

A large, abstract graphic of a network or sphere made of interconnected blue nodes and lines, positioned in the upper right background of the page.

Costa Rica

Regulation

FUNDS AND FUND MANAGEMENT 2009

2.1 Type of funds

The Securities Market Regulation Act of 1998 No. 7732, articles 61-100 (LRMV), and the General Regulations of Investment Companies and Mutual Funds, provide for the formation and operation of mutual funds, which are treated as independent estates owned by a plurality of investors. The participation units of the investors are represented by participation certificates, issued with the same characteristics and under the same conditions for each investor. Only mutual funds authorized by the local securities regulatory authority, Superintendencia General de Valores (SUGEVAL), may conduct a public offering of its participation units or be quoted on a local securities exchange. These funds may only invest in certain qualified foreign securities, and in other non-financial assets, such as real estate property. A newly created mutual fund type, risk capital mutual fund, allows also investing in a non-public offering of securities.

Costa Rican regulations allow five different types of mutual funds:

- Open-end funds have a variable and unlimited patrimony and the participation units have an undefined duration term and cannot be submitted to operations other than reimbursements. This means that since open-ended funds are not securities, they shall not be sold to third parties by means of stock mechanisms. In addition, they cannot be negotiated in secondary markets, or be objects of repurchase, but may be transferred by operations different from those of the stock exchange market such as assignments.
- Closed-end funds have a fixed patrimony and the participation units are not redeemed directly by the fund, except for some circumstances and procedures established by law.
- Open-end or closed-end financial investment funds whose main purpose is investing in financial assets.
- Open-ended or closed-end non-financial investment funds, which invest in assets of a non-financial nature such as real estate.
- Mega funds or funds of funds. The SUGEVAL regulates their operations through the General Regulations of Investment Companies and Mutual Funds, as well as the type of funds in which they can invest, the

commission rules, expenses and regulatory dispositions. Currently, six mega funds exist and are administered by the Nacional, BCR, BAC San José, and HSBC banks, as well as Aldesa Sociedad Fondos de Inversión.

Another collective investment vehicle is the investment trust. Investment trusts are usually known as trusts that invest the resources provided by the trustors in a wide variety of securities, obtaining profits from income and capital gains originated from these securities. Unlike investment funds, which must only operate in the organized securities market, investment trusts may operate as private investment vehicles and invest in over-the-counter and privately held securities. However, if the investment trust is structured as a mutual fund and it engages in the public offering of its participation units, these investment trusts would be subject to regulation by the banking regulatory agency Superintendencia General de Entidades Financieras or SUGEF, as well as local securities regulatory authority SUGEVAL, and would be subject to monetary controls by the Costa Rican Central Bank (BCCR). If the trust is structured as a capitalization or a pension fund, it would be subject to the corresponding legislation and authorities.

Real estate investment funds

Real estate investment funds are those in which neither the investors nor the individuals or entities related to them, or that form part of the same economic interest group, are allowed to lease the real estate that comprises the assets of the fund; or to hold rights over such assets, other than those derived from their position as investors.

2.2 Laws

Mutual funds are governed by the LRMV; the General Regulations of Investment Companies and Mutual Funds; and administrative regulations.

Investment trusts organized and operated by authorized banking and financial institutions, which are structured and operate as mutual funds, fall within the authority of the banking regulatory agency SUGEF; however, if a public offering is made by them, they would be subject to local securities regulatory authority - SUGEVAL. The general regulations of mutual funds are also applicable to investment trusts.

The BCCR sets the monetary controls and restrictions to investment trusts, as per the Costa Rican Central Bank Organization Act No. 7558 of 1995 (LOBCCR) and regulations thereto.

