



Webinar UCITS series - 5/8

UCITS Costs and Fees

Insight on the recent EU developments and regulators expectations on undue costs and potential impact in a UCITS environment



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UCITS Costs and Fees

Your contacts/speakers



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Where do we come from?

- UCITS Level 2 Directive (CSSF regulation 10-04)
- AIFMD level 2

Regulatory principle

2010
2013

2020
2022

- EU Commission report on cost and charges
- ESMA supervisory briefing
- ESMA CSA
- CSSF data collection
- CSSF report
- CSSF communiqué de presse
- CSSF ORC template

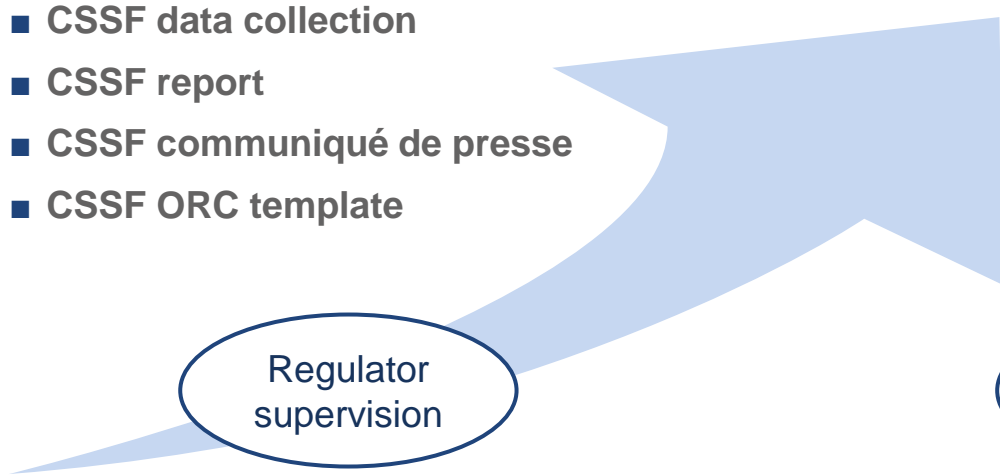
Regulator supervision

2023



- ESMA opinion

Re-inforced regulation



Regulator supervisory actions

Outcome of CSSF reviews in the context of the CSA



- Weak documentation of pricing process especially for smaller IFMs
- Over-reliance on delegated PM
- No consolidated pricing process but different procedures (e.g. FA control, internal control, KIID production, etc.)
- Absence of periodic review, lack of review of costs vs performance
- Attention to EPM
- Conflict of interest with related parties



1. IFM must define and implement a structured formal pricing process
2. Perform an **independent** analysis
3. Annual review process

Undue cost concept

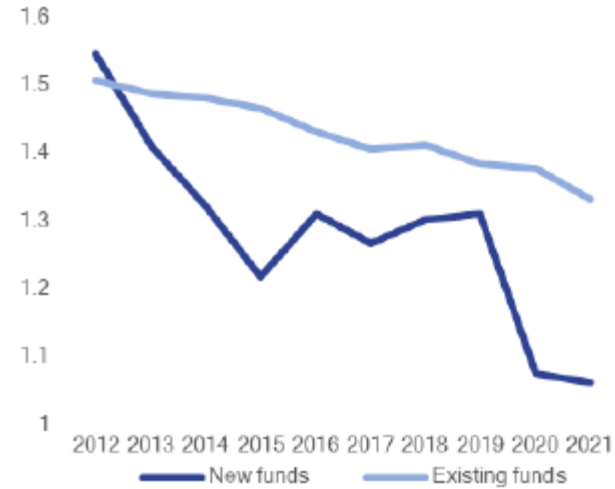
- **be consistent** with the investment objective and the characteristics of the fund
- **be linked to a service** provided in the **investor's best interest**
- **be proportionate** compared to market standards
- **be sustainable/viable** (perf/risk/cost/size)
- ensure investors' **equal treatment**
- **not be duplicated**
- Be clearly **disclosed**

