



IN THIS EDITION

Undertakings for Collective Investment in Transferable Securities (UCITS)

1. General

1.1 Definition and legal framework

Within the framework of the single European market, the European regime for undertakings for collective investment in transferable securities (**UCITS**) was launched by Directive 85/611/EEC dated 20 December 1985 relating to undertakings for collective investment in transferable securities (the **UCITS I Directive**), and was implemented in Luxembourg by the law dated 30 March 1988.

After the failure of a UCITS II Directive, European Directives 2001/107/EC¹ and 2001/108/EC² (the **UCITS III Directives**) amended the UCITS I Directive resulting in today's applicable UCITS III regime, implemented in Luxembourg by the law dated 20 December 2002 relating to undertakings for collective investments, as amended (the **UCI Law**) which supersedes the law dated 30 March 1988.

UCITS, which fall under the UCITS III regime, are known as "**Coordinated UCITS**" and are governed in Luxembourg by part I of the UCI Law.³ They are defined as entities:

- the sole object of which is the collective investment of savings;
- the investments of which are made in transferable securities and/or other specific liquid financial assets according to the principle of risk-spreading;
- which use savings raised from the public for the collective investment;

¹ Directive 2001/107/EC of the European Parliament and of the Council of 21 January 2002 amending Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions to undertakings for collective investment in transferable securities (UCITS) with a view to regulating management companies and simplified prospectuses.

² Directive 2001/108/EC of the European Parliament and of the Council of 21 January 2002 amending Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions for undertakings for collective investment in transferable securities (UCITS) with regard to investments of UCITS.

³ Other undertakings for collective investment are governed in Luxembourg by part II of the UCI Law or by the law dated 13 February 2007 relating to specialised investment funds.

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- which are marketed in at least one of the Member States of the European Economic Area;
- which are open-ended, i.e. the shares/units of which are freely redeemable upon the request of their shareholders or unit-holders; and
- the investment and borrowing policies of which comply with the criteria set out in part I of the UCI Law.

Coordinated UCITS are mainly governed in Luxembourg by the UCI Law, by Grand Ducal regulations and by the circulars issued from time to time by the Commission for the Supervision of the Financial Sector (*Commission de Surveillance du Secteur Financier* - the **CSSF**).

Additionally, and insofar as the UCI Law does not derogate from the law dated 10 August 1915 on commercial companies, as amended (the **Company Law**), UCITS formed as corporate entities are also subject to the general provisions applicable to commercial companies under the Company Law.

1.2 European passport

Coordinated UCITS benefit from a “European passport”. As a consequence, they may be distributed and marketed in other EU Member States upon simple notification to the regulatory authority of the country of distribution. The notification procedure requires Coordinated UCITS to provide an attestation issued by their home country regulatory authority and a notification letter to the host country regulatory authority under the standardised form defined by the Committee of European Securities Regulators (**CESR**). In addition, the constitutional documents, the full and simplified prospectuses and the annual report must also be provided in their latest version, and translated, if necessary.

This notification procedure was designed to be fast and cost efficient and to guarantee the right to market a Coordinated UCITS throughout the EU.

Investment funds which do not benefit from the European passport have to comply with local legal and regulatory provisions if they want to publicly

distribute their shares/units in other EU Member States. Consequently, they have to request the approval of the local regulatory authority under the host State’s specific registration procedure.

1.3 Listing

Shares/units issued by Coordinated UCITS are outside the scope of the Luxembourg law dated 10 July 2005 relating to prospectuses for securities (the **Prospectus Law**). Consequently, they can obtain admission on the Luxembourg Stock Exchange (**Lse**) on the basis of the prospectus issued under the UCI Law provisions without being required to issue a specific prospectus compliant with the Prospectus Law.

Shares/units issued by Coordinated UCITS are eligible for listing on the Lse according to the rules and regulations of the Lse and may be exempt from fulfilment of certain listing conditions.

