



**FINANCIAL SERVICES COMMISSION**  
**DISCUSSION PAPER - PROPOSED AMENDMENTS TO THE SECURITIES (MUTUAL FUND) REGULATIONS**  
**APRIL 21, 2005**

---

**1.0 BACKGROUND**

- 1.1 The new Companies Act, which came into effect on February 1, 2005, specifically provides for mutual funds to be incorporated in the form of a company. Section 27A (1) of the new Companies Act states: -

*“ A "mutual fund company" means a company having a share capital and incorporated for the purpose of investing the moneys of its members for their mutual benefit, stating in its articles that it is a mutual fund, having the power to redeem or purchase for cancellation its shares without reducing its authorized share capital and is registered under the Securities Act as a mutual fund”*

- 1.2 Provisions in the previous Companies Act limited the circumstances under which a company could redeem its own shares; therefore, making it virtually unfeasible for potential operators to establish local mutual funds in the form of a company<sup>1</sup>. These restrictions, combined with the fact that the Securities (Mutual Fund) Regulations, 1999 (“MFR”) only contemplated local mutual funds being in the form of a company, did not allow for the registration and the approval by the Financial Services Commission (“FSC”) of local mutual funds.
- 1.3 The new Companies Act, however, removes the obstacles that prevented the establishment of local mutual fund companies in Jamaica. With this development the FSC is expeditiously seeking to amend the MFR as it realizes the need to have an expanded set of regulations which are consistent with international regulatory standards balanced against the commercial realities that exist in Jamaica today.

---

<sup>1</sup> The new Companies Act, unlike the old Act, contains provisions that allow for a mutual fund company to redeem its own shares – a feature that is essential to the operation of a mutual fund. Section 27A(2) states “A mutual fund company may, on the redemption of its own shares, repay the capital paid up on such shares out of its stated capital account or reserves, on such terms and in such manner and at such price as may be determined having regard to the asset values of shares as ascertained in accordance with the articles of the company.”

1.4 As such the FSC intends to have a regulatory framework that will not only provide adequate safeguards for investors but enhance the flexibility and creativity that are required for the growth of the mutual funds industry in Jamaica. The following section highlights the amendments to the MFR that are at this time being proposed.

## **2.0 PROPOSED CHANGES TO THE SECURITIES (MUTUAL FUND) REGULATIONS**

2.1 The FSC views mutual funds and collective investment schemes (“CIS”) generally, as one of the avenues for achieving the disintermediation of client obligations from the balance sheets of licensed securities dealers. High levels of balance sheet intermediation are viewed as being undesirable since it often creates significant exposures to liquidity and interest rate risk.

2.2 There is currently a moratorium on the registration of unit trusts which limits the growth in funds that can be invested in this type of CIS. This explains why the FSC has been encouraging its licensees to consider establishing local mutual funds.

2.3 Against this background, the FSC is proposing to remove a number of the anomalies that exist in the MFR while introducing a number of provisions which should strengthen the provisions in the regulations to ensure transparency in the operations of mutual funds.

2.4 The proposed amendments, along with the rationale for the amendments, are set out in tabular format in two Appendices as follows:

- **Appendix I** contains details of **New Provisions** being proposed which are largely designed to expand disclosure requirements and enhance the transparency of mutual funds
- **Appendix II** contains details of **Amendments to Existing Provisions** that are being proposed. Many of these amendments are designed to address anomalies and discrepancies in the MFR.

2.5 We would appreciate receiving your comments on these guidelines on or before the close of business on Tuesday, May 24, 2005. Comments may be submitted by electronic mail to [securities@fscjamaica.org](mailto:securities@fscjamaica.org) or be directed to Mr. George Roper, Senior Director, Securities at the following address:

