



DEAR CEO LETTER No. 7/2008

about the principles applicable during the conversion of open-end property investment funds to closed-end property investment funds

Due to the large-scale withdrawal of capital from open-end property investment funds and the funds of property funds, and in order to reach the targeted objectives, i.e. minimise the expected losses of investment unit holders of the property investment funds, provide more extensive information to investors, maintain the efficient operation of property investment funds and the investment fund management sector, as well as the smooth operation of the real estate sector, as the targeted objectives, the Hungarian National Financial Supervisory Authority (hereinafter referred to as 'HFSA') has decided on the suspension of trading with the investment units issued by such funds for 10 days in its Resolution No. J-III-200/2008.

Since capital withdrawal has continued even after the suspension, pursuant to Section 260 of Act CXX of 2001 on the capital market (hereinafter Capital Market Act) several open-end property investment funds have decided on or are considering conversion to closed-end funds.

In connection with the conversion of open-end property funds to closed-end property funds the HFSA has established a group of principles that will – in its opinion – ensure the enforcement of the investors' interests.

By way of this Circular letter the *HFSA* hereby draws the attention of investment fund management companies to the fact that the principles stipulated herein shall be observed during each conversion, and that it will increasingly check compliance with them. *However, by exercising its right provided by Section 260 (7) of the Capital Market Act, due to the different nature of the individual conversions, in the case of certain funds, and in well-justified cases the HFSA may set individual terms and conditions for conversion in order to protect the investors' interests.*

In terms of investor protection, the HFSA finds it paramount that the investors of the fund to be converted should make responsible decisions about their investments, for which they should be given sufficient time and information.

For the achievement of the above goal we recommend that the following principles be observed during the conversion of open-end property funds to closed-end property funds:

1. The responsible decision-making of the investors is best served if the information leaflet on conversion approved by the HFSA and published by the Company *contains a comprehensive set of relevant information*, including the components concretely identified in the act (cause, date, and terms and conditions of conversion), as well as information on settlement with the investors (so called settlement plan), on the investment policy to be followed while operating as a closed-end fund, as well as on the portfolio. The investment fund manager must comply with its information supply obligation towards the investment unit holders pursuant to Section 260 (9) of the Capital Market Act, concurrently with the submission of the information leaflet on conversion to the HFSA.

2. The information leaflet on conversion shall expressly call the investors' attention to the ***risks of conversion***, including the fact that the ratio of redemption assignments influences the date and exchange rate of performance, and that in an unfavourable case it may trigger the liquidation of the fund instead of its conversion. Furthermore, the sale of properties required for compliance with the redemption assignments may influence the property composition of the closed-end property fund that comes into being following conversion.
3. During the measures taken by the fund manager (sale of property, borrowing, etc.) in order to create the liquidity required for the fulfilment of the accepted redemption assignments, extreme diligence must be exercised.
4. With regard to the legal provisions stipulated in Section 260 (10) of the Capital Market Act, the HFSA's approval for the conversion of an open-end property fund to a closed-end fund can only be *provisional* in the sense that conversion can take place on the scheduled date, if all redemption assignments have been fulfilled. In case this condition is not met, conversion cannot take place, the HFSA will revoke the permit for conversion pursuant to Section 260 (11) of the Capital Market Act, and the fund may continue to operate as an open-end fund, or the fund manager may decide on the liquidation of said fund pursuant to Section 256 (2) of the Capital Market Act. **The HFSA finds that for the protection of the investors' interest this risk, as well as the practice to be followed in case conversion fails, shall be explained to the investors in the announcement on conversion.**
5. The entire timeframe, or most of the timeframe between the issuance of the announcement on conversion stipulated in Section 260 (6) of the Capital Market Act ***at least thirty days before the scheduled date of conversion and the value date of settlement***, shall be a period in which the investors may – based on the information required for decision-making – use their right of redemption stipulated in Section 260 (10) of the Capital Market Act. It serves the adequate protection of the investors if – in conformity with Sections 260 (6) and (10) – the length of the timeframe available for the submission of redemption assignments is as close to 30 calendar days as possible.
6. Redemption assignments that were accepted before the issuance of the announcement on conversion, but not fulfilled until the value date of settlement, as well as purchase assignments given prior to conversion, in the period available for redemption assignments too, as well as in the subsequent period available for the acceptance of purchase assignments only, ***shall be calculated with the same settlement value date, at the net asset value for the same single unit, prior to the conversion date***. Purchase assignments given before the end of the period available for the submission of redemption assignments, too, before conversion shall be accounted according to the management regulation in force. ***Redemption assignments (including payments) shall be fulfilled by the trader before the conversion date.***
7. According to the opinion of the HFSA, ***suspension pursuant to Section 251 (2) of the Capital Market Act has no dilatory effect*** regarding accounting and the calculation of the accounting periods, i.e. ***assignments that were received prior to the starting date of suspension and have not been accounted shall be fulfilled according to the accounting rules irrespective of the fact of suspension.***
8. The Fund Manager shall disclose the content of Section 260 (6) of the Capital Market Act in the form of an extraordinary announcement, and shall display the fact of conversion at the trader's premises of the investment units. In addition to the place of disclosure specified in the management regulation of the fund, ***pursuant to Section 260 (9) of the Capital Market Act the HFSA finds it necessary that the investment unit holders be***

informed in writing, too, about the cause, planned date, as well as the terms and conditions of conversion. The trader shall be able to credibly certify that the aforementioned notification was sent to each unit holder. The documented use of any form of written notification specified in the internal regulatory documents and in the agreements signed with the customer can be accepted for the aforementioned objective (e.g. postal book entry allowing individual identification, fax-receipt confirmation, 'e-mail sent' confirmation, etc.).

Furthermore, I inform you that the HFSA will publish this Circular Letter for Chief Executive Officers on its website under PSZÁF/Regulations/Recommendations, policies, guidelines and DEAR CEO Letters.

Budapest, 19 December 2008.

Sincerely yours:

Csaba Varga
director general of the HFSA