COMMISSION OF THE EUROPEAN COMMUNITIES

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Proposal for a

EUROPEAN PARLIAMENT AND COUNCIL DIRECTIVE

AMENDING DIRECTIVE 85/611/EEC ON THE COORDINATION OF LAWS, REGULATIONS AND ADMINISTRATIVE PROVISIONS RELATING TO UNDERTAKINGS FOR COLLECTIVE INVESTMENT IN TRANSFERABLE SECURITIES (UCITS)

(presented by the Commission)

EXPLANATORY MEMORANDUM

1. INTRODUCTION

With the adoption of the UCITS Directive ([1]) in 1985 the first important step was taken toward co-ordinating the laws and regulations for certain collective investment undertakings. The Directive laid down provisions concerning the authorisation, supervision, investment policy and transparency requirements for UCITS ("undertakings for collective investment in transferable securities"). The main purpose of the co-ordination was to approximate the conditions of competition between UCITS at Community level and to ensure effective and uniform protection for investors. The Directive also introduced – for the first time in the financial sector- the principle of mutual recognition on the basis of which a UCITS authorised in its home Member State is permitted to market its units in other Member States without being subject to any further authorisation by host Member States.

The collective investment undertakings which, for the time being, are covered by the Directive are those of the open-ended type which promote the sale of their units to the public and the sole objective of which is to invest in transferable securities (e.g. essentially in listed shares and bonds). However at the time of adoption of the Directive there was a consensus that other types of collective investment undertakings should be harmonised at a later stage ([2]).

The Commission presented in 1993 a proposal amending the UCITS Directive the main aim of which was to extend the scope of the Directive to other types of collective investment undertakings. However, Member States failed to agree on a common approach. It was therefore necessary for the Commission to explore new solutions.

As highlighted by the Commission Action Plan for the Single Market which was endorsed by the European Council in June 1997, the sector of collective investment undertakings is one of the financial services areas in which the Single Market is still

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1 Council Directive 85/611/EEC of 20 December 1985 on the co-ordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), OJ N° L 375, 31.12.1985, p.3.

2 Sixth recital of the preamble of Directive 85/611/EEC.

incomplete. Existing barriers to a free cross-border marketing of units issued by such undertakings need urgently to be removed through further legislative actions which extend the Single Market benefits to other types of collective investment undertakings, while preserving a uniform minimum level of investor protection. For the completion of the Single Market in this area, the Action Plan also considered it necessary to introduce harmonised market access rules and operating conditions for management companies lacking for the time being – so as to ensure the level-playing field among operators in the financial services area.

The Commission has therefore prepared a package of measures distributed in two separate proposals: one ("proposal n° 1") focusing essentially on the "product" (the types of investment funds), the other ("proposal n° 2") focusing essentially on the "service provider" (the management company) and on prospectuses for UCITS. The separation of topics involving different problems could facilitate the negotiating process in the Council. It will not matter if one of the two Directives is adopted more rapidly than the other one.

Summary

The aim of proposal n° 1 is to remove barriers to cross-border marketing of units of collective investment undertakings through:

(a) the extension of the freedom to be marketed throughout the EU to collective investment undertakings investing in financial assets other than transferable securities such as: units of other collective investment undertakings; money market instruments; bank deposits; standardised options and futures contracts. New transparency requirements will ensure adequate information of investors;

(b) the revision of some other provisions of the UCITS Directive in order to up-date the Directive in the light of new portfolio management techniques which have been developed since 1985;

(c) the removal of interpretative uncertainties relating to a number of provisions of the UCITS Directive which hinder a uniform application of the Directive.

2. GENERAL CONSIDERATIONS

2.1. Member States and operators share the view of the Commission that the adaptation of the Directive to market developments can no longer be delayed. A wider co-ordination of investment funds at Community level, as envisaged in the 1985 UCITS Directive, will remove existing barriers to the free circulation across borders of units and will therefore represent an important step towards the creation of a fully integrated European Market in this area.

Recent discussions with the interested parties showed that the harmonisation of new types of "products" needs to be consistent with the basic principles of the UCITS Directive, which puts a special emphasis on investor protection, and that any solution moving away from them should be avoided. There is also general agreement that harmonised risk spreading rules and the rules concerning the UCITS depositary, though fundamental, are not sufficient to achieve investor protection; these rules need to be combined with rules ensuring an appropriate information of the investing public. Thus, the revision of the existing disclosure requirements for UCITS has been considered a further important step.

