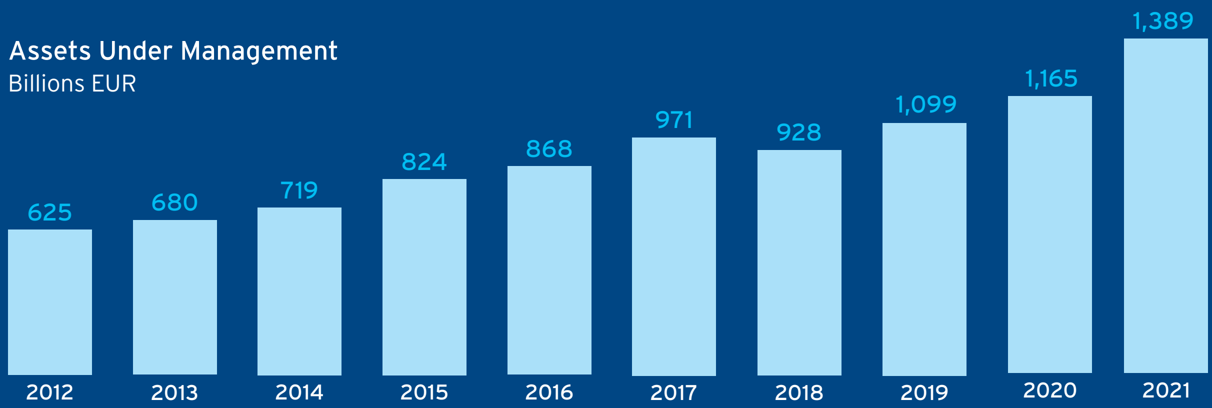
How to Launch a UCITS Fund

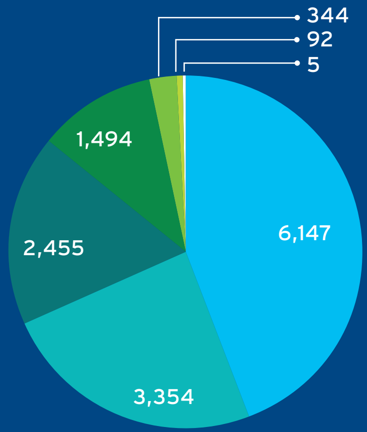
Securities Services

UCITS at a Glance

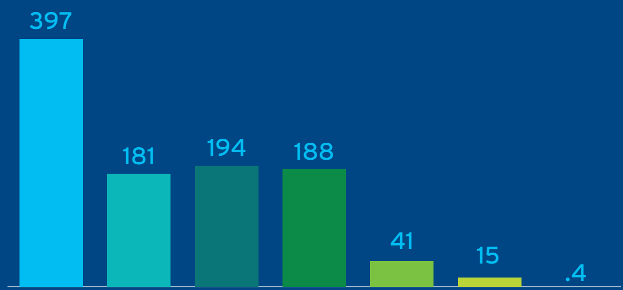
Assets Under Management
Billions EUR



Asset Classes
Billions EUR



Net Sales
Billions EUR



Equity Bond Multi-Asset Money Market Other Absolute Return Guaranteed

Source: EFAMA (as of 31 December 2021)

So You Want to Launch a UCITS?

Europe's Undertakings for Collective Investment in Transferable Securities (UCITS) framework has evolved from a European fund product to become the preeminent global cross-border fund vehicle. With over €13 trillion in assets and distributed in over 80 countries, UCITS is the go-to option for asset managers looking at global fund distribution and is a trusted brand with regulators and investors.

The harmonized regulatory framework allows managers to create a cross-border platform to sell their funds to retail and institutional investors worldwide in a scalable and cost-efficient manner.

This playbook will help you understand the key elements of the framework and important considerations you should think about when launching a UCITS fund.

Fund Structure

The UCITS framework provides a range of fund structures to choose from that offer the flexibility needed to establish your cross-border platform.

Umbrella Fund

A single legal entity that is comprised of separate sub-funds with different investment policies that, in effect, operate as individual funds. There is segregated liability between the sub-funds, meaning the assets and liabilities of the individual sub-funds are separated from each other.

