

ASSET MANAGEMENT &
INVESTMENT FUNDS

CBI notice of intention on UCITS side-pocket arrangements

The Central Bank of Ireland (CBI) issued a [notice of intention on UCITS side-pocket arrangements](#).

The CBI notice confirms that it will permit a UCITS to implement a side-pocket arrangement only for Russian, Belarusian and Ukrainian assets that are directly and/or indirectly impacted by the Russian invasion into Ukraine and/or impacted by sanctions that have been imposed as a result of Russia's invasion of Ukraine.

The notice suggests that a side pocket arrangement may be implemented by way of the establishment of a clone fund into which the liquid assets may be transferred. This approach would be seen as a "de-merger" of liquid assets to a new sub-fund, as distinct from a traditional side-pocket arrangement.

A CBI fast track process will be available for the establishment of the clone UCITS fund if certain conditions are met.

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The CBI notice confirms that it will permit a UCITS to implement a side-pocket arrangement only for Russian, Belarusian and Ukrainian assets that are directly and/or indirectly impacted by the Russian invasion into Ukraine and/or impacted by sanctions that have been imposed as a result of Russia's invasion of Ukraine (Affected Securities). The Affected Securities have become illiquid or untradeable as a result of the Russian invasion of Ukraine and at this time, are difficult to value accurately.

The notice suggests that a side pocket arrangement may be implemented by way of the establishment of a clone UCITS fund and the transfer of the liquid assets of the (original) UCITS into the newly authorised/ approved clone UCITS leaving the Affected Securities in the original UCITS. This would be seen as a "de-merger" of liquid assets to a new sub-fund, as distinct from a traditional side-pocket arrangement.

The side-pocketing of UCITS assets is only available in the context of Affected Securities and should not be interpreted as creating a precedent by the CBI for any other current or future situations. A side-pocket by way of a new UCITS is established when liquid assets of an (original) UCITS are transferred into a newly authorised/ approved clone UCITS. The Affected Securities which have become illiquid or difficult to value remain in the original UCITS. Investors in the newly established clone UCITS hold shares in that fund pro-rata to their holdings in the original UCITS. Investors in the original UCITS continue to have a pro-rata holding in the original UCITS. The original UCITS would be wound down over time with any realised value being paid out to investors.

CBI requirements

An original UCITS may establish a side-pocket by way of a newly established clone UCITS provided that:

- The proposal is in the best interests of investors.
- Investors have approved transfer into the newly established clone UCITS side-pocket.
- The UCITS has obtained prior written approval of the CBI for the proposal.
- The UCITS provides a clear description to investors of the costs and fees associated with establishing the side-pocket. The UCITS must also provide details of the ongoing costs and fees payable in its prospectus.
- The original UCITS is placed in wind-down mode at the same time as the creation of the new clone UCITS
- The original UCITS has established written policies in relation to management of the Affected Securities, including policies relating to the costs and fees associated with maintenance of the original UCITS.

- The original UCITS reports to the CBI on an annual basis confirming whether or not the parameters and policies continue to be respected and outlining the prospects and/or plans for the side-pocketed assets and liquidation of the original UCITS.

Streamlined Process

The CBI has proposed that a streamlined authorisation/approval process will be available for the establishment of the clone UCITS fund. An application for authorisation/approval of a new fund/sub-fund should be made in the normal manner, accompanied by:

1. A confirmation from the directors of the fund that the new fund/sub-fund is identical to the original UCITS.
2. A copy of the resolution approving the establishment of the new fund/sub-fund.
3. A mark-up of the investment objective and policy against that of the original UCITS.

Where such complete applications are received, these will be processed within five working days.

Applications which are not accompanied by the confirmation outlined in (1) above will be processed within normal time-frames.

Context

The Russian invasion of Ukraine has resulted in some securities with exposure to Russia, Ukraine and Belarus becoming illiquid or untradeable and consequently difficult to value accurately. On 16 May 2022, the European Securities and Markets Authority (**ESMA**) published a public statement on actions to manage the impact of the war in Ukraine on investment funds. The CBI recognises that due to the specific and exceptional market conditions brought about by the war in Ukraine, certain asset classes are subject to pronounced devaluation and / or their ability to trade has been wholly impaired.

ESMA's public statement on the implications of Russia's invasion of Ukraine on investment fund portfolios provides messages to fund managers of both UCITS and AIFs, including general principles in situations of material liquidity issues and

valuation uncertainties. The statement notes that the selection of the most suitable liquidity management tools as well as the valuation to be applied to affected assets falls under the responsibility of the fund manager which shall act in the best interest of all investors.

The statement also includes high level guidance on:

- the appropriate action in case of exposures to Russian, Belarusian and Ukrainian assets, given valuation and liquidity uncertainties
- the process fund managers should follow when evaluating these assets
- the option of side-pockets or similar arrangements to segregate these assets (including detail on the comprehensive analysis and disclosure which would be expected).

ESMA expects fund managers of investment funds with exposures to assets facing liquidity issues to assess whether a fair value of these assets can still be determined and adapt the valuation without undue delay.

ESMA will continue to closely monitor the situation and take or recommend any measures necessary to mitigate the impact of the Russian invasion of Ukraine on investment funds. ESMA will, where necessary, reassess any potential need to supplement the guidance provided in this public statement or provide additional guidance on other issues arising from this crisis.

For more information on this topic please contact any member of [A&L Goodbody's Asset Management & Investment Funds team](#).

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