2.2. A number of provisions of the existing UCITS Directive are drafted in a somewhat imprecise manner which causes problems of interpretation of basic rules of the Directive. In order to facilitate a uniform understanding and application and to clarify the borderlines of the Directive, these interpretative uncertainties have to be urgently removed. Member States and operators share the view of the Commission that this measure is a pre-condition of the expansion of the scope of the Directive.

3. MAIN OBJECTIVES

3.1. The main objective of this proposal is to extend the scope of the UCITS Directive to other types of collective investment undertakings ([3]).

Essentially, the proposed approach is based on an extension of the investment possibilities for UCITS to liquid financial assets other than transferable securities.

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[3] It should be noted that the expression "UCITS" refers to two types of collective investment undertakings: common funds/unit trusts managed by a management company and investment companies.

According to the proposed solution, UCITS are permitted to invest also in: money market instruments; bank deposits, units of other collective investment undertakings of the open-ended type, standardised financial futures and options dealt in on regulated markets.

It is up to the UCITS to chose its own investment profile: whether to specialise in investments in a particular category of instrument ([4]) or economic sector or geographic area or whether to chose a combination of different types of investments.

Moreover, the proposal takes into account a widely adopted management technique for collective investment undertakings specialised in investments in shares (equity funds), based on the replication of stock-indices ([5]). In order to facilitate the replication of qualified stock-indices, the proposal introduces more flexible risk-spreading rules for investments in shares representing the underlying assets of such indices. This amendment would represent a further measure encouraging investments in equities; it may also favour the replication of sectoral stock-indices of pan-European shares.

In general, the extension of a EU passport to a wider range of collective investment undertakings will favour the development of cross-border activity and prompt beneficial effects since it will offer more opportunities to the European collective investment undertakings industry and a wider choice of investments to investors. The broadening of the scope of the UCITS Directive therefore represents a necessary step to create a fully integrated Single Market in the area of collective investment undertakings.

3.2. The aim of a second set of amendments of proposal n° 1 is to remove interpretative uncertainties relating certain provisions of the UCITS Directive which prevent a uniform understanding and application of basic rules of the Directive.

For that reason this proposal would:

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4 For instance, a UCITS could be specialised in investments in bank deposits (so-called cash fund) or in units of other collective investment undertakings (so-called fund of funds) or in financial futures and options (so-called futures and options fund) or in shares (so-called equity fund), etc.

5 The assets of such funds are invested in such a way as to reproduce the composition of the underlying assets of a certain stock-index. Thus, the weighting of each type of share in the fund's portfolio reflects the weighting of each such shares within the basket on which the index is based.

- introduce a definition of "transferable securities" (referring essentially to shares and securitised debt instruments). Moreover, taking into account existing regulatory solutions in Member States, it would make clear that "money market instruments" are types of "transferable securities";

- introduce minimum risk control measures with regard to some of the most relevant transactions which Member States allow UCITS to enter into for purposes of "efficient portfolio management". In particular, the proposal would regulate the use of financial derivatives, including over-the-counter derivatives, and securities lending transactions in which the UCITS acts as a lender;

- clarify that subsidiaries of investment companies – which are considered a part of the organisational structure of such types of UCITS – must normally be incorporated in a Member State.

3.3. Finally, the proposal would ascribe to the UCITS Contact Committee, set up by the UCITS Directive, comitology powers for the introduction of technical adaptations to that Directive. As to the procedural rules, it is proposed to make reference to a self-standing Directive, to be developed at a later stage.

4. Commentary on individual amendments

Amendment n° 1 - Article 1(2) (definition of UCITS)

This amendment announces that harmonised investment funds may invest, in addition to transferable securities, in certain other types of liquid financial assets (see amendment 3).

Amendment n° 2 - Article 1, new paragraph 8 (definition of transferable securities)

The concept of "transferable securities" may comprise different types of instruments. In order to ensure a clear understanding of this concept among Member States, this amendment clarifies which types of securities qualify as "transferable securities". The proposed definition, though based on that included in the Investment Services Directive (ISD), has been adapted to the needs of the UCITS Directive:

- the expressions "negotiable in the capital market" and "excluding instruments of payments" of the ISD definition have not been reproduced, because they were considered irrelevant (UCITS have to invest essentially in listed transferable securities; according to the amending proposal UCITS would be permitted to invest also in bank deposits);

- "money market instruments" are considered to be comprised in the category of "transferable securities" as they have characteristics similar to those of bonds and scuritized debt instruments. This solution takes into consideration the implementing legislation already adopted by most Member States. Moreover, considering the different classes of instruments negotiated on national money markets, it appeared desirable to leave to Member States the power to identify the instruments which fulfil the conditions for being considered eligible money market instruments for UCITS.

