Can Fund Managers set up multiple share classes for common UCITS fund?

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As stated in the Undertaking for Collective Investment in Transferable Securities (UCITS) Directive, a single UCITS funds can be subdivided by multiple share classes. Share classes are the different types of units or shares belonging to same fund. UCITS Directive has not clearly defined the scope of share classes and only recognises their existing. Therefore, there is no common legal or regulatory framework for share classes throughout the European Union (EU). Different countries in EU have divergent approaches for permitted types of share classes ranging from very simple classes (e.g. with different level of fees) to much more sophisticated share classes (which may have different investment strategies).

The European Securities and Market Authority (ESMA) has issued an opinion on the extent to which multiple shares classes of the same UCITS Funds differ from one another. ESMA's opinion which is addressed to the National Regulators also known as National Competent Authorities (NCA), sets out four broad level principles which UCITS funds must follow while setting up multiple share classes. The principles which are focused to ensure a harmonised approach across all jurisdictions in EU are as follows:

- Common investment objective: Share classes of the same fund should have a common investment objective reflected by a common pool of assets. ESMA considers that hedging arrangements at share class level, except for currency risk hedging – are not congruous with the requirement for a fund to have a common investment objective;
- Non-contagion: UCITS management companies should implement appropriate procedures to minimise the risk that features specific to one share class could have a potentially adverse impact on other share classes of the same fund;
- Pre-determination: All features of the share class should be pre-determined before the fund is set up; and
- Transparency: Differences between share classes of the same fund should be disclosed to investors when they have a choice between two or more classes

ESMA specifies that these principles will have an impact on investment fund markets in countries where share classes can currently be set up and do not comply with them. To attenuate the impact on investors in share classes established prior to this opinion which are not in line with these principles, ESMA is of the view that they should be allowed to continue. However, such share classes should be closed for investment by new investors within 6 months of publication of the opinion, and for additional investment by existing investors within 18 months of publication.