Financial Services Commission  
39 – 43 Barbados Avenue  
Kingston 5  
JAMAICA

## APPENDIX I - NEW PROVISIONS

PROPOSED CHANGES	RATIONALE FOR CHANGE
<p>1. Insert in Part VI of the regulations provisions for “Plain Language Presentation “ which would require that a prospectus and all forms of communication should be written in plain language, i.e. language that can be understood by a reasonable person without specialized knowledge, applying a reasonable effort.</p>	<p>This would assist in readability and comprehension of prospectuses.</p>
<p>2. Include within regulation 15 (4) the following provisions regarding the contents of custodian and sub-custodian agreements</p> <p>(A) All custodian and sub- custodian agreements of a mutual fund shall include provisions for matters relating to the following;</p> <ul style="list-style-type: none"> <li>a) the location of the assets of the mutual fund</li> <li>b) the appointment of a sub-custodian ( if applicable)</li> <li>c) the method of holding the assets - the agreement should include the following requirements <ul style="list-style-type: none"> <li>(i) Assets of a mutual fund shall be registered in the name of the mutual fund, the name of the custodian or a sub-custodian of the mutual fund. An account number or other designation in the records of the custodian or sub-custodian must show that the beneficial ownership of the asset is vested in the mutual fund.</li> <li>(ii) Assets of a mutual fund issued in bearer form shall be designated or segregated by the custodian or sub-custodian of the mutual fund so as to show that the beneficial ownership of the asset is vested in the mutual fund.</li> <li>(iii) A mutual fund shall not pay additional fees to a custodian or sub-custodian for the transfer of beneficial ownership of assets of the mutual fund. Only fees for safekeeping and administrative services should be paid to the custodian or sub -custodian.</li> </ul> </li> <li>d) that the agreement may be amended from time to time by duly executed instrument in writing and that it shall be so amended where necessary to comply with any law in force in Jamaica.</li> </ul>	<p>These amendments specify minimum obligations which should be placed on the custodian.</p>

**APPENDIX I - NEW PROVISIONS**

PROPOSED CHANGES	RATIONALE FOR CHANGE
<p>e) that the agreement shall be governed by and construed in accordance with the laws of Jamaica and that the parties submit to the [exclusive] jurisdiction of the Jamaican Courts.</p> <p>f) the standard of care and responsibility for loss - the agreement should include the following requirements</p> <p>(i) Every custodian and sub-custodian in carrying out their duties concerning the safekeeping of assets, shall exercise</p> <p>a) the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances; or</p> <p>b) at least the same degree of care as they exercise with respect to their own property of a similar kind, if this is a higher degree of care than the degree of care referred to in paragraph (a).</p> <p>(ii) A mutual fund shall not relieve the custodian or a sub-custodian from liability to the mutual fund or to a security holder for loss that arises out of the failure of the custodian or sub-custodian to exercise the standard of care imposed by subsection (i). However, where a successful claim is made against a mutual fund for losses resulting from the failure of a custodian or sub-custodian to observe the required standard of care, the custodian shall indemnify the mutual fund fully with respect to such claims.</p> <p>(B) All sub-custodian agreements should provide for the safekeeping of assets on terms that are consistent with the custodian agreement.”</p>	
<p>3. Include within the regulations the following provisions regarding the duties of custodians and sub-custodians:</p> <p>(i) The custodian of a mutual fund shall on a periodic basis</p> <p>a) review the custodian agreement and all sub-custodian agreements of the mutual fund to determine that the agreements are in compliance with the regulations (annually)</p>	<p>These amendments specify minimum obligations which should be placed on the custodian.</p>

**APPENDIX I - NEW PROVISIONS**

PROPOSED CHANGES	RATIONALE FOR CHANGE
<ul style="list-style-type: none"> <li>b) ensure a 100% physical verification of securities and prepare reconciliations with the records of the fund (quarterly)</li> <li>c) permit the auditor of the Mutual Fund to have access to the books and records of the custodian and sub-custodian that pertain to the portfolio of securities of the mutual fund, for the purposes of their audit.</li> <li>d) require the custodian and sub-custodian's auditors to provide a report to the regulator regarding the custodian's internal controls and operating procedures at least once per year.</li> </ul>	
<p>4. Expand the provisions of the regulations to include requirements in respect to the following:</p> <p><b>Net Asset Values - Minimum Requirements</b></p> <p>(A) The current net asset value (NAV) of any redeemable security issued by a registered mutual fund used in computing periodically the current price for the purpose of distribution, redemption, and repurchase means an amount which reflects calculations, whether or not recorded in the books of account, made substantially in accordance with the requirements listed below, with estimates used where necessary or appropriate. Requirements in respect to the NAV's calculation are:-</p> <ul style="list-style-type: none"> <li>a) Portfolio securities with respect to which market quotations are readily available shall be valued at current market value, and other securities and assets shall be valued at fair value as determined in accordance with International Financial Reporting Standards (IFRS). Portfolio securities for which market quotations are not readily available shall be valued in accordance with IFRS. These valuations should be kept for review by the Financial Services Commission;</li> <li>b) Changes in holdings of portfolio securities shall be reflected no later than in the first calculation on the first business day following the trade date;</li> <li>c) Changes in the number of outstanding shares of the registered mutual fund resulting from distributions, redemptions, and repurchases shall be reflected no later than in the first calculation on the first business day following such change;</li> <li>d) Expenses, including any investment advisory fees, shall be</li> </ul>	<p>These provisions will ensure some consistency in the calculation of the NAV and unit prices of registered funds while enhancing the levels of transparency and disclosure.</p>