2. FCP VS. SICAV / SICAF

Coordinated UCITS may adopt two legal forms: that of a common fund (**FCP**), which is similar to that of a common law unit trust, or a corporate form (i.e. an investment company with variable or fixed capital - **SICAV** or **SICAF**, respectively).

2.1 FCP

An FCP (*fonds commun de placement* – common fund) is an undivided pool of assets made up and managed according to the principle of risk-spreading on behalf of joint owners. An FCP has no legal personality. Investors are not shareholders but rather joint owners whose ownership interest in the FCP’s assets is represented by units. They are called “unit-holders” and are liable only up to the amount of their contribution to the FCP. They are only granted a limited right of decision as expressly set out in the management regulations governing the FCP. This fund type has no fiscal personality and is transparent for tax purposes.

The FCP is managed by a management company which is responsible for implementing the FCP's investment objectives and policies. The management company must act in the exclusive interests of the unit-holders as a whole.

The management company draws up the management regulations for the FCP and assumes the management of the FCP's assets. The management regulations set out the rights and obligations of the unit-holders, the management company and the depository bank.

An FCP must have at least EUR 1,250,000 of net assets to be reached within six months of its approval by the CSSF.

2.2 SICAV / SICAF

SICAV (*société d'investissement à capital variable* – investment company with variable capital) and SICAF (*société d'investissement à capital fixe* – investment company with fixed capital) are corporate entities that have legal personality. They must be set up before a Luxembourg notary.

The investors are shareholders of the investment company and, consequently, have the right to vote and make decisions within the framework of the Company Law and of the articles of association of the SICAV / SICAF. The SICAV / SICAF may appoint a management company or may designate itself as self-managed. In this case, the board of directors appointed by the general meeting of shareholders is responsible for implementing the investment objectives and policies of the SICAV / SICAF.

The minimum share capital of a SICAV / SICAF is EUR 1,250,000 to be reached within six months of its approval by the CSSF.

2.2.1 SICAV

The UCI Law provides that a SICAV must be incorporated in the form of a public limited liability company (*société anonyme*).

The share capital of a SICAV is at all times equal to the value of its net assets. No formalities are

required for the increase or decrease of a SICAV's share capital.

2.2.2 SICAF

The UCI Law permits a SICAF to adopt any one of a number of corporate forms existing under the Company Law. The public limited liability company (*société anonyme*) or the corporate partnership limited by shares (*société en commandite par actions*) are the most commonly chosen.

The share capital of a SICAF is equal to the amount of the capital contributions made by its shareholders. In contrast to a SICAV, the share capital of a SICAF varies only by virtue of a decision of an extraordinary meeting of shareholders or by virtue of a decision of the board of directors acting within the limits of the authorised share capital. Any share capital modification requires the involvement of a notary and publication of such modification.

2.3 Compartments

Coordinated UCITS may have several compartments which ensure segregation of assets and liabilities between each compartment so that each compartment corresponds to a distinct portion of the assets and liabilities of the Coordinated UCITS, unless the constitutional documents specify to the contrary.

Compartments may differ as to their investment policy, their currency and the type of investors allowed to invest in them. An umbrella structure allows for a single Coordinated UCITS to have several compartments each with a different investment policy or dedicated to specific investors.

The rights of investors in and creditors of a compartment are limited to the assets of that compartment.

2.4 Classes of shares/units

Coordinated UCITS may have several classes of shares/units. Generally, the different classes of shares/units differ from each other with respect to the investors allowed to subscribe (institutional or retail investors for instance) but also regarding the dividend distribution policy or the applicable fees.

3. Management Company

3.1 Introduction

Since 2002, Coordinated UCITS have been subject to new obligations derived from the European directives and implemented by the UCI Law. In particular, a management company managing a Coordinated UCITS must be approved under Chapter 13 of the UCI Law.

To fulfil its stated purpose, a Coordinated UCITS in the form of an FCP has to appoint a management company, in contrast to a Coordinated UCITS in a corporate form which can choose to be self-managed. Consequently, any SICAV / SICAF which does not elect to be self-managed, and any FCP, must appoint a management company which complies with Chapter 13 of the UCI Law.

