The CNMV Advisory Committee has been set by the Spanish Securities Market Law as the consultative body of the CNMV.
It is composed by market participants and its opinions are independent from those of the CNMV.

COMMENTS BY THE ADVISORY COMMITTEE OF THE CNMV ON THE CALL FOR EVIDENCE OF ESMA REGARDING THE REVIEW OF THE UCITS ELIGIBLE ASSETS DIRECTIVE (EAD)

I. INTRODUCTION

The CNMV's Advisory Committee (hereinafter Advisory Committee) welcomes the opportunity to comment on the call for evidence of ESMA on the revision of Directive 2007/16/EC of the Commission, of 19 March 2007, that sets out the applicable provisions of Council Directive 85/611/ECC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (**UCITS**) regarding the clarification of certain definitions (hereinafter **Eligible Assets Directive** or its acronym, **EAD**).

The report is structured into the following Sections:

- **Section II. Background.** Explains the origin of the Directive, the reason for the review and the structure of the public consultation.

- **Section III. General comments.** Highlights the general ideas underlying the responses to the questionnaire.

- **Annex.** Includes the answers to each of the 25 questions making up the questionnaire.

II. BACKGROUND

Directive 85/611 of 20 December, regulating undertakings for collective investment in transferable securities, was adopted in 1985. This Directive was repealed by Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (**UCITS**) (hereinafter **UCITS Directive**) which included many amendments of the initial text of 1985 and which, together with its later amendments, regulates in great detail a specific type of vehicle and its operation, among others, relating to eligible assets, diversification rules and concentration limits, portfolio management techniques, methods to evaluate certain risks and transparency requirements.

The actual Directive lists the eligible assets for investments by UCITS in Article 50. Certain aspects of this list are further developed and specified by the Eligible Assets Directive, to establish a harmonised understanding of these assets. Since the EAD is prior (2007) to the current UCITS Directive, it continues to refer to the list of eligible assets stated in Directive 85/611.

As indicated in the ESMA document, the number, type and variety of financial instruments traded in financial markets have increased considerably since 2007, **making it necessary to revise the Eligible Assets Directive to improve the UCITS brand, adapting it to the present times by incorporating what has been done so far in the market and with a common supervisory approach to avoid fragmentation, while keeping investor protection requirements unaltered**.

The document consists of 25 questions, divided into 2 sections described as follows:

(i) Convergence issues, clarity of concepts and definitions (Section 3.1, questions 1-19).

(Ii) Direct and indirect exposures of UCITS to specific asset classes and data collection and analysis (Section 3.2, questions 20-24).

III. GENERAL COMMENTS

This section includes a series of **general comments on which the answers to the questions of the ESMA consultation are based**.

As a premise of all these, **it is considered that the changes deriving from the review of the EAD should be to modernise the framework of the eligible assets of UCITS and to rationalise the obligations regarding certain assets, while taking into account the regulation approved after the EAD (e.g., Benchmark Regulation) and, under no circumstance, remove or cutback eligible assets for investment**, considering the proper functioning of the UCITS brand both at national and international level.

A restrictive interpretation of the assets in which UCITS could invest has a negative effect on the actual diversification of the product, while also regarding the possibility of **gaining certain exposure, even if residual, to assets whose returns or correlation could be interesting to participants in the product**. Thus, there are certain assets, commodities, crypto-assets or catastrophe bonds, among others, that allow for decorrelation of the portfolio with regard to the financial markets and regarding which it would be interesting to admit, given that they are not eligible per se for direct investments by UCITS, indirect exposure (via Investment Funds or via exchange traded products (ETPs or delta-one instruments), at least residual. In reference to the **admission of indirect exposures to these new assets, the balance between this relaxation and the opening up of the UCITS brand to new investment possibilities that have arisen since the approval of the Directive is also very relevant, while also not distorting the ultimate nature of the UCITS brand as an investment vehicle within a context of scrutiny by regulators worldwide of the macroprudential risks deriving from non-banking financial intermediation.**

Hereunder, and according to the aim of the European Commission (**EC**) to *"preserve and strengthen the well-functioning of the UCITS framework and the operation of UCITS in the best interest of investors, as well as the quality of investment products offered to retail investors"* in the technical advice, the following general comments on which the answers to the questions in the survey are based are included.

