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UK UCITS and
regulated funds



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General introduction to UCITS schemes

UCITS are open-ended collective investment vehicles which comply with the requirements of the UCITS Directive. The purpose of the UCITS Directive is to facilitate the cross-border marketing within the European Union of open-ended investment funds which are available to the general public, while incorporating certain investor protection mechanisms. The UCITS Directive thus establishes common basic rules for the authorisation, supervision, structure and activities of UCITS schemes in the European Union.

A UCITS scheme must be authorised by the Member State in which it is established. Once it is authorised, the scheme may then be promoted in every other Member State, provided it complies with the local marketing regulations, without needing further re-authorisation.

Conditions

In order to qualify as a UCITS scheme a fund must meet the following conditions:

- (i) The sole object of the fund must be to invest capital collected from the public in transferable securities and other liquid assets based on the principle of risk spreading;
- (ii) Units or shares issued by the fund must be directly or indirectly redeemable out of the fund's assets at the request of the unitholders/shareholders i.e. a UCITS fund must be open-ended; and
- (iii) The head office of the fund must be situated in the same Member State as the registered office.

Exclusions

The following types of funds are not UCITS schemes:

- Closed-ended funds.
- Funds not directly available to the general public.
- Funds sold only in non-Member States.
- Funds investing in physical assets such as property or commodities.

Investment restrictions

The UCITS Directive imposes several restrictions on the investment policies of a UCITS scheme, including:

- (i) In general, it may invest no more than 10% of its assets in transferable securities or approved money-market instruments which are issued by any single body and all holdings in excess of 5% of its assets may not, in aggregate, exceed 40% of the assets.
- (ii) No more than 20% of scheme property may be in transferable securities or approved money-market instruments issued by entities in the same group.
- (iii) No more than 20% of assets may be invested in any one single collective investment scheme (both UCITS and non-UCITS schemes) with a general restriction of a maximum of 30% of assets invested in non-UCITS schemes.
- (iv) Maximum over-the-counter counterparty exposure is limited to 5% (10% in the case of approved banks).
- (v) No more than 20% of assets may be invested in a combination of transferable securities and approved money-market instruments issued by, and deposits or OTC derivative transactions made with, a single body.
- (vi) No more than 35% of assets may be invested in the government or public securities of a single body (subject to (vii) below).
- (vii) Over 35% of scheme property may be invested in a single government or public securities body, but there is a restriction that



no more than 30% of the scheme property consists of securities of any single issue and a requirement that the securities must come from at least six different issues.

UCITS IV

The general aim of UCITS IV (in force with effect from 1 July 2011) was to increase economies of scale and reduce costs for UCITS investors by introducing an improved regulatory environment to increase cross-border efficiencies while enhancing choice, transparency and investor protection. In addition, the range of UCITS funds has been widened to include some alternative fund products.

Key Features

- **Key Investor Information Document (KIID).** A standardised two page document with pre-determined key headings and minimum technical content.
- **Management Company Passport.** A UCITS domiciled in one Member State can be managed and distributed and administered by a Management Company authorised and supervised in another Member State to facilitate cross-border management.
- **Cross-border Mergers.** A harmonised framework for cross-border mergers of investment funds to facilitate the consolidation of fund ranges.
- **Master-feeder Structure.** Master feeder structures can be used to facilitate asset pooling from local market UCITS feeder funds.
- **Simplified Notification Process.** The home regulator has 10 days to transmit the filing, reducing the previous notification from 2 months to 10 days.

UK UCITS

UCITS schemes in the UK can be established in the form of an authorised unit trust or as an open-ended investment company (or OEIC). Contractual schemes (also known as “tax transparent funds” (TTFs)) have also been introduced in the UK pursuant to UCITS IV, as

the Financial Services and Markets Act 2000 (“FSMA”) does not provide for authorisation of TTFs (see further below).

Authorised Unit Trust

This is a unit trust which has been approved by the FCA as being suitable for general promotion and sale to the public in the UK under section 243 of FSMA. An AUT is a collective investment scheme for the purposes of FSMA and unitholders must be entitled to have their units redeemed at a price relating to the NAV of the property to which the units relate.

