

Share class structures and types of hedging allowed at this level

Regulatory news alert

[ESMA consults on different share classes of UCITS – The European Securities and Markets Authority \(ESMA\) 23/12/2014](#)

“ESMA has identified diverging national practices as to the types of share class that are permitted, ranging from very simple share classes (e.g. with different levels of fees) to much more sophisticated share classes (e.g. with potentially different investment strategies). Therefore, ESMA sees merit in developing a common understanding of what constitutes a share class of UCITS and of the ways in which share classes may differ from each other.

ESMA will take into account the feedback from stakeholders with a view to establishing a common position on the use of share classes by UCITS”

[In this discussion paper](#), ESMA states principles that should be used in assessing the legality of different share classes:

- Share classes of the same UCITS should have the same investment strategy
- To offer new investment strategies, management companies should create new UCITS

ESMA also confirms existing market practices:

- Features that are specific to one share class should not potentially impact other share classes of the same UCITS
- Differences between share classes should be disclosed to investors when they have the choice between two or more classes

ESMA has identified the following non-exhaustive list of types of share classes that would **not** be compatible with the principles:

- Exposed to different pools of underlying assets
- If the same underlying portfolio is swapped against different portfolios of assets which would create different exposures
- Different degrees of protection against some market risks such as interest rate risk or volatility risk
- Difference in level of capital protection and/or payoff
- Difference in level of leverage

According to the wording, even if specific share class structures frequently met on the market are missing from the descriptions, the acceptance matrix of hedging structures would be as follows:

Type of Share Class Hedging	Allowed by ESMA	Reason	Motivation
Standard NAV FX Hedging	Yes	Produces “same results of the investment strategy”	Section 9
Look-Through FX Hedging	Yes	Not directly mentioned but produces “same results of the investment strategy” even if share class currency can be the same than the portfolio currency	Section 9
Double and Triple-Decker	No	Not directly mentioned but new exposures to exotic high interest rate currencies are created: principle of a common investment strategy would not be respected anymore	Section 10 Point 2
Duration Hedging	No	Interest rate hedging “does not comply with the principle of having the same investment strategy because it modifies the investment strategy of the share class”	Section 11
Delta Hedging / Market Hedging / Smart Beta	No	Not directly mentioned but this market hedging would not comply with the principle of having the same investment strategy because it modifies the investment strategy of the share class. In addition, it might also create some capital protection which would not be allowed at share class level.	Section 10 Point 1 & 4

The deadline for the ESMA’s consultation on this topic is scheduled for 27 March 2015.

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