

ALTERNATIVE INVESTMENT FUND MANAGERS (AIFM) DIRECTIVE (UPDATE)

ISSUES FOR INVESTMENT TRUSTS - BRIEFING NOTE

BACKGROUND

The AIFM Directive was first issued by the European Commission in April 2009. It aims to increase regulation of those investment managers whose activities spread or amplify risks through the financial system, with investment strategies that are not adapted to the investment profile or needs of retail investors, offering funds which are illiquid and subject to high risk of substantial risk of capital loss. These characteristics are diametrically opposed to the investment policy of Alliance Trust and similar investment trusts. However the scope of the directive is such that investment trusts will be required to comply with it.

If the Directive had passed into law in its original form, the current legal structure of investment trusts could not have been maintained, with the result that trusts would be forced to liquidate and transfer investors into alternative structures complying with the new requirements. An assessment of the original directive undertaken by the FSA identified a cost of some 500m Euros across the industry, which would fall to be met by the trusts concerned and ultimately their shareholders.

Alliance Trust, along with other investment trusts, has engaged actively and constructively with the European Union legislators to seek changes to the directive which will address our concerns.

PROGRESS

The Council of Ministers, the body which through which member state governments' views are represented, proposed revisions to the Directive which were formulated first in the Swedish Compromise in November 2009 and, in April 2010, in the Spanish Compromise, reflecting the country which held the Presidency of the European Union at the time. These alterations were definitely an improvement from the perspective of the investment trust industry, but still proposed a significant increase in the level and cost of regulation applied to the industry. The regulations proposed would at times duplicate and at others contradict the Stock Exchange rules to which investment trusts already adhere.

The principal improvements to the original draft were to acknowledge and permit the structure of an investment trust, and to accept that holders did not have a right to demand a redemption of shares. The requirement for a separate depositary will remain a problem as will the requirement that the Trust is managed by a regulated manager. However, they did propose that more detail should be provided on the remuneration of the manager; a requirement that was not in the original Directive. There are still therefore fundamental areas of difference.

PARLIAMENTARY DRAFT

The EU Parliament produced its own amendments to the directive in November 2009. This draft was then subject to a consultation period during which over 1,700 amendments were tabled leading to a further draft in May 2010. This draft addresses many of the points made by Alliance Trust and other investment trusts. While Alliance Trust continues to believe that investment trusts should be exempted from the directive in its entirety, we support the revised Parliament draft rather than the draft proposed by the Council of Ministers because:

- It exempts investment trusts, by definition if not by name, from the more onerous requirements of the directive
- The additional regulatory requirements for the industry are more proportionate
- The responsibility for the interpretation of the regulations would largely be devolved to country level.

NEXT STAGE

A "Triologue" process began in May 2010 with the objective of reconciling the different drafts of the directive produced by the Council of Ministers, the EU Parliament and the original Directive. The intention was to finish the Triologue by July, so that the revision could then be voted on by the EU Parliament. This would then allow implementation in 2012.

CURRENT POSITION, AS AT 27 JUNE 2010

The European Parliament has decided to postpone the vote on the Directive until September 2010. This will allow more time for completion of the negotiations over outstanding areas of difference between the drafts.

QUESTIONS

If you have any questions or comments, then please email them to investor@alliancetrust.co.uk

Alliance Trust
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