**APPENDIX I - NEW PROVISIONS**

PROPOSED CHANGES	RATIONALE FOR CHANGE
<p>included to the date of calculation.</p> <p>e) Dividends receivable shall be included to the date of calculation either at ex-dividend dates or record dates, as appropriate;</p> <p>f) Interest income and other income shall be included to the date of calculation.</p> <p>(B) The items which would otherwise be required to be reflected by subparagraphs (A)(d) and (A)(f) above need not be so reflected if cumulatively, when netted, they do not amount to as much as one cent per outstanding share.</p> <p><b>Frequency and Currency of Calculation of Net Asset Values per Security</b></p> <p>a) The NAV per security of a mutual fund shall be calculated at least once in each week</p> <p>b) Despite paragraph (a), a mutual fund that, at the date that these regulation comes into force, calculates NAV per security no less frequently than once a week may continue to calculate NAV per security at least as frequently as it does at that date.</p> <p>c) The NAV per security of a mutual fund shall be calculated in the currency of the fund.</p>	
<p>5. Include a provision requiring that the NAV per security of every mutual fund be published in a widely circulated local newspaper at least once per week.</p>	<p>This will provide additional information which will be of value to investors and potential investors. This requirement is also in keeping with similar requirements that exist for unit trusts.</p>
<p>6. Insert under regulation 30 the following requirement in respect to derivatives:</p> <p>A mutual fund shall include in the statement of investment portfolio, in its annual and interim financial statements of the mutual fund, detailed information related to any form of derivatives which are being used in the mutual fund.</p>	<p>This will ensure adequate disclosure and enhance accountability.</p>
<p>7. Insert under regulation 30 the following disclosure requirements :</p> <p>(1) The annual financial statements of a mutual fund shall</p>	<p>This will provide information to investors on the level and types of expenses paid by the fund and also provide historical information as to the performance of the fund.</p>

## APPENDIX I - NEW PROVISIONS

PROPOSED CHANGES	RATIONALE FOR CHANGE
<p>a) set out the amounts of all fees, charges and expenses, if any, that have been charged to the mutual fund during each financial year reported upon; and</p> <p>b) set out the net asset value per security of the mutual fund as at the end of the last completed financial year and as at the end of each of the four preceding completed financial years, or such fewer number of financial years as the mutual fund has been in existence.</p>	

## APPENDIX II - AMENDMENTS TO EXISTING PROVISIONS

PROPOSED CHANGES	RATIONAL FOR CHANGE
<b><u>Part I- Preliminary</u></b>	
1. Revise the definition of “material change” in Regulation 2 by replacing the word “extra-ordinary” with the word “significant”.	The word significant would be more appropriate as it would capture a larger range of events.
<b><u>Part II- Overseas Mutual Funds</u></b>	
2. In regulation 7(1) insert the word “annual” between “the” and “renewal fee”; and in regulation 7(3) insert the word “renewal” between the words “annual” and “fee” – in order to make both paragraphs consistent with the Second Schedule which uses the term “annual renewal fee” to describe the fee payable on each anniversary of a mutual fund’s registration.	These regulations give the impression that two fees have to be paid.
3. In regulation 7(2) the words “Certificate of renewal” are to be replaced with “Notice of Renewal”.	The FSC does not issue a certificate of renewal.
4. Provisions similar to Regulation 8(1)(b) and (2) (Additional Documents) to be included in Part III of the MFR which pertains to Local Mutual funds.	There are presently no such requirements for local mutual funds in respect to prospectuses.
5. Make regulation 9 (Suspension or Cancellation of Registration) applicable to both overseas and local mutual funds.	There is currently no such provision in the local requirements.
6. Include regulation 10 (Re-registration) in “Part V - General Obligations” to make its provisions applicable to both overseas and local mutual funds.	There is currently no such provision in the local requirements.
<b><u>Part III- Local Mutual Funds</u></b>	
7. Regulation 13(3) to be restructured in order to clarify the meaning as it gives the impression that <b>all</b> applicants should be given the opportunity to be heard.	The offer of an opportunity to be heard should only be applicable to those persons who have been notified of the Commission’s intention to refuse approval.
8. In regulation 13(4)(a), the word “ <i>applicant</i> ” which appears between the phrases “ <i>the experience of the</i> “ and “ <i>in the field of</i> ” should be deleted and replaced with the term “ <i>management company</i> ”.	This will ensure that the experience requirement is clearly
9. Regulation 13(4)(d) needs to be removed	The “applicant” should not be required to own 40% of the management company.
10. Add the requirements of “five years experience” included in regulation 13(4)(a) to regulation 4(1)(c) which applies to Overseas Mutual funds.	We believe that all applicants, both local and overseas, should meet the same experience requirements.