3.2 Coordinated UCITS' management company legal requirement

A Chapter 13 management company must be established in one of the different corporate forms available. The public limited liability company (*société anonyme*) and the private limited liability company (*société à responsabilité limitée*) are the most common corporate forms adopted for management companies.

A management company can exercise its functions only when it has been approved by the CSSF and it will only be approved if:

- (i) it is sufficiently capitalised. In order to establish its financial status, each entity which seeks to operate as a management company must have a minimum capitalisation of EUR 125,000 with an additional amount of own funds of 0.02% of the amount of the portfolios managed by that management company in excess of EUR 250 million but capped to a total of EUR 10 million. An increase in the additional share capital of up to 50% may be in the form of a credit or insurance institution's guarantee;

- (ii) it has the human, technical and physical infrastructure to undertake its duties;
- (iii) its shareholders and managers have the necessary skills and reputation. In particular, due to the four eyes principle, each management company under Chapter 13 must designate two members of management as representatives for the Coordinated UCITS and will determine the conduct of the Coordinated UCITS. These designated members may be employees of the Coordinated UCITS or independent parties. It is not compulsory for them to be responsible for day-to-day management. However, they may not be employees of the depository bank. In addition, at least one of them must be based in Luxembourg; and
- (iv) its head and registered office are in Luxembourg.

3.3 Management company activities

Thanks to the UCITS III regime, the scope of permitted activities of management companies has been widened. In addition to the normal collective management of portfolios (including portfolio management, central administration and marketing), the management company may also undertake the management of portfolios of investments on a discretionary client-by-client basis and, on an ancillary basis, investment advice (limited to certain instruments), safekeeping and administration in relation to units of UCIs (undertakings for collective investment). In order to mitigate any possible conflicts of interest, if the management company agrees to manage an investment portfolio, its client has to give its prior approval to the management company in case the management company proposes to invest all or part of that client's portfolio in units or shares of a Coordinated UCITS that the management company manages.

The level of supervision will depend on the selection of activities undertaken by the Coordinated UCITS. If the Coordinated UCITS initiates activities other than portfolio management, it will be under the supervision of the CSSF and, in addition to Chapter 13 of the UCI Law, will also be governed by European Directive 93/22/EC.⁴

⁴ Directive 93/22/EC of the European Parliament and of the Council of 10 May 1993 on investment services on the securities field.

Management companies authorised under Chapter 13 of the UCI Law may manage UCITS, UCIs, foreign UCIs and SIFs.

3.4 Delegation

The UCI Law provides the management company with the opportunity to delegate its functions under certain conditions which can be summarised within the four pillars of:

a) Information

Such delegation must be disclosed in the Coordinated UCITS documents in order to inform investors.

b) Skills

The delegated entity should be authorised or registered for the purposes of asset management and it must be qualified to and capable of undertaking all the delegated functions.

c) Control – prevention - safeguard

The delegated entity is subject to the supervision of the CSSF and any delegation may not, in any event, impede the effectiveness of such supervision. No delegation may be made if there is a conflict of interests. The management company must always monitor the delegated entity.

At any time, the management company must be able to withdraw the delegation with immediate effect.

d) Independence (responsibility)

The management company must have the power to give instructions to its delegates. The management company will be the entity ultimately liable.

4. Eligible Assets

According to the UCI Law, Coordinated UCITS may exclusively (except for a 10% “trash ratio”) invest in

(a) transferable securities (**TS**) and money market instruments (**MMI**) admitted to or dealt in on a regulated market, (b) units of Coordinated UCITS and/or units of other UCIs provided that such other UCIs are subject to sufficient supervision, unit-holders’ protection and disclosure, (c) deposits with credit institutions, (d) financial derivative instruments, admitted to or dealt in on a regulated market, and (e) over-the-counter (**OTC**) derivatives, provided that (i) the underlying assets consist of eligible instruments, financial indices, interest rates, foreign exchange rates or currencies, (ii) the counterparties are solid institutions, and (iii) the OTC derivatives are subject to reliable and verifiable valuation on a daily basis and can be sold, liquidated or closed out by an offsetting transaction at any time at their fair value on the initiative of the Coordinated UCITS.

