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PRESS RELEASE

CESR launches a second consultation on its draft advice to the European Commission on the eligible assets of UCITS

Having listened to the comments from market participants during the first round of consultations and following careful consideration, CESR publishes today a second consultation paper (Ref. CESR/05-490b) on its draft advice to the European Commission (Commission) regarding clarification of definitions concerning eligible assets for investments of UCITS. CESR therefore requests comments and reactions to its revised proposals and to the specific questions raised in the document by 21st November 2005 from both market participants and from retail investors. A public hearing will also be held in Paris at CESR's premises on 7th November to enable interested parties to express their views in person. CESR will submit its final advice to the European Commission by mid-January 2006.

CESR has worked to develop the draft advice on the basis of the results of the first consultation (Ref. CESR/05-064b, see also the press release Ref. CESR/05-172), on which CESR received more than 50 responses, mostly from asset managers and their associations. The first CESR consultation paper presented a proposed 'overall' approach to the substantive questions related to eligible assets. Amongst the responses, it was suggested by many consultation respondents that a distinction be made between possible comitology measures at Level 2 and issues that would need to be addressed at Level 3. The second consultation paper therefore makes a distinction between suggested comitology measures and other measures.

Furthermore, CESR has developed the advice on the basis of consultation responses especially regarding the following issues:

- **The liquidity of transferable securities:** A number of respondents to the first consultation questioned the CESR position on instrument liquidity and what a UCITS must do in assessing whether an individual transferable security is sufficiently liquid for the portfolio. The revised key proposal concerns the liquidity of the transferable security which must not compromise the UCITS' ability to comply with Art. 37 of the UCITS Directive, this requires that a UCITS "must re-purchase or redeem its units at the request of any unit-holder". Where a transferable security is admitted to trading on a regulated market the UCITS may consider such a security to be liquid unless the UCITS knows or ought reasonably to know that the security is not liquid. CESR advice now suggests a UCITS may buy or hold transferable securities of varying liquidities. However, where the portfolio contains a significant number of less liquid securities, the UCITS must keep the situation under appropriate review, to ensure continued compliance with Art. 37.
- **The eligibility of closed end funds:** Respondents to the first consultation raised a concern that the wording of CESR's advice could rule out UCITS investing into closed end real estate funds. CESR is of the opinion that the revised requirements will allow for UCITS to invest into these kind of funds.
- **The valuation of money market instruments - amortization:** Respondents to the first consultation raised a concern that the wording of CESR's advice could rule out money market funds using the so-called amortization method. The revised draft advice clarifies that fulfilling the criteria that has been developed, the valuation systems can be based on market data or, on valuation models and include systems based on amortised cost methodology.



- **The eligibility of derivative instruments on financial indices:** The asset management industry, through the comments received to the first consultation, expressed a strong interest in allowing derivatives on financial indices based on non-eligible assets. In CESR's view, indices based on financial derivatives on commodities may be eligible provided they comply with the criteria of the draft advice.
- **Index replicating UCITS:** In the first consultation CESR asked feedback on whether its advice should require UCITS to provide an estimate of the quality of the index replication. On the basis of responses, CESR notes that a standardized method of calculation for the assessment of the quality of replication by UCITS would enhance competition between index funds and improve the quality of products accessible to retail investors. CESR considers that in the first place this should be achieved by industry action. CESR therefore calls for the professional associations to develop such a method of standardization, taking into account the regulations already in force in some Member States in this area.

The Commission originally asked CESR to deliver its technical advice by the end of October 2005. Nevertheless, following requests from consultation respondents for the possibility of a second consultation, given the difficult nature of this exercise and the interests involved, CESR requested an extension of the deadline for its advice to enable this second round of consultation to take place. As such, the European Commission extended CESR's deadline for this mandate from the end of October 2005 to mid-January 2006.

The adoption of implementing legislation on eligible assets of UCITS has been included into the list of priority actions in the Commission Green Paper on the enhancement of the EU framework for investment funds, published 14th July 2005.



Notes for Editors:

1. Preparation of CESR's advice on this mandate is being undertaken by the CESR Expert Group on Investment Management, which is chaired by Mr Lamberto Cardia, Chairman of the Italian securities regulator, the Commissione nazionale per le società e la Borsa (CONSOB). A permanent member of the CESR Secretariat, Mr Jarkko Syyrilä assists the Chairman and acts as Rapporteur of the Expert Group.
2. Furthermore, a consultative working group composed of 16 market practitioners and consumers has also been formed to provide technical advice to the Expert Group on Investment Management. The market participants are experts in different fields of investment management drawn from across the European markets. They are not intended to represent national or a specific firms' interest and do not replace the important process of full consultation with all market participants. For a full list of the individuals, please visit the page dedicated to Investment Management on the CESR website.
3. **Background on eligible assets:** In the context of the implementation of the so-called UCITS III Directive (Directive 85/611/EEC as amended by Directives 2001/107/EC and 2001/108/EC), the issue of whether, or to what extent, some financial instruments could be considered eligible investments (i.e. "eligible assets") for a UCITS to invest in has arisen. In particular, the definitions of "transferable securities" under Art. 1 (8), of "money market instruments" under Art. 1 (9) and the list of authorised investments under Art. 19 has caused some difficulties of interpretation.
4. Ensuring consistent implementation and interpretation of EU legislation across the Member States is a crucial dimension of the building up of the internal market in financial services. The European Commission has therefore identified the need to clarify certain definitions of eligible assets of the UCITS Directive as short term priority for the implementation of the amendments made by Directive 2001/108/EC of 21 January 2002 to the UCITS Directive. This approach was endorsed at the European Securities Committee meeting of 5th July 2004.
5. In view of this, DG Internal Market indicated that it intends to make use of the delegated powers conferred by Art. 53a of the UCITS Directive to the Commission, to clarify some of the definitions pertaining to eligible assets which are contained in the UCITS Directive. In its preparation of possible draft comitology instruments, the Commission requested technical advice of CESR by publishing a mandate to CESR on 28th October 2004: "The Formal Mandate to CESR for Advice on Possible Modifications to the UCITS Directive in the Form of Clarification of Definitions concerning Eligible Assets for Investments of UCITS".
6. For further information please contact:

CESR

Fabrice Demarigny
Secretary General of CESR

or Victoria Powell
Information Officer

Tel: +33 (0)1.58 36 43 21
Fax: +33 (0)1.58 36 43 30
Email: secretariat@cesr-eu.org
Web site: www.cesr-eu.org

Indicative CESR work plan on the clarification of definitions of the UCITS Directive (Updated following the extension of the deadline for CESR's advice)