A. A balance between the modernisation and flexibilization of investment rules and the need to de preserve the UCITS brand

Within a context of global regulatory scrutiny of macroprudential risks deriving from non-banking financial intermediation, **it is especially relevant to preserve the UCITS brand as product characterised by its liquidity and limited leverage and that is theoretically not susceptible to generate from a macroprudential risk point of view, excessive price volatility or liquidity pressures in financial markets.**

Therefore, although the asset eligibility rules require a review to update them in accordance with financial market developments, it is necessary to preserve the essential characteristics of the UCITS vehicle underlying the position expressed in the recent statement[1] on the macroprudential approach in asset management of the main four European market authorities, including the Spanish National Securities Market Commission (**CNMV**)., which in a general manner dismisses capital requirements

[1] The financial market authorities of Spain, Austria, France and Italy highlight their priorities regarding a macroprudential asset management approach (15 April 2024)

and liquidity buffers for investment funds and proposes focusing supervisory attention on those cases in which the asset management characteristics generate excessive price volatility and liquidity pressures.

Moreover, vehicles such as UCITS, due to their transparency, strict regulation and supervision, are to have an essential role within Capital Markets Union (**CMU**), with retail investor participation in capital markets being a basic strategic pillar.

B. The importance of a general approach when reviewing the framework of eligible assets for UCITS

The functionality of the Eligible Assets Directive is positively valued. However, as indicated by the EC in its mandate, it is considered important to assess the market practices to guarantee that the eligibility rules are implemented in a uniform manner throughout the Member States, taking into account both market and regulatory developments in the past 16 years.

In this sense, when analysing and improving the regulatory framework of eligible assets for UCITS, since the suitability of assets for investment is not only determined by the EAD, but also by the remaining requirements stated in the general framework of the UCITS Directive, **it would be convenient to use the review of the EAD to, in turn, reflect on the framework as a whole, without limiting the review to the issues addressed in the Eligible Assets Directive,** as they stem from the UCITS Directive itself.

Thus, the ongoing review should be used to **improve some specific level 1 issues of the UCITS Directive, such as the exposure to other CISs, even within the joint 10% of Article 50(2)(a) of the UCITS Directive and the removal of the rule of diversification into six issuances when investing more than 35% in public debt of the same issuer.**

The following topics stand out in this general approach to the review:

i) Analysis of asset eligibility versus market liquidity and negotiability

The consultation considers the possible modification of the current presumption of liquidity and negotiability of transferable securities admitted to trading stated in Article 2(1) of the EAD.

In this respect, it is considered that the task of managers is to manage the investment risks, for which reason, in the case of transferable securities admitted to trading in a regulated market, **issues such as liquidity or negotiability of a specific asset, should be dealt with within the scope of the liquidity management of the vehicle. That is to say, the rule should not include additional liquidity and negotiability requirements of transferable securities admitted to trading in regulated markets, notwithstanding that the manager must analyse the liquidity of each specific asset (both before its inclusion in the portfolio and in a continuous manner) within the framework of its liquidity management policy, even though it is admitted to trading in a regulated market.**

In this sense, the EAD revision should take into account the entire UCITS regulatory framework under which managers have increasingly specific and detailed obligations regarding liquidity management, allowing for this risk to be minimised. Directive (EU) 2024/927 of the European Parliament and of the Council of 13 March 2024, has recently included liquidity tools in the

UCITS regulation to strengthen this aspect. Moreover, **ESMA in its results regarding the 2020 Common Supervisory Action on UCITS liquidity management indicates in paragraphs 9, 10 and 11, that there were few cases in which the NCAs identified significant liquidity risks that could endanger the capacity of the analysed UCITS to meet reimbursement requests or any other obligation.** In a very limited number of UCITS, liquidity profiles indicated possible asset-liability mismatch risks, which were only sometimes mitigated by liquidity management tools. **In most cases, this exercise found that the level of compliance with applicable liquidity management rules was satisfactory and that entities complied with their regulatory obligations.**

