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Revised Central Bank Guidance on the use of Financial Indices by UCITS

The Central Bank of Ireland (the "**Central Bank**") has issued revised guidance (the "**Guidance**") on the use of financial indices by UCITS. A copy of the Guidance can be found here.

The purpose of the Guidance is to clarify the Central Bank's requirements where a UCITS intends to use a financial index for investment or efficient portfolio management purposes. In particular, it introduces a self-certification regime for those UCITS management companies or SMICs (the "**Responsible Person**") seeking to use financial indices and sets down the process relating to that certification.

Key Changes

The key changes in the Guidance are outlined as follows:

- Previously where a UCITS utilised a financial index which comprised of either (i) eligible assets but which would result in the UCITS breaching the applicable risk diversification limits; or (ii) ineligible assets, such financial indices had to be cleared by the Central Bank prior to use. The Central Bank will no longer review any such financial indices;

- The Responsible Person must assess each financial index that the UCITS intends to use in order to determine whether the index meets all of the regulatory requirements. Similar to the previous guidance, the Central Bank sets out specific criteria which must be met by the financial index in order for it to meet the regulatory requirements;

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- A director of the Responsible Person must now certify in writing to the Central Bank that the relevant index meets all of the regulatory requirements when seeking approval of the relevant UCITS;

- In the case of an index-tracking UCITS which wants to have the ability to invest up to 35% of net assets in a single issuer as permitted under Regulation 71(2) of the UCITS Regulations, the Responsible Person must make a submission to the Central Bank when seeking approval of the relevant UCITS confirming that the UCITS intends to avail of this flexibility and explaining why this is justified by exceptional market circumstances;

- The Central Bank will carry out spot-check assessments of financial indices utilised by UCITS to determine whether or not the financial index meets the regulatory requirements. If selected, the Responsible Person will have to provide "*immediately upon request*" a written submission (with supporting documentation) demonstrating how the regulatory requirements have been met.

When is the certification required?

Where a UCITS uses a financial index solely as a performance benchmark, the Responsible Person is not required to provide any certification to the Central Bank.

A certification will be required for all other uses of a financial index, regardless of whether the index is being used for investment purposes or efficient portfolio management purposes or whether exposure is generated directly or via a financial derivative instrument (FDI).

Next Steps

In view of the above, UCITS will need to ensure that prior to gaining exposure to a financial index for investment or efficient portfolio management purposes;

(i) taking into account the specific criteria identified in the Guidance, the Responsible Person can confirm to the Central Bank that the relevant index is eligible for use by the UCITS; and

(ii) the Responsible Person will be in a position to provide the Central Bank with a submission (together with supporting documentation) as to why this is the case "*immediately upon request*". Noting the requirements of the Central Bank with respect to "document retrievability" under the CP86 framework, we would expect that the Central Bank will interpret this as meaning within 24 hours of the request being made.

Where a new UCITS or a UCITS sub-fund intends to use an index, the signed certification should be included with the initial application seeking authorisation or approval from the Central Bank.

Where an existing UCITS (including those UCITS approved by the Central Bank prior to the issue of the revised Guidance) proposes to use a new index, the signed certification should be submitted to fundspostauthorisation@centralbank.ie prior to the UCITS gaining exposure to the relevant index.

Should you require further information on this matter, please contact the authors or your usual Dillon Eustace contact.

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