The replication of an index is also possible provided the index is sufficiently diversified, represents an adequate benchmark and offers acceptable public access to information.

In addition, Coordinated UCITS are authorised to use “techniques and instruments” relating to TS and MMI, such as securities lending, sale with a right to repurchase, repurchase and reverse repurchase, for the purpose of efficient portfolio management.

Direct holdings of precious metals, commodities or real estate is strictly prohibited.

4.1 Diversification ratio

Coordinated UCITS may not acquire substantial stakes or voting rights in any issuer.

In addition, the UCI Law provides for numerous investment ratios to which there are numerous exceptions. The basic ratios are set out below:

- Maximum 10% of the assets of a Coordinated UCITS may be invested in TS or MMI issued by the same issuer.
- Maximum 20% of the assets of a Coordinated UCITS may be deposited with the same institution.

- Maximum 20% of the assets of a Coordinated UCITS may be invested in the units of a single Coordinated UCITS or other UCIs⁵ and investments in other UCIs (including Coordinated UCITS) may not in aggregate exceed 30% of the assets of the Coordinated UCITS.
- The risk exposure to a counterparty of the Coordinated UCITS in an OTC derivative transaction may not exceed 10% of the Coordinated UCITS assets (5% if the counterparty is not subject to “acceptable” prudential rules).
- Maximum 35% of the assets of the Coordinated UCITS may be invested in aggregate in TS or MMI issued by and deposits or derivative instruments made with the same issuer. This means that the limit set out in the first bullet point may not be combined.
- Exposure to the underlying assets of derivatives may not exceed in aggregate the investment limits imposed on the direct investment in such assets (i.e. maximum 200% global market exposure).

4.2 Borrowing limits

A Coordinated UCITS may only borrow the equivalent of up to 10% of the value of its net assets and on a short term basis. Direct short selling is prohibited (although synthetic short positions are allowed). The maximum global exposure relating to derivatives is the total net asset value of the portfolio.

4.3 Risk management requirement

Pursuant to article 42 of the UCI Law, a “Coordinated UCITS must employ a risk management process which enables it to monitor and measure at any time the risk of the positions and their contribution to the overall risk profile of the portfolio”. Applicable rules of conduct have been issued by the CSSF in circular 07/308.

First, each Coordinated UCITS is required, on a preliminary basis, to conduct a self-assessment of its risk profile (such risk assessment to be verified on an ongoing basis during the life of the Coordinated UCITS).

Each “non-sophisticated” Coordinated UCITS must determine its global exposure related to positions on derivatives on the basis of the “commitment approach” in accordance with the guidelines established by the CSSF for the most common derivative financial instruments.

Each “sophisticated” Coordinated UCITS must entrust the risk management of their portfolio to a distinct group of personnel separate from the group in charge of portfolio management or delegate such task to a specialised third party.

Each “sophisticated” Coordinated UCITS must use an “internal model” meeting a certain number of qualitative and quantitative criteria. The CSSF’s pre-approved method is based on the “Value at Risk” (**VaR**) model implemented by stress tests.

Currently, Coordinated UCITS investment policies sometimes include CDOs, MBSs, ABSs, CDSs, on loans, commodities futures indices, hedge fund indices, property indices, real estate funds, hedge funds, funds of hedge funds, private equity funds, commodities funds, structured notes, CAT bonds, pair trade, etc. This list only mentions a few examples of the extent of the diversity of investments Coordinated UCITS are currently permitted to hold. However, each instrument to be acquired by a Coordinated UCITS is subject to preliminary verification and must meet specific criteria in order to be considered as eligible. Moreover, specific ratios may apply to each type of asset.

