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| 6 April 2016 |

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| Reply form for the Discussion Paper on Share Classes |
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| Date: 6 April 2016 |

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the Discussion Paper on Share Classes (SC), published on the ESMA website.

*Instructions*

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, ESMA will only be able to consider responses which follow the instructions described below:

* use this form and send your responses in Word format (pdf documents will not be considered except for annexes);
* do not remove the tags of type < ESMA\_QUESTION\_DP\_SC\_1> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
* if you do not have a response to a question, do not delete it and leave the text “TYPE YOUR TEXT HERE” between the tags.

Responses are most helpful:

* if they respond to the question stated;
* contain a clear rationale, including on any related costs and benefits; and
* describe any alternatives that ESMA should consider

***Naming protocol***

In order to facilitate the handling of stakeholders responses please save your document using the following format:

ESMA\_DP\_SC \_NAMEOFCOMPANY\_NAMEOFDOCUMENT.

E.g. if the respondent were XXXX, the name of the reply form would be:

ESMA\_DP\_SC \_XXXX\_REPLYFORM or

ESMA\_DP\_ SC \_XXXX\_ANNEX1

***Deadline***

Responses must reach us by **6 June 2016.**

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘Your input/Consultations’.

***Publication of responses***

All contributions received will be published following the end of the consultation period, unless otherwise requested. **Please clearly indicate by ticking the appropriate checkbox in the website submission form if you do not wish your contribution to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.** Note also that a confidential response may be requested from us in accordance with ESMA’s rules on access to documents. We may consult you if we receive such a request. Any decision we make is reviewable by ESMA’s Board of Appeal and the European Ombudsman.

***Data protection***

Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the headings ‘Legal notice’ and ‘Data protection’.

# Introduction

Please make your introductory comments below, if any:

<ESMA\_COMMENT\_ DP\_SC\_1>

Please find below comments from the Swedish Investment Fund Association (SIFA)[[1]](#footnote-2).

<ESMA\_COMMENT\_ DP\_SC\_1>

1. Would you agree with the description of share classes?

<ESMA\_QUESTION\_DP\_SC\_1>

Yes.

<ESMA\_QUESTION\_DP\_SC\_1>

1. Do you see any other reasons for setting up share classes?

<ESMA\_QUESTION\_DP\_SC\_2>

We would like to add that share classes may provide more transparency to investors when it comes to fee structures. Where share classes have different fees, for example due to the size of the investment or the way it is distributed, this provides more clarity compared to internal “rebates”. Share classes (e.g. different fee structures) could also provide flexibility for fund management companies and investors in a post MiFID II environment, facilitating new ways of distribution combined with different investment services.

<ESMA\_QUESTION\_DP\_SC\_2>

1. What is your view on the principle of “common investment objective”?

<ESMA\_QUESTION\_DP\_SC\_3>

We agree with ESMA, also when it comes to currency risk hedging being compatible with the principle of a common investment objective.

<ESMA\_QUESTION\_DP\_SC\_3>

1. Which kinds of hedging arrangements would you consider to be in line with this principle?

<ESMA\_QUESTION\_DP\_SC\_4>

FX/currency hedging.

<ESMA\_QUESTION\_DP\_SC\_4>

1. What is your view on the principle of “non-contagion”?

<ESMA\_QUESTION\_DP\_SC\_5>

We agree with ESMA:s views that any additional risk or costs associated with a share class should be borne by the investors in that share class, as stated in paragraph 26.

<ESMA\_QUESTION\_DP\_SC\_5>

1. Are you aware of any material evidence of investors in one share class suffering losses as a result of the crystallisation of risk in another share class?

<ESMA\_QUESTION\_DP\_SC\_6>

No.

<ESMA\_QUESTION\_DP\_SC\_6>

1. Where do you see a potential for contagion risk arising from the use of derivative hedging arrangements? What are the elements of this contagion risk? (cf. paragraph 23)

<ESMA\_QUESTION\_DP\_SC\_7>

We agree with ESMA:s description in paragraph 23, and also on how the risk should be mitigated as described in paragraph 26.

<ESMA\_QUESTION\_DP\_SC\_7>

1. Do you agree with the operational principles set out in paragraphs 28 and 29?

<ESMA\_QUESTION\_DP\_SC\_8>

In paragraph 28 (d) it is mentioned that the management company should be able to evidence, ex ante, that the implementation of a derivative overlay will lead to a share class which better aligns with “the specific risk profile of the investor”. It is unclear what the purpose of this paragraph is. Since funds are collective portfolios rather than individual ones SIFA believes that reference should not be made to “the investor” but rather to ”the fund”. Moreover, since using currency hedging is a way to ensure that the funds’ common investment strategy will result in the same outcome regardless of the currency in which a share class is nominated a reference to “the risk profile of the fund” would seem more appropriate.

In paragraph 29 (c) it is stated that the management company should ensure that under-hedged positions do not fall short of [95] per cent of the net asset value of the share class, unless it has been “explicitly stated in the investment strategy of the share class”.

Since share classes should not be allowed to have different investment objectives it could be clearer to say “the hedging strategy of the share class” or “the investment strategy of the fund”. It could also be made clearer whether “explicitly stated” refers to information in the prospectus or any other type of information.