Amendment n° 3 - Article 19 (1) (other types of eligible investments for UCITS)

This amendment is the most substantial of the proposal, because it broadens the investment opportunities for UCITS (up to now UCITS were essentially permitted to invest in listed shares and bonds).

The amendment identifies some liquid financial assets, other than listed transferable securities, which also qualify as eligible investment for UCITS. The list includes: units of other UCITS, bank deposits, financial futures and options dealt in on regulated markets and non listed money market instruments issued by qualified issuers.

More comments on such investments will be given when providing comments to amendments n° 7, 8 and 9 which lay down the conditions under which UCITS may invest in these other instruments.

Amendments n° 4 and 5 - Articles 19, (2)(b) and (3), and 20

They refer to technical consequences of including money market instruments in the definition of "transferable securities".

Amendment n° 6 - Article 21 (use of financial derivatives and securities lending transactions)

Article 21 of the existing UCITS Directive permits UCITS to employ "techniques and instruments" for efficient portfolio management without further specification of the types of techniques and instruments.

Taking into account the new portfolio management and hedging techniques which have been developed since the adoption of the Directive in 1985 and the solutions already adopted by a number of Member States, this amendment is intended to make clear that – for purposes of efficient portfolio management – UCITS:

- may conclude transactions involving all sorts of financial derivatives, including derivatives not dealt in on regulated markets (over-the-counter derivatives) and
- notwithstanding Article 41 of Directive 85/611/EEC which prevents UCITS from granting loans, may act as lenders in securities lending transactions.

The conclusion of such transactions would be subject to the respect of some specific measures eliminating or reducing to an acceptable degree the risks involved with such transactions (i.e. counter-party risks).

Amendment n° 7 – new Article 22a (replication of stock-indices)

According to the existing Article 22, a UCITS may invest no more than 10% of its assets in securities issued by the same issuer.

Today a widely adopted management technique for UCITS investing primarily in shares (equity funds), is based essentially on the replication of the composition of certain stock-indices which represent a useful benchmark for such investments. The aim of this amendment is therefore to introduce more flexible risk-spreading requirements for investments in shares representing the underlying assets of qualified stock-indices which should facilitate the replication of such indices. Only indices complying with a number of pre-conditions, identified by the amendment, are considered to be replicable by UCITS. The compliance with such pre-conditions must be verified by the competent authorities of the Member State authorising such UCITS.

In order to inform supervisors and operators about the stock-indices which UCITS may replicate, the amendment would ensure a periodical publication in the Official Journal of the European Communities of the list of replicable stock-indices, to be drafted by the Commission on the basis of indications furnished by Member States.

Amendment n° 8 – Article 24 (investment in units of other UCITS)

Today UCITS may invest only up to 5% of their assets in units of other UCITS of the open-ended type.

This ceiling has been considered unnecessarily restrictive by Member States and the investment fund industry, considering that the investment in units of investment funds of the open-ended type is very liquid (such UCITS must redeem or re-purchase the units at the request of the unit-holder) and has generally proven profitable.

Taking into account market developments, the aim of this amendment is therefore to permit UCITS to invest – even all their assets - in units of other UCITS of the open-ended type, provided that minimum risk-spreading rules and transparency requirements are respected.

Amendment n° 9 – Articles 24a (investment in bank deposits) and Article 24b (investment in standardised futures and options)

- Article 24a

Today UCITS are not permitted to invest, as a part of their general investment policy, in bank deposits. UCITS may only hold "ancillary liquid assets", which means essentially cash and bank deposits at sight of an amount strictly necessary to enable payments to be made to unit-holders and representing funds which UCITS exceptionally hold after sales of securities and before their reinvestment.

The aim of this amendment is to remove the existing restriction for investments in bank deposits. As a consequence, a UCITS could chose to specialise in investments in bank deposits (so-called cash fund). Also for this type of investment certain risk-spreading rules and transparency requirements have to be respected. Moreover, only bank deposits complying with the general requirement of liquidity (see amendment n° 1) can be considered eligible for UCITS. Finally, in application of the existing principle of

independence between the depositary and the management company and in order to prevent conflicts of interest, the amendment would prevent UCITS holding deposits with their depositaries.

- Article 24b

Today UCITS are permitted to invest in derivatives instruments only for purposes of "efficient portfolio management".

