

Central Bank publishes new UCITS regulations – effective 1 November 2015



Background

In January 2014, the Central Bank of Ireland issued a consultation document (CP77) on the publication of a new UCITS Rulebook to replace the UCITS Notices and Guidance Notes. The final outcome of the consultation is the issuance of new regulations, rather than a UCITS Rulebook.

The new regulations consolidate into one location all of the requirements which the Central Bank imposes on UCITS, their management companies and depositaries. The publication of the new regulations marks a significant milestone for the Central Bank as it is the first time it has issued investment fund rules in the form of Central Bank regulations. The Central Bank believes that new regulations will bring additional clarity and certainty to investment fund providers as to what is required of them.

The new regulations – SI No. 420 of 2015 Central Bank (Supervision and Enforcement) Act 2013 (Section 48(1) (Undertakings for Collective Investment in Transferable Securities) Regulations 2015 – have binding legal effect and include a number of important changes notably in relation to:

- The end of the requirement for a UCITS to have a promoter
- The Central Bank no longer publishing a list of permitted markets for a UCITS
- Additional financial report filing requirements to the Central Bank
- Requirements on depositary
- Requirements on collateral
- Redemption gates
- Short positions
- New organisational requirements
- Impact on existing funds.

Changes to the Promoter requirement

The new regulations put an end to the requirement for a UCITS to have a promoter. Instead the Central Bank will rely on the regulatory regime for UCITS management companies and on the obligations of directors of these management companies where a UCITS fund gets into financial difficulties.

Permitted Markets

UCITS are currently permitted to invest in securities and/or derivatives that are listed on regulated stock markets, and the Central Bank published a list of those markets that it considers are in compliance with UCITS regulations.

The new regulations mean that from November 1st 2015 the Central Bank no longer maintains a list of permitted markets – instead the onus is placed on UCITS management companies to ensure that the markets in which the UCITS invests comply with the requirements of the new UCITS regulations. A depositary must also confirm that it can provide safekeeping of the assets in the stock exchange selected by the UCITS management company for the listing of the fund.

Financial Reporting

Until now management companies and depositaries are required to submit management accounts for the first six months of the financial year and audited accounts for the full year to the Central Bank. The new regulations introduce an additional financial requirement – as well as management accounts for the first six months management accounts for the second six months of the financial year must also be submitted to the Central Bank. The requirement for full-year audited accounts remains.

Requirements on Depositary

New rules mean that as well as reporting “material” breaches of regulations to the Central Bank within four weeks, a depositary must now also report “non-material” breaches which remain unresolved for four weeks from the time the depositary becomes aware of the breach.

Requirements on Collateral

The new regulations address some concerns that the Central Bank had about how “high quality” collateral should actually be defined. This means that from November 1st when the quality of collateral is being assessed, its credit rating must be taken into account. This requirement to complete a credit assessment is an additional safeguard and deviates from the revised ESMA Guidelines on ETFs and other UCITS issues.

Where sovereign debt is held as collateral, the new regulations require that UCITS must receive securities from at least six different users and that no single issue should make up more than 30 per cent of the UCITS net asset value. This is in line with the revised ESMA guidelines.

Redemption Gates

Where a UCITS applies a redemption gate to limit redemptions from a fund, redemption requests which have not been fulfilled on the dealing day will not get priority on succeeding days but will be treated on a pro rata basis. This is a measure generally seen as safeguarding the interests of small investors.

Short Positions

Where a UCITS intends to take short positions, this must be disclosed in its prospectus in relation to each category of asset in which it intends to invest, whether the fund will take short and long positions and also the proposed allocation of its assets which will be held in long and short positions.

Organisational requirements

The new regulations set out strict organizational requirements for funds. Regulation 97 sets out clear prescriptive requirements for directors to ensure compliance with “every legal and regulatory requirement”. Regulation 98 creates the “organisational effectiveness” role and also requires that a board of a management company must adopt a statement detailing the responsibilities attached to the new managerial functions. These developments are significant, particularly as the Central Bank has indicated that a review of the quality of the board’s discussions is on its agenda for next year.

Impact on existing funds

There are some transitional provisions in the new regulations which apply to existing UCITS funds, specifically in relation to redemption requests (which apply from November 1st 2016) and the new organisational requirements (which apply from June 30th 2016). Also, if the prospectus needs to be updated to reflect the new regulations’ requirements on short positions then this should be done at the next update.

In general, however, the impact of the new regulations on existing funds are manageable. Nevertheless, given that the new regulations have statutory backing, UCITS management companies should be assessing their impact on the management of their funds, particularly where there have been previous derogations from the UCITS notices. In particular UCITS should assess whether these derogations have been built into the new regulations. If not, UCITS should have reapplied for the derogation before 1 November 2015.

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