IRISH FUNDS
INDUSTRY
ASSOCIATION

SUBMITTED ONLINE AT:
www.esma.europa.eu *under "Your input – Consultations"*
European Securities and Markets Authority
103, rue de Grenelle
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France

30 March 2012

RE: Response to ESMA Consultation Paper: *ESMA's Guidelines on ETFs and Other UCITS Issues*

INTRODUCTION

The Irish Funds Industry Association (IFIA) is the industry association for the international investment fund community in Ireland, representing the custodians, administrators, managers, transfer agents and professional advisory firms involved in the international fund services industry in Ireland.

Ireland is the leading centre for Exchange Traded Funds (ETFs); with EUR 62 billion of assets in Ireland domiciled ETFs, which accounts for nearly one third of all Europe domiciled ETFs. In addition, to the ETF industry, Ireland is also a leading center for UCITS funds with EUR 847 billion in Ireland domiciled UCITS. Accordingly, all developments in both the Exchange Traded Funds and UCITS arena are of particular importance to the Irish industry.

The IFIA welcomes the publication of, and the opportunity to comment on, ESMA's Consultation Paper on Guidelines on ETFs and Other UCITS Issues. We have responded, in detail, to the questions in Consultation Paper. However, we want to highlight some of the core themes of our response.

Firstly, we welcome that ESMA has expanded the scope of the consultation paper, where applicable, to include all UCITS funds. This was a key item of concern that we had flagged in our response to the 2011 Discussion Paper. We also welcome ESMA's continued push for increased transparency and harmonization, which will a great benefit to the UCITS brand and EU retail investors.

However, we do have concerns about some of the proposals. Namely, we strongly disagree with the proposed approach to collateral, both in the context of TRS and Securities Lending. We believe the proposals fundamentally misunderstand the role that collateral plays. In addition, we think that some of the issues raised in the consultation are too complicated to be handled within the context of this consultation and should be dealt with separately. Finally, we think that these proposals should take into account other open regulatory initiatives, such as MiFID II, MAD, AIFMD and PRIPS. As we note in our response, some of the issues highlighted by ESMA are better addressed by these regulatory frameworks.

I. Index-tracking UCITS

Q1: Do you agree with the proposed guidelines?

We agree with the need to provide a clear description of the index and its underlying components. However, with respect to the proposal to direct investors to a web site where the exact composition of the index is published, we note that index data remains proprietary to the index provider. It is not uncommon that there are restrictions as to the full composition and weightings of the index or that the data supplied is subject to a time delay. This is to protect the position of the provider and ensure that no mandate may be run against that index without entering into the appropriate licensing arrangements with the provider.

We believe that UCITS Index Funds are already transparent with regard to the method by which an index is tracked and the implications for investors. The risks relating to counterparty exposure and impacts of replication method would already be comprehensively detailed in the prospectus.

We agree that it is appropriate to disclose certain information concerning the tracking error of an Index tracking UCITS. However, while Tracking Error is an important metric, it should not be considered the sole metric for evaluating an index fund. We believe that there is excessive focus on ex-post tracking error. While the measure is of relevance to the short term institutional investor, it is of less significance to the buy and hold investor who will may be more concerned with performance against a benchmark

Q2: Do you see merit in ESMA developing further guidelines on the way that tracking error should be calculated? If yes, please provide your views on the criteria which should be used, indicating whether different criteria should apply to physical and synthetic UCITS ETFs.

We support the principle of creating a harmonized EU framework for the calculation of tracking error. However, creating a harmonized frame work will require agreement on the definition of tracking error, the circumstances in which it is generally expected to be met, whether these differ for different replication methodologies and caveats around why it might not be met. We believe that this is a large and complex issue that should be dealt with in a separate consultation. We would welcome the opportunity to work with ESMA on this effort.

Q3: Do you consider that the disclosures on tracking error should be complemented by information on the actual evolution of the fund compared to its benchmark index over a given time period?

Yes, we believe that disclosure on tracking error should be complemented by additional information. As noted above, tracking error is an important data point, but it is not the only one that investors use to judge a fund. Additionally, tracking error is already complemented by information that is found in the KIID.