5. Necessary Documentation

5.1 For the constitution of a Coordinated UCITS

A Coordinated UCITS may only be set up after authorisation by the CSSF. The documents and information to be submitted for that purpose are *inter alia*: constitutional documents (i.e. the articles

⁵ Each compartment of any umbrella fund is considered as a separate issuer for the purpose of this provision, provided that the principle of segregation of the liabilities of the various compartments of that fund towards third parties is ensured.

of association or the management regulations); full and simplified prospectuses; agreements with third parties; information on the promoter (recent financial statements); certified true copy of passport, *curriculum vitae* and excerpt of criminal records of each person to be approved by the CSSF. After analysis and approval by the CSSF, an authorised Coordinated UCITS is registered on the UCITS list published in the Luxembourg Official Gazette (the *Mémorial*). The approximate timescale for the application and approval process typically ranges from 30 to 90 days depending on the complexity of the Coordinated UCITS.

5.2 Documentation and information to be periodically disclosed

A Coordinated UCITS must publish the following documents:

- a full prospectus;
- a simplified prospectus;
- an annual report; and
- a semi-annual report.

These documents must be available, free of charge, for all the investors who wish to consult them.

The simplified and the full prospectuses both must include the information necessary for investors to be able to make an informed judgement of the investment proposed to them, and, in particular, of the risks attached thereto. The content of both the simplified and the full prospectuses is governed by the UCI Law and in particular by Chapter 17 and Annex I, Schedules A and C.

The purpose of both the annual and the semi-annual reports is to help investors make an informed judgment on the development of the activities and the results of the Coordinated UCITS. They must, therefore, include a balance sheet or a statement of assets and liabilities, a detailed income and expenditure account for the financial year, a report on the activities of the past financial year and comply with Chapter 17 of the UCI Law.

6. Involved Parties

The setting up and subsequent operation of a Coordinated UCITS involves the following parties: (i) promoter, (ii) depository, (iii) auditor and (iv) central administration. In addition, other service providers, such as investment managers, advisers or distributors, for instance, can be appointed, if needed.

6.1 Promoter

There is no legal provision defining the concept of promoter. Administrative practice defines the promoter as the entity which initiates the creation of the Coordinated UCITS, operates the Coordinated UCITS, determines its orientation and ultimately benefits from its establishment.

The promoter generally puts its name and reputation behind the Coordinated UCITS to be established. It is the entity which ultimately may be held liable by the CSSF and may have to indemnify investors.

The promoter will often act as investment adviser or manager for the Coordinated UCITS. In addition, it is common for the promoter to assume a distribution and marketing function in respect of the shares/units of the Coordinated UCITS.

There is no requirement for a promoter to be a Luxembourg entity.

The promoter must provide the CSSF with all relevant documents in order to demonstrate its good reputation and financial standing.

Co-promotion is frequent in practice when, for example, a single promoter does not provide the required financial strength.

6.2 Depository

A Coordinated UCITS must appoint a depository bank which is entrusted with the physical custody of its assets. It ensures that the sale, issue, repurchase and cancellation of shares/units effected by or on

behalf of the Coordinated UCITS is carried out in accordance with the applicable laws and regulations and the constitutional documents of the Coordinated UCITS. Furthermore, it ensures that not only the consideration for transactions involving the assets of the Coordinated UCITS is remitted to it within the applicable time limits but also that the income of the Coordinated UCITS is applied in accordance with its constitutional documents.

The depository may delegate the custody of some or all of the assets to a correspondent. When delegating its functions, it must exercise care and diligence in choosing and appointing the correspondents and must maintain an appropriate level of supervision over each correspondent. The depository's liability shall not be affected by the fact that it has entrusted all or some of the assets in its custody to a third party.

The depository must be established as a credit institution within the meaning of the law dated 5 April 1993 concerning the financial sector, as amended.

6.3 Auditor

A Coordinated UCITS must have its accounts audited at least once a year by an authorised external auditor that it appoints with the prior approval of the CSSF. The auditor must report to the CSSF any fact or decision of which he/she has become aware during the audit of a Coordinated UCITS and which is likely to constitute a material breach of the UCI Law, affect the ongoing functioning of the Coordinated UCITS, or lead to a refusal to certify the accounts or to the expression of reservations on them.