Multiple-Class Fund

A fund or sub-fund with different class of units of the same fund that may have different characteristics such as fees, base currency, or distribution policies.

Fund of Funds

A fund that invests into other UCITS funds, with no more than 20% invested in any one UCITS fund.

Master-Feeder Fund

A fund that invests exclusively into another UCITS fund. The feeder has at least 85% of its assets invested in another UCITS, with the remaining 15% of its assets invested in ancillary liquid assets.

Evolution of the Framework

Since its introduction, the UCITS framework has evolved to meet the needs of investors and asset managers. Like software updates, the core operating system remains, but each version of UCITS builds on the previous rules. The industry is now on its fourth iteration, which introduced new depositary rules and remuneration rules for asset managers in 2016.

UCITS

Foundation of pan-European market for open-ended funds is established

1987

UCITS 3

Management Directive

UCITS Passport for European distribution and simplified prospectus is created

Product Directive

Range of eligible investment asset classes is expanded

2003

UCITS 4

UCITS Passport Upgrades

Regulator-to-regulator notification procedure for fund approvals is streamlined

Management Company Passport

Management companies are given the ability to oversee funds on a cross-border basis

Key Investor Information Document (KIID)

The simplified prospectus is replaced with a prescriptive two-page document

Master-Feeder Fund Structures

The use of master-feeder structures is permitted

Fund Merger Regime

Framework for fund mergers is created

2011

UCITS 5

Depositary Regime

Stricter rules for safekeeping duties, delegation, and overall liability of the fund's depositary are introduced

Remuneration Policies

Prescriptive rules on fund manager pay, which include deferred compensation requirements are established

Sanctions Regime

Harmonized framework for fining firms in breach of UCITS rules is introduced

Whistle-Blowing

Procedures for reporting incidents to authorities are formalized

2016

Key Investment Rules

A hallmark of the UCITS framework is its focus on investor protection. UCITS funds have a number of investment restrictions designed to mitigate risk and ensure that funds invest in liquid securities. There are also specific manager remuneration rules that are designed to align a portfolio manager's risk appetite with that of the fund. These rules often differ from the rules of other domiciles, so it's important that managers understand the differences when considering a UCITS fund.

Cash/Deposit

No more than 20% of the Net Asset Value (NAV) can be invested in cash/deposits with the same credit institution.

Remuneration

At least 50% of the manager's variable remuneration must be paid in non-cash and at least 40% of it must be deferred for at least 3 years.

5/10/40

A maximum of 10% of UCITS net assets may be invested in listed securities and money market instruments issued by the same body. Exposures greater than 5% to single issuers may not exceed 40% of NAV.

Asset Eligibility

Direct investment in illiquid investments are prohibited including:

- real assets
- commodities
- private equity

Investments in non-UCITS funds is tightly restricted and investments in US ETFs is prohibited.

There can be no more than 5% exposure to a single over-the-counter derivative counterparty, with a 10% limit for certain credit institutions.

Short Selling

Physical short selling is not permitted.

Control Rule

A UCITS fund may not acquire more than the following limits:

- 10% of the non-voting shares of the same issuer
- 10% of the debt securities of the same issuer
- 25% of the units of the same UCITS funds and/or other funds
- 10% of the money market instruments issued by the same issuer

Key Regulators

The regulation of UCITS funds is driven at the European and local market level.

European Level

Any modifications to the UCITS framework go through the European legislative process that sees the European Commission, Parliament, and Council work together to create and agree on any changes. This process often involves multiple consultations that give the industry a chance to provide feedback on any proposed changes.

After new regulations are finalized, it is up to the European Securities and Markets Authority (ESMA) to draft the detailed rules that are used to implement the new regulations. ESMA is also responsible for overseeing European financial markets, increasing cooperation among national regulators, and ensuring harmonization of rules across Europe. ESMA has the power to provide guidance and introduce new rules, as long as doing so doesn't contradict any of the primary legislation.

