EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 13 September 2001

at the request of the Austrian Ministry of Finance on a draft federal law concerning real estate funds (Real Estate Investment Fund Act – ImmoInvFG) and to amend the Banking Act, the 1993 Investment Fund Act, the Money Market Act, the Securities Regulation Act, the Insurance Regulation Act, the Pension Fund Act, the Finance Market Regulator Act, the Income Tax Act, the Corporation Tax Act and the Federal Law establishing a Federal Pension Fund Public Limited Company [*Bundespensionskasse AG*]

(CON/2001/24)

1. On 30 July 2001 the European Central Bank (ECB) received a request from the Austrian Ministry of Finance for an opinion on a draft federal law concerning real estate funds (Real Estate Investment Fund Act – ImmoInvFG) and to amend the Banking Act, the 1993 Investment Fund Act, the Money Market Act, the Securities Regulation Act, the Insurance Regulation Act, the Pension Fund Act, the Finance Market Regulator Act, the Income Tax Act, the Corporation Tax Act and the Federal Law establishing a Federal Pension Fund Public Limited Company (*Bundespensionskasse AG*) (hereinafter referred to as the "draft law").
2. The ECB's competence to deliver an opinion is based on the second indent of Article 105(4) of the Treaty establishing the European Community, the second indent of Article 4(a) of the Statute of the European System of Central Banks and of the European Central Bank and the fifth indent of Article 2(1) of Council Decision 98/415/EC of 29 June 1998 on the consultation of the ECB by national authorities regarding draft legislative provisions[1], as the legislative proposal contains rules applicable to financial institutions which materially influence the stability of financial institutions and markets. The Governing Council of the ECB has adopted this opinion in accordance with the first sentence of Article 17.5 of the Rules of Procedure of the ECB.
3. The main features of the draft law are:
   (i) that the issue and administration of real estate funds represent a bank transaction, and are therefore subject to prudential supervision;

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1 OJ L 189, 3.7.1998, p. 42.

(ii) that the valuation of property in real estate funds will be undertaken at least once a year by two independent experts;

(iii) the establishment of statutory minimum spread requirements for individual funds;

(iv) the requirement of involvement by a deposit bank (“*Depotbank”*) and the establishment of insolvency protection measures in favour of investors.

The explanatory memorandum to the draft law notes that the rapid advance of foreign real estate funds on the Austrian market requires the introduction of an Austrian Real Estate Investment Fund Act and a number of accompanying amendments. The intention of the Amendment to the 1993 Investment Fund Act and the Amendment to the Money Market Act is to treat foreign real estate funds as equivalent to all other foreign investment funds in terms of public sales in Austria. The investment rules will extend to Austrian real estate funds that are currently regulated by the Amendments to the Insurance Regulation Act and the Pension Fund Act.

4. The ECB welcomes the draft law as it establishes a regulatory framework to supervise Austrian Real Estate Investment Funds with particular attention paid to achieving the level playing field by harmonising the regulation of investment funds. Another item worth particular attention is the forward-looking perspective of the draft law as it aims to address future capital flows due to pension provisions. Specifically, the intention of the draft law is to ensure secure long-term high yield investment opportunities also for investors with limited funds. Finally, the draft law recognises the close relationship between banks and investment funds by particularly highlighting the role of the deposit bank in Article 35.

5. The ECB would like to highlight the fact that investment funds may face liquidity shortages, even when they are considered solvent, in cases where long-term investments are illiquid while the funding is potentially of shorter maturity. Investments in real estate assets can generally be considered as long term and illiquid. Furthermore, Article 11 of the draft law provides for the possibility that the share certificates may be returned to the fund for redemption of the share at the request of the shareholder. Consequently, this concern may materialise for individual real estate investment funds. The ECB recognises that Article 32 of the draft law expressly addresses concerns over liquidity and also provides for a temporary waiver of the investor’s payment of the redemption price under extenuating circumstances in Article 11. Nevertheless, as a limit on this waiver to one year (or to two years where foreseen by the fund’s rules) is also implemented, liquidity shortage may arise in extreme circumstances. As the real estate sector has been the source of instability in many countries, the ECB would like to emphasise that supervision should continue to focus on liquidity issues. In the implementation of the law, supervisors should actively monitor the funds’ liquidity.

Furthermore, the ECB would like to draw attention to the possible impact on asset prices of the expected capital inflows from investors into the real estate sector through real estate investment funds. As the reaction of the supply-side tends to be sluggish in the real estate sector, an increase in demand may predominantly influence prices and also increase price volatility. Furthermore, the determination of asset value may be of particular concern as the valuation of the share certificate will mostly not be verifiable by market prices. Article 29 of the draft law provides for the appointment of at least two suitable experts for the valuation of the fund's assets. Thus, the ECB would recommend that supervisors, in implementing the law, focus their attention particularly on price development in those assets that are eligible for investment under Article 21.

6. The ECB notes that the continuous monitoring of business conduct by deposit banks is to become mandatory. The ECB welcomes the supervision of companies investing in real estate by the financial markets supervisory authority (*Finanzmarktaufsichtsbehörde*).

7. The ECB notes that the draft law aims, *inter alia*, at facilitating the management of: (i) real estate funds for the public at large; and (ii) the management of special real estate funds for major investors who are not natural persons by Austrian real estate companies (which must pay particular attention to the protection of the interests of the investors).

8. The ECB notes that the draft law defines "real estate fund" and "real estate investment companies". The ECB welcomes the detailed provisions on liability conditions, the mandatory involvement of a deposit bank, the winding up of real estate funds, property companies, the valuation of assets, risk spread, liquidity provisions and derivative products in the draft law.

9. The ECB welcomes criminal law provisions in the draft law, which are similar to those of the Investment Fund Act, with the intention of creating an efficient tool guaranteeing adherence to the provisions of the draft law. In this context, the draft law also imposes fines for deposit banks violating the rules laid down in the draft law.

10. The ECB recommends that the draft law expressly acknowledge that the reporting obligations it imposes do not prejudice any statistical reporting requirements imposed by the ECB on the entities subject to the draft law in accordance with Article 2 of Council Regulation (EC) No 2533/98 of 23 November 1998 concerning the collection of statistical information by the European Central Bank.

11. The ECB confirms that it has no objection to the publication of this opinion by the competent national authorities.

Done at Frankfurt am Main on 13 September 2001.

The President of the ECB

[signed]

Willem F. DUISENBERG