Furthermore, the auditor must issue a long form report in which he/she has to report the findings over the course of the audit concerning the financial and organisational aspects of the Coordinated UCITS. In particular the auditor has to detail the organisational structure of the Coordinated UCITS and its relationship with the different parties involved. The anti-money laundering rules, the valuation method and the internal risk management system are also to be specifically addressed in the long form report.

6.4 Central administration

The human and technical means necessary to organise the central administration of a Luxembourg Coordinated UCITS must be located in Luxembourg and include the following services:

6.4.1 Domiciliary/Corporate agent

The domiciliary or corporate agent is responsible for providing a registered office, for the safekeeping of all corporate documents of the Coordinated UCITS, for handling all notices and circulars to investors, accepting all correspondence on behalf of the Coordinated UCITS, organising and taking care of all formalities with respect to investors and board meetings, publishing all compulsory legal notices and publications and initiating payment out of the assets of the Coordinated UCITS of fees and charges billed by third parties, if duly authorised.

6.4.2 Registrar and transfer agent

A registrar and transfer agent typically maintains the register of shareholders/unit-holders and handles the processing of subscriptions, redemptions and transfers of shares/units.

6.4.3 Administrative agent

The administrative agent of a Coordinated UCITS typically keeps all records of the Coordinated UCITS; prepares each annual report as well as the Coordinated UCITS' consolidated annual report; prepares all documents for, and assists the corporate agent in organising any general meeting; provides all required corporate secretarial and domiciliation services to the Coordinated UCITS if there is no domiciliary/corporate agent; ensures the daily administration of the assets of the Coordinated UCITS; determines the net asset value of the UCITS and of each share/unit or class, if applicable; and provides investors with applicable net asset values, as well as any additional reports that may be prepared. Where the UCITS is an umbrella fund, the administrative agent will provide the services mentioned above on a consolidated basis as well as in relation to each compartment, as applicable.

6.4.4 Paying agent

The paying agent is the financial institution through which dividends and other financial payments are made to shareholders or unit-holders.

6.5 Other service providers

6.5.1 Investment managers and investment advisers

The investment managers are entrusted with the power to make investment/divestment decisions on behalf of the Coordinated UCITS, in accordance with the objectives and policies of the Coordinated UCITS. This delegation will not relieve the board of directors or the management company from its duties and liability under the UCI Law.

This delegation is to be distinguished from investment advisory arrangements that can be entered into with investment advisers for specialised markets. In such a case, the investment management functions are not delegated.

6.5.2 Distributors of shares/units

A Coordinated UCITS or its management company can market the shares/units by using the help of specialised distributors. In other words, the distributor is the intermediary appointed to distribute the shares/units of the Coordinated UCITS and to receive subscription and repurchase orders. The appointment of distributors is permitted but not required.

Another possibility is to distribute shares/units through nominees which are intermediaries intervening between the investors and the Coordinated UCITS, and which appear as shareholders or unit-holders of the Coordinated UCITS on behalf of the investor. The use of a nominee in the distribution process is subject to specific conditions and disclosures.

6.6 CSSF supervision

Luxembourg investment funds are authorised and supervised by the CSSF. The CSSF's prudential

supervision of entities of the financial sector aims at: promoting a thoughtful and prudent business policy in compliance with the regulatory requirements; protecting the financial stability of the supervised entities and of the financial sector as a whole; supervising the quality of the organisation and internal control systems; and strengthening the quality of risk management.