## APPENDIX II - AMENDMENTS TO EXISTING PROVISIONS

PROPOSED CHANGES	RATIONAL FOR CHANGE
<p>11. Expansion of Custodian requirements by inserting in regulation 15(2) a provision to make companies meeting the following criteria eligible to be appointed as a custodian:</p> <p>“A company incorporated under the laws of Jamaica, licensed under the Securities Act. The company shall maintain a capital base of \$500 million or six percent of its total asset; which ever is greater.”</p>	<p>This provision aims to expand the type of institutions that may be used as custodians in light of BOJ mandating that merchant and commercial banks can no longer act as custodians.</p> <p>A capital base of \$500 million should help to ensure that a dealer that is approved as custodian will have adequate capital to provide the necessary infrastructure to deal with this new function.</p>
<p>12. Amend regulation 15(2) by removing paragraph (c) (ii).</p>	<p>Regulation 15 (5) states that “where a registered local mutual fund appoints as custodian a foreign banking institution or a trust company incorporated outside Jamaica, that institution or trust company shall perform the functions of custodian only in relation to foreign assets held by that registered local mutual fund.”</p> <p>Since oversees custodians can only hold foreign assets, we believe that the provision requiring registration under the local Companies Act is unnecessary.</p>
<p>13. Remove regulation 20(a)</p>	<p>Management companies will not necessarily be required to be engaged primarily in the business of mutual fund management.</p>
<p>14. In respect to regulation 20(d) delete “ in accordance with the formula set out in the Fourth Schedule”</p>	<p>This formula is inappropriate as it is based on a Net Capital Rule that is applied to broker dealers in other jurisdictions and is not deemed to be suitable for mutual funds.</p>
<p>15. Insert the word “mutual” immediately before the word “fund” in paragraph 1(a) of regulation 24 and wherever else it appears in the regulations without being preceded by the word “mutual”.</p>	<p>This is to ensure consistency and clarity.</p>
<p>16. In regulation 26 delete paragraph (3) and replace it with the following-  “(3) The directors of the mutual fund shall as soon as is reasonably practicable , or in any event, not less than seven days after deciding to remove the management company, inform the Commission of that decision.”</p>	<p>Existing provision was not practical.</p>
<p><b><u>Part IV- General Obligations of Mutual Funds</u></b></p>	
<p>17. In regulation 28 delete paragraph (5) and replace it with the following -  “<i>In paragraph (2), ‘relevant <b>accounting date</b>’ means the date on which the company’s financial year ends.</i>”</p>	<p>The existing provision did not properly define “relevant accounting date”</p>