Therefore, and in line with the idea that the EAD review should consider the entire general UCITS framework, **it can be concluded that the current rules regulating liquidity management are enough to guarantee adequate liquidity of UCITS assets without the need for additional requirements in the asset eligibility rules for transferable securities admitted to trading.**

ii) Modification of certain aspects of the UCITS Directive

- **Update of the percentage of 10% investment in other assets of Article 50(2)(a) of the UCITS Directive. ESMA's opinion**

  Recital (39) of the UCITS Directive indicates that **the development of opportunities for a UCITS to invest in UCITS and in other collective investments undertakings should be facilitated.**

  It is essential that the UCITS investment in other UCIs is permitted and boosted, such as, European long-term investment funds (ELTIFs) for example, which not only give the chance of providing UCITS to invest in a wide range of assets but also offer the highest investor protection safeguards as they are aimed at retail investors, or open AIFs, a vehicle regulated at EU level.

  In addition, a restrictive interpretation of the assets in which UCITS can invest has a negative impact on the diversification of the product itself, as well as on the possibility of gaining certain residual exposure to assets whose returns or correlation could be interesting to the product's participants. Thus, there are more sophisticated assets in which investing via Collective Investment Schemes (CISs) would allow UCITS to access their specialised management. The inclusion in 50(2)(a) of investments in CISs other than those of 50(1)(e) would allow UCITS to indirectly gain exposure via investment funds to certain assets (e.g., commodities, catastrophe bonds, crypto-assets) through vehicles with specialised management of such assets that have the necessary experience and knowledge to invest in them. This exposure would also be limited both by the 10% and the diversification rules.

  Article 50(2)(a) of the UCITS Directive should be taken as a discretionary coefficient for investment in financial assets that do not comply with one of the requirements foreseen for each type of assets envisaged in Article 50(1) inasmuch, except for the prohibition on investing in precious metals, the Directive sets no other specific restriction on investing. So, for example, it should be possible to include CISs that do not comply with the requirements stated in Article 50(1)(e) in the 10% rule of Article 50(2)(a).

Although **it would be ideal to amend Article 50(2)(a) itself, a different interpretation from that of ESMA in its Opinion on Article 50(2)(a) would also be possible, and this article could be interpreted as a general repeal of what is stated in Article 50(1)**, and not as numerus clausus only applicable to transferable securities or to money market instruments.

In any case, **at least ESMA's opinion** could be reinterpreted by **considering as all those open funds admitted to trading (ETFs) that do not comply with the provisions of Article 50(1)(e) as transferable securities, in the same way the Eligible Assets Directive considers transferable closed funds to be transferable securities.** In this case, the diversification rules provided for transferable securities would be applied to ETFs included in Article 50(2)(a).

Notwithstanding the above, transparency and information is essential to participants and, therefore, the investment policy of UCITS should be appropriately reflected both in the prospectus and the CIS investor information document, clearly envisaging the type of assets that may be included in the vehicle via such indirect exposure.

If the above is considered appropriate, the option of directly investing in this type of assets within the same percentage could also be evaluated.

- **Removal of the obligation to diversify into 6 issuances, when investing more than 35% in public debt of the same issuer.**

Non-compliance with certain diversification requirements foreseen in level 1 of the UCITS Directive, such as that of diversifying into at least 6 issuances when investing more than 35% in public debt of the same issuer (last paragraph of Article 54 of the UCITS Directive), forces a series of funds designed for retail investors to be qualified as alternative investment funds, with the implications this qualification has regarding their distribution.

In this sense, to back this proposal, it is convenient to update the **context under which this requirement was included and the risk the Directive attempted to mitigate by doing so**.

In the original EC directive proposal (in July 1976) there was no such requirement for six issuances. In its place there was a general clause (Article 26(3)) that allowed Member States to waive the diversification limits in the case of securities issued or guaranteed by "qualified issuers".