We also seek clarification to whether this means that a share class may never be partially hedged (for example to have a 50 per cent hedge in mixed funds).

<ESMA\_QUESTION\_DP\_SC\_8>

1. Do you consider the exposure limits in paragraphs 29.b and 29.c to be appropriate?

<ESMA\_QUESTION\_DP\_SC\_9>

SIFA agrees with the limits. However, daily subscriptions and redemptions may in particular situations lead to conditions where the limits may not suffice. It should therefore be possible, as according to Article 57(2) of the UCITS Directive, to remedy such a situation as soon as possible.

<ESMA\_QUESTION\_DP\_SC\_9>

1. Which stresses should be analysed as part of the stress tests?

<ESMA\_QUESTION\_DP\_SC\_10>

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<ESMA\_QUESTION\_DP\_SC\_10>

1. Which hedging arrangements would you consider as compatible with the operational principles outlined above? Insofar as you consider some (or all) of the hedging strategies in paragraph 30(a)-(b) as being compatible with these operational principles, please justify how such strategies are compatible with each one of the principles.

<ESMA\_QUESTION\_DP\_SC\_11>

SIFA agrees that hedging arrangements as mentioned in paragraph 30 (a) is compatible with the principles. SIFA believes that there may also be other arrangements in line with the principles, but has no information on this from the Swedish market.

<ESMA\_QUESTION\_DP\_SC\_11>

1. Notwithstanding the fact that ESMA considers the above operational principles as minimum requirements, are there additional operational principles that should apply to address the non-contagion principle?

<ESMA\_QUESTION\_DP\_SC\_12>

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<ESMA\_QUESTION\_DP\_SC\_12>

1. What effect would these additional measures have on the compatibility of the operational principles with further hedging arrangements?

<ESMA\_QUESTION\_DP\_SC\_13>

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<ESMA\_QUESTION\_DP\_SC\_13>

1. What is your view on the principle of “pre-determination”?

<ESMA\_QUESTION\_DP\_SC\_14>

SIFA agrees with ESMA that all features of a share class should be pre-determined before the share class is set up.

<ESMA\_QUESTION\_DP\_SC\_14>

1. Are there additional requirements necessary to implement this principle?

<ESMA\_QUESTION\_DP\_SC\_15>

No.

<ESMA\_QUESTION\_DP\_SC\_15>

1. What is your view on the principle of “transparency”?

<ESMA\_QUESTION\_DP\_SC\_16>

SIFA shares the view that the existence and nature of all share classes should be disclosed to all investors of a fund. This is already achieved today through the description in the prospectus, where, at least for Swedish funds, all share classes and their different characters shall be described.

However, SIFA finds it somewhat unclear how paragraphs 35 and 36 coincides. In paragraph 35 it is mentioned that, since some kinds of share classes, namely those with derivative overlays, introduce counterparty and operational risk, new and existing investors should be informed about the creation and existence of such share classes in a timely fashion, including updates in periodic reports. ESMA than states in paragraph 36 how transparency should be achieved. SIFA suggests that it is made clear that the actual transparency requirements are (only) the ones mentioned in paragraph 36. Otherwise it could be read as if paragraph 35 introduces other transparency requirements for share classes with derivative overlays.

SIFA would specifically like to stress that the creation of a share class in a fund normally should not require specific communication to existing unitholders of the fund or another share class. Existing unit holders are in general not affected by the creation of a new share class. Our experience is that investors seek information only where it as affecting their investment and information sent to them where it is not relevant often tends to lead to confusion and questions from investors. Another thing is of course that the introduction of a new share class should be stated in the prospectus and the periodic reports.

<ESMA\_QUESTION\_DP\_SC\_16>

1. Do you consider the disclosure requirements to be sufficient?

<ESMA\_QUESTION\_DP\_SC\_17>

SIFA believes that information as suggested by EFAMA in paragraph 36 is sufficient. It could be added that information under paragraph 36 (b) should be available on the management company’s website.

<ESMA\_QUESTION\_DP\_SC\_17>

1. Notwithstanding the fact that ESMA considers the above operational principles on transparency as minimum requirements, which modifications would you deem necessary?

<ESMA\_QUESTION\_DP\_SC\_18>

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<ESMA\_QUESTION\_DP\_SC\_18>

1. Do you see merit in further disclosure vis-à-vis the investor?

<ESMA\_QUESTION\_DP\_SC\_19>

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<ESMA\_QUESTION\_DP\_SC\_19>

1. If a framework for share classes, based on the principles as outlined in this paper, was introduced at EU level, what impact on the European fund market could this have?

<ESMA\_QUESTION\_DP\_SC\_20>

The proposed framework is very much in line with existing Swedish rules why there will be little impact on a national level for Swedish management companies. For investors a framework would ensure a uniform treatment and a high level of protection which could enhance the UCITS brand.

<ESMA\_QUESTION\_DP\_SC\_20>

1. Given ESMA’s view that certain hedging arrangements currently in place might not be compliant with the common principles of share classes as outlined above, which kinds of transitional provision would you deem necessary?

<ESMA\_QUESTION\_DP\_SC\_21>

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<ESMA\_QUESTION\_DP\_SC\_21>

1. The Swedish Investment Fund Association with its 50 member companies represents the majority of fund-based savings in the Swedish investment fund market. [↑](#footnote-ref-2)