



**JUNE 2008**

**ADVANCED INVESTMENT SCHEMES ADMINISTRATION**

**MARK SCHEME**

**Section A contains 10 short answer questions each carrying two marks. In order to obtain maximum marks in each question candidates should provide two clear and relevant sentences appropriate to the question.**

**Answer ALL questions in this section**

- 1 Explain the key aspects of the Capital Gains position of UK Investment Schemes. (2 marks)

*Capital Gains from the underlying assets are free of tax.  
Gains are taxed from investors at eventual disposal from scheme.  
Life funds are taxed at a special composite rate each year.*

- 2 Why might a fund manager prefer to have a regular savings scheme for contributions to their fund? (2 marks)

*Brings in a steady stream of predictable income.  
Not affected by stock market sentiment so can take long term view.  
Better management of cancellation / creation of units.*

- 3 Give TWO duties / responsibilities of the Authorised Corporate Director. (2 marks)

*Must provide information as to how the duties are being carried out.  
Must provide accounts, details of contracts etc. (at regular Board meetings).*

- 4 Most OEICs are non-certificated because they fall into certain categories. Identify TWO of these categories. (2 marks)

*Instrument of incorporations says will not issue.  
Shares are in uncertified form for CREST system.  
Shareholder has said in writing that does not want them.  
Shares are in the name of the ACD.  
Shares are issued / transferred to a nominee of recognised investment exchange.*

- 5 The COLL Rules state what must NOT be contained in an instrument constituting a pooled fund. Give TWO examples. (2 marks)

*Must not conflict with any COLL rule.  
Prevent units or shares being marketed in the UK.  
Not be unfairly prejudicial to the interests of the holders generally, or the holders of any specific class of units.*

- 6 Identify TWO instances whereby, in an authorised collective investment scheme, the “swinging single price” might be applied. (2 marks)

*The AFM uses the mid-market single price method for what is determined to be normal size transactions.*

*Switches to dual pricing for large deals.*

*OR Swings for all deals when the net movement in or out of fund on a given day is deemed material.*

- 7 What are the minimum pricing checks that must be made by a trustee / depositary according to the FSA? (2 marks)

*Thorough review of system to assess reliability when trustee appointed.*

*Thorough review when a major change in system (or numerous minor changes).*

*Check valuation of each fund annually (at least) including liabilities, accruals etc. on a sample basis.*

- 8 Double Taxation Agreements are becoming more common; however Investment Schemes face complex rules to be able to deal with tax reclaims. Give TWO factors that affect the level and success of a reclaim? (2 marks)

*The countries involved and the timing of reclaim approvals (months to several years).*

*Different rates of withholding tax (range from 10-30%).*

*Requirement to prove entitlement to tax relief from double taxation.*

- 9 In October 2002, HMRC announced a relaxation of the requirements for overseas investors who wish to receive gross interest from collective investment schemes. For example, previously they had to make a declaration that they were not ordinarily resident. Give ONE further example of change and a reason why it was made. (2 marks)

*A class of share which is not normally marketable to a UK resident.*

*AND they invest through a local intermediary e.g. Bank.*

*Intended to make UK CISs more attractive to foreign investors and allow the funds to compete on a more equal footing.*

- 10 List TWO of the main requirements of FRS17 for Pension Schemes. (2 marks)

*Assets measured using market values.*

*Liabilities measured using a projected unit method and discounted at an AA corp bond rate.*

*Scheme surplus / deficit is recognised in the balance sheet.*

*Movement in deficit / surplus analysed into*

- *current service cost and past service costs are in operating profits;*
- *actuarial gains / losses recognised in statement of recognised gains / losses.*

**Answer TWO questions in this section**

- 11 Explain SEVEN of the distinctive features of a Qualified Investor Scheme. (10 marks)

