

26th of November 2004

Mandate to CESR for advice on possible modifications to the UCITS Directive in the form of clarification of definitions concerning eligible assets for investment of UCITS

Reply of Euronext to CESR's call for evidence dated 28th of October 2004
(Ref. CESR/04-579)

Euronext is grateful for the possibility to comment on the mandate given to CESR in relation to the UCITS III Directive. We have focused our comments on issues relating to indices replicating UCITS.

CESR is asked for technical advice on the factors to be used to determine whether and under what conditions, in a given situation, a UCIT can be considered as replicating the composition of a certain index (Art.22a(1)) having regard, in particular, to the three criteria set out in the provision and the elements relating to overall limits in investment in securities issued by any one issuer.

Euronext welcomes the work CESR intends to achieve in this respect. We however wish that such work be extended to the definition of the notion of 'replicating the composition' of an index. Indeed, we think it should be possible for Index Funds not only to reproduce the composition of an index as it is composed but also to use, to some extent, additional financial instruments that would enable the fund to replicate the index by other means than directly investing in the shares concerned, e.g. derivative products. CESR could even consider the possibility to draw up a list of index related products in which UCITS would be permitted to invest while keeping their 'UCITS III compliant' Index status. Furthermore, it would be useful to make clear what can be considered as an 'index'. This definition could include not only indices using specific and transparent rules but also other 'baskets of shares', which do not comply with such rules but are representative from, for example, a particular sector.

Art.22a(1) provides that the UCITS' investment policy must be to replicate the composition of a certain stock or debt securities index which is recognised by the competent authority. Euronext believes that it would be useful to clarify the way this kind of recognition can be obtained and ensure that the way to obtain recognition agreement is the same in all Member States.

Euronext also proposes that CESR should consider the possibility both for UCITS and for interested parties (e.g. exchanges) to ask for index recognition. This would favour the creation of a level playing field and make it easier for UCITS to launch new funds.

Moreover, CESR should make sure that an index recognition obtained in one Member State would mean recognition in all Member States. This would make it easier for UCITS to use both indices from its own Member State and indices created in any other Member State.

CESR is also invited to provide advice in the following fields:

- Factors to be taken into account in assessing whether the composition of the index is 'sufficiently diversified' as provided by Art.22a(1) 1st indent;

- Conditions under which the index can be deemed to ‘represent an adequate benchmark for the market to which it refers’ as provided for by Art.22a(1) 2nd indent;
- The index is ‘published in an appropriate manner’ as provided for by Art.22a(1) 3rd indent.

Euronext welcomes and supports the work that will be done in order to ensure that all Member States will use the same criteria in their evaluation and recognition process. For the purpose of diversification and benchmarking, we underline the need to remain flexible. We would like to ensure that the factors used would take into account the various characteristics of the index (e.g. geographical or sector considerations) but also technical considerations and not only the number of shares that compose the index.

It would be useful to refer, when dealing with the ‘adequate benchmark’ criterion, to the degree of representativeness. Indices always need to find the balance between tradability and representativeness. If the index is updated for every change in the market place, representativeness is high but the costs of tracking the index are also high. It is important to note that a stable index is in the interest of investors as it gives them an efficient tool to invest in the market.

About publication, it should not require the index to be published in a newspaper. The Internet and data-vendors should be sufficient. An obligation to publish in newspapers can lead to a situation where publication of index information is made too expensive. Furthermore, compulsory publication of index data for free should be avoided. It could deprive index provider of an important source of income and be harmful for indices for smaller markets, which do not generate enough income from licences. Only delayed publication should be made available for free.