Luxembourg market insight

1. CSSF question to board in respect of AUM size and costs
2. CSSF on site inspection (request for pricing policy and justifications for funds that are too small and too expensive)
3. Some funds identified to be too small or expensive have been liquidated (March 2023 +/-7)
4. Increase of CSSF questions during fund set-up and approval regarding fee levels or in case of fee increase and prospectus change
5. Other questions
 1. Allocation PM / advisor fee
 2. Special case - regarding the “Quantitative algorithms”

Interesting trends

ASR-CP.2
TER of new and existing funds
Pronounced decline in on going costs



Note: EU UCITS retail funds, total expense ratio (TER), new and existing funds, %.
 Sources: Refinitiv Lipper, ESMA.

Source: ESMA50-165-2357

ASR-CP.19
UCITS net performance and costs over one year
ESG funds outperformed in 2021

	ESG	Non-ESG
All funds (equity, bond and mixed UCITS)		
Costs	1.3%	1.4%
Net performance	22.8%	16.8%
Nb of funds	1,916	12,137

Source: ESMA50-165-2357

Interesting trends

Passive vs Active

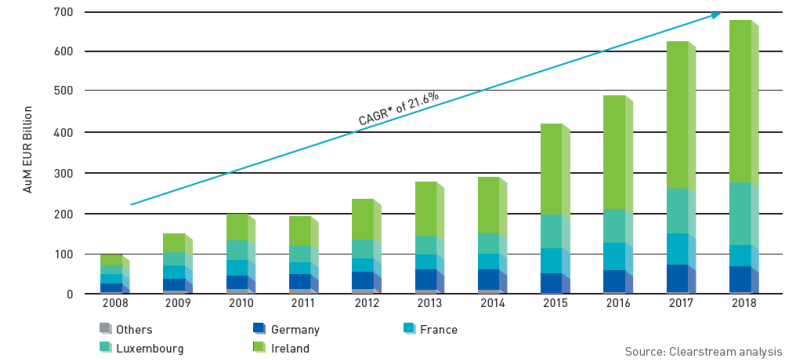
PASSIVE vs. ACTIVELY MANAGED EQUITY ASSETS: NET FLOWS OF U.S. STOCK MUTUAL AND EXCHANGE TRADED FUNDS

Sources: Morningstar; Note: Does not include money market funds



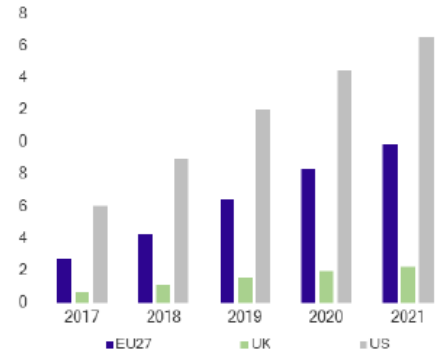
.....but do we have to oppose them?

Figure 1: Evolution of AuM for ETFs in Europe



ASR-CP.8

Number of neo-brokers users
Use of neo-brokers on the rise



Note: Number of customers (or accounts) of the selected region, millions per year. Neo-brokers exclude cryptocurrencies and robo-advisors.
Sources: Statista, ESMA.