II. Index-tracking leveraged UCITS

Q4: Do you agree with the proposed guidelines for index-tracking leveraged UCITS?

Yes, we generally agree with the proposed guidelines. However, we note that the actual costs of leverage should only be disclosed if of a material nature. In addition, the appropriate place for these disclosures is in the annual report.

Q5: Do you believe that additional guidelines should be introduced requiring index tracking leveraged UCITS to disclose the way the fund achieves leverage?

No, we do not believe that additional guidelines, beyond what is proposed here, are necessary.

III. UCITS Exchange Traded Funds

Definition of UCITS ETFs and Title

Q6: Do you agree with the proposed definition of UCITS ETFs? In particular, do you consider that the proposed definition allows the proper distinction between Exchange- Traded UCITS versus other listed UCITS that exist in some EU jurisdictions and that may be subject to additional requirements (e.g. restrictions on the role of the market maker)?

Yes, we agree with the proposed definition of a UCITS ETF. However, we note that there may be no formal relationship between an ETF issuer and a Market Maker that would oblige a market maker to take any action to ensure units trade in line with NAV.

We support the idea of harmonizing market making rules; however, we believe that the regulation of market making activities should be handled within the MiFID/MiFIR framework

Q7: Do you agree with the proposed guidelines in relation to the identifier?

In our response to the 2011 Discussion Paper, we noted that there was some debate amongst our members about the necessity of a specific ETF identifier. However, if ESMA believes that an identifier is necessary, than, yes, we agree with the proposed guidelines in relation to the identifier.

However, we believe there is a need for further clarification regarding the use of the identifier. For example, is the use of the identifier mandatory or voluntary? Is the ID to be used at the umbrella or sub-fund level?

Finally, we wonder how ESMA can enforce the use/non use of an ETF ID by a non-UCITS fund through the UCITS framework. Given that this issues touches upon both UCITS and non-UCITS and is concerned with the misselling of funds to retail investors, we believe that issue might be better handled in the existing MiFID review process and the PRIPS initiative.

Q8: Do you think that the identifier should further distinguish between synthetic and physical ETFs?

There are differing opinions expressed by members as to whether creating further identifiers to distinguish synthetic and physical ETFs is warranted. However, most members disagree that further distinction is required and, in addition, feel the terms "synthetic" and "physical" are too ambiguous to be effectively used as identifiers.

However, there is agreement that there are differences between the strategies and types of ETFs and that knowing how the ETF is constructed and managed is in the interest of the investor. To this end, we believe that there should be clear and comprehensive disclosure of portfolio management techniques in both the KIID and prospectus.

Q9: Do you think that the use of the words 'Exchange-Traded Fund' should be allowed as an alternative identifier for UCITS ETFs?

We think that it is preferable to have a single uniform ETF Identifier. However, we have no strong objection to the use of "Exchange-Traded Fund", though it should be noted that this may have implications for non-English speaking counties.

Q10: Do you think that there should be stricter requirements on the minimum number of market makers?

We do not believe there is a need to require more than one active market maker. In addition, we believe that the regulation of market makers is an issue for the local exchanges and is outside the bounds of this consultation.

Actively-managed UCITS ETFs

Q11: Do you agree with the proposed guidelines in relation to actively-managed UCITS ETFs? Are there any other matters that should be disclosed in the prospectus, the KIID or any marketing communications of the UCITS ETF?

Yes, broadly we agree with the proposed guidelines. However, we note that the "portfolio transparency" needs to be handled judiciously. The portfolio of an actively managed ETF contains the proprietary trading strategy of the Investment Manager; therefore the portfolio transparency should be restricted to the Market Makers, who need this information to perform their function.

We do not believe that additional disclosures are necessary. In fact, as we mentioned in our response to the 2011 Discussion Paper, we believe that all the requirements around risks, investment policy, iNAV and active nature of the funds are met in existing documentation.

Secondary market investors

Q12: Which is your preferred option for the proposed guidelines for secondary market investors? Do you have any alternative proposals?

