*connectedthinking

PricewaterhouseCoopers

assisted by external legal advisers in certain countries

UCITS III News

Pan-European UCITS III Newsletter

Issue 11
May 2005

Following the final recommendations of CESR published in February 2005 regarding the transitional provisions of UCITS III, most European regulators have responded favorably to the proposed truncated deadlines as regards UCITS III transition. Having said this, some constraints with regard to cross-border distribution of UCITS are still pending such as the treatment of self-managed SICAVs (they were not included in CESR's recommendations!) and the contents of the simplified prospectus. In addition, CESR's recent consultation paper on eligible assets under UCITS III may lead to renewed divergence across the regulator population.

UCITS III transitional provisions and self-managed SICAVs

CESR's recommendations on transitional provisions of UCITS III only refer to products that are managed by a management company and, unfortunately, do not address the situation of self-managed SICAVs. This omission implies in particular that UCITS I SICAVs having launched a UCITS I sub-fund after 13 February 2002 are still in a grey zone: should they be compliant as regards their "substance" by 31 December 2005, 30 April 2006 or even 13 February 2007?

In addition, it appears that European regulators do not have a common position when considering the activities (and hence substance) of self-managed SICAVs. For example, the Italian authorities consider that a self-managed SICAV may not entirely delegate its functions (even if adequate monitoring procedures are in place) but should at least carry out itself a portion of the asset management process. Moreover, in case of a foreign fund, the SICAV's involvement in this process must be confirmed by a written attestation by the directors of the self-managed SICAV!

Similar interpretations seem to be emerging from other Member States, such as Spain, Germany and France, where activities of self-managed SICAVs (or, for that matter, UCITS III ManCos) should not be limited to merely controlling what third parties do.
This is clearly in contradiction with the position of other European regulators (such as UK, Luxembourg and Ireland) which allow for a full delegation of functions subject to, amongst others, existing measures enabling the managers to effectively monitor the activities of the delegates. As a result, the critical question is to know whether the passporting of self-managed SICAVs will be adversely impacted by varying interpretations.

The content of the simplified prospectus

Is the following information required for local simplified prospectus?	AT	BE	DE	DK	ES	FR	IR	IT	LU	NL	SE	UK
(1) Total Expense Ratio	Y	Y	Y	Y	Y	Y	Y	Y	N	Y	Y	Y
(2) Audited Total Expense Ratio	N	N	N	N	N	Y	Y	N	N	N	N	N
(3) Portfolio Turnover Rate	Y	Y	Y	Y	Y	Y	Y	Y	N	Y	Y	Y
(4) Fee-sharing	Y[1]	Y	Y[1]	N	N	Y	N	N	N	N	N	Y
(5) Soft commission	Y[1]	Y	Y[1]	N	N	Y	Y	N	N	N	N	Y

[1] Reference must be made to the full prospectus which must contain more detailed information.

The above table indicates that, to date, European regulators have not entirely followed the Commission's recommendations on the contents of the simplified prospectus (dated April 2004) as regards their local funds. Even if the TER and PTR seems to be required by all Member States (save for Luxembourg), information on fee-sharing arrangements and soft commissions are not commonly requested. In addition, France and Ireland are more stringent with regard to the TER, since the latter must also be audited.

Fortunately, these local divergences are not yet affecting the cross-border distribution of UCITS III products. According to our information, it would seem that regulators are not requiring visa-stamped simplified prospectus of foreign funds to observe their local rules.

Eligible assets and CESR's consultation paper

To assist the Commission in clarifying definitions concerning eligible assets for UCITS III products, CESR in March 2005 released a consultation paper, which in its current form is rather disconcerting for promoters.

Without necessarily focusing on the questions raised by the Commission, CESR proposes to confer to transferable securities six additional conditions to the current requirement of being an instrument as indicated in article 1 (8) of the Directive and being listed. These conditions are to be applied to any transferable security to be acquired by a UCITS fund, be it under the form of a structured financial instrument, one falling under the 10% limit of article 19 (2) (a) or a listed closed-end fund.

If the CESR advice were to become final in its current form…:

- Then Belgium, Austria, Ireland and France would no longer be able to use the 10% limit of art 19 (2) (a) of the Directive as they do today, since the advice provides explicitly that only transferable securities/money market instruments meeting these six conditions, but nonetheless not listed, fall under this ratio.
- Luxembourg, Ireland and UK can no longer treat any listed closed-end funds as listed transferable securities, as the advice imposes conditions on the type of eligible closed-end funds which de facto excludes any vehicle not closely resembling a "closed-end UCITS"!

But the biggest surprise could come from the interpretation given in connection with derivatives. A strict reading of CESR's advice for consultation, shared by many people on the market, is that derivatives must be used only if (i) the underlying is an eligible asset and (ii) only for the purpose of "efficient portfolio management". Moreover, transactions must be economically appropriate and entered into only for reducing the risks and/or the cost and/or for generating additional capital or income for the UCITS with an acceptably low level of risk. In other words, derivatives, even if now an eligible asset, can still only be used as under UCITS I, i.e. as a technique for the purpose of efficient portfolio management. How can this be reconciled with the wish of the industry for "real" derivative funds, where derivative instruments would be used as an investment strategy?

We are now seeing the first examples of local regulators refusing registration of foreign UCITS III funds as a result of differing interpretations of eligible assets.

The consultation period on its advice ends 10 June 2005. We expect (hope that) the level of industry response will be quite high!

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	Emmanuelle Attout	PricewaterhouseCoopers	(32) 2 710 40 21
	assisted by Koen Vanderheyden	Lawfort	(32) 2 710 78 59
Czech Republic	Zenon Folwarczny	PricewaterhouseCoopers	(420) 2 5115 2580
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	Wojciech Andrzejczak	Landwell	(48) 22 523 44 62
Portugal	Sofia Pereira	Ommea	(351) 21 79 14 225
The Netherlands	Martin Eleveld	PricewaterhouseCoopers	(31) 20 568 43 17
Spain	Enrique A. Fernández Albarracín	Landwell	(34) 91 568 45 04
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

This document is issued solely for informative purposes. It should not be considered as an advice and should not be relied upon to make business decisions.

© 2005 PricewaterhouseCoopers. All rights reserved. PricewaterhouseCoopers refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.