the direct and indirect expenses incurred relating to each type of securities financing transactions (e.g. the amount of revenue retained by the fund and the amount of direct and indirect expenses borne by the fund and paid to the UTMC, fund manager, trustee or any parties related to them);
- (h) Details on re-investment of cash collateral required under item (f) of the *Holding of collateral*; and
- (i) Details on custody/safe-keeping arrangement of collateral under item (h) of the *Holding of collateral*.

Holding of collateral

Where a fund utilises derivatives or undertakes securities financing transactions, the Fund Reports of a fund must contain description of its holdings of collateral, including the following:

- (a) Nature of the collateral, including asset types and currency denomination;
- (b) Identity of counterparty providing the collateral;
- (c) Value of the fund (by percentage) secured/covered by collateral, with breakdown by asset class/nature and credit rating (if applicable);
- (d) Credit rating of the collateral (if applicable);
- (e) Maturity tenor of the collateral, including open transactions;
- (f) Data on re-investment of cash collateral, i.e. –
 - (i) share of cash collateral received that is re-invested, compared to the maximum amount specified in the prospectus; and
 - (ii) returns from re-investment of cash collateral;
- (g) Custody/safe-keeping arrangement, including the following:
 - (i) Number and names of custodians and the amount of collateral received/held by each of the custodians for the fund; and
 - (ii) The proportion of collateral posted by the fund that are held in segregated accounts, pooled accounts, or in any other accounts.

5.1.2 In addition to the above, we are also proposing to enhance the disclosures in the fund report to provide greater transparency and allow for better comparability of funds:

(a) **Fund performance: Basis of performance calculation**

We propose to prescribe the basis for performance calculation, i.e. the returns on the fund must be calculated on a **NAV-to-NAV basis with distributions reinvested at the NAV per unit.**

The goal is to ensure consistency and allow for better comparability of the performance of unit trust funds offered in Malaysia.

*Proposal
28b*

(b) **Expense ratio: Additional disclosure for fund with performance fee**

*Proposal
28c*

Where performance fee is charged based on the fund's performance, the fee charged may vary significantly from one year to another. To enable investors to distinguish between costs that are charged to the fund regardless of its performance, we propose that the following be disclosed in Fund Reports:

- (i) The TER excluding this remuneration; and
- (ii) The TER including this remuneration.

(c) **Transactions with related parties: New disclosure requirements**

*Proposal
28d*

We are proposing that the following disclosures in Fund Reports:

- (i) Details of any direct or indirect interest held by the UTMC, UTMC's director and substantial shareholder in another corporation carrying on a similar business³⁵; and
- (ii) The amount of related-party transactions during the period under review.

The disclosure must comply with the applicable accounting standards. For the purpose of Fund Reports, the said accounting standards would be *Malaysian Financial Reporting Standard 124: Related Party Disclosures*.

Consequently, we will also be removing the requirements under Paragraphs (23)(F)(e)(iii) and (iv) of Schedule E³⁶ as the new requirement above expects all related-party transactions to be disclosed in the Fund Reports.

(d) **Additional disclosure requirement for Fund Reports of a feeder fund**

*Proposal
28e*

Considering the performance of the feeder fund is heavily, or solely, dependent on the target fund's performance, we see the need for disclosure on investment holdings at target fund level. As such, we are proposing that the Fund Reports for a feeder fund also contain disclosure

³⁵ This is currently a requirement in the CIS Prospectus Guidelines i.e. paragraph 11.03, Part II. With this amendment, the requirement in the CIS Prospectus Guidelines will be removed.

³⁶ Requirement for the disclosure of transactions with the top 10 brokers or dealers, highlighting parties related to the UTMC or fund manager, and providing a statement as to whether dealings with related parties have been transacted at an arm's length basis.

on the target fund's top 10 holdings at market value and as a percentage of NAV as at the end of the period under review and a year ago. We believe this information should be readily available where the target fund is managed by a foreign manager that belongs to the same group of companies as, or has a formal arrangement or investment agreement with, the UTMC. Nevertheless, we recognise there could be situations where the information is not readily available to the UTMC and in that scenario, we will not require such disclosure.