We strongly support Option 1. As we noted in our response to the 2011 Discussion Paper, almost all funds in the EU are bought and sold through financial intermediaries. There is no material difference between a nominee account on the register of a traditional UCITS fund and the nominee account within the CSD for an ETF. In both cases, the underlying beneficial owner of the fund is not recognized as the legal owner of shares/units in the funds.

Additionally, the ESMA guidance seems to suggest that allowing secondary market investors to directly redeem is a straight forward process. In fact, this would create significant operational and workflow issues for the industry, which would require substantial development to meet.

Q13: With respect to paragraph 2 of option 1 in Box 5, do you think there should be further specific investor protection measures to ensure the possibility of direct redemption during the period of disruption? If yes, please elaborate.

No, we have no further suggestions at this time.

Q14: Do you believe that additional guidelines should be provided as regards the situation existing in certain jurisdictions where certificates representing the UCITS ETF units are traded in the secondary markets? If yes, please provide details on the main issues related to such certificates.

We believe that secondary market investors would benefit greatly from harmonization of EU exchanges. We would welcome the opportunity work with ESMA on such an initiative. In addition, we welcome the proposed MiFID II extension of the post trade reporting and transparency to cover ETF trading.

Q15: Can you provide further details on the relationship between the ETF's register of unit-holders, the sub-register held by the central securities depositaries and any other sub-registers held, for example by a broker or an intermediary?

We have no further information at this time.

IV. Efficient portfolio management techniques

Q16: Do you agree with the proposed guidelines in Box 6? In particular, are you in favour of requiring collateral received in the context of EPM techniques to comply with CESR's guidelines on Risk Measurement and Calculation of Global Exposure and Counterparty Risk for UCITS?

We broadly agree with the goals to increase transparency and harmonize rules. However, we have some serious objections to many of the proposals around collateral. These objections are articulated in the answers to the ensuing question. In addition, we want to highlight the following issues with the proposed guideline 3.

There is general consensus that disclosure of fee sharing arrangements in relation to EPM techniques is desirable; however, it needs to be clear as to how this disclosure would operate. Maximum percentages would be possible, as these could be set in advance in a prospectus. It is noted that the general rule is the expectation that fees arising from EPM techniques would be returned to the UCITS. Clarification as to what this means in practice is requested. For example, securities lending is often carried out by a third party agent. In this scenario, a third party agent is usually reimbursed through a fee sharing arrangement rather than charging a flat fee. Under this arrangement, the third party will take its fee out of the income arising from the securities lending activity, before passing the remainder on to the UCITS.

Clarification is also requested in relation to the requirement that the UCITS should ensure that it is able, at any time, to recall "any security that has been lent". In this regard, it is normal practice that the security or <u>equivalent</u> securities are returned and it is important that this process remains, to allow the process operate efficiently.

Q17: Do you think that the proposed guidelines set standards that will ensure that the collateral received in the context of EPM techniques is of good quality? If no, please justify.

No, we do not believe that the proposed guidelines set standards that will ensure that the collateral received in the context of EPM techniques is of good quality. Our view is that the proposed guidelines in relation to collateral have the possibility to result in collateral received being less beneficial than might be the case under current requirements. Collateral is received to reduce or mitigate the risks of the default of the counter party. This is its core benefit.

In addition, to require that collateral be combined with the fund portfolio for the purposes of risk management, global exposure or counterparty risk would be operationally complex, if not impossible, for administrators, custodians and management companies to implement. This complexity may completely negate any economic benefit from EPM activities.

We believe that the criteria in Box 26 of CESR's guidelines on risk management are appropriate in setting requirements for good quality collateral and should be sufficient.

Q18: Do you see merit in the development of further guidelines in respect of the reinvestment of cash collateral received in the context of EPM techniques (the same question is relevant to Box 7 below)?

We believe that it would be worthwhile to provide further detail as to the criteria to be used in determining the meaning of "risk-free assets" as used in Box 26 of the CESR Guidelines on Risk Management as the current guidance (which refers to investments providing a return equivalent to short-dated high-quality government bonds) may be open to criticism as being (i) slightly unclear in that no guidance is given as to what is a high-quality government bond other than to cite US T-Bills and (ii) potentially restrictive in that it might restrict certain AAA rated money market funds as eligible for investment of cash collateral.