After the amendments introduced by the Council, the finally adopted Directive (85/611/ECC of 20 December 1985) included the requirement for six issuances in Article 23. To put Article 23 into context, the last but one recital of the Directive, explaining the aim of this requirement, should also be recalled: *"Whereas the free marketing of the units issued by UCITS authorized to invest up to 100 % of their assets in transferable securities issued by the same body (State, local authority, etc.) may not have the direct or indirect effect of disturbing the functioning of the capital market or the financing of the Member States or of creating economic situations similar to those which Article 68 (3) of the Treaty seeks to prevent".*

The conclusion is that the requirement for six issuances included in the UCITS Directive was not aimed so much at investor protection but at guaranteeing the proper functioning of the capital market and the financing of Member States.

Furthermore, considering that:

- Once the Directive allows a UCITS to invest up to 100% of its assets in a single issuer, **credit risk is the main risk faced by such UCITS, affecting all issuances in the same manner.** Therefore, the credit risk is not mitigated by this requirement.

- For certain **Funds with passive management investment strategies and a minimum recommended holding period** (such as guaranteed funds or similar), whose portfolio is frequently based on a zero coupon bond, the more ISIN references are included in the portfolio, the harder and more expensive its management is and the greater the duration risk faced by managers and investors, to the detriment of the product's performance.

- In the Consultation on the revision of the provisions on diversification of collateral in ESMA's guidelines on ETFs and other UCITS issues, the convenience of extending the requirement for six issuances of government bonds received by UCITS as guarantee was questioned. In its final report[2], **ESMA acknowledges the operational challenges for its implementation, but still extends this collateral requirement, simply to guarantee that it complies with Article 54(1) of the UCITS Directive**.

In short, there are strong arguments for the elimination of the requirement for six issuances from the UCITS Directive and we encourage ESMA, within the context of the revision of this Directive, to highlight aspects which, like this one, despite being level I, should be amended in order to improve the UCITS investment framework.

C. Avoidance of market fragmentation encouraged by divergences in the interpretation and application of the regulation by NCAs.

It is essential for the supervisory practices to be coherent, efficient and effective, while also guaranteeing a common, uniform and coherent application of EU Law, as laid down in Article 16 of Regulation (EU) No. 1095/2010 establishing ESMA, otherwise there would be a risk of regulatory arbitrage and market fragmentation.

i) One of the priority issues is the need to harmonise the obligation or not of performing a look-through, being in the general interest to establish common criteria on when this should be performed and when not. Thus, the greater or lesser flexibility with which each jurisdiction currently applies this principle implies a greater or lesser possibility of obtaining indirect exposure (via derivatives, indices, delta-one instruments or other CISs) to underlying assets that are not per se eligible for UCITS. **The main issues with regard to performing a look-through are indicated as follows:**

- <u>Financial indices</u>:

[2] ESMA/2014/294

A way in which, depending on the jurisdiction, exposure to non-eligible assets is possible is via financial indices, as neither the UCITS Directive nor EAD include the obligation to perform a look-through.

However, some national regulations do require financial indices to be referenced to eligible or previously authorised underlying assets (Article 5(1)(b)(ii) Order EHA/888/2008, of 27 March, on transactions by collective investment schemes of a financial nature with financial derivative instruments and which clarifies certain concepts of the Regulation of Spanish Law 35/2003, of 4 November, on Collective Investment Schemes, approved by Spanish Royal Decree 1309/2005, of 4 November).

In this respect, the possibility of exposure to non-eligible assets per se for UCITS should be harmonised with a flexible approach, that is to say, allowing this possibility as long as the index fulfils the diversification requirements established in the regulation.

– Delta-one instruments:

The Committee acknowledges that any additional criterion to invest in Delta-one ETPs is more restrictive than that stated in the Directive. However, if the current draft of the EAD is revised or specified further regarding this point, the Spanish supervisor's criteria to consider eligible for UCITS ETPs that are traded daily and whose market price is determined through third-party trading operations, would seem a reasonable option in order not to have to look through the underlying assets.