The manager of the scheme and the trustee (which must be separate entities) apply to the FCA for an authorisation order. The application must contain such information as is reasonably required for the purpose of determining the application and additional information may be required after the application has been made.

Authorisation may be granted by the FCA if:

- A satisfactory application has been made (in accordance with section 242 of FSMA).
- The scheme complies with the trust scheme rules and scheme particulars rules made under sections 247 and 248 of FSMA (i.e. the rules in the FCA’s Collective Investment Schemes sourcebook (COLL)).
- A copy of the scheme particulars and the trust deed has been sent to the FCA accompanied by a solicitor’s certificate stating that the trust deed complies with regulations as to its contents under section 243(1) of FSMA.

The scheme must also meet certain other requirements which are set out in section 243 of FSMA. The application process generally takes between 4 – 6 weeks. Upon authorisation, a certificate will be issued by the FCA stating that the scheme complies with relevant conditions.

Consequences of authorisation

- (i) An AUT scheme is subject to COLL on an ongoing basis and to sections 242 to 261 of FSMA.



- (ii) An AUT scheme may be promoted and sold to the public in the UK subject to compliance with COLL and the FCA's Conduct of Business sourcebook (COBS) (to which the manager will usually be subject).
- (iii) AUTs are exempt from UK capital gains tax but do pay UK tax on their income.

Principal documentation required

- A trust deed between the manager and the trustee.
- A prospectus, which must comply with the detailed content requirements set out in COLL.
- The solicitor's certificate referred to above.
- If the AUT is also authorised as a UCITS scheme, a simplified prospectus which is a mandatory disclosure document for UCITS schemes. This must be given to retail clients prior to investment, subject to certain exceptions.

Authorised open-ended investment companies (OEIC) or ICVCs

An authorised OEIC is established in the UK under a corporate code which is almost entirely separate from the Companies Act 2006 and which can be promoted and sold to the general public in the UK. It is still not possible to establish an unauthorised OEIC in the UK.

The OEIC Regulations provide the legal framework for OEICs in a similar way that FSMA does for AUTs. COLL provides the detailed rules for OEICs as an investment product.

Application for authorisation is made to the FCA by submitting an application form, together with a fee, and drafts of the various documents. If the FCA is satisfied with the application, the FCA will issue a certificate of incorporation and the OEIC comes into existence at this point.

In common with the AUT, an OEIC is a collective investment scheme for the purposes of FSMA and shareholders redeem their shares at a price relating to the NAV of the property to which the shares relate.

Unlike an AUT, OEICs are bodies corporate and have a separate legal personality. The OEIC owns its portfolio of investments and shareholders in an OEIC simply own shares in a company and have no beneficial interest in the underlying portfolio.

Directors and Depositary

An OEIC must have at least one director, although additional directors are allowed. A sole director, or one particular member of the board, will have special responsibilities as the authorised corporate director (ACD). The ACD must be an authorised person under FSMA. In essence, the ACD runs the day-to-day operations of the OEIC and where the ACD is the sole director, this means that it will also be the manager. Almost all OEICs have only one director which is the ACD.

OEICs are obliged to entrust their assets to a depositary for safe keeping. The depositary must be independent of the OEIC and of its director(s), including the ACD. The depositary must also be an authorised person under FSMA.

The legal ownership of an OEIC's portfolio will be vested in the Depositary, or its nominee. Unlike an AUT, however, the beneficial interest in the portfolio will be vested in the OEIC itself and not the OEIC's shareholders.

Consequences of authorisation

- (i) An OEIC is subject to the OEIC Regulations and COLL on an ongoing basis.
- (ii) An OEIC may be promoted and sold to the general public in the UK subject to compliance with COLL and COBS (to which the ACD will usually be subject).
- (iii) An OEIC, like an AUT, is exempt from UK tax on its capital gains, but does pay tax on its income.

Principal documentation required

- An instrument of incorporation (similar to the trust deed for the AUT), which must comply with the content requirements set out in the OEIC Regulations.
- A prospectus, which must comply with the



content requirements set out in COLL.