## APPENDIX II - AMENDMENTS TO EXISTING PROVISIONS

PROPOSED CHANGES	RATIONAL FOR CHANGE
18. In regulations 28(1) and 30(3) remove the word “local” where it appears before the words “mutual funds”.	These regulations contain a requirement which should be applied to both local and overseas mutual funds.
19. Regulation 29 – In the 1 <sup>st</sup> paragraph insert before the words “local newspaper” the words “widely circulated”.	To ensure that required disclosures are not published in newspapers which are not widely read.
20. In paragraph (2)(a) of Regulation 30 delete the words “ <i>once per year</i> ” and replace them with the words “ <i>within ninety days after the relevant accounting date.</i> ”	The existing provision does not specify a due date for the submission of audited accounts by mutual funds.
21. Regulation 30(2)(b) is to be reworded to include a due date for the submission of the following documents:-  <ul style="list-style-type: none"> <li>(i) Quarterly statements showing movement in net assets</li> <li>(ii) Quarterly portfolio statements, including changes from the previous period.</li> </ul> <p>The amended regulation should indicate that the reports referred to in the paragraphs above shall be filed within forty-five (45) days after the end of each calendar quarter.</p>	This amendment specifies a time period for submission of certain reports.
22. Regulation 30(3) – In the 1 <sup>st</sup> paragraph insert before “local newspaper” the words “widely circulated”.	To ensure that the publications are not put in newspapers which are not widely read.
<b><u>Part V - Inspection and Disciplinary Proceedings</u></b>	
23. In regulation 32(1)(c) insert the word “and” between the words “carry out” and “report”.	This change is required to correct the sentence structure of the regulation.
24. In regulation 32(4) remove the words “paragraph (1) or (2)” and replace with “paragraph (1)(a)”.	The existing provision is deemed to be unduly onerous.
<b><u>Part VI-General</u></b>	
25. In regulation 35(6) insert the words “widely circulated” in front of “local newspaper”.	To ensure that the publications are not put in newspapers which are not widely read.
26. In regulation 37(a) the words “fifty thousand” are to be changed to “two million”.	Fifty thousand dollars was not considered an adequate amount for a fine and is not consistent with the current level of fines set out in the Securities Act.

## APPENDIX II - AMENDMENTS TO EXISTING PROVISIONS

PROPOSED CHANGES	RATIONAL FOR CHANGE
<p><b><u>First Schedule</u></b></p>	
<p>27. In the First Schedule under the sub-heading “For each Fund” remove the words “equity and bond Funds” and insert “all Mutual Funds” in paragraph (b).</p>	<p>This change will make the provision applicable to all mutual funds and not just to equity and bond funds.</p>
<p><b><u>Third Schedule</u></b></p>	
<p>28. Prospectus requirements to be enhanced to include the following provisions;</p> <p>(A). Insert under the heading “26. ADDITIONAL INFORMATION” a sub-heading “<i>What is a mutual fund and what are the risks associated with investing in a mutual fund</i>”.</p> <p>Under this sub-heading the following requirements should be detailed.</p> <p>(i) The prospectus should contain:-</p> <p>(a) a brief description of the nature of a mutual fund</p> <p>(b) the risk factors or other investment consideration that an investor should take into account that are associated with investing in mutual funds generally.</p> <p>(c) a disclosure of this nature:-</p> <p>“Mutual funds own different types of investments depending on their investment objectives. The value of these investments will change from day to day, reflecting changes in interest rates, economic conditions and company news. As a result the value of the fund’s units may go up or down and the value of your investment in the fund may be more or less when you redeem it than when you purchased it.</p> <p>The full amount of your investment is not guaranteed”</p> <p>(B). Insert under the heading “26. ADDITIONAL INFORMATION” the sub-heading “<i>Who should invest in the fund?</i>” and include the following requirements:</p>	<p>This change will ensure that investors are advised of the risks associated with the investment.</p>

**APPENDIX II - AMENDMENTS TO EXISTING PROVISIONS**

<b>PROPOSED CHANGES</b>	<b>RATIONAL FOR CHANGE</b>
<p>(i) Describe the characteristics of the investor for whom the fund may or may not be an appropriate investment, and the portfolio for which the fund is suited or for which the fund should not be used.</p> <p>(ii) Indicate the level of risk tolerance that would be appropriate for investment in this type of fund.</p>	
<p>29. In paragraph (1)(b) under the heading "16. PERIODIC CHANGE" - change the word "maxmum" to the word "maximum"</p>	<p>This change is required to effect a spelling correction.</p>
<p>30. Under heading "25. HEALTH WARNING" - the words "Securities Commission" are to be changed to "Financial Services Commission" and the heading to be changed from "HEALTH WARNING" to "GENERAL DISCLAIMER"</p>	<p>This change is required to update the regulations.</p>
<p><b><u>Fourth Schedule</u></b></p>	
<p>31. Delete the Fourth schedule</p>	<p>This formula is inappropriate as it is based on a Net Capital Rule that is applied to broker dealers in other jurisdictions and is not deemed to be suitable for mutual funds.</p>