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CESR The Committee of European
Securities Regulators
11-13 avenue de Friedland

75800 Paris
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Wien, am 31. Mai 2005

CESR´s Advice on Clarification of Definitions concerning Eligible Assets for Investments of UCITS (Consultation Paper)

Dear Sirs!

The Austrian Association of Investment Funds[1] (VÖIG) welcomes the opportunity to comment on "CESR´s Advice on Clarification of Definitions concerning Eligible Assets for Investments of UCITS (Consultation Paper)".

Re BOX 1 "Treatment of structured financial instruments"

Q 1: Do you agree with the approach to the treatment of transferable securities and structured financial instruments outlined in this draft advice?
VÖIG advocates that alternative investments (AI) should be considered eligible underlying assets for structured financial instruments. Therefore VÖIG asks CESR to clarify that alternative investments are considered eligible underlying assets for structured financial instruments (SFI) where these take the form of transferable securities.
Moreover, CESR should more clearly define the criteria listed in Box 1 that decide whether a security can be regarded as a transferable security. Practical examples should also be included to illustrate the various deciding factors.
As to the "liquidity" factor, so as to eliminate any differences that might distort competition, it will be necessary to find a consistent interpretation throughout the EU on whether the redemption of units - as provided in Art. 37 of the UCITS Directive - should be limited to the frequency as laid down in Art. 34 of the UCITS Directive or whether unit-holders may redeem their units on a daily basis.

Q 2: What would be the practical effect in your view if such an approach were adopted?
CESR should clarify that shares are not considered SFIs and that, for shares, a look-through approach is not required.

Re BOX 2 "Closed end funds as transferable securities"

[1] VÖIG represents the interests of the Austrian investment fund management industry. Its 23 members currently have 133 Mrd Euro assets under management. For more information please visit www.voeig.at.

VÖIG takes the view that there is no need for a separate "closed end fund" category as closed end funds are only permitted in the form of "transferable securities" (shares, as a rule) and thus need to meet the criteria listed in Box 1. It would be impossible to administer the regulation envisaged, as there is no definition of *"closed end funds"* as opposed to other shares. Closed end funds do not fall under the category of UCITS/UCIs nor of derivative financial instruments but should be treated like any other share. Above all, it will not be necessary to check in which instruments a closed end fund has invested, as, in general, there is no obligation to do this for shares.

Re BOX 3 "Other eligible transferable securities"
Q 7 Are there any practical difficulties in your experience in defining the boundary between Art.19 (1) (a) to (d) and Art. 19 (2) (a)? Do you consider the suggested approach in Box 3 as appropriate?
As already laid out above, closed end funds, by their nature, must be transferable securities to meet the requirements of Box 1; therefore, this falls within the scope of Box 1.

Re BOX 6 "Art. 19 (1) (h)"
Investment funds also invest in money market instruments from issuers who, being regular issuers, are granted certain privileges in accordance with Section 3 of the Austrian Capital Market Law. As, according to the Austrian Capital Market Law, they do not need to provide a prospectus, these instruments would not meet the criteria in Box 6 and would therefore be excluded.
For this reason VÖIG suggests dropping the three requirements concerning the information memorandum, if the EU Prospectus Directive (Directive 2003/71/EC) does not require the publication of a prospectus for money market instruments.

Re BOX 11 "Embedded derivatives"
1. VÖIG is of the opinion that credit linked notes, convertibles and all other structured financial instruments with a fully guaranteed nominal capital do not qualify as structured financial instruments that fall under the provisions of Art. 21 (3) of the UCITS Directive. They are simply structured products whose portfolios are not put at much greater risk by their derivative components. Separating these financial instruments from their host contracts bears no additional benefit for the investor; there is no need or only a negligible need to further safeguard these products against risks. The overall risk limits envisaged in the UCITS Directive would suffice. Also the Austrian National Bank supports this view that convertibles are not regarded as structured products, and it is not recommendable or in some cases even impossible to separate them from their host contracts (http://www.oenb.at/de/img/Structured_Products_HB_tcm14-16320.pdf).

2. Often the percentage of structured financial instruments in portfolios is very small or negligible. With regard to an efficient portfolio management, and given that separating a derivative from its host contract does not have any additional benefit for the investor, and that there is no further need for investor protection, VÖIG recommends not to separate a derivative from its host contract provided that these structured instruments account for a minor percentage of the portfolio's total assets (these structured products must not bear any obligation to make further contributions). VÖIG thinks that this percentage of structured products should not exceed 10 percent of a UCITS's assets (de minimis rule). Up to this limit of 10%, the contribution of a derivative embedded in a structured product to a portfolio's overall risk profile can be ignored.
The view expressed in points 1 and 2 is in line with the idea of total management responsibility of investment companies for portfolios (an idea recently favoured by the competent supervisory authorities) and is supported by the statutory Code of Conduct. ("Liquid financial instruments may be acquired provided they are consistent with the investment objective and the risk profile of the respective portfolio.")

Re BOX 12 "Other collective investment undertakings"
The criteria listed in Box 12 under indents 2 to 7 and referred to as indicators of "equivalence of supervision" should really be called "equivalence of legal protection".
As provided in Art. 19 (1) (e) first indent of the UCITS Directive, it is not up to the investment company to decide on the equivalence of supervision (in contrast to the equivalence of legal protection), but this falls within the scope of responsibility of the competent authorities (*"..considered by the UCITS competent authorities to be equivalent to that laid down in Community law…").* It does not seem practicable that the supervisory authorities should approve every single portfolio.

Re BOX 14 "The eligibility of derivative instruments on financial indices"

It is VÖIG's view that not only financial indices based on eligible assets but also those financial indices that are based on alternative investments like commodities should be considered eligible underlying assets for derivatives. Art. 19 (1) (g) of the Directive correctly provides that a look-through approach is not necessary when considering derivatives on financial indices (index-based financial derivative instruments). Moreover the VÖIG is of the opinion that it should be possible to invest in derivatives on financial indices of commodities-based financial instruments as well as in derivatives on financial indices directly based on commodities.

Re BOX 15 "OTC derivatives"
In accordance with Art. 21 (1) of the UCITS Directive the investment company has to provide for a valuation procedure which enables the accurate and independent assessment of the value of a OTC derivative. The demand made by the CESR in Box 15, point 2, that the valuation of the OTC derivative should be reviewed by an "independent third party" needs clarification according to VÖIG (a review of the valuation by the UCITS's auditor should be considered sufficient).

Finally we want to point out that this view is also shared by the Austrian Circle of auditors responsible for Investment Funds auditing.

Yours sincerely

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