– Investment in other CISs:

Finally, regarding investments in other CISs, some jurisdictions require a look through of the investment in other CISs UCITS precisely due to the current divergences regarding the application of the asset eligibility requirements of the UCITS Directive. The need for a look through should disappear insofar these divergences are eliminated.

ii) In relation to the techniques for efficient management of portfolios foreseen in the UCITS Directive and its implementing regulations, it is essential to remind that, due to a lack in the national regulatory development, **securities lending,** which improves market functioning and provides additional profitability to the participants in the transaction**, can be carried out in all countries of the European Union except in Spain, placing Spanish CISs at a competitive disadvantage.**

D. The review of the EAD Directive should be used to align concepts and requirements which have been surpassed by regulatory developments

The UCITS Directive states a series of additional requirements concerning the use of benchmarks by UCITS. With the inclusion in the European financial legislative framework of Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June on indices used as benchmarks in financial instruments and contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) no 596/2014 ("**Benchmark Regulation**") that aims to *ensure the accuracy and integrity of indices used as benchmarks in financial instruments and financial contracts, or to measure the performance of investment funds in the Union*, **the removal of additional charges regarding the governance and transparency of the benchmarks should be considered, limiting the financial index suitability analysis, in those cases in which the administrator and/or index are authorised or registered in accordance with the Benchmark Regulation, to the appropriate diversification of the underlying assets.**

ANNEX

Q1: In your opinion, what issue to be considered in the Eligible Assets Directive is most pressing with a view to improve investor protection, clarity and convergence regarding supervision throughout the EU?

A general approach to the revision of the eligible assets framework, considering not only the revision of the EAD but also the UCITS eligible assets framework, including level I.

In this sense, not only should the Eligible Assets Directive be revised, but also the complete UCITS eligible assets framework, allowing for adaptation to the markets and harmonisation in the application and, thus, investment protection, to be adequately addressed. For that purpose, we refer to that stated in point (b) of the general comments and, specifically, to (i) the possibility of investing in open CISs within the Article 50(2)(a) of the UCITS Directive and (ii) the elimination of the obligation to diversify into 6 issuances, when investing more than 35% in public debt of the same issuer included in the UCITS Directive.

However, attending to the mandate foreseen by the EC, the essential issue is the need for harmonisation regarding the obligation or not to look through the assets, it being in the general interest to establish common criteria on when to carry out this exercise and when not.

Q2: Have you experienced any recurrent or significant problem with the interpretation or consistent application of the Eligible Assets Directive[3] regarding **financial indices**?

If so, describe any recurrent or significant problem you have experienced and your proposal on how to amend the Eligible Assets Directive to improve investor protection, clarity and supervisory convergence. Where applicable, specify the indices you refer to and the specific characteristics of these indices that generated doubts or concerns. Wherever possible, provide data justifying the material nature of the problem.

For the purpose of investing in financial indices, the Eligible Assets Directive should be limited to requiring, in those cases in which the administrator and/or index are authorised or registered in accordance with the Benchmark Regulation, that the financial indices are sufficiently diversified, inasmuch the issues regarding governance and transparency of financial indices are regulated in the Benchmark Regulation.

On the other hand, there is no uniform application throughout all jurisdictions regarding the exposure to non-eligible assets via financial indices. Although neither the UCITS Directive nor the EAD require a look through, some national regulations require financial indices to be referenced to eligible or previously authorised underlying assets.

In addition, with regard to the new requirements on governance and conflicts of interest of administrators, it should be clarified that, if a derivative based on an index is contracted, there is no restriction for the counterparty to be from the same financial group[4].

Q3: Have you experienced any recurrent or significant problem with the interpretation or consistent application of the Eligible Assets Directive[5] regarding **money market instruments**?

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[3] In particular, Articles 9 and 12 of the Eligible Assets Directive.

[4] In particular, the Benchmark Regulation requires:(i) Taking adequate steps to identify and to prevent or manage conflicts of interest between themselves and, among others, the users (with CISs among these) (Article 4(1)); (ii) The provision of a benchmark shall be operationally separated from any part of an **administrator's business** that may create an actual or potential conflict of interest (Article 4(2); (iii) As benchmark administrators under the BMR, these entities are subject to the supervision of the competent supervisory authority (the CNMV in Spain) (Articles 34 to 36). The aforementioned articles are not modified by the amendment text adopted by the European Parliament on 24 April,

[5] In particular, Articles 3 to 5 of the Eligible Assets Directive.

