

Regulatory News Alert

ESMA Opinion on UCITS share classes

1 February 2017

Following the last consultation paper on UCITS share classes published in April 2016, ESMA introduced on 30 January 2017 an [Opinion paper](#) on this topic with an applicable framework for UCITS share classes.

This Opinion states high-level guidelines and new operational principles on the following:

1. Common investment objective

- Hedging arrangements at share class level are not compatible with the requirement for a fund to have a common investment objective with the exception of currency risk hedging.

2. Non-contagion

- Costs and materialization of risks generated by the currency hedging should be monitored and only be allocated to the relative hedged share classes,
- A set of operational rules should apply:
 - Accounting segregation should be operationally in place to allocate the hedging contracts and their P&L for each NAV;
 - The UCITS management company should implement stress tests to quantify the impact of losses on all investor classes of a fund that are due to losses relating to share class-specific assets that exceed the value of the respective share class;
 - **The UCITS management company should monitor that hedging positions are at all time be within 95% of the portion of the NAV to hedge and 105% of the net asset value of the share class; and**
 - Hedging positions should be rebalanced at least monthly.

3. Pre-determination for all features of share classes

- All features of a share class should be pre-determined before the share class is set up. This will help investors gain a full overview on the rights and/or features attributed to his investment.

4. Transparency

- The information about existing share classes should be provided via the fund prospectus as part of the details of the types and main characteristics of the units;
- In regard to the share classes with a contagion risk, the UCITS management company should provide a list of share classes in the form of readily available information which should be kept current;
- The stress test results should be made available to national competent authorities on request.

With this paper, ESMA excludes duration, volatility and generally, all non-currency risk related hedging at share class level, as they might prove difficult to make compliant with the principles above.

By allowing a lower threshold of 95% of the portion of the NAV to be hedged, look-through currency hedging and benchmark currency hedging at share class level will still be allowed.

Even though UCITS management companies will need to implement a monitoring of the share class hedging, the Opinion does not limit the type of instruments to be used for the currency hedging.

The timeline for non-compliant existing share classes is set as per below:

- All share classes established before the publication of this paper that do not comply with the principles laid out should be closed to new investors as of the 30/07/2017.
- All share classes established before the publication of this paper that do not comply with the principles laid out should be closed to additional investment by existing investors by 30/07/2018.

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