This amendment is intended to permit UCITS to invest, as a part of their general investment policy, in standardised financial futures and options dealt in on regulated markets ensuring transparency, a high degree of liquidity and netting mechanisms which practically eliminate the counter-party risk.

The amendment lays down general criteria on how the exposure related to transactions on such instruments has to be covered and special transparency requirements.

Amendments n° 10 and 11 – Article 25 (2)

They refer to technical consequences of including money market instruments in the definition of "transferable securities".

Amendment n° 12 – Article 25, (3)(e)

Taking into account discussions with Member States, this amendment is intended to clarify that subsidiaries of investment companies (6) - which carry out on their behalf the business of management, advice or marketing - must normally be incorporated in a Member State. The reason is that such subsidiaries are considered a part of the organisational structure of such companies which, in order to ensure an effective supervision, has to be entirely located within the EU. This conclusion is confirmed by the principle laid in paragraph 3 (d) of Article 25, which identifies the exceptional cases in which UCITS may hold subsidiaries in third countries.

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6 Investment companies are a special type of UCITS constituted as companies having a variable capital, also obliged to redeem or re-purchase the shares at the investor's request. The investors are the shareholders of such companies.

Amendments n° 13, 14 and 15 – Article 26 (1), second subparagraph, Article 41 (2), Article 42

These amendments refer to technical consequences of broadening the investment possibilities for UCITS.

Amendment n° 16 – Article 53a (comitology)

This amendment would identify comitology powers to be exercised at a later stage by the UCITS Contact Committee set up by Article 53 of Directive 85/611/EEC. This will in due course facilitate technical amendments to be made to that Directive. For the UCITS Contact Committe to effectively exercise comitology powers, a further self-standing Directive will be needed.

5. Justification in the light of the principle of subsidiarity

5.1 What are the objectives of the proposed action with respect to the obligations placed upon the Community?

The objective is to complete the internal Market in the field of collective investment undertakings.

5.2 Is the action envisaged a matter of exclusive Community competence or one shared with Member States?

Considering that the main objective of this proposal is to ensure the free cross-border marketing of the units of a wider range of collective investment undertakings while providing a uniform minimum level of investor protection, only a binding Community Directive laying down agreed minimum standards can achieve the desired objectives.

5.3 What means of action are available to the Community?

Only a Community Directive laying down agreed minimum standards can achieve the desired objective.

5.4 Are uniform rules necessary?

Apart from the basic minimum standards (e.g. investment and risk-spreading rules, investor information, etc.) Member States are free to define in detail the regulation for collective investment undertakings covered by this proposal, prescribing possibly stricter or additional requirements. The scope left for national discretion is therefore large.

PROPOSAL FOR A EUROPEAN PARLIAMENT AND COUNCIL DIRECTIVE AMENDING DIRECTIVE 85/611/EEC ON THE COORDINATION OF LAWS, REGULATIONS AND ADMINISTRATIVE PROVISIONS RELATING TO UNDERTAKINGS FOR COLLECTIVE INVESTMENT IN TRANSFERABLE SECURITIES (UCITS)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION

Having regard to the Treaty establishing the European Community, and in particular Article 57(2) thereof,

Having regard to the proposal from the Commission ([1]),

Having regard to the opinion of the Economic and Social Committee ([2]),

Acting in accordance with the procedure laid down in Article 189b of the Treaty,

(1) Whereas the scope of Council Directive 85/611/EEC ([3]), as last amended by Directive 88/220/EEC ([4]) was confined initially to collective investment undertakings of the open-ended type which promote the sale of their units to the public in the Community and the sole object of which is investment in transferable securities (UCITS); whereas it was envisaged in the preamble to Directive 85/611/EEC that undertakings falling outside its scope would be the subject of co-ordination at a later stage;

(2) Whereas, taking into account market developments, it is desirable that the investment objective of UCITS is widened in order to permit them to invest in financial assets, other than transferable securities, which are sufficiently liquid;

(3) Whereas the definitions of transferable securities and money market instruments included in this Directive are valid only for this Directive and consequently in no way affect the various definitions of financial instruments used in national legislation for other purposes such as taxation; whereas, furthermore, the definition of transferable securities covers negotiable instruments only, normally dealt in on the capital market; whereas, consequently, shares and other securities equivalent to shares issued by bodies, such as building societies and

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1 OJ No C ....