Q19: Would you be in favour of requiring a high correlation between the collateral provided and the composition of the UCITS' underlying portfolio? Please explain your view.

No, we do not believe a high level of correlation between the collateral provided and the composition of the UCITS' underlying portfolio is desirable. We believe that the requirements to have collateral correlated to the investment policy of the UCITS are counterproductive and could result in the collateral being less liquid than the collateral that would be taken if the obligation were not imposed. The danger is that if UCITS need to "match" collateral with fund investment policy you could end up accepting collateral of a lesser quality than you previously would have simply to ensure compliance with "matching" proposals. This could lead to liquidity issues if a default event occurs.

In the event of a counterparty default, collateral is not intended to directly replace portfolio assets. Typically, in the event of a counterparty default, collateral is liquidated and the proceeds are used to acquire the appropriate replacement securities. This is why liquidity is a key characteristic of collateral.

Q20: Do you agree that the combination of the collateral received by the UCITS and the assets of the UCITS not on loan should comply with the UCITS diversification rules?

No, we do not believe that the collateral should be aggregated with portfolio assets of the UCITS for the purposes of compliance with the UCITS diversification rules. It is an important principle that collateral is not considered part of the fund portfolio and should not be viewed in that context until such time as there is a default

The purpose of collateral is as a mitigant for default of the fund's counterparty and is only relevant upon crystallization of such a default. It was never envisaged that the purpose of collateral would be to reflect the fund's investment policy. The overriding requirement for collateral is that it is of good quality and liquid so that if default ever occurs the fund can quickly sell good liquid assets to mitigate its potential loss due to counterparty default.

While diversification at portfolio level is necessary to ensure risk spreading of the Fund's market exposure, this is not appropriate for collateral. The collateral is not usually taken in by the UCITS as part of its underlying portfolio. Requiring diversification could result in additional costs for the investors with no material benefits.

Q21: With regards to eligibility of assets to be used as collateral, do you have a preference for a list of qualitative criteria (as set out in CESR's guidelines on risk measurement) only or should this be complemented by an indicative list of eligible assets?

We support the idea of a qualitative framework for collateral. Within this construct, we support the creation of a list of eligible assets that is purely indicative and not exhaustive. We do not support a prescribed list of eligible assets.

We also believe that the UCITS IV guidelines have already sufficiently addressed this point.

Q22: Do you believe that the counterparty risk created by EPM techniques should be added to the counterparty risk linked to OTC derivative transaction when calculating the maximum exposure under Article 52.1 of the UCITS Directive?

Yes, we think that the counterparty risk created by EPM techniques should be added to the counterparty risk linked to OTC derivative transactions when calculating the maximum exposure under Article 52(1) of the UCITS Directive. In fact, this is already the case for Irish domiciled UCITS and we would welcome EU harmonization on this point.

Q23: Alternatively, do you see merit in prescribing an exhaustive list of assets eligible for use as collateral? If so, please provide comments on whether the list of assets in paragraph 52 is appropriate.

No, as explained above, we do not see a merit in the proposal. The investment manager of the UCITS is best placed to make the appropriate judgments at the time in accordance with the requirements of the CESR Paper on Risk Measurement (July 2010). The quality of collateral is important to any UCITS fund and the CESR Guidelines referred to above cater for that. In addition, managers should have the flexibility of determining what collateral is received while complying with the CESR Guidelines referred to above.

Q24: Do you agree that entities to which cash collateral is deposited should comply with Article 50(f) of the UCITS Directive?

Yes, we believe that is appropriate.

Q25: Do you believe that the proportion of the UCITS' portfolio that can be subject to securities lending activity should be limited? If so, what would be an appropriate percentage threshold?

No, we do not consider that it is appropriate for ESMA to prescribe such a limit. With appropriate collateral parameters, overcollateralization and a robust counterparty approval and monitoring process, securities lending can be performed in a low risk manner that does not require it being limited at the fund or counterparty level.