Issues for Consultation – Proposal 28

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.

5.2 INFORMATION ON FUNDS ON A UTMC'S WEBSITE

5.2.1 Presently, the Unit Trust Guidelines requires a UTMC to maintain a website incorporating information relating to the UTMC and its funds³⁷. The Unit Trust Guidelines also prescribe information to be included, which are mainly information on the UTMC and parties appointed by the UTMC for its funds.

Proposal
29

³⁷ Paragraph 3.08 of the Unit Trust Guidelines.

- 5.2.2 It is important that information on unit trust funds are disseminated in an accessible and timely manner, to enable the investing public the ability to effectively compare between funds that are available in the Malaysian market and consequently, make an informed decision on their investment. UTMCs' websites are good avenues for this purpose and we note that many UTMCs have been providing information on their funds through this channel.
- 5.2.3 Taking into consideration some of the best practices in the market, and to facilitate a better experience for investors, we propose to expand the list of information required to be published by a UTMC on its website to include the following information on its funds:
- (a) Offering document (including product highlights sheet);
 - (b) Circulars, notices, and announcements;
 - (c) Fund reports;
 - (d) Latest available NAV of funds; and
 - (e) Distributions declared, including the composition of distribution (income and capital) in percentage terms.
- 5.2.4 The information mentioned above is the basic information that we expect an investor to receive to make appropriate assessment of a fund. As such, a UTMC must make available such information without charge or registration. This is also in line with our efforts for greater digitisation of the capital markets.

Issues for Consultation - Proposal 29	
Question 29.1	: Do you agree with the proposal for UTMC to make available to the public the information mentioned in paragraph 5.2.3 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.

5.3 REQUIREMENT TO DISCLOSE A PERFORMANCE BENCHMARK

5.3.1 Paragraph 4.02(o), Part II of the CIS Prospectus Guidelines requires disclosure on a fund's performance benchmark in the prospectus of the fund. The purpose of this requirement is to provide investors with a benchmark for the fund's performance.

5.3.2 We note that in jurisdictions such as Hong Kong and Singapore as well as UCITS Directive, a performance benchmark is not a mandatory requirement. We also note in Hong Kong and Singapore, performance benchmark is only required when a fund's principle objective is to track or replicate an index.

5.3.3 Towards this end, we would like to see your feedback on this requirement.

Proposal
30

Issues for Consultation - Proposal 30	
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.

GLOSSARY OF TERMS

CIS	collective investment scheme
CIS Prospectus Guidelines	<i>Prospectus Guidelines for Collective Investment Schemes</i>
CMSA	<i>Capital Markets and Services Act 2007</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
ETF Guidelines	<i>Guidelines on Exchange-traded Funds</i>
FIMM	Federation of Investment Managers Malaysia
FM Guidelines	<i>Guidelines on Compliance Function for Fund Management Companies</i>
fund	unit trust fund
IOSCO	International Organization of Securities Commissions
IUTA	institutional adviser registered with FIMM
MAS	Monetary Authority of Singapore

MMF	money market fund
NAV	net asset value
OTC	over-the-counter
PRS	private retirement scheme
PRS Guidelines	<i>Guidelines on Private Retirement Schemes</i>
REIT	real estate investment trust or property fund
RM	Ringgit Malaysia
RMP	risk management process
SFC	Securities and Futures Commission of Hong Kong
UCITS	undertakings for collective investment in transferable securities that are established in accordance with the UCITS Directive
UCITS Directive	European Parliament and Council Directive of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (No 2009/65/EC), as amended
Unit Trust Guidelines	<i>Guidelines on Unit Trust Funds</i>
UTMC	unit trust management company
VaR	Value at Risk approach, including any other variants of the VaR approach
Variable Price Fund	unit trust fund in which the price of a unit is the NAV per unit of the fund