

Chapter 9

Meaning of open-ended investment company



9.11 Frequently Asked Questions

9.11.1 **G** Table There are some frequently asked questions about the application of the definition of an *open-ended investment company* in the following table. This table belongs to ■ PERG 9.2.4 G (Introduction).

Question	Answer
1	<p>Can a <i>body corporate</i> be both open-ended and closed-ended at the same time?</p> <p>In the <i>FCA's</i> view, the answer to this question is 'no'. The fact that the investment condition is applied to BC (rather than to particular shares in, or securities of, BC) means that a <i>body corporate</i> is either an <i>open-ended investment company</i> as defined in section 236 of the <i>Act</i> or it is not. Where BC is an <i>open-ended investment company</i>, all of its securities would be treated as <i>units</i> of a <i>collective investment scheme</i> for the purpose of the <i>Act</i>. A <i>body corporate</i> formed in another jurisdiction may, however, be regarded as open-ended under the laws of that jurisdiction but not come within the definition of an <i>open-ended investment company</i> in section 236 (and vice versa).</p>
2	<p>Can an <i>open-ended investment company</i> become closed-ended (or a closed-ended body become open-ended)?</p> <p>In the <i>FCA's</i> view, the answer to this question is 'yes'. A <i>body corporate</i> may change from open-ended to closed-ended (and vice versa) if, taking an overall view, circumstances change so that a hypothetical reasonable investor would consider that the investment condition is no longer met (or vice versa). This might happen where, for example, an <i>open-ended investment company</i> stops its policy of redeeming shares or securities at regular intervals (so removing the expectation that a reasonable investor would be able to realise his investment within a period appearing to him to be reasonable). See also PERG 9.7.5 G.</p>
3	<p>Does the liquidation of a <i>body corporate</i> affect the assessment of whether or not</p> <p>The <i>FCA</i> considers that the possibility that a <i>body corporate</i> that would otherwise be regarded as closed-ended may be wound up has no effect at all on the nature of the <i>body corporate</i> before the winding up. The fact that, on a winding</p>

Question	Answer
	<p>the body is an <i>open-ended investment company</i>?</p> <p>up, the shares or securities of any investor in the <i>body corporate</i> may be converted into cash or money on the winding up (and so 'realised') would not, in the FCA's view, affect the outcome of applying the expectation test to the <i>body corporate</i> when looked at as a whole. The answer to Question 4 explains that investment in a closed-ended fixed term <i>company</i> shortly before its winding up does not, in the FCA view, change the closed-ended nature of the <i>company</i>. For <i>companies</i> with no fixed term, the theoretical possibility of a winding up at some uncertain future point is not, in the FCA's view, a matter that would generally carry weight with a reasonable investor in assessing whether he could expect to be able to realise his investment within a reasonable period.</p>
4	<p>Does a fixed term closed-ended investment <i>company</i> become an <i>open-ended investment company</i> simply because the fixed term will expire?</p> <p>In the FCA's view, the answer to this is 'no'. The termination of the <i>body corporate</i> is an event that has always been contemplated (and it will appear in the <i>company's</i> constitution). Even as the date of the expiry of the fixed term approaches, there is nothing about the <i>body corporate</i> itself that changes so as to cause a fundamental reassessment of its nature as something other than closed-ended. Addressing this very point in parliamentary debate, the Economic Secretary to the Treasury stated that the "aim and effect [of the definition] is to cover companies that look, to a reasonable investor, like open-ended investment companies". The Minister added that "A reasonable investor's overall expectations of potential investment in a company when its status with respect to the definition is being judged will determine whether it meets the definition. The matter is therefore, definitional rather than one of proximity to liquidation". (Hansard HC, 5 June 2000 col 124).</p>
5	<p>In what circumstances will a <i>body corporate</i> that issues a mixture of redeemable and non-redeemable shares or</p> <p>In the FCA's view, the existence of non-redeemable shares or securities will not, of itself, rule out the possibility of a <i>body corporate</i> falling within the definition of an <i>open-ended investment company</i>. All the relevant circumstances will need to be considered (see PERG 9.6.4 G, PERG 9.2.8.8G and PERG 9.8.9 G). So the</p>

Question	Answer
	<p>securities be an <i>open-ended investment company</i>?</p> <p>following points need to be taken into account.</p> <p>(1) The precise terms of the issue of all the shares or securities will be relevant to the question whether the investment condition is met, as will any arrangements that may exist to allow the investor to realise his investment by other means.</p> <p>(2) The proportions of the different share classes will be relevant to the impression the reasonable investor forms of the <i>body corporate</i>. A <i>body corporate</i> that issues only a minimal amount of redeemable shares or securities will not, in the <i>FCA's</i> view, be an <i>open-ended investment company</i>. A <i>body corporate</i> that issues a minimal amount of non-redeemable shares or securities will be likely to be an <i>open-ended investment company</i>. A <i>body corporate</i> that falls within the definition of an <i>open-ended investment company</i> is likely to have (and to be marketed as having) mainly redeemable shares or securities. However, whether or not the <i>body corporate</i> does fall within the definition in any particular case will be subject to any contrary indications there may be in its constitutional documents or otherwise.</p> <p>(3) Where shares or securities are only redeemable after the end of a stated period, this factor will make it more likely that the <i>body corporate</i> is open-ended than if the shares or securities are never redeemable.</p>
6	<p>Does "realised on a basis calculated wholly or mainly by reference to..." in section 236(3)(b) apply to an investor buying investment trust company <i>shares</i> traded on a <i>recognised investment exchange</i> because of usual market practice that the <i>shares</i> trade at a discount to asset value?</p> <p>In the <i>FCA's</i> view, the answer is 'no' (for the reasons set out in PERG 9.9.4 G to PERG 9.9.6 G).</p>

Question	Answer
7	<p>Does the practice of UK investment trust companies buying back <i>shares</i> result in them becoming <i>open-ended investment companies</i>?</p> <p>In the <i>FCA's</i> view, it does not, because its actions will comply with company law: see section 236(4) of the Act and PERG 9.6.5 G.</p>
8	<p>Would a <i>body corporate</i> holding out redemption or repurchase of its shares or securities every six months be an <i>open-ended investment company</i>?</p> <p>In the <i>FCA's</i> view a period of six months would generally be too long to be a reasonable period for a liquid securities fund. A shorter period affording more scope for an investor to take advantage of any profits caused by fluctuations in the market would be more likely to be a reasonable period for the purpose of the realisation of the investment (in the context of the 'expectation' test, see PERG 9.8 and, in particular, PERG 9.8.9 G which sets out the kind of factors that may need to be considered in applying the test).</p>
9	<p>Would an initial period during which it is not possible to realise investment in a <i>body corporate</i> mean that the <i>body corporate</i> could not satisfy the investment condition?</p> <p>In the <i>FCA's</i> view, the answer to that question is 'no'. In applying the investment condition, the <i>body corporate</i> must be considered as a whole (see PERG 9.6.3 G). At the time that the shares or securities in a <i>body corporate</i> are issued, a reasonable investor may expect that he will be able to realise his investment within a reasonable period notwithstanding that there will first be a short-term delay before he can do so. Whether or not the 'expectation test' is satisfied will depend on all the circumstances (see PERG 9.8.9 G).</p>