Termination causes

The mutual funds may be terminated due to the following causes:

- By expiration of the term set forth in the by-laws and prospectus, except for renovation
- By agreement of the investors assembly in case of closed-end funds
- Upon cancellation of the authorization granted by SUGEVAL to the investment company to operate and manage mutual funds, and specifically, such fund

2.3 Managers, trustees, and custodians

Managers

Only authorized investment companies (IC) can manage mutual funds. The SUGEVAL authorizes the formation and operation of ICs upon verification of compliance with the minimum required share capital, corporate purpose, and structure requirements. A Costa Rican company or the branch office of a foreign company may request authorization to operate as an IC, provided it complies with the statutory requirements established by law, particularly in the Commercial Code, and proving that its exclusive purpose is the management of mutual funds as described herein. The ICs shall initiate operations in a term no longer than 12 months as of the communication of the respective agreement. Otherwise, the SUGEVAL may cancel such authorization. The authorization cannot be transferred either directly or indirectly, nor be subject to any lien or encumbrance.

Regarding the establishment of fund management agreements between local and foreign entities, the ICs are ruled by specific regulations issued by the SUGEVAL for such purposes.

The IC shall be compensated solely through commissions based on the fund's equity and/or its returns. The IC may also charge commissions for entering or withdrawing from the fund. These commissions must be disclosed in the fund's prospectus. The SUGEVAL is in charge of ruling the methodology used for the calculation of the commissions and expenses in which the funds incur, as well as their application. Neither the LRMV nor the SUGEVAL have specific limits regarding the fees of the IC or the entities in charge of the custody of the funds.

Any change in management of the IC has to be previously authorized by the SUGEVAL, and duly communicated to the investors of each fund, in the domicile established for such purposes. In any case, the IC is allowed to resign as long as all the requirements and procedures established for the designation of a substitute are complied with.

In the aforementioned cases, the investors will have the right to request the reimbursement of their participations without deduction of the related commissions or expenses. Such a request has to be made within one month as

of the date in which the investor was informed of the IC's substitution or management change.

Trustees

As stated above, under Costa Rican law, a mutual fund is deemed a separate and independent estate by statute, in the same fashion as a trust. Local laws do not contemplate the need for or require the existence or participation of a trustee in addition to the investment company.

In general, Costa Rican law has no limitations as to who may act as trustee in a trust. In the case of legal entities, the corporate purpose included in the articles of incorporation must specifically allow it to act as trustee. As stated above, investment trusts organized and operated by authorized banking and financial institutions fall within the regulations of the SUGEF.

In addition, pursuant to article 661 of the Commercial Code of Costa Rica, the trustee shall not receive any commission, rewards, or economic advantages other than the fees established in the trust agreement. In the event that such fees are not stipulated, a judge shall decide based on the criteria of experts appointed for such purposes.

Participation deposit

The mutual funds participations shall be deposited before any of the custodians authorized by the SUGEVAL, with the purpose of protecting the investor's rights. Such custodians have the legal custody and management of the income and assets of the funds, in an independent account for each.

In the event of ICs having no custodians for the purposes above mentioned, the SUGEVAL may impose additional requirements on the IC, including minimum share capital. In extreme cases, the SUGEVAL can authorize the custody of the investment funds to be managed by foreign custody entities, according to the regulations issued by it.

2.4 Investment restrictions

Mutual funds shall be invested exclusively for the benefit of the investors, providing the necessary equilibrium between security, profitability, diversification, and term compatibility, according to their purposes and the limits established by law.

These funds must invest in securities traded on organized and authorized primary and secondary markets in Costa Rica. They may also invest in foreign securities provided that such securities are admitted to trade on an organized market.

In general, mutual funds and investment companies are bound by the investment policy stated in the fund's prospectus. With the exception of non-financial investment funds, to which special restrictions may be applicable by regulation, an authorized fund may not acquire a controlling interest in any company. Unfortunately, the LRMV does not contain a statutory definition of controlling interest for this purpose. However, a controlling interest is understood as an interest in a company that gives the investor its control, which in most cases requires an ownership or control of more than half the voting shares, or in this case, participation units.