2 OJ No C ....

3 OJ No L 375, 31.12.1985

4 OJ No L 100, 19.4.1988

industrial and provident societies, the ownership of which cannot in practice be transferred except by the issuing body buying them back, are not covered by this definition;

(4) Whereas money market instruments cover those classes of transferable instruments which are normally dealt in on the money market, for example treasury and local authority bills, certificates of deposit, commercial paper and bankers' acceptances; whereas Member States should have the option of choosing the list of eligible money market instruments on the basis of objective criteria to take account of the existing structural differences in the money markets of different countries;

(5) Whereas it is desirable to permit a UCITS to invest its assets in units of other collective investment undertakings of the open ended type which also invest in transferable securities and which operate on the principle of risk-spreading; whereas the requirement of risk spreading for UCITS investing in other collective investment undertakings is indirectly respected since such UCITS can only invest in units issued by collective investment undertakings complying with the risk spreading criteria of Directive 85/611/EEC; whereas, it is important that such UCITS adequately disclose to investors the fact that they invest in units of other collective investment undertakings;

(6) Whereas to take market developments into account and in consideration of the completion of the EMU it is desirable to permit UCITS to invest in bank deposits;

(7) Whereas, in addition to the case in which a UCITS invests in bank deposits according to its fund rules or instruments of incorporation, it may be necessary to allow all UCITS to hold ancillary liquid assets, such as bank deposits at sight and/or cash; whereas the holding of such ancillary liquid assets may be justified, for example, in the following cases: in order to cover current or unexpected payments; in the case of sales, for the time necessary to reinvest in transferable securities and/or in other financial assets provided for by this Directive; for a period of time strictly necessary when, because of unfavourable market conditions, the investment in transferable securities and in other financial assets needs to be suspended;

(8) Whereas, for prudential reasons, UCITS should avoid assuming an excessive concentration in deposits with a single credit institution;

(9) Whereas UCITS should be permitted to invest their assets in standardised options and futures contracts dealt in on regulated derivatives markets; whereas, in order to ensure that the risks involved are adequately covered, it is necessary that such UCITS hold at any time assets of sufficient value and of the right kind (i.e. securities, if the exposure is in terms of securities; cash or securities which are, or, on being turned into money in the right currency, if the exposure is in terms of money); whereas, such UCITS too have to operate on the principle of risk-spreading; whereas, considering that the value of the portfolio of such

UCITS may fluctuate widely, such UCITS should address only experienced investors or investors whose financial situation allows them to bear the risks involved in the investment in units of such UCITS; whereas the risks involved should be adequately disclosed to the investing public in the UCITS' prospectuses and in any promotional literature;

(10) Whereas new portfolio management techniques for collective investment undertakings investing primarily in shares are based on the replication of stock-indices; whereas it is desirable to permit UCITS to replicate well known and recognised stock-indices; whereas therefore it is necessary to introduce more flexible risk-spreading rules for UCITS investing in shares; whereas in order to ensure transparency of the stock-indices which the Member States consider to be replicable by harmonised UCITS and a wide acceptance of such indices, it is desirable to provide for adequate publication of the list of replicable stock-indices;

(11) Whereas the employment of techniques and instruments for the purpose of efficient portfolio management may never be permitted if they do not comply with the principles enshrined in the Directive and if they hinder the competent authorities from exercising effectively their supervisory functions;

(12) Whereas, considering the new portfolio management techniques which have been developed in recent years, it is desirable to permit UCITS to make use of all sorts of derivative instruments for an efficient portfolio management; whereas, in order to ensure investor protection, it is necessary to provide for a harmonised framework for the utilisation of financial derivatives and for an adequate cover for exposure deriving from such transactions; whereas, transactions on financial derivatives not dealt in on specialised derivatives markets (over-the-counter derivatives) involve counter-party risks; whereas therefore the counter-parties for such transactions shall be chosen only among qualified institutions approved by the UCITS' competent authorities;

(13) Whereas, notwithstanding Article 41 of Directive 85/611/EEC, it is desirable to permit UCITS to enter into securities lending transactions for the purposes of efficient portfolio management; whereas, in order to limit the risks involved in such transactions, it is necessary to regulate the conditions under which a UCITS may be permitted to act as a lender in securities lending transactions;