Q26: What is the current market practice regarding the proportion of assets that are typically lent?

There is no specific market practice regarding the proportion of assets that are typically lent. The decision on the proportion of assets lent is typically a matter decided by the Board of the relevant Fund. The decision is based on the specific circumstances of the Fund, the nature of the portfolio, the liquidity profile and the risk return profile.

Q27: For the purposes of Q25 above, should specific elements be taken into account in determining the proportion of assets (e.g. the use made by the counterparty of the lent securities)?

As we stated, we do not believe there should be a limit on the proportion of assets that can be lent.

Q28: Do you consider that the information to be disclosed in the prospectus in line with paragraphs 1 and 2 of Box 6 should be included in the fund rules?

No, we do not think it is appropriate that this information be included in the fund rules. We believe that it would be detrimental to investors to have such information set out in the fund rules. Incorporation of this information into the fund rules would result in costs to investors should these principles change, as changes to fund rules require formal approval of shareholders. We believe that disclosure of these items in the prospectus is sufficient.

Q29: Do you see the merit in prescribing the identification of EPM counterparties more frequently than on a yearly basis? If yes, what would be the appropriate frequency and medium?

No, we do not see any merit in prescribing the identification of EPM counterparties more frequently than on a yearly basis. We believe the annual audited report is the appropriate place to identify the EPM counterparties and see no basis for any more frequent disclosure.

Q30: In relation to the valuation of the collateral by the depositary of the UCITS, are there situations (such as when the depositary is an affiliated entity of the bank that provides the collateral to the UCITS) which may raise risks of conflict of interests? If yes, please explain how these risks could be mitigated? The question is also valid for collateral received by the UCITS in the context of total return swaps

In Ireland, the valuation of collateral is the responsibility of the fund or Management Company, depending on the legal form of the fund. The valuation duties are then delegated. Typically, this function is not delegated to the depositary. Where the matters outlined in your question arise, it is important that proper disclosure be made and then the investor will make a decision in relation to how they perceive the risk.

Q31: Do you think that the automation of portfolio management can conflict with the duties of the UCITS management company to provide effective safeguards against potential conflicts of interest and ensure the existence of collateral of appropriate quality and quantity? This question is also relevant to Box 7 below.

We do not fully understand to what this question relates. Before we can make an informed response, we would like further clarification from ESMA

V. Total return swaps

Q32: Do you agree with the proposed guidelines?

No, we do not agree with the proposed guidelines. We have several fundamental issues with the proposals.

We do not think it is appropriate or correct to deem a swap counterparty as an investment manager of the fund (as proposed in paragraph 5d in Box 7). It is clear under UCITS that only the fund and its investment management delegates (as approved by the relevant competent authority and disclosed in the prospectus) have discretionary management of a UCITS. The board of directors of a fund have a fiduciary duty in such regard to ensure that the fund is appropriately managed by an approved person. Further, the MiFID directive, and each implementing country of such directive, sets out in detail who can manage client assets, on what basis, and what approvals are necessary.

In addition, we do not agree with the proposal that, in the case of a funded swap, the collateral posted by the counterparty should be sufficiently diversified to comply with UCITS diversification rules, taking into account both the investments made by the UCITS and the collateral. There are already detailed requirements regarding the aspects of collateral set out in the CESR Guidelines on Risk Management (July 2010). The additional cost and expense that a UCITS would incur (which would be passed to its investors) is not appropriate in light of the limited additional benefit of complying with the collateral diversification guidelines that are proposed. In addition, service providers to UCITS have in the past had difficulties monitoring a combination of a UCITS' investments and its collateral.

Providing a haircut for a "class of assets" is inappropriate as different assets within the same broad class should be viewed separately. Some may not warrant a haircut (in light of the liquidity and limited bid-offer spread) where others may warrant a haircut.

A fund should not be obliged to have to identify particular counterparties just because it uses total return swaps. A UCITS may use a number of counterparties and may change counterparties on a regular basis (in certain strategies). We have no difficulty with the prospectus setting out the criteria that any counterparty will meet rather than identifying particular counterparties. Identifying counterparties in the annual report should be sufficient.