Retail investors and Value-for-Money

Value-for-Money



ESMA has taken several actions to improve transparency across the EU

Novel approach in EU to defining, conceptualising and measuring the utility that investors can derive from investing in certain products

Defining and identifying well-designed and cost-efficient products, allowing consumers to seek higher returns and providing them with good value for the money they invest is crucial

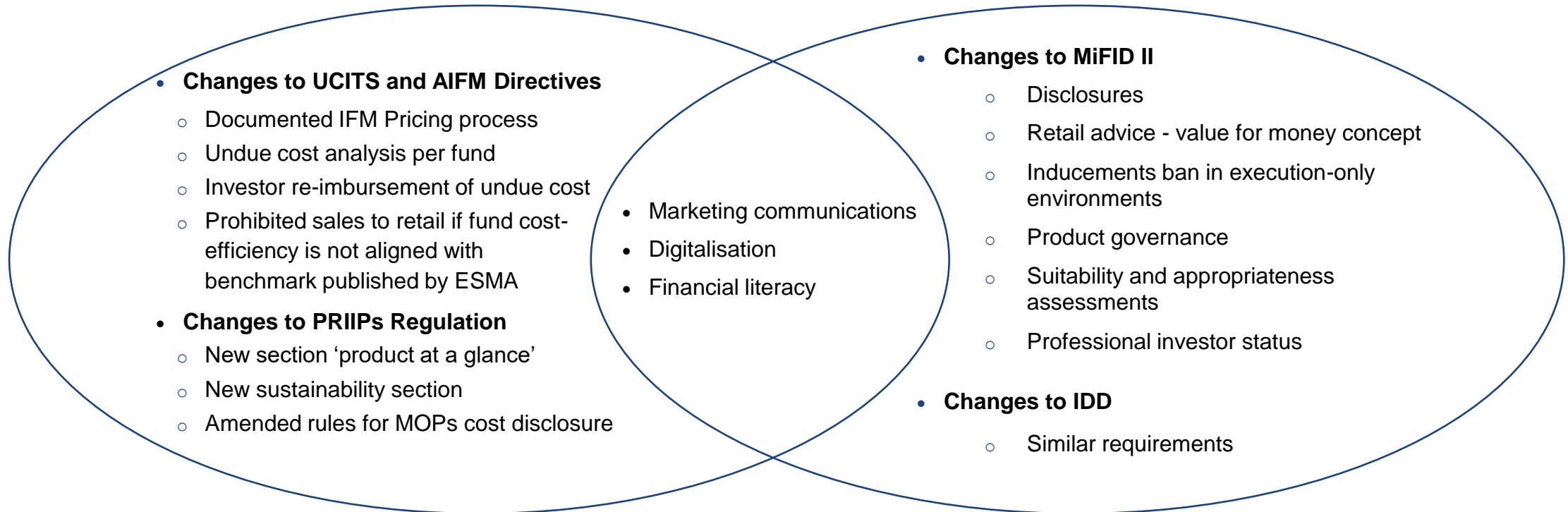
“Costs are, therefore, a particularly important factor to be aware of when investing.”

- Identification of UCITS with high costs (Data collection exercise @national level)
- Harmonisation of the way fund managers charge performance fees (ESMA guidelines)
- Identification of UCITS potentially engaging in closet indexing activities
- Common Supervisory Action (CSA) on costs and fees for investment funds (ESMA supervisory briefing) “Duty to prevent undue cost”

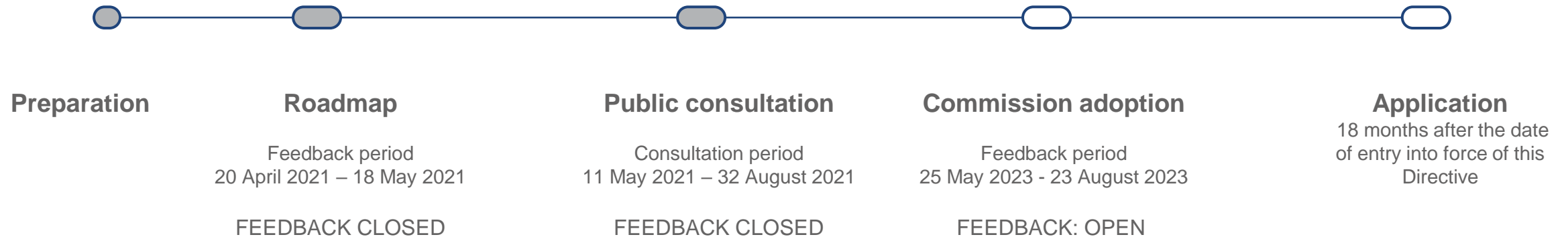
The EU Retail Investment Strategy package – at one glance