If so, describe any the problems you have experienced and your proposal on how to amend the EAD to improve investor protection, clarity and supervisory convergence. Where applicable, please describe the specific characteristics of the money market instruments causing doubts or problems.

No problems were detected in relation to the interpretation of the rules relating to money market instruments.

Q4: Have you experienced any recurrent or significant problem with the interpretation or consistent application of the Eligible Assets Directive[6] regarding concepts **“liquidity” or “liquid financial assets”**?

If so, describe any the problems you have experienced and your proposal on how to amend the EAD to improve investor protection, clarity and supervisory convergence. Where applicable, explain the differences that should be established between the different asset classes[7].

The inclusion of additional requirements to the definitions of the Eligible Assets Directive is not considered necessary. In this respect, please refer to the next question.

Q5: ESMA’s 2020 Common Supervisory Action (CSA) on UCITS liquidity risk management detected problems regarding the **presumption of liquidity and negotiability** established in the Eligible Assets Directive[8].

In the light of the changes in market conditions since 2007, do you consider this presumption of liquidity and negotiability continues being appropriate? As far as possible, provide opinions, data or estimates regarding the possible impact of eliminating the presumption of liquidity and negotiability established in the Eligible Assets Directive.

The presumption of liquidity and negotiability, provided in the last paragraph of Article 2(1), already states that **when the manager has information leading to another conclusion, it will not consider the presumption of liquidity and negotiability of the market**, however, if otherwise, the regulation states that it may presume liquidity, negotiability and capacity to cover UCITS reimbursements.

Moreover, it should be indicated that in paragraphs 9, 10 and 11 of the aforementioned CSA, ESMA also stated that there were few cases in which the NCAs identified significant liquidity risks that could endanger the capacity of the UCITS analysed to fulfil reimbursement requests or any other obligation. In a very limited number of UCITS, liquidity profiles indicated possible asset-liability mismatch risks, which were only sometimes mitigated by liquidity management tools. In the majority of cases, this exercise found that the level of compliance with applicable liquidity management rules was satisfactory and the entities complied with their regulatory obligations.

Since the task of managers is to manage investment risks and that, in accordance with the CSA, no liquidity problems were detected in UCITS, joined to the fact that the recent amendment of the UCITS Directive has included liquidity tools allowing for better management of liquidity risk, it is considered that **issues such as the liquidity or negotiability of assets should be dealt with separately and, therefore, remain outside the debate regarding the eligibility of the UCITS portfolio assets**. That is to say, the regulation should not include additional liquidity and negotiability requirements of transferable securities admitted to trading to

[6] In particular, Article 2(1)(c) of the Eligible Assets Directive.
[7] For example, differences between the liquidity of the liquidity and debt instruments.
[8] Article 2(1), last subparagraph of the Eligible Assets Directive. Also see pages 3 and 4 of ESMA’s report on the 2020 Common Supervisory Action on UCITS liquidity risk management regarding issues observed in this respect.

be eligible for investment, notwithstanding that the manager must analyse the liquidity of each specific asset within the framework of its liquidity management policy, even if it is listed in a regulated market..

Q6: Explain your understanding of the **ancillary liquid assets**[9] concept and any recurrent or significant problem you may have experienced in this context. Please clarify if they are held as bank deposits at sight and what else is used as ancillary liquid assets. Where applicable, distinguish between supplementary liquid assets denominated in (1) the base currency of the Fund and (2) foreign currencies.

No comments in this regard.

Q7: Beyond holding currencies for liquidity purposes, do you believe UCITS should be allowed to also acquire or hold **currencies** for investment purposes, taking into account the high volatility and the devaluation/depreciation of some currencies?[10] Where applicable, distinguish between direct and indirect investments.

No comments in this regard.

Q8: Have you observed any recurrent or significant problem regarding the interpretation or consistent application of the **10% limit** established in the UCITS Directive for investments in transferable securities and money market instruments other than those mentioned in Article 50(1) of the UCITS Directive?[11]

If so, explain the issues and your proposal on how to tackle them in the Eligible Assets Directive with a view to improve investor protection, clarity and convergence regarding supervision?

