

ESMA
103, rue de Grenelle
F-75007 Paris

Copenhagen 22nd September 2011

Dear Sirs

Reply to ESMA Discussion Paper - ESMA's policy orientations on guidelines for UCITS Exchange-Traded Funds and Structured UCITS

InvesteringsForeningsRådet (IFR)¹ welcomes the possibility to reply to the above mentioned discussion paper.

We only have comments regarding the possible introduction of an identifier.

8. Do you agree with the proposed approach for UCITS ETFs to use an identifier in their names, fund rules, prospectus and marketing material? If not, please give reasons.

In principle IFR agrees with ESMA's proposal that ETFs should use an identifier (such as "ETF") in their names, fund rules, prospectus, and marketing material. It could be very useful to create an "ETF" label that is well defined and protected.

However, we strongly oppose to an identifier if the criteria for its use are not clearly defined in order to avoid catching UCITS which are listed or admitted to trading on Regulated Markets, but are not ETFs.

We urge ESMA to devote the necessary time to develop such proper identifier in collaboration with the European fund industry.

The reason for this strong statement is twofold:

1. There are 420 non-ETF² funds traded on a tailor made marketplace called IFX which is run by Nasdaq OMX. Danish funds have been listed and traded on this exchange for more than 25 years.
2. The ETF market and other markets for stock listed funds function differently.

¹ IFR is the representative fund association for the Danish fund industry.

² Danish listed funds have not by any bodies ever been considered or described as ETF funds, and are not mentioned in any of the ETF surveys being published over the years.



We refer to the annex where we have described how the Danish fund market works. We highlight the following characteristics:

- There is an extensive regulation of the market place through the “Rules for issuers of investment undertakings” issued by Nasdaq OMX. They impose a series of obligations that the fund company must meet. For your information we attach the rules to this letter.
- Danish fund companies are obliged to supply NAV, subscription price and redemption price to IFX at least three times a day according to the official rules for the market place. This mechanism combined with the market maker’s obligation to ensure best execution ensures that trading prices will always lie within the boundaries set by the subscription and redemption prices. This means that the fund manager’s prices are guiding the prices in the secondary market which is not the case for ETF’s.
- If the fund company cannot supply price information under extraordinary circumstances it cannot ensure that investors are treated equally according to Danish law³. In this case it has to ask IFX to stop the trading of the fund(s) in question.
- The market maker and all other investors have the unconditional option to redeem the fund shares directly with the fund manager.
- The unit in which the fund company issues or redeems fund shares is always identical to the units traded on the exchange i.e. the units on the primary and the secondary market are identical.

Summary

In short Danish funds are traditional mutual funds which offer a cheap and simple way to buy and sell fund shares by using any online trading platform. Even though they are traded on the exchange, most transactions are executed on the basis of financial advice according to the MIFID rules by the bank the investor normally uses. The exchange listing, however, implies that the bank can buy and sell the fund shares on behalf of the investor at more favorable prices than the subscription and redemption prices.

Yours sincerely

Jens Jørgen Holm Møller
Chief Executive

Cc: Ugo Bassi, Head of Unit G3, DG Markt, European Commission

Annex A: Listed Danish UCITS funds description

Annex B: OMX rules for issuers of investment undertakings

³ The rule implemented is coming from the UCITS-directive. Equal treatment of investors is a required by law for UCITS as well as non-UCITS.



Annex A

Listed Danish UCITS funds - description

Danish retail funds have been traded at Copenhagen Stock Exchange for more than 25 years and in the last four years on a tailor made marketplace created by Nasdaq OMX (See www.ifx.dk).

More than 420 funds are listed and almost 400 of the funds are actively managed, whereas almost none of the Danish UCITS funds use alternative investment strategies. The exchange listing of Danish funds is only a technical way to help investors trade the existing shares, so issues and redemptions happen less frequently and make bid and offer spread as narrow as possible.

Most Danish funds collaborate with a bank that acts as a market maker. The market maker is an ordinary investor who has agreed to be active in the market and trade frequently if needed.