Q33: Do you think that the proposed guidelines set standards that ensure that the collateral received in the context of total return is of good quality? If not, please justify.

No, we do not believe that the proposed guidelines set standards that will ensure that the collateral received in the context of EPM techniques is of good quality. Our view is that the proposed guidelines in relation to collateral have the possibility to result in collateral received being less beneficial than might be the case under current requirements. Collateral is received to reduce or mitigate the risks of the default of the counter party. This is its core benefit.

In addition, to require that collateral be combined with the fund portfolio for the purposes of risk management, global exposure or counterparty risk, would be operationally complex, if not impossible, for administrators, custodians and management companies to implement. This complexity may completely negate any economic benefit from EPM activities.

Q34: Do you consider that the information to be disclosed in the prospectus in line with paragraph 5 of Box 7 should be included in the fund rules?

We do not agree with this proposal. Shareholder consent may be required to amend fund rules and this is wholly inappropriate if a UCITS wanted to change counterparties, change the type and level of collateral or change its reinvestment policy, for example. The fund rules often include provisions regarding the use of derivatives in accordance with the requirements of applicable law and the requirements of the relevant regulator, which is sufficient for such a document. In addition, disclosure of this information in the prospectus is sufficient.

Q35: With regards to eligibility of assets to be used as collateral, do you have a preference for a list of qualitative criteria (as set out in CESR's guidelines on risk measurement) only or should this be complemented by an indicative list of eligible assets?

We support the idea of a qualitative framework for collateral. Within this construct, we support the creation of a list of eligible assets that is purely indicative and not exhaustive. We do not support a prescribed list of eligible assets.

We also believe that the UCITS IV guidelines have already sufficiently addressed this point.

Q36: Alternatively, do you see merit in prescribing an exhaustive list of assets eligible for use as collateral? If so, please provide comments on whether the list of assets in paragraph 73 is appropriate.

No, as explained above, we do not see a merit in the proposal. The investment manager of the UCITS is best placed to make the appropriate judgements at the time in accordance with the requirements of the CESR Paper on Risk Measurement (July 2010). The quality of collateral is important to any UCITS fund and the CESR Guidelines referred to above cater for that. In addition, managers should have the flexibility of determining what collateral is received while complying with the CESR Guidelines referred to above.

Q37: Do you agree that the combination of the collateral received by the UCITS and the assets of the UCITS not on loan should comply with the UCITS diversification rules?

No, we do not believe that the collateral should comply with the UCITS diversification rules. The purpose of collateral is as a mitigant for default of the fund's counterparty and is only relevant upon crystallisation of such a default. It was never envisaged that the purpose of collateral would be to reflect the fund's investment policy. The overriding requirement for collateral is that it is of good quality and liquid so that if default ever occurs the fund can quickly sell good liquid assets to mitigate its potential loss due to counterparty default.

Q38: Do you consider that the guidelines in Box 7 and in particular provisions on the diversification of the collateral and the haircut policies should apply to all OTC derivative transactions and not be limited to TRS?

Where we agree with the provisions in Box 7, we believe that the rules should apply to all OTC derivatives.

VI. Strategy indices

Q39: Do you consider the proposed guidelines on strategy indices appropriate? Please explain your view.

We have a number of issues with the proposed guidelines, foremost of which is the uncertainty of the scope of the guidelines and the definition of strategy indices. We think that further clarity is required on what constitutes a strategy index and whether the guidelines are applicable to all indices or solely to the, yet undefined, strategy indices.

We do not agree that daily or intra-day rebalancing should automatically exclude an index from approval for use by UCITS or creates a public policy problem. Many traditional indices, commonly accepted as eligible for investment by UCITS, may be rebalanced every second, in line with market movements in the prices of their components. While it may be appropriate for an equally weighted index to only infrequently rebalance, this would be less so for a market capitalization based index. In a strategy based index such as value or growth or momentum, input parameters used for index composition (which are objective, externally derived, model based parameters) can require composition to change in order to properly achieve the index mandate. To prohibit such changes may not be consistent with the interests of investors and may prevent efficient risk management tools on indices such as stop loss mechanism in case of loss in value of index components (as index sponsors would be forced to wait until the next rebalancing date instead of taking immediate action). Ultimately, it should be for the investors to determine whether the rebalancing frequency as disclosed (including their cost effects) fits their purpose or not.