Although there is not a problem regarding interpretation divergence as ESMA has given an opinion on the matter, we would like to highlight the relevance of including in the 10% limit open-ended CIS that do not meet the requirements of Article 50(1)(e) of the UCITS Directive by either amending Article 50(2)(a) of the UCITS Directive or of Article 2(2) EAD, or via the amendment of ESMA's opinion. This would allow for investing in units/shares of other types of Funds, which already have a strict general regulation at management level, such as EU's AIFs, or specific regulation at product level, such as ELTIFs.

It should also be possible to include in this 10% CISs with exposure to non-eligible underlying assets for UCITS (commodities, crypto-assets, catastrophe bonds) that allow indirect access to a type of asset that requires professional experience and management, particularly when dealing with ETFs listed in regulated markets of EU jurisdictions or those of countries like the US. The limitations would be established via diversification and transparency requirements regarding investor information.

If the above is considered appropriate, the option of directly investing in this type of assets within the same percentage **could also be evaluated.**

Q9: Are the **"transferable assets" criteria** set out in the Eligible Assets Directive[12] sufficiently clear and appropriate? Otherwise, describe any recurrent or significant problem you have observed and your proposal

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[9] In accordance with the second paragraph of Article 50(2) of the UCITS Directive. Also see recital 41 of the UCITS Directive.
[10] Please specify to what extent this is performed in accordance with Article 50(1)(f) in relation to Article 52(1)(b) of the UCITS Directive.
[11] Article 50(2)(a) of the UCITS Directive. Also take into account ESMA's aforementioned 2012 opinion on this provision.
[12] In particular, Article 2(1)(a–g) of the Eligible Assets Directive.

on how to amend the Eligible Assets Directive to improve investor protection, clarity and supervisory convergence.

The criteria established regarding the asset transfer concept are considered appropriate.

Q10: How are the **valuation and risk management criteria** set out in the Eligible Assets Directive[13] interpreted and applied in practice, particularly the need for: (1) the risks to be "adequately captured" by the risk management process; and (2) having "reliable" valuations/prices?

Describe any recurrent or significant problem you have observed with the interpretation or consistent application of these criteria and your proposal on how to amend the Eligible Assets Directive to improve investor protection, clarity and supervisory convergence.

The valuation and risk management criteria should remain outside the valuation of the eligibility of market traded transferable securities. See the answer to question 5.

Q11: Are the provisions in the Eligible Assets Directive on **financial instruments backed by assets other than those listed in Article 50(1) of the UCITS Directive** sufficiently adequate and clear? [14]

Describe any recurrent or significant problem you have observed with the interpretation or consistent application of these criteria and your proposal on how to amend the Eligible Assets Directive to improve investor protection, clarity and supervisory convergence.

One of the priority issues is the need to harmonise whether there is the obligation to perform a look-through or not, it being in the general interest to establish common criteria on when this should be performed and when not. Thus, the greater or lesser flexibility with which each jurisdiction currently applies this principle implies a greater or lesser possibility of obtaining indirect exposure (via derivatives, indices, delta-one instruments or other CISs) to underlying assets not eligible per se for UCITS.

See the answer to question 13.

Q12: Is the concept of **embedded derivatives** set out in the Eligible Assets Directive[15] sufficiently adequate and clear?

Describe any recurrent or significant problem you have observed with the interpretation or consistent application of this concept and your proposal on how to amend the Eligible Assets Directive to improve investor protection, clarity and supervisory convergence.

We have no knowledge of the existence of any problem regarding the embedded derivatives concept.

Q13: In relation to Questions 11 and 12, ESMA is aware of the diverging interpretations regarding the treatment of **delta-one instruments** according to the Eligible Assets Directive, taking into account that they could provide UCITS exposure to asset classes that are not eligible for direct investment (also see Section 3.2). How would you propose the Eligible Assets Directive was amended to improve investor protection,

[13] In particular, Article 2(1)(c) and (g) of the Eligible Assets Directive.
[14] Article 2(2)(c) of the Eligible Assets Directive.
[15] In particular, Article 2(3) and Article 10 of the Eligible Assets Directive.

clarity and supervisory convergence? Provide details on the evaluation of the eligibility of different types of delta-one instruments, identify the problems per product and provide data backing your reasoning.