Main facts about the Danish market place for funds

- Most retail funds are listed on the marketplace fund market place, Copenhagen Investment Fund Exchange, IFX, ifx.dk, a part Nasdaq Copenhagen OMX Exchange
- Most fund companies collaborate with a market maker
- 95% of all funds are actively managed
- Use of the “double pricing methodology” is required to be listed on the OMX Copenhagen, according to the Investment Associations etc. Act

Facts about the double pricing methodology

- Fund shares are issued at an issue price higher than NAV, and fund shares are redeemed at redemptions price lower than NAV. The difference between the issue/redemption price and NAV are the costs for the fund incurred by buying or selling the underlying securities in the fund portfolio, i.e. each new investor (or leaving investor) pay for the costs involved by changing the fund portfolio. In this way, NAV is used as base for all issues and redemptions, and the subscription and redemption price are the outside boundaries for the trading in the fund.
- To reduce the spread between issue/redemption prices, a secondary market with a market marker is established. The existence of market maker, who trades already issued fund shares implies that investors typically can sell at a higher price than the redemption price.

Facts about Danish secondary market

- A market maker is active on the secondary market at all times.
- The main job for the market maker is to make sure that investors can buy and sell fund shares at prices that are at least as favorable as the issue and redemption prices set by



the fund company.

- Fund shares are only traded in the same unit sizes at they are issued or redeemed by the fund company
- Prices of the fund shares are not only determined by supply and demand during the day, but also by NAV during the day. When a NAV is distributed during the day, the issue and redemption prices are moved as well, and the bid and offer prices will ceteris paribus move accordingly.

Facts about exchange trading

- The Exchange is not involved in the calculation of iNAV of any kind, and iNAV is not used by Danish funds.
- Only NAVs calculated by the fund company are used as basis for the setting of bid and ask prices.
- Exchange trading is mainly a technical setup (to support the secondary markets) which insures that bid and ask spreads are as narrow as possible and that fund prices are distributed to newspapers and online platforms as easily as possible.
- The rules or issuers of investment funds traded on the Nasdaq OMX Copenhagen includes rules
 - a) Conditions governing admissions of units to trading
 - b) The admission procedure
 - c) Obligations regarding announcements and corporate actions(see the full list of rules of issuers of investment funds in the attachment A, “Rules for issuers of investment undertakings, July 2009”)
- Nasdaq OMX Copenhagen has special rules for issuers of ETF on Nasdaq OMX Copenhagen.
(see attachment B “Rules for issuers of ETF’s on Nasdaq OMX Copenhagen A/S, July 2011). They cannot be admitted to trading on the Investment Fund eXchange – www.ifx.dk.
- OMX Copenhagen Stock Exchange has rules for listed funds that ensure that governance rules for calculation of NAV are very high. For example, for listed funds, the fund companies are obliged to calculate and distribute to the exchange a NAV, subscription price and a redemption price, at least three times daily. Furthermore, in case of significant changes in the values, such changes shall be published (see section 3.8.2 in rules for issuers).
- The exchange may remove a unit from trading if the unit no longer applies the rules of the exchange. Deletion shall not be made though, if there is a possibility that it would be materially detrimental to the interests of the investors or the proper functioning of the market (see section 1.11 in rules for issuers).
- Observation list. The exchange may decide to transfer the units on an investment undertaking to the observation list, if for example the fund company fails to satisfy the requirements for admission to trading or it is deemed that exceptional circumstances



exist which mean that care should be exercised in fixing the price (see full list in section 1.9 in rules for issuers).

- Delisting is possible in Denmark, however a delisting can imply that the bid and ask spread on the secondary market will not be as narrow as before.
- The Danish funds cannot be traded OTC.

Facts about Danish market maker model

- Market maker agreements are used both for listed and unlisted Danish funds
- The market maker ensures investors can always sell and buy fund shares.
- The market maker is an ordinary investors which has just agreed to be active. The market maker has also agreed to make sure that the number of funds shares available at the market is always positive. If a lot of investors want to buy/sell, the market maker will typically be the market participant who subscribes/redeems nearly all fund shares.

Facts about portfolio disclosure

- Portfolios of Danish funds are published monthly or quarterly.

Facts about issues and redemption options

- Investors will rarely need to go to the fund company to redeem the fund shares, as they on the secondary market typically will receive a price that is higher than NAV less redemption fees.
- The market maker and all other investors have the option to redeem the fund shares directly with the fund manager.
- When new fund shares are created, the fund company will receive cash from investors and will allocate fund shares in return, by investing the cash received according to the fund's investment mandate.

Facts about active /passive management

- 95% of all listed Danish funds are actively managed. Typically, ETF's are recognizes as passively managed funds

Ownership and registration

- All fund shares are registered by name with the Danish CSD, called VP Securities.
- The market maker is registered as owner for the fund shares he owns.
- All ownership rights are transferred to the new investor when a fund share is traded.