(14) Whereas collective investment undertakings falling within the scope of this Directive shall not be used for purposes other than the collective investment of the money raised from the public according to the rules laid down in this Directive; whereas, in the cases identified by this Directive, a UCITS may hold subsidiaries only when necessary to carry out effectively on behalf of that UCITS certain activities, also identified by this Directive; whereas it is necessary to ensure an effective supervision of UCITS; whereas therefore the establishment of a UCITS' subsidiary in third countries should be permitted only in the cases and under

the conditions identified in the Directive; whereas the general obligation to act solely in the interest of unit-holders and, in particular, the objective to increase cost efficiencies, never justify a UCITS undertaking measures which may hinder the competent authorities from exercising effectively their supervisory functions;

(15) Whereas the depositary of the assets of a UCITS carries out crucial controlling functions over the compliance of a UCITS with the law and its fund rules or instruments of incorporation; whereas therefore it is important to ensure an effective independence between the management company and the depositary; whereas when both the management company and the depositary belong to the same economic group or when the depositary has a qualifying holding in the management company's capital, or vice versa, or in all other cases in which the depositary may exercise a significant influence over the management company, or vice versa, it is necessary to undertake all measures assuring the independence between the two entities; whereas, when a management company, acting on behalf of the common funds or investment companies it manages, is permitted to enter into transactions with the depositary, arrangements have to be made preventing conflicts of interests and ensuring the compliance of the transaction with the law and the UCITS' fund rules or instruments of incorporation;

(16) Whereas, considering the depositary's liabilities towards the management company and the unit-holders and the complexity of its controlling functions, only institutions which have adequate financial resources and an adequate organisational structure and which are subject to prudential supervision should fall within the categories of institutions eligible to be depositaries;

(17) Whereas, considering the need to ensure the free cross-border marketing of the units of a wider range of collective investment undertakings, while providing a uniform minimum level of investor protection; whereas, therefore, only a binding Community Directive laying down agreed minimum standards can achieve the desired objectives; whereas this Directive effects only the minimum harmonisation required:

HAVE ADOPTED THIS DIRECTIVE :

Article 1 [5]

Directive 85/611/EEC is amended as follows:

1) In Article 1, paragraph 2, the first indent shall be replaced by the following:

"- the sole object of which is the collective investment in transferable securities and/or in other liquid financial assets mentioned in Article 19 of this Directive of capital raised from the public and which operate on the principle of risk-spreading."

2) In Article 1 the following paragraph shall be added:

"8. For the purpose of this Directive

(a) *transferable securities* shall mean:

- shares in companies and other securities equivalent to shares in companies,
- bonds and other forms of securitized debt,
- any other negotiable securities which carry the right to acquire any such transferable securities by subscription or exchange,

excluding the techniques and instruments referred to in Article 21;

(b) money market instruments, which, for the purposes of this Directive shall be regarded as transferable securities, shall mean those classes of transferable instruments normally dealt in on the money market which Member States consider to:

- be liquid, and
- have a value which can be accurately determined at any time or at least with the frequency stipulated in Article 34, excluding the techniques and instruments referred to in Article 21."

3) In Article 19 the following shall be added to paragraph 1:

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5 Changes compared with the text of the existing Directive 85/611/EEC are underlined.

"(e) *units of other collective investment undertakings within the meaning of the first and second indent of Article 1 (2)* ; and/or

(f) *deposits with credit institutions*; and/or

(g) *standardised financial-futures contracts*, including equivalent cash-settled instruments, dealt in on a regulated market mentioned in the previous subparagraphs (b) and (c); and/or

(h) *standardised options* to acquire or dispose of any instruments falling within this article, including equivalent cash-settled instruments, dealt in on a regulated market mentioned in the previous subparagraphs (b) and (c). This category includes, in particular, options on currency and on interest rates; and/or

(i) *money market instruments* which are not dealt in on a regulated market, unless the issue of such instruments is itself regulated for the purpose of protecting investors and savings, and provided that they are:

- issued by a central, regional or local authority, a central bank of a Member State, the European Central Bank, the European Union or the European Investment Bank, a non-Member State or, in the case of a Federal State, by one of the members making up the federation, or by a public international body to which one or more Member States belong, or

- issued by an undertaking any securities of which are admitted to official listing on a stock exchange or are dealt in on other regulated markets which operate regularly, are recognised and are open to the public, or

- issued or guaranteed by an establishment subject to prudential supervision, in accordance with criteria defined by Community law or by establishment which are subject to and comply with prudential rules considered by the competent authorities to be at least as stringent as those laid down by Community law."

4) Article 19, paragraph 2 (b) and paragraph 3 shall be deleted.

5) Article 20 shall be deleted.