*1 ½ marks available for each relevant point up to a maximum of 10*

1. *Unlike retail funds spread of risk not stipulated in rules*
2. *FSA impose rule requiring AFM to take reasonable steps to ensure spread of risk*
3. *Suitable diversification of risk re capital & income required (disclosed in Prospectus)*
4. *Derivatives & Commodities are permitted but exposure limited to value of net assets*
5. *Borrowing restricted to 100% of net asset value (must be able to close quickly)*
6. *Limited issue & redemption but in instruments & prospectus*
7. *Prices to be published and be available on request*
8. *Depository must be appointed to oversee AFM re valuation etc.*
9. *Only fundamental change so the fund require approval by investors*
10. *Instrument of Incorporation & prospectus to be more detailed then retail funds*

- 12 By law, Pension Trustees must keep records of all the scheme's financial transactions. Outline, giving relevant details, FIVE types of financial transactions where such records should be kept. (10 marks)

*1 mark for each transaction and 1 mark for relevant details up to a maximum of 10*

1. *Contributions received (member and employer) and date*
2. *Payments made to leavers (inc. name, date of leaving benefits at that date, how calculated and paid (2 marks)*
3. *Other payments made (inc. professional fees) inc. name and addresses, reason, date etc.*
4. *Any movement / transfer of scheme assets inc. name, address and reason*
5. *If winding up and buying a policy to secure protected rights inc. name of company, name of members, amount and dates (2 marks)*
6. *Any payment to employer and why*
7. *Any other payment into / out of the scheme inc. name, address etc. of person paying / receiving*

- 13 Investor services providers have to produce reports to meet the requirements of different investor types. Give FIVE detailed examples of the reporting requirements of a retail investor. (10 marks)
1. *Periodic confirmation of the total holding value inc. number of units / shares held and price per*
  2. *Will depend on producer but can be ¼ or ½ yearly but probably annual for pensions*
  3. *Qualitative reports for performance of fund against peers & market*
  4. *Can be paper based annual report & account and also interim report from investment manager as well giving reasons for performance*
  5. *Can also give monthly update from website etc.*
  6. *Must comply with Principle 7 of Principles of Business that requires a firm to pay due regard to info needs of clients and communicate info to them in a way which is clear, fair and not misleading (2 marks)*
  7. *If with profits product then follow consumer friendly principles version of PPFM*
  8. *Reports to allow completion of tax returns inc. tax warrant, chargeable event certificate, tax credit etc. (2 marks)*

## **SECTION C**

**TOTAL 30 MARKS**

### **Answer ONE question in this section**

- 14 a) UCITS Schemes can be marketed in the European Economic Area. What must the Authorised Fund Manager do to comply with the regulations? (4 marks)
- *Must notify the FSA*
  - *Must specify the country*
  - *Must notify the other state*
  - *(FSA no later than this notification)*
- b) Outline the FOUR key COLL requirements relating to the drafting of a Prospectus to provide information to investors. (4marks)
- *Contain the detailed information as prescribed by the COLL*
  - *Not contain anything which is prejudicial*
  - *Not conflict with Sourcebook*
  - *Must be kept up to date*

c) The Prospectus contains information on numerous aspects of the operation of the scheme which investors may require. Explain in detail what must be specified with regard to the following items:

- i) The description of the authorised fund; (9 marks)
- ii) Contractual relationships; (5 marks)
- iii) Payments. (8 marks)

i)

- *Type (1 mark)*
- *ICVC sub-funds (1 mark)*
- *OEIC requirements (2 marks)*
- *Date of authorisation (1 mark)*
- *Currency (1 mark)*
- *Circumstances in which it may be wound-up (1 mark)*
- *Summary of the procedure (1 mark)*
- *Rights of unit / shareholders under such (1 mark)*

ii) *1 mark for each valid point up to a maximum of 5*

- *Material provision of OEIC / AFM*
- *Including provisions (if any) relating to remuneration etc.*
- *OEIC / Director*
- *Delegated functions*
- *Contract with manager of AUT / depositary*

iii) *1 mark for each valid point up to a maximum of 8*

- *Payment out to whom*
- *What for*
- *Rate or amount*
- *How calculated / accrued*
- *When*
- *Performance fee examples and max amounts*
- *Also if capital expense*
- *And policy for allocation and impact*

15 Different types of investment funds calculate the return to investors in different ways. Explain how returns are calculated for the following types of investment fund:

- a) Life Funds; (6 marks)
- b) Pension Funds; (3 marks)
- c) Pooled Funds; (11 marks)
- d) How this information is conveyed is subject to certain standards. Explain why these standards have been set by organisations such as NAPF. (10 marks)

a)

- Actual return computed over term of policy, comparison with alternative types of investments
- Usually compared with similar companies
- During term bonus declaration compared with other Life Cos
- (inc. terminal bonus)
- Will have comparison for various years (usually in a table) for a standard policy
- Similar for with-profit binds but for a single investment, showing SV with MVR if applicable

b)

- Same as for with profit policies (basically)
- Period is often lesser term e.g. 10 years
- and premium will be higher

c) 1 mark for each relevant point up to a maximum of 11 marks and to include the following

- Return is aggregate of capital change plus income received for period
- Assumes standard amount
- Used to purchase units / shares at buying price at start of period (inc. charges)
- Income is re-invested in further shares / units at earliest possible time
- Holding at end is valued as if selling
- Can compute as % of original
- Convention allows it in £ terms e.g. 5 years ago worth today on basis offer / bid income re-invested
- Thus managers of a growing fund set bid price at level spread down from buying rather than lower SP
- Comparison with similar objective funds (can cover OEICs etc.)
- IMA can be used to set comparison funds

d) 1 mark available for each valid point

- Chaos could ensue if presented in different ways
- Client would need to unravel to allow comparison
- Demonstrates a mature outlook by industry

- *Creates a level playing field for managers to be compared on their merits only*
- *Facilitates comparisons*
- *Introduces independence in measurement and verification*
- *Assists adoption of best practice*
- *Discourages misleading adverts etc.*
- *Adoption of GIPS to allow worldwide comparison*
- *Can provide information on risks being taken e.g. by giving beta etc.*

## **SECTION D**

**TOTAL 30 MARKS**

### **Answer ONE question in this section**

- 16 The FSA requires Authorised Fund Managers to provide annual and interim reports to investors. The COLL Sourcebook requires Long and Short Reports to be available to investors. You are employed by Apolachian Investment Funds and you have been asked by your marketing department to summarise briefly the main sections of the Long and Short reports, outlining how these might be of particular interest to the retail investor. *(30 marks)*

*(Marks awarded for explaining and giving examples)*

*1 mark available for each valid point / example where appropriate to include the following:*

- *AFM must produce both*
- *Umbrella Fund must have short report for each sub fund*
- *but not for umbrella as a whole*
- *Long funds has sep accs for each sub-fund*
- *together with aggregated set of accounts*
- *If less than 12 months no need for short*

*Long*

- *Available to any investor who requests a copy*
- *Audited full accounts*
- *AFMs report (details to be given)*
- *Comparative table (explained and example given)*
- *Trustees report*
- *Auditors report*
- *Interim report does not need comparative table of Trustee report*
- *and is unaudited no auditor's report*

*Short*

- *Sent to every investor*
- *Must be written to allow average investor to understand it*
- *No info to be added*
- *Single short report is permitted to have details of more than one sub fund in umbrella*
- *Intended to be briefer / friendlier document*
- *Not subject to SORP Standard as less accounting data*
- *Must be consistent with Long Report*
- *Details of scheme*
- *Review of investment activities / performance*
- *Comparative table*
- *Sufficient info to inform investor*

- 17 Apalachian Investment Funds are finalising the launch of their first investment fund in the UK. You have been asked by the managers to outline what is required in their fund's Key Features Document (using examples where necessary to illustrate your meaning). (30 marks)

*The answer will include coverage of the following aspects*

1. *Aims of fund*
2. *Subscription detail*
3. *Risk factors*
4. *Who they are*
5. *How investment works*
6. *Choice of funds*
7. *Calculation of prices*
8. *Identification requirements*
9. *Documents issued*
10. *Change of mind*
11. *Switching*
12. *Monitoring*
13. *Income*
14. *Withdrawals*
15. *Sales*
16. *Charges*
17. *Transaction costs*
18. *Cost of advice*
19. *Further information*
20. *Documentation*
21. *Taxation*
22. *Queries / complaints*
23. *Special needs clients*

- 24. *Other information*
- 25. *Data protection*