- A solicitor's certificate stating that the instrument of incorporation complies with the OEIC Regulations as to its contents.
- Material contracts between the OEIC and each of the ACD and the Depositary.
- If the OEIC is also authorised as a UCITS scheme, a simplified prospectus which is a mandatory disclosure document for UCITS schemes. This must be given to retail clients prior to investment, subject to certain exceptions.

Tax transparent funds (TTFs) or authorised contractual scheme (ACS)

Established under the Collective Investment in Transferable Securities (Contractual Scheme) Regulations 2013, authorised contractual schemes, or tax transparent funds as they are more commonly known, came into force on 6 June 2013. ACSs are intended to offer a UK tax transparent vehicle that can compete to win an appropriate share of European pooled funds; both Luxembourg and Ireland have already introduced such structures, which were formally known as the *Fond commun de placement* (FCP) and the Common contractual fund (CCF).

Contractual schemes may take one of two forms, namely a co-ownership scheme or limited partnership scheme and may be established as UCITS, non-UCITS retail schemes (NURS) and qualified investor schemes (QIS) (that is, any one of the three categories of authorised fund defined by the FCA).

The authorised fund manager of the scheme applies to the FCA for an authorisation order. The application must contain such information as is reasonably required for the purpose of determining the application and additional information may be required after the application has been made.

Authorisation may be granted by the FCA if:

- A satisfactory application has been made (in accordance with section 261C of FSMA).
- The scheme complies with the rules in

COLL (i.e. the authorised fund manager and the depositary must be independent body corporates, must be authorised persons with appropriate permissions and the manager must pass the FCA's fitness and proprietary test).

- A copy of the scheme particulars and the contractual scheme deed has been sent to the FCA accompanied by a solicitor's certificate stating that the scheme complies with regulations as to its contents under section 261H of FSMA.

The scheme must also meet certain other requirements which are set out in section 261 of FSMA. The application must be determined by the FCA within 6 months of receipt, or 2 months if the ACS is a UCITS. Upon authorisation, a certificate will be issued by the FCA stating that the scheme complies with relevant conditions.

Consequences of authorisation

- (i) An ACS is subject to COLL on an ongoing basis and to sections 242 to 261 of FSMA.
- (ii) An ACS may only be promoted and sold to a professional ACS investor (i.e. a professional client), a large ACS investor (i.e. makes a payment or contributes property of no less than £1 million) or an existing ACS investor. Further, where the ACS is a QIS, units may only be issued to a person who is an eligible investor for the purposes of COLL 8 Annex 1R.
- (iii) Units may only be transferred to those categories set out in (ii) above.

Principal documentation required

- (i) In the case of a co-ownership scheme
 - Form 261C.
 - Contractual scheme deed between the manager and the depositary, which must comply with the detailed content requirements set out in COLL.
 - A prospectus, which must comply with the detailed content requirements set out in COLL.
 - The solicitor's certificate referred to above.



- A model portfolio.
 - If the ACS is also authorised as a UCITS scheme, a KIID which is a mandatory disclosure document for UCITS schemes. This must be given to retail clients prior to investment, subject to certain exceptions.
- (ii) In the case of a limited partnership scheme
- Form 261C.
 - Certificate of partnership registration
 - Partnership deed between the general partner as manager (although it can delegate the management function) and the limited partners, which must comply with the detailed content requirements set out in COLL.
 - A prospectus, which must comply with the detailed content requirements set out in COLL.
 - The solicitor's certificate referred to above.
 - A model portfolio.
 - If the ACS is also authorised as a UCITS scheme, a KIID which is a mandatory disclosure document for UCITS schemes. This must be given to retail clients prior to investment, subject to certain exceptions.

An ACS is a collective investment scheme (CIS or fund) that is taken to be tax transparent under which income and gains accrue to the investors directly as they arise. HM Treasury expects such contractual schemes to be attractive vehicles for UCITS master funds (which are recognised under UCITS IV). Tax transparency means that, for direct tax purposes, investors are treated as if they had invested directly in the underlying assets and are subject to tax accordingly.

**This document is for general guidance only. It does not constitute advice.
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42 Brook Street, London W1K 5DB +44 20 7585 1406 | Neuhofstrasse 3d, CH-6340 Baar +41 41 544 5549

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