6) In Article 21, the following paragraphs shall be added:

"3. In this context, a UCITS may carry out transactions in financial derivative instruments, also other than those mentioned in Article 24b, provided that the exposure relating to such instruments is covered according to the rules laid down in Article 24b.

If the UCITS carries out transactions in financial derivative instruments which are not dealt in on a regulated market (over-the-counter derivatives), the counter-parties to such transactions must be qualified institutions belonging to the categories approved by the UCITS' competent authorities .

4. Further, in the context of efficient portfolio management, a UCITS may enter into securities lending transactions in which it acts as a lender, provided that the following conditions are fulfilled:

a) securities lending transactions may be concluded only with a recognised securities clearing house or exchange; or with a counter-party which is an authorised person specialised in that type of transaction and subject to prudential supervision at Community level; or is a Zone A credit institution as defined in Directive 89/647/EEC or an investment firm as defined in Directive 93/22/EEC; or is a recognised third country investment firm which is subject to and complies with prudential rules considered by the UCITS' competent authorities to be at least as stringent as those laid down in Directive 93/6/EEC;

b) in relation to each securities lending transaction appropriate collateral shall be given covering the risk of default of the borrower. The value of collateral must be, during the entire period of the contract, at least equal to the total value of the financial instruments lent.

When a UCITS is permitted to conclude securities lending transactions with the depositary which performs for that UCITS the duties mentioned in Articles 7 and 14 of this Directive, the competent authorities shall ensure that the collateral is entrusted, during the entire period of the contract, with a third party custodian and that measures are undertaken preventing the depositary from using it."

7) The following Article 22a shall be inserted:

"Article 22a

"1. Without prejudice of the limits laid down in Article 25, the Member States may raise the limits laid down in Article 22 to a maximum of 35% for investment in shares issued by the same body when, according to the fund rules or instruments of incorporation, the aim of the UCITS' investment policy is to replicate the composition of a certain stock- index.

2. Replicable stock indices shall be indices which Member States consider to:

- have a composition which is sufficiently diversified;

- be easy to replicate;

- represent an adequate benchmark for the equity market to which they refer,

- be published in an appropriate manner.

3. Each Member State shall send to the Commission the list of stock-indices which they consider replicable by UCITS, together with details of the characteristics of such stock-indices. A similar communication shall be effected in respect of each change to the aforementioned list. The Commission shall publish the complete list of replicable stock-indices and updates thereto in the Official Journal of the European Communities at least once a year. This list may be subject to exchanges of views within the Contact Committee in accordance with the procedure laid down in Article 53 (4).

4. The UCITS fund rules or instruments of incorporation, its prospectuses and any promotional literature shall describe the characteristics of the replicated stock-index.

These documents shall also contain a prominent statement drawing attention to the fact that the aim of the UCITS' investment policy is to replicate a certain stock-index and that therefore it may invest a relevant part of its assets in shares issued by the same issuer."

8) Article 24 shall be replaced by the following

"Article 24

1. A UCITS may acquire the units of other collective investment undertakings within the meaning of the first and second indent of Article 1 (2), provided that it invests no more than 10% of its own assets in units of a single UCITS.

2. The Member States may raise the limit laid down in paragraph 1 to a maximum of 35%. However, in that case the UCITS must invest at least in five different collective investment undertakings mentioned in paragraph 1.

3. A UCITS may not invest in units of a collective investment undertaking within the meaning of the first and second indent of Article 1 (2), which invests more than 10% of its own assets in units of other collective investment undertakings.

4. Investment in the units of a unit trust managed by the same management company or by any other company with which the management company is linked by common management or control, or by a substantial direct or indirect holding, shall be permitted only in the case of a unit trust which, in accordance with its rules, has specialised in investment in a specific geographical area or economic sector, and provided that such investment is authorised by the competent authorities. Authorisation shall be granted only if the unit trust has announced its intention of making use of that option and if that option has been expressly stated in its rules.

A management company may not charge any fees or costs on account of transactions relating to a unit trust's units where some of a unit trust's assets are invested in the units of another unit trust managed by the same management company or by any other company with which the management company is linked by common management or control or by a substantial direct or indirect holding.

5. Paragraph 4 shall also apply where an investment company acquires units in another investment company to which it is linked within the meaning of the previous subparagraph.

Paragraph 4 shall also apply where an investment company acquires units of a unit trust to which it is linked or where a unit trust acquires units of an investment company to which it is linked.

6. The UCITS' fund rules or instruments of incorporation, its prospectuses and any promotional literature shall describe the characteristics of the other collective investment undertakings in the units of which the UCITS is authorised to invest.