We believe that the frequency of the rebalancing should not form a concern where the index is rebalanced according to a non-discretionary and clearly disclosed model. It does not matter very much that it is rebalanced intra-day, if such rebalancing is purely model-based, whereas, a monthly rebalancing on a purely discretionary basis, should be prohibited. Ultimately, the rebalancing has to take account of the strategy (and market conditions) the index seeks to represent, and, if such strategy (and market conditions) suggests an intra-day rebalancing, it could be harmful to the industry and to the investors to limit the rebalancing frequency.

We note the comments on replication. However, it is the case that many standard indices cannot be replicated by (retail) investors in practice. Highly diversified indices with a thousand or more components (e.g. Russell 1000 or 3000) are likely to be much more difficult to replicate than an index of, say, 25 components with daily rebalancing. Similarly, many mainstream index providers see their methodology as being proprietary and wish to avoid arbitrage by other market participants in case of markets with lower trading volume. Many standard market indices do not provide full public disclosure of every detail of the index calculation methodology and often some index data is available to subscribers only.

Indices have evolved over time in order to measure performance of a variety of risk return profiles in all possible asset classes. Excluding any indices where replication to (retail) investors is difficult or impracticable would unnecessarily limit the investment universe of UCITS funds and seem contradictory to the aim of many such funds to provide efficient access to the respective markets (where exposure may be difficult to generate/replicate by investors individually).

The requirement to publish index components would also discriminate against funds investing in strategy indices compared to other funds, which do not have to publish their full holdings after each dealing day. It is also doubtful what advantages investors will get from this information while serving to open up arbitrage possibilities to other market participants**.**

We disagree with the proposal that, for example, a WTI contract and a Brent contract should be seen as only one asset for the purposes of diversification. They are considered as separate commodities by the markets, because, simply, they have different underlying physical assets and their markets respond to different economic conditions.

In respect of Box 8, section 5, we suggest there is no requirement for prospectus disclosure on the effects of rebalancing frequency on the costs within the strategy. In many cases the "strategy calculation fee" or "replication and hedging fee" found in strategy indices is there to account for the fact that the counterparty will face dealing costs such as bid-offer spreads in managing a dynamic portfolio in order to replicate an index or strategy. If a UCITS were following such a strategy directly, it would face similar dealing costs, and these would not be required to be disclosed to investors directly. Accordingly, it seems to be inconsistent to require disclosure of such a cost. In addition, the practical drafting challenges of meeting such a disclosure requirement (where future dealing may be unknown) may prove difficult to achieve in advance.

Q40: Do you think that further consideration should be given to potential risks of conflict of interests when the index provider is an affiliated firm of the management company?

We do not think that there is inherently a conflict when the index provider is an affiliated firm of the management company. That said, we believe any potential conflict can be handled with the proper disclosures and hierarchical separation of duties. This is consistent with the current policy in Ireland.

VII. Transitional provisions

Q41: Do you consider the proposed transitional provisions appropriate? Please explain your view.

At this stage, it is hard to make specific comments on transitional provisions. The transitional provisions can only be assessed once the extent of the changes to the regulatory framework is established. Currently, there are a number of open questions with this consultation.

As a general note, we believe that the timelines presented in the consultation are not feasible. Depending on the final regulatory framework, there could be considerable preparation needed to implement the several policies such as collateral policy, haircut policy, reinvestment policy and tracking error policy which need considerable preparation in order to become operational. Therefore, we think that, at a minimum, the guidelines should come into effect not less than twelve months after their final publication.

Finally, we think that consideration needs to be given to grandfathering, clauses should be considered for existing structured UCITS, funds that use stagey indices and existing collateral arrangements.