

CSSF Circular 08/356 dated June 2008

On June 4, 2008, the CSSF issued its long-awaited Circular 08/356 on rules applicable to Luxembourg Funds when they enter into securities lending, repurchase or “réméré” agreements.¹

This new Circular repeals and replaces the rules as set out in Chapter H of IML Circular 91/75.

The key changes compared to the provisions of Chapter H of IML Circular 91/75 are as follows:

1. Diversification and counterparty rules for repos and “rémérés”

The new Circular 08/356 foresees that securities purchased under a repurchase agreement or securities purchased “à réméré” shall comply with the usual diversification rules applicable to all securities in portfolio. Moreover, any potential counterparty risk linked to transactions made under securities lending agreements, repurchase or “réméré” agreements must be monitored and must comply with the relevant counterparty limit.

2. Reinvestment of cash collateral on securities lending

The new Circular clarifies the type of securities in which cash collateral can be reinvested, clearly stating that reinvestment of cash collateral has no impact on the diversification of the portfolio². It also fixes the level of required collateral at 90% (at least) of the market value of the securities lent. Note however the application of the counterparty limit of 5% or 10% is made to the part not covered by collateral.

3. No quantitative limits for securities lending






The previous limits relating to lending transactions have been removed, namely that securities lent could not represent more than 50% of the total market value of the securities in portfolio and the lending period was limited to a maximum of 30 days.

At the back of this flash news, you will find a table summarizing the main rules and principles applicable to securities lending and repurchase or “réméré” agreements. Please refer to the original text of the Circular for more details.

This new Circular, that is applicable to all UCITS and UCIs, does not completely close the door to Funds wishing to sell securities purchased under a repurchase agreement. This could certainly be of some interest for certain market participants, notably those using alternative strategies.

¹ Please refer to the definition overleaf

² Funds must however avoid excessive concentration both compared to issuers and/or instruments

	Securities lending	Repurchase agreements		« Réméré »	
		Fund lends money and receives collateral « Repurchase agreement »	Fund borrows money and provides collateral « Reverse repurchase agreement »	Securities purchased	Securities sold
Definition	Technique by which the owner of securities can make them available to others whilst retaining the benefits of ownership	Technique which consists in the purchase and sale of securities where, at maturity, the seller has the obligation to take back the asset sold		Technique which consists in the purchase and sale of securities where the terms reserve the right to the seller to repurchase the securities from the buyer at a price and at a time agreed between the two parties at the time when the contract is entered into	
Eligible for a Part I UCITS					
Specific requirements					
Used for EPM ³	Yes	Yes	Yes	Yes	Yes
Investment policy	N/A	Securities ⁴ purchased should be in line with the investment policy & may not be sold during the lifetime of the contract except if the UCITS has other assets to meet its obligation at the end of the contract	N/A	Securities ² purchased should be in line with the investment policy & may not be sold during the lifetime of the contract except if the UCITS has other assets to meet its obligation at the end of the contract	N/A
Disclosure in the prospectus	Yes	Yes		Yes	
Counterparty	Should be subject to rules of prudential supervision considered by the CSSF as equivalent to those laid down by Community law	Should be subject to rules of prudential supervision considered by the CSSF as equivalent to those laid down by Community law		Should be subject to rules of prudential supervision considered by the CSSF as equivalent to those laid down by Community law	
Liquidity	Cannot compromise the liquidity of the UCITS to face redemptions	Cannot compromise the liquidity of the UCITS to face redemptions		Cannot compromise the liquidity of the UCITS to face redemptions	
At maturity	N/A	N/A	Should have assets to pay the agreed price at maturity	N/A	Should have assets to pay the agreed price at maturity
Concentration risk					
Diversification limits	Yes ⁵ (market risk)	Yes (market risk)	N/A	Yes (market risk)	N/A
Counterparty risk					
Counterparty limits (10% if credit institutions, 5% in other cases)	Yes	Yes	Yes	Yes	Yes
Collateral	Counterparty risk can be reduced by appropriate collateral ⁶ The market value of the collateral should represent at least 90% of the global value of the securities lent during the lifetime of the contract	Counterparty risk can be reduced by appropriate collateral ⁶	Counterparty risk can be reduced by appropriate collateral ⁶	Counterparty risk can be reduced by appropriate collateral ⁶	Counterparty risk can be reduced by appropriate collateral ⁶
Disclosure in the financial statements					
Type	Global market value of securities lent	For purchases and sales subject to repurchase obligations, the total amount of outstanding transactions under repurchase agreements		For purchases and sales, the total amount of outstanding transactions under “réméré” agreements	

³ EPM = efficient portfolio management (reduction of risk or reduction of cost or creation of additional capital or income)

⁴ Bank certificates or money market instruments, debt instruments issued or guaranteed by an OECD country or by a supranational issuer, shares or units of money market funds rated AAA with a daily NAV, liquid corporate debt instruments, shares admitted to an official stock exchange located in an OECD country and included in a main index

⁵ Securities lent should remain in portfolio and are therefore submitted to the diversification rules (10%, 5%/40%, 35%,...)

⁶ Appropriate collateral: liquidities (cash, bank deposits, money market instruments), debt instruments issued or guaranteed by an OECD country or a supranational issuer, shares or units of money market funds rated AAA with a daily NAV, liquid debt instruments issued or guaranteed by highly rated issuers, equities listed on an OECD official stock exchange and included in a main index, shares or units of funds mainly invested in equities or debt instruments mentioned above

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