7. Taxation of UCITS

7.1 Fixed capital duty and subscription tax

A Coordinated UCITS is not subject to any tax in Luxembourg except a fixed amount of EUR 75 due on transactions held before a notary and the annual subscription tax (*taxe d'abonnement*) of 0.05 or 0.01% (or 0.0025% paid quarterly) based on the entire net assets valued on the last day of each quarter which are not expressly exempt.⁶

7.2 Taxation of the investors

7.2.1 Withholding tax

Under current legislation, and without prejudice to the possible application of the law dated 21 June 2005 implementing Directive 2003/48/EC on the taxation of savings income in the form of interest payments or under the law dated 23 December 2005 introducing a withholding tax on certain interest payments from securities, the amount distributed by the Coordinated UCITS (whether or not in corporate form) will not be subject to any withholding tax in Luxembourg.⁷

7.2.2 Taxation of income derived from and capital gains realised on the shares/units in a Coordinated UCITS by non-Luxembourg residents

Holders of shares/units in a Coordinated UCITS who are non-residents of Luxembourg and who have neither a permanent establishment nor a

⁶ Art. 129 UCI Law.

⁷ Art. 100 2) LIR (loi sur l'impôt sur le revenu).

permanent representative in Luxembourg to which the shares/units are attributable, are not liable to any Luxembourg income tax on dividends or other payments derived from the shares/units in the Coordinated UCITS. Capital gains realised on a substantial participation are taxable if they are realised either within six months after the acquisition of the substantial participation, or by a person who has been a Luxembourg resident taxpayer for more than 15 years and who has become a non-resident taxpayer less than five years before the realisation takes place. A participation is deemed to be substantial where a shareholder or unit-holder holds, either alone or together with his spouse and/or minor children, directly or indirectly at any time within the five years preceding the realisation, more than 10% in value of the shares/units of the Coordinated UCITS.⁸ These rules apply unless a favourable tax treaty applies.

The exceptional taxation of capital gains realised on substantial participations within six months after the acquisition should not apply to an FCP because it is not a share capital company.⁹

7.2.3 Income derived from, and capital gains realised on, the shares/units in a Coordinated UCITS by Luxembourg residents

Individual holders of shares/units

Where a Coordinated UCITS has a corporate form, distributions received by an individual shareholder resident in Luxembourg will be taxed in Luxembourg.

Capital gains realised on the disposal of the shares by resident individual shareholders who act in the course of the management of their private wealth, are not subject to income tax, unless those capital gains qualify either as speculative gains or as gains on a substantial participation.

Capital gains realised on the disposal of the shares by resident individual shareholders who act in the course of their professional / business activity, are subject to income tax at ordinary rates (possibly in addition to Municipal Business Tax).

There should be a difference in the tax treatment of units in an FCP and shares in a Coordinated UCITS formed as a company. In principle, an FCP is a transparent entity for tax purposes, therefore the unit-holder should be taxed on the income as it arises in the Coordinated UCITS. Nevertheless, in practice, the distinction is not applied by the Luxembourg tax administration.¹⁰ An individual unit-holder resident in Luxembourg will be taxed upon distributions received and upon capital gains realised as described above in relation to shares.

Luxembourg resident corporate holders of shares/units

Dividends and other payments derived from the shares in a Coordinated UCITS in corporate form by a Luxembourg fully taxable resident company are subject to income tax. The effective rate is currently 28.59% for companies located in Luxembourg City.¹¹ The shares in such a Coordinated UCITS held by a Luxembourg fully taxable resident company are furthermore subject to Luxembourg net wealth tax at a rate of 0.5% per annum.

The tax administration does not seem to make any distinction in the taxation of an FCP in spite of the principle of transparency of such entity.¹²

7.3 Benefiting from tax treaties

Luxembourg has a wide network of double tax treaties. Some extend their benefits to Luxembourg SICAVs and SICAFs. As an FCP is transparent for tax purposes, it is the unit-holder himself who may have the right to claim a refund of withholding tax.

⁸ Art. 129 UCI Law.

⁹ Organisme de placement collectif, Kremer, p. 618 n°1281.

¹⁰ Les impôts sur le revenu et sur la fortune, Winandy, p. 768 ; Organisme de placement collectif, Kremer, p. 618 ; Luxembourg in international tax planning, Warner, p.422.

¹¹ Art. 2 law dated 19 December 2008 on new tax measure per 2009 (loi "modification de certaines dispositions en matière des impôts directs").