Product manufacturer

Product distributor



The EU Retail Investment Strategy package – timeline



https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13395-Retail-investment-new-package-of-measures-to-increase-consumer-participation-in-capital-markets_en

Undue cost definition



« White list »

Eu Commission Delegated act expected on list of **eligible costs** that can be charged to UCITS and AIFs

Cf. Annex VI of PRIIPS regulation?



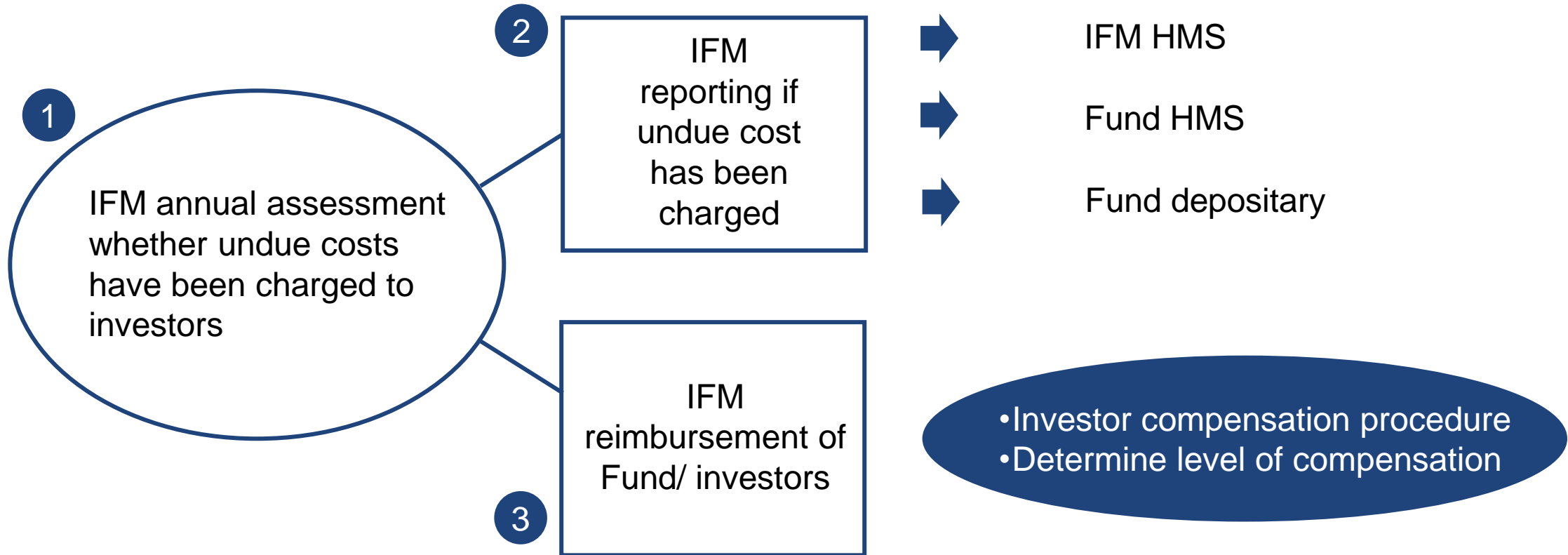
Pricing process

1 IFMS have to implement and document a structured and formalised pricing process

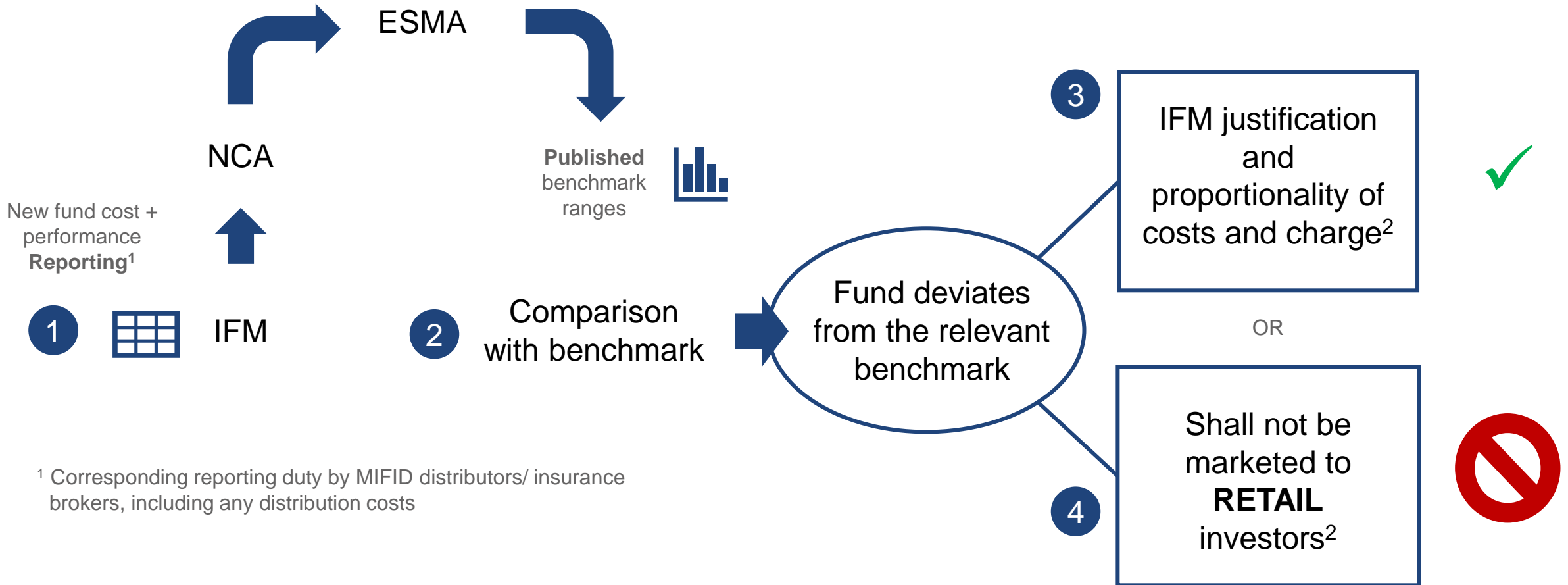
1. Policy document subject to periodic review
2. Evidencing management body involvement



Undue cost has been identified



Deviation from benchmark



¹ Corresponding reporting duty by MIFID distributors/ insurance brokers, including any distribution costs

² Corresponding equivalent provisions apply as well to MIFID firms and insurance companies

Public benchmark – what is not clear today

EFAMA “How quantitative benchmarks (to be developed at a later stage by ESMA) would work in practice is not yet clear.”

- Will benchmarking rely on simplistic or granular product categorisation?

EFAMA “Cost is only one of many measurements of value and that value means different things to different investors. There should be scope for other factors to be taken into account, like sustainability goals or income generation for instance. “

- Will active/ passive portfolio management criteria be considered to identify in which benchmark category you belong?
- Will the deviation detection be an annual process or is it required to implement additional ongoing routine controls?

Key Takeaways

■ Potential impact on the product range

- Urgency to conduct product cost-efficiency/ attractiveness analysis (documentation)
- Deal with too small funds
- Review product range if required
- Assess value of services to funds

■ Potential high impact on fund distribution

- Assess the impact on distribution model/network
- Identify potential alternatives to trailer fee system

Questions?



Your contacts/speakers



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