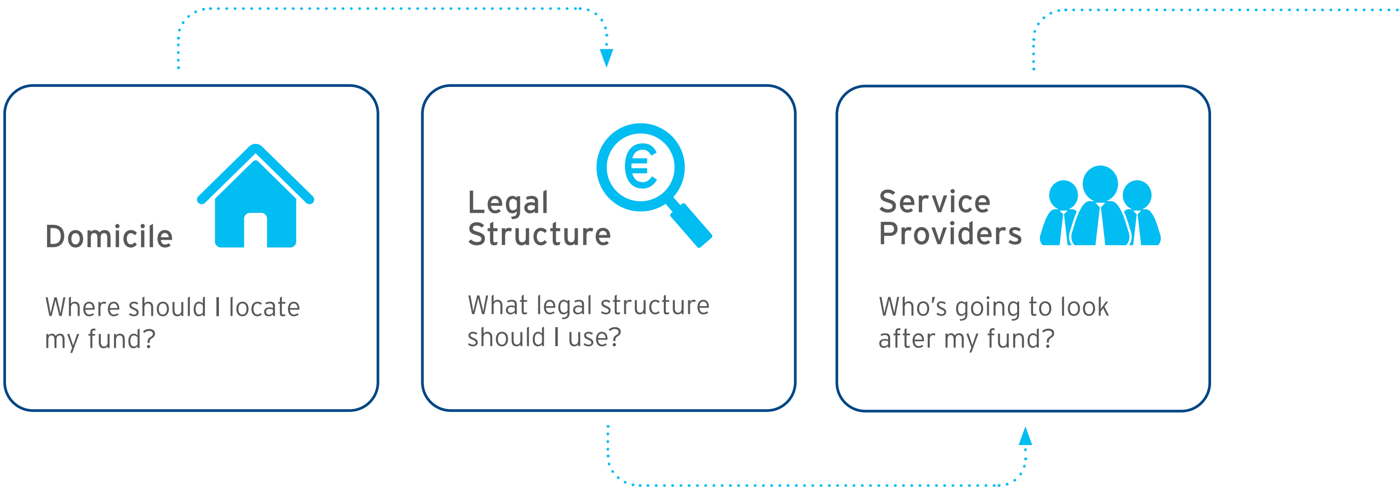
Local Market Level

The local regulators are responsible for implementing and enforcing European regulations along with overseeing the local fund markets, including authorizing new fund launches. They are also the prime regulator for the UCITS funds and asset managers. Key regulators include:

- The Central Bank of Ireland
- Commission de Surveillance du Secteur Financier

How to Launch a UCITS Fund

When launching a UCITS fund, there are a few initial decisions you'll need to make. Selecting your domicile, fund structure, and service providers needs to be done in order to receive authorization.



Documentation

What paperwork do I need to have in place?

Authorization

What do I need to get approved?

Launch

Domicile

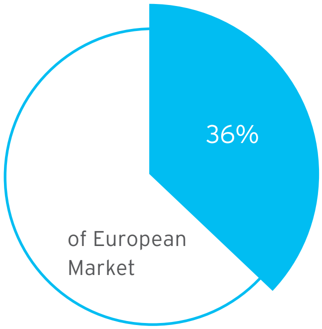
For firms pursuing a cross-border distribution strategy, there are two main domiciles: Luxembourg and Ireland. Between them, they account for nearly 60% of the UCITS market. Both have developed strong reputations as global fund hubs and have local ecosystems to support cross-border distribution.

When selecting which domicile to use, there are some key considerations:

- Distribution strategy and location of investors
- Native language(s) spoken in domicile and cultural alignment
- Ability to leverage relationships with current service providers
- Location of asset manager
- Legal system, i.e. Common vs. Civil Law

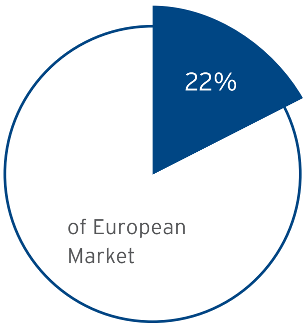
AUM
€4.9T

2021 Net Sales
€348B



AUM
€3.1T

2021 Net Sales
€237B



Source: EFAMA (as of 31 December 2021)

Legal Structure

The legal structure of the UCITS fund drives a number of factors such as the governance and contractual arrangements. Ultimately, the decision on legal structure comes down to a combination of distribution strategy, investor preference, and specific product requirements. Luxembourg and Ireland offer a variety of legal structures.