Mutual funds must comply with minimum diversification rules issued by SUGEVAL. In general, these rules state that no more than 10 percent to 15 percent of the fund's fair market value may be invested in securities issued by one company or economic group. Furthermore, the SUGEVAL, by way of administrative regulation, may establish special liquidity requirements to authorized mutual funds. In addition, mutual funds can participate directly in initial public offering procedures, prior approval to by the SUGEVAL.

ICs are not allowed:

- to invest the profits of the mutual funds they manage in participations issued by them;
- to invest their capital in the funds they manage;
- to grant credit with the fund's money;
- to grant the investor, directly or indirectly, by means of any type of contract, a determined yield;
- to discriminate the investors by their revenues;
- to participate in the capital of other ICs; or
- any other action prohibited by the SUGEVAL.

Mutual funds cannot control any corporation nor appoint corporate comptrollers or directors on any corporation's board of directors, and cannot participate in any management activity in regards to a corporation in which it has invested.

There are no specific investment restrictions applicable to investment trusts. However, general commercial regulations do not allow the trustee to invest more than one third of the trust's fund in a single company or concern, unless the trust's grantor specifically and expressly authorizes it.

2.5 Borrowing

Under Costa Rican law, a closed-end fund may not issue debt securities or leverage itself with debt, unless so authorized by the meeting of investors. Special limits to authorize a fund's debt financing may be set by the SUGEVAL through administrative regulation. Notwithstanding, open-end funds may seek

debt financing to cover temporary liquidity needs of up to 10 percent of its assets. In the case of general liquidity problems, the SUGEVAL may set this limit at 30 percent.

In general, and with the exception of specific situations described above, an investment fund may not encumber, or lien its assets to obtain debt financing.

2.6 Accounts and prospectus

As a requirement for authorization, an investment fund must file before the SUGEVAL a statement of investment policy. This statement must include the following information:

- The fund's name, which must be accompanied by the phrase investment fund.
- The fund's purpose.
- The names and addresses of the investment and custodian companies.
- The fund's managing regulations, containing at the minimum those which the SUGEVAL requires, including:
 - the fund's term;
 - the investment policy;
 - characteristics of the participation units and of the issuance and reimbursement procedures, among others;
 - fund's general management guidelines;
 - proceeds determination and distribution;
 - the requirements for modifying the contract and the regulations for managing the fund, and for the substitution of the investment company and the custodian company ;and
 - administration, subscription; and reimbursement commissions.

Additionally, the fund shall file a copy of a prospectus, which shall include the same information as the statement of investment policy and be approved by the SUGEVAL.

Furthermore, ICs shall procure that a copy of the prospectus and of all prior quarterly and annual reports be sent, at no cost, to all prospective investors. After subscription of participation units, all of the fund's quarterly and annual reports must be sent also at no cost to the investor. By special regulation, the SUGEVAL determines the specific periodic information requirements and filings applicable to mutual funds.

2.7 Supervision

For mutual funds and investment trusts engaged in public offerings:

Superintendencia General de Valores SUGEVAL
P.O. Box 10677-1000
San José, Costa Rica
Telephone (506) 243-4700
Facsimile (506) 243-4646
E-mail: correo@sugeval.fi.cr
Web site: www.sugeval.fi.cr

For regulated mutual trusts:

Superintendencia General de Entidades Financieras SUGEF
P.O. Box 2762-1000
San José, Costa Rica
Telephone (506) 243-4848
Facsimile: (506) 255-4849
e-Mail: webeditor@sugef.fi.cr
Web site: www.sugef.fi.cr

2.8 Fund ownership

The minimum number of unitholders in a Costa Rican mutual fund is 50, except real estate development funds and funds oriented to sophisticated and institutional investors with a minimum number of 25. This requirement must be achieved within nine months as of the communication of public offering authorization, except real estate development funds within eighteen months.

If at any time the number or unit holders are reduced to less than 50, the IC has six months to reach again the established minimum level. If not accomplished, SUGEVAL may cancel the mutual fund; resulting in the cancellation of the authorization to perform public offering.

