PRICEWATERHOUSECOOPERS assisted by external legal advisers in certain countries

Issue 7
May 2004

UCITS III News

Pan-European UCITS III Newsletter

**Three countries are clearly trailing behind the other Member States in respect of the implementation of the UCITS III directives locally. Belgium should complete the implementation process any day now, however the Netherlands and Greece still seem to be far from enacting their UCITS III laws.
On the contrary, almost all new joiners have shown their European motivation by passing primary legislation on time for the accession date of 1st May.**

The big news of the past two months is clearly the adoption by the EU Commission, on April 27, of the long awaited recommendations on the Simplified Prospectus ("SP") for UCITS and on the use of Derivatives.

Many countries had been eagerly awaiting the issuance of EU guidelines, to help them process the authorisation of new UCITS III funds and the corresponding legal documentation.

The following table, updated as at April 27, shows the status of specific regulation issued on these two topics by selected countries. A ☺ indicates specific regulation on the subject has already been issued and/or additional guidance is expected. A ☹ indicates that no regulation has been issued and/or none is expected, either because the existing regulation is deemed sufficient or for other reasons.

Supplementary Regulation	AUT	BEL	DEN	FIN	FR	GER	IR	IT	LUX	NL	POR	SP	SW	UK
Simplified Prospectus	☺	☹	☺	☺	☺	☹	☹	☹	☺	☹	☺	☹	☺	☹
Additional Guidance expected	☺	☺	☹	☹	☹	☹	☺	☺	☹	☺	☹	☺	☹	☺
Derivatives	☺	☹	☹	☺	☺	☺	☺	☹	☹	☹	☺	☹	☺	☺
Additional Guidance expected	☺	☺	☺	☹	☹	☺	☹	☺	☺	☺	☹	☺	☹	☹

Clarification on the SP

The EU recommendation clarifies five sections of Schedule C of the Profession Directive, which sets out the content of the SP. While underlining in the recommendation's preamble that it is critical for investor protection to ensure a common reading of Schedule C, the EU Commission recognises its limited powers in clarifying key aspects such as the definition of ratios relating to economic information (i.e. total expense ratio ("TER") and portfolio turnover rate ("PTR")).

Interestingly, countries that had already enacted rules in respect of the SP support the recommendation of the EU Commission. The preliminary Irish guidance note on SP is largely inspired from it and the French "Instruction" dated November 2003 also includes most of its elements. Luxembourg, that had already issued a Circular on the matter back in December, derogates to the EU text in that CSSF Circular 03/122 does not impose the inclusion of a TER or of a PTR in a SP.

It seems that some countries may now have to revise their regulations to conform with the EU recommendation, in particular on the disclosure of fee-sharing arrangements and soft commissions, both topics whose inclusion is not obvious at all from looking at Schedule C!

Unfortunately, the EU recommendation remains mute on the type of funds to which the SP applies (i.e. UCITS III only, grandfathered UCITS I funds?) and as from when. While it repeats in its preamble that the SP only needs a translation for cross-border registration, countries are already toying with the idea of requiring local investor-specific rules to be inserted in the SP. With different views on the date of first use of a SP, countries such as Spain, the UK and France have already forced promoters to issue a SP, while it was not required for locally domiciled funds!

Clarification on the use of financial derivatives

The EU recommendation on derivatives clarifies at least two open questions, regarding (i) the UCITS risk exposure and (ii) the applicable risk-measurement methodologies.

On the first issue, the recommendation confirms the understanding that the UCITS overall risk exposure may not exceed 200% of the NAV on a permanent basis. On the second, the EU recommendation validates the choice of certain countries like Germany and Ireland that had already issued guidance, in indicating that a distinction should be made for the determination of appropriate risk-measurement methods, between plain vanilla UCITS and "sophisticated UCITS". Only sophisticated UCITS would require the use of a Value-at-Risk (VaR), method whereas non-sophisticated UCITS could rely on a commitment method. An AMF consultation seems also to indicate that such distinction would be favoured by the French regulator.

The recommendation does not give a definition of a sophisticated UCITS, which may lead to differences between countries. As an example, the German "Derivateverordnung" provides that the use of only one sophisticated derivative will trigger the use of a VaR method, even if the fund as a whole remains rather "classic". The German industry itself is not too pleased with such a strict approach, which may lead German firms to look to more flexible domiciles when setting up their funds!

Another welcome clarification concerns the recognition of netting in the context of OTC derivatives and the reference to the procedures laid down in Directive 2000/12/EC relating to the taking up and pursuit of the business of credit institutions, which give useful guidance and should lead to a common position across EU members.

Finally, the recommendation confirms the flexibility in relation to cover rules to short-sales transactions with both listed and OTC financial derivative instrument.

Both the SP and Derivatives recommendations have no legal force as such, although the EU Court would certainly refer to them in case of a dispute. They politely request Member States to take steps towards implementing them no later than February 28, 2005, without having however any coercive powers.

More than their contents, it is what they do not cover that should worry fund promoters around Europe: with no guidance on passporting and grandfathering issues, regulators are starting to take a very restrictive attitude towards foreign funds. The French AMF now seems to refuse any new UCITS I sub-fund, whatever the date of its creation, and if a UCITS III fund has no real UCITS III ManCo, it may also be rejected. The BaFin may well follow this look-through approach. CESR, which has replaced the Contact Committee in its interpretation duties of the Directives, is meant to give an answer to these issues before year-end 2004. Until then … consider carefully your UCITS III transition!

For further information on this newsletter, please contact one of the following specialists:
Odile Renner European Coordinator, Luxembourg odile.renner@lu.pwc.com (352) 49 48 48-2615

Location	Contact Name	Company	Phone Number
Austria	Gerald Schwab	PricewaterhouseCoopers	(43) 1 501 88 37 25
Belgium	Koen Vanderheyden	Lawfort	(32) 2 710 78 59
Czech Republic, Slovakia	Martin Svalbach	PricewaterhouseCoopers	(420) 2 5115 2584
Denmark	Michael E. Jacobsen	PricewaterhouseCoopers	(45) 39 45 92 69
Finland	Karin Svennas	PricewaterhouseCoopers	(358) 9 22 801 801
France	Marie-Christine Jetil	PricewaterhouseCoopers	(33) 1 5657 8466
Germany	Robert Welzel	PricewaterhouseCoopers	(49) 69 9585 6758
Hungary	Marc-Tell Madl	Dezsö, Réti & Antall Law Firm	(36) 1 46 19 721
Ireland	Aidan Conlon	PricewaterhouseCoopers	(353) 1 704 87 58
Italy	Francesco Mantegazza	Pirola Pennuto Zei & Associati	(39) 02 66 995 505
Luxembourg	Odile Renner	PricewaterhouseCoopers	(352) 49 48 48 2615
Poland	Rafal Wyszomierski	PricewaterhouseCoopers	(48) 225 23 44 19
Portugal	Sofia Pereira	Ommea	(351) 21 79 14 225
The Netherlands	Frank van Groenestein	PricewaterhouseCoopers	(31) 10 400 8444
Spain	Gemma Moral	Landwell	(34) 91 568 4467
Sweden	Sussanne Sundvall	Ohrlings PricewaterhouseCoopers	(46) 85 553 32 73
Switzerland	Philipp Amrein	PricewaterhouseCoopers	(41) 61 270 57 18
United Kingdom	Roger Turner	PricewaterhouseCoopers	(44) 20 780 43 249

www.pwc.com/lu