Luxembourg

Corporate

- **Société d'Investissement à Capital Variable** is an open-ended investment company with variable capital and is generally organized as a public-limited company (S.A.) or a European Company (S.E.).
- **Société d'Investissement à Capital Fixe** is an investment company with fixed-share capital.

Contractual

- **Fonds Commun de Placement** is a contractual arrangement with no legal identity that is managed by a management company.

Ireland

Corporate

- **Variable Capital Company** is an open-ended investment company structured as a public-limited company and subject to Irish company law requirements.

- **Irish Collective Asset-Management Vehicle (ICAV)** is a vehicle designed specifically for investment funds and has its own legislative regime, avoiding compliance with certain requirements in European and Irish company law. The ICAV can elect to check-the-box for US tax purposes.

Trust

- **Unit Trust** is an investment fund established under a trust deed between the management company and the trustee. The trustee acts as the legal owner of the fund's assets on behalf of the investors.

Contractual

- **Common Contractual Fund (CCF)** is a contractual arrangement established under a deed that allows investors to participate as co-owners of the assets of the fund. It's not a separate legal entity and it's transparent for Irish legal and tax purposes. The CCF can only be used for institutional investors.

Service Providers

In order to launch a UCITS fund, a number of service providers need to be appointed. All service providers must be located in the domicile of the fund and authorized by the local regulator.

Administrator

Responsible for day-to-day operational support to the fund and provides NAV calculation, maintenance of books and records, and financial reporting services.

Depositary

Provides asset safekeeping, income collection, corporate action processing, and fiduciary and oversight services.

Transfer Agency

Provides shareholder services to the fund; such as processing subscriptions and redemptions, shareholder account opening, and correspondence.

Management Company

Responsible for general investment management, administration, and distribution of the UCITS fund.

May retain all administration and portfolio management or can delegate these functions but must retain the oversight functions.

Others

Include legal advisors, auditors, tax advisors, corporate secretary, and listing agent.

Documentation

When establishing a UCITS fund, there are a number of documents that must be put in place. The fund's legal advisors should manage drafting and filing the documents with local regulators, along with any subsequent updates or changes.

- **Prospectus** contains the details to the fund's investment objectives and policies, risks, distribution policy, dealing procedures, expenses, valuation, and fund service providers.
- **Risk Management Process** articulates the funds policies for managing the fund's main risks, with a particular focus on derivative risk monitoring and calculation methodologies.
- **Business Plan** outlines how the fund will be governed and designates the individuals who will take on each of the specified management functions.
- **Custodian, Administration, and Investment Management Agreements** establish legal relationships and appoint key service providers to the fund.
- **KIID** is a two-page document using a set template that provides investors with key information, including: investment objective, risks, a risk/reward rating, and fees. The KIID is required to be translated into the official languages of all EU jurisdictions where the UCITS fund is sold.

Authorization

Before launch, all UCITS funds need to apply to the local regulator for authorization. The authorization submission must include all relevant application forms, the draft versions of the fund documentation, along with the proposed service providers. All directors of a fund must also be approved by the local regulator.

The application and all supporting documentation will be reviewed by the regulator and feedback on the application will be provided. This process will be repeated until the regulator is satisfied with the application. Firms should expect to go through several rounds of feedback before receiving final approval. Depending on the complexity of the fund, the process can take between 6-16 weeks.

How can we help?

Whether you're looking to establish a UCITS fund or grow an existing platform, Citi can help. Our offices in Luxembourg and Ireland offer a full range of fund services that provide a scalable platform and local expertise to support your cross-border ambitions.

Citi Securities Services supports the world's leading asset managers, institutional investors, and financial institutions. We provide a full suite of solutions in over 100 custody markets, including 64 proprietary branches, and 25 fund domiciles, including: custody, clearing, asset servicing, fund administration, ETF services, middle office, agency securities lending, collateral management, transfer agency, and fiduciary services. The combination of our global end-to-end service capabilities and Citi Velocity℠ Clarity, our industry-leading data and technology platform, enables our clients to futureproof and grow their business, while mitigating risks and reducing their infrastructure costs.

Let's Talk

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