2.9 Fund structure

Costa Rican law authorizes the operation of mutual funds of funds (mega funds). Umbrella funds, which are offshore funds consisting of a fund of funds that invest in offshore funds, are not yet permitted under local legislation.

Participation units must be issued in the name of the owner, (nominative participation units). Bearer participation units are not allowed.

2.10 Stock exchange registration

Closed-end mutual funds are required by law to register for trading on an organized local exchange. Open-end investment funds cannot be listed since its participation units are only subject to redemption by the fund. Open-end investment funds' participation units are not considered securities.

Participation units of foreign funds, as for any other foreign securities, may be registered for trading at a local exchange, provided they are authorized by the SUGEVAL.

2.11 Bank secrecy

The Law on Narcotics, Psycho tropics, and Unauthorized Drugs prohibits and punishes money laundering and related activities. National banks have the obligation to prevent such activities, and if the SUGEVAL suspects about money laundering related activities, immediately it must inform the judicial branch.

Additionally, Costa Rica has adopted several international treaties about the subject such as:

- the agreement between Central America and Dominican Republic for the prevention and reprehension of money laundering and other assets regarding the illegal drug traffic and related crimes, and
- the United Nations agreement against drug illegal traffic and narcotics.

2.12 Fund set-up

If all requirements are met upon filing, the estimated term for obtaining authorization for an mutual fund oscillates around three months under several compliance conditions such as to make the respective publications and comply or submit the additional requirements in order to be able to market the mutual funds.

The mutual fund must initiate operations no later than nine months after the compliance conditions mentioned above are completed. Otherwise, the authorization will be cancelled.

Costs related to the set-up of the fund are comprised of legal fees involved in the preparation of legal documentation required for the filing, for example, sworn declarations, legal certifications, and others. However, no specific fee shall be paid to the SUGEVAL in order to file such request.

2.13 Foreign funds

The General Regulation of Investment Companies and Mutual Funds, issued on 8 May 2006, establishes the requirements on the marketing of mutual funds, organized and managed under the laws of a territory outside the Costa Rican jurisdiction. Such regulations establish that, only the mutual funds that have been previously authorized by the SUGEVAL, can be offered in the Costa Rican market. The authorization may only be requested by the entities that are allowed to perform the marketing of the mutual fund, which may be: the investment company through a branch office established in Costa Rica, or the Costa Rican local investment companies or brokerage firms that are previously authorized by the foreign fund investment company to market the mutual fund locally.

Local securities law regulates the public offering of securities or participation units within the territory of Costa Rica. A public offering is defined by statute as any offer, implied or explicit, with the purpose of issuing, allocating, negotiating, or trading securities, transmitted by whatever means to the public or a specific group.

If a foreign fund desires to market its participating units in a public and widespread fashion, a request and filing for authorization must be made to the SUGEVAL. The new regulation establishes very specific requirements that must be complied, in order to obtain the authorization to offer participation units of foreign mutual funds within the Costa Rican territory.

Once the request has been filed and all the requirements have been complied, the SUGEVAL must give the authorization according to related dispositions of the General Public Administration Act. The entity authorized to market the foreign fund must comply with the reporting duties and other obligations with the SUGEVAL, which are set forth by the General Regulation of Investment Companies and Mutual Funds. The SUGEVAL shall inform the corresponding supervisory authorities of the country where the mutual fund are registered, of any violation of the legal dispositions regulating the funds. In these cases, the Consejo Nacional de Supervisión del Sistema Financiero, CONASSIF, may suspend the public offer of the fund's participation units and cancel the marketing authorization.

2.14 Bearer shares

Bearer shares are securities which are not issued under the name of a determined person, and are transferred by simple delivery. These shares are negotiable instruments with no record of ownership. Therefore, title is held by anyone who possesses the security and holds it in good faith. Under Costa Rican legislation, corporations cannot issue bearer shares.

2.15 Use of the internet

The use of the internet to market investment funds in Costa Rica is deemed as a public offering, and as such, is subject to regulation and authorization by the SUGEVAL, since the internet is considered a massive communication media.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.