¹² Les impôts sur le revenu et sur la fortune, Winandy, p.768.

7.4 Value added tax (VAT)

A Coordinated UCITS formed as a company is considered as a taxable person for VAT purposes, following a decision of the European Court of Justice.¹³

The applicable Luxembourg laws and regulations have confirmed that investment vehicles have the status of taxable persons for VAT purposes.¹⁴

According to article 44(1)(d) of the Luxembourg law dated 12 February 1979 regarding the value added tax, services relating to management of undertakings for collective investment are VAT exempt.

8. UCITS IV

In July 2008, the European Commission issued a proposal for amendments to the current legal framework.

On 22 June 2009, the Council adopted the proposal (**UCITS IV Directive**).

We have summarised below the relevant objectives and means of implementation.

8.1 Fund passport: improvements of the notification procedure

Objective: Removing the administrative barriers and delays to and uncertainties of the cross border marketing of UCITS.

Implementation: Through the issuance of a simple notification letter (including the key elements of, *inter alia*, subscription, redemption, paying agent) to the host country. Three days after the home country regulatory authority sends the notification letter, the UCITS will be able to market its shares/units. There will be no opportunity for the host country authorities to subsequently stop the marketing of the shares/units.

8.2 Facilitating fund mergers

Objective: Having a clear process and specifying common terms and conditions regarding pan-European mergers.

Implementation: The UCITS IV Directive encompasses the possibility of three different merger techniques (merger by absorption, by amalgamation and by creation of a new UCITS). These should apply internally and in pan-European laws. Furthermore, the merging UCITS will not be required to have similar investment policies. The regulatory authority of the resulting UCITS will not have any veto right and will have to give its approval within 15 business days. Nevertheless, the relevant regulatory authority will have the power to stop the process if the obligations described in the UCITS IV Directive are not fulfilled. It is worth mentioning that the related fees cannot be charged to the shareholders or unit-holders.

8.3 Simplified prospectus

Objective: Replacing the simplified prospectus.

Implementation: Issuance of a new document (which will replace the simplified prospectus) called Key Investor Document (**KID**)¹⁵ which will focus on the fees and the subscription–redemption process and will exclude all the legal information currently contained in the simplified prospectus.

8.4 Authorising master-feeder structures

Objective: Providing the opportunity to create a master-feeder structure.

Implementation: The specific investment policy of a feeder UCITS needs to be approved by the regulatory authority of the feeder UCITS' home Member State and the UCITS IV Directive requires the feeder UCITS and the master UCITS to enter into a legally binding agreement. Furthermore, if the feeder UCITS and the master UCITS have different depositaries or auditors, the UCITS IV Directive requires the latter to enter into an information-

¹³ ECJ, Banque Bruxelles Lambert S.A. (BBL) c. Etat belge, C-8/03, 21 octobre 2004.

¹⁴ VAT circular N. 723 of 29 December 2006.

¹⁵ Formerly referred to as « Key Investor Information » or KII.

sharing agreement. Finally, provisions within the UCITS IV Directive must prevent the master UCITS from charging the feeder UCITS subscription and redemption fees.

8.5 Supervision cooperation

Objective: Improving cooperation processes between national regulatory authorities.

Implementation: The cornerstone of cooperation between national regulatory authorities needs to improve the current mechanism of liaison between them and allow the regulatory authority of one country to investigate and control information within the scope of another regulatory authority. It is also contemplated that, in some extreme cases where events occur which are contrary to the interests of the local shareholders or unit-holders, the host regulatory authority may intervene.

8.6 UCITS management passport

Objective: Passporting management company rights.

Implementation: Despite the fact that the management company passport raised some issues at the level of the EU member states, the Economic and Monetary Affairs Committee at the European Parliament (ECON) adopted, on 2 December 2008, the report on the revision of the UCITS Directive legislation including the management company passport.

As previously mentioned, the UCITS IV Directive was approved by the European Parliament as at 13 January 2009 and by the Council as at 22 June 2009. Member States will need to enact national legislation to apply the main changes by 1 July 2011.

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