If you cannot see our e-mail, please click here

arendt
arendt & medernach

Luxembourg newsflash

31 January 2017

Common principles for share classes in UCITS issued by ESMA

In the absence of a common EU framework for share classes of UCITS funds*, ESMA has identified diverging national practices as to the types of share classes that are permitted, ranging from very simple share classes (*e.g.* with different levels of fees) to much more sophisticated share classes (*e.g.* which may potentially have different investment strategies).

In order to ensure a harmonised approach across EU Member States, ESMA has issued an Opinion which sets out four high-level principles which a UCITS must follow when setting up different share classes:

> Common investment objective. Share classes of the same fund should have a common investment objective reflected in a common pool of assets. ESMA takes the view that hedging arrangements at share class level are not compatible with the requirement for a fund to have a common investment objective, with the exception of currency risk hedging.

> Non-contagion. UCITS management companies should implement appropriate procedures to minimise the risk of contagion between share classes. Derivative overlays used to hedge currency risk must be scaled and managed appropriately in accordance with a set of minimum requirements, including limitation of potential loss, counterparty risk limits, operational and accounting segregation and stress tests, in each case at share class level.

> Pre-determination. All features of a share class should be pre-determined before it is set up in order to allow the potential investor in the fund to gain a full overview of the rights and/or features attributed to his/her investment. This requirement does not limit the discretion of the UCITS management company as to the type of derivative instrument used to hedge currency risk or its operational implementation.

> Transparency. Differences between share classes of the same fund should be disclosed to investors when they have a choice between two or more classes. New and existing investors should be informed about the creation and existence of currency hedged share classes in a timely fashion, including updates in periodic reports, as ESMA takes the view that these share classes introduce counterparty and operational risk.

ESMA is of the view that share classes established prior to the Opinion and which do not comply with the above principles should be allowed to continue to operate. However, in order to level the playing field across the EU, these share classes should be closed

Contacts:

Michèle Eisenhuth,
Partner, Investment Management

Nicolas Bouveret,
Counsel, Investment Management and Private Equity & Real Estate

for investment by new investors within 6 months of publication of the Opinion (that is, by 30 July 2017) and for additional investment by existing investors within 18 months of publication of the Opinion (that is, by 30 July 2018).

The Opinion was published on 30 January 2017 and may be downloaded here. The Opinion follows two discussion papers previously issued by ESMA on the same subject in December 2014 and April 2016.

The Opinion is addressed to national competent authorities under the powers given to ESMA by Article 29(1) of Regulation No 1095/2010, which aims at building a common EU supervisory culture and consistent supervisory practices. We are currently liaising with the CSSF and ALFI to discuss the impact of the Opinion on Luxembourg UCITS.

We remain at your disposal for any further questions.

* The term “fund” should be understood to refer to a UCITS fund or one or more of its sub-funds. The term “share class” should be understood to refer to a class of shares or units of a fund.