These documents shall also contain a prominent statement drawing attention to the fact that the UCITS invests a part of or all its assets in units of other collective investment undertakings."

9) The following Articles 24a and 24b shall be inserted:

"Article 24a

1. Notwithstanding the provision laid down in Article 19(4), a UCITS may invest its assets in deposits with credit institutions furnishing sufficient financial and professional guarantees, provided that the UCITS places no more than 10% of its assets in deposits with the same credit institution or with credit institutions within the same group.

2. Member States may raise the limit laid down in paragraph 1 to a maximum of 35%. However, in that case a UCITS must invest in deposits with at least five different credit institutions. For the purpose of this rule, credit institutions belonging to the same group are considered to be one single institution.

3. The UCITS' fund rules or instruments of incorporation, its prospectuses and any promotional literature must include a prominent statement drawing attention to the fact that the UCITS invests all or a part of its assets in deposits with credit institutions.

4. Member States shall not permit UCITS to invest in deposits with a credit institution which performs for that UCITS the duties of a depositary mentioned in Articles 7 and 14.

Article 24b

1. Notwithstanding the provisions laid down in Article 21, a UCITS may invest, as a part of its general investment policy, in financial-futures contracts and options mentioned in Article 19, paragraph 1 (g) and (h), provided that the maximum potential exposure relating to the conclusion of each such derivative transaction is covered, during the entire period of the contract, by assets belonging to the UCITS of the right kind and sufficient in value.

2. The UCITS' fund rules or instruments of incorporation, its prospectuses and any promotional literature must include a prominent statement drawing the attention to the fact that the UCITS invests, as a part of its general investment policy, in the financial-futures contracts and options.

These documents shall also contain a warning that the investment in the units of such a UCITS is only suitable for experienced investors and for investors whose financial situation allows them to bear the risks involved in the investment in units of such UCITS."

10) In Article 25, paragraph 2, the following indent shall be added:

"- 10% of the money market instruments of any single issuing body."

11) In Article 25, paragraph 2, the second sentence shall be replaced by the following :

"The limits laid down in the second and fourth indents may be disregarded at the time of acquisition if at that time the gross amount of the debt securities or of the money market instruments, or the net amount of the securities in issue cannot be calculated."

12) Article 25, paragraph 3 (e) shall be replaced by the following:

"(e) shares held by an investment company in the capital of subsidiary companies incorporated in a Member State carrying on the business of management, advice or marketing exclusively on its behalf."

13) Article 26, paragraph 1, second sentence shall be replaced by the following:

"While ensuring observance of the principle of risk-spreading, the Member States may allow recently authorised UCITS to derogate from Articles 22, 22a, 23, 24, 24a and 24b for six months following the date of their authorisation."

14) Article 41, paragraph 2, shall be replaced by the following:

"2. Paragraph 1 shall not prevent such undertakings from acquiring transferable securities or other financial instruments mentioned in Article 19 (1) (e), (g), (h) and (i) which are not fully paid."

15) Article 42 shall be replaced by the following:

"Article 42

"Neither:

- an investment company, nor

- a management company or depositary acting on behalf of a unit trust

may carry out uncovered sales of transferable securities or of other financial instruments mentioned in Article 19 (1) (e), (g), (h) and (i)."

16) After Article 53 the following Article 53a is inserted:

"Article 53a

The technical modifications to be made to this Directive in the following areas shall be adopted in accordance with the procedure to be regulated at a later stage by a Directive amending this Directive:

- clarification of the definitions in order to ensure uniform application of this Directive throughout the Community;

- adaptation of the ceilings referred to in Section V and in Article 36(2) in order to take account of developments on financial markets, where such adaptations will not lead to stricter requirements for the UCITS;

- alignment of terminology on and the framing of definitions in accordance with subsequent acts on UCITS and related matters."

Article 2

1. No later than 30 June 2002 Member States shall adopt the laws, regulations and administrative provisions necessary for them to comply with this Directive.

These provisions shall enter into force no later than 31 December 2002 The Member States shall forthwith inform the Commission thereof.

When Member States adopt these provisions they shall include a reference to this Directive or accompany them with such a reference on the occasion of their official publication. The manner in which such references are to be made shall be laid down by the Member States.

Article 3

This Directive enters into force 20 days after the date of publication in the Official Journal of the European Communities.

Article 4

This Directive is addressed to the Member States.

Done at Brussels

For the European Parliament
The President

For the Council
The President

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