For greater legal certainty, it is necessary to determine the situations in which the Management Companies must look through the asset and when not.

In this sense, even though any additional criterion to invest in Delta-one ETPs is more restrictive than that set out in the Directive, in the case that the actual drafting of the EAD regarding this was to be reviewed or specified even further, the Spanish supervisor's criteria of considering eligible for UCITS those ETPs that are traded daily and whose market prices are determined via third-party trading operations, would seem a reasonable option in order not to have to look through the underlying asset[16].

Q14: Have you observed any recurrent or significant problem with the interpretation or consistent application of the rules for **UCITS investments in other UCITS and Alternative Investment Funds (AIFs)?** In this context, have you observed any problem in terms of clarity, interaction and logical consistency between (1) the rules for investment in UCITS and other open-end funds set out in the UCITS Directive[17] and (2) the provisions for UCITS investments in closed-end funds set out in the Eligible Assets Directive[18]?

Describe any recurrent or significant problem you have observed with the interpretation or consistent application of these criteria and your proposal on how to amend the pertinent rules to improve investor protection, clarity and supervisory convergence. Whenever relevant, distinguish between the different types of AIFs (e.g., closed, open, etc.), investment strategies (real estate, Free Investment Funds (FIL), private equity, venture capital, etc.) and location (e.g., EU, outside the EU, specific countries). In this context, please also share your opinions on whether it is necessary to update the legal drafting of the Eligible Assets Directive and the UCITS Directive given that, for example, they refer to "Open-Ended Funds" and "Closed-Ended Funds", while it may seem preferable to now use the "AIF" concept given the subsequent introduction of the AIFM Directive[19] in 2011.

The current distinction made by the EAD between Open-Ended Funds and Closed-Ended Funds, so that only the former are within the 10% of Article 50(2)(a), as they are compared to transferable assets, does not seem to make sense from the point of view of being eligible for investment by UCITS. Thus, the current regulatory framework prevents the investment by UCITS in units/shares of other types of Funds, simply for being Open-Ended Funds, which already have a strict general regulation at management level such as open-ended AIFs of the EU or specific regulation at product level such as ELTIFs, while allowing investment in venture capital vehicles in non-EU jurisdictions (if certain requirements are fulfilled) which, in many cases, may have lower liquidity than Open-Ended Funds.

Therefore, including a reference to AIFs in Article 50(2)(a), without distinguishing between Closed-Ended and Open-Ended Funds, would be more reasonable than the current drafting of Article 2(2) of the EAD. This reference should be accompanied by the chance to invest in Funds similar to AIFs (regarding issues such as manager supervision, valuation availability, etc.) of non-EU jurisdictions.

Likewise, exposure via ETFs to certain assets not eligible per se for UCITS (commodities, crypto-assets, etc..) should be allowed in this percentage, as long as they are ETFs admitted to trading in EU regulated markets or from jurisdictions offering a similar protection level (e.g., the US). From an economic point of view they are similar to the marketable securities of Article 50(1)(a) of the UCITS Directive but by being

[16] Question 39 of the questions and answers document on the regulation of CISs, CCPs and other closed-ended collective investment vehicles.
[17] Article 50(1)(e) of the UCITS Directive.
[18] Article 2(2)(a) and (b) of the Eligible Assets Directive.
[19] Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers.

considered CISs and not transferable securities according to the Directive and not being similar to UCITS (due, among others, to their underlying asset), are currently outside the investment realm of UCITS.

See the answer to question 15.

Q15: More specifically, have you observed any recurrent or significant problem with the interpretation or consistent application of the rules for **UCITS investments in (1) EU ETFs; and (2) Non-EU ETFs?**

Please describe any problem you have observed in this respect and your proposal on how to amend the pertinent rules to improve investor protection, clarity and supervisory convergence.

Spanish UCITS Funds cannot invest in ETFs of States not belonging to the European Union.

ETFs have the same consideration as CISs in such a way that their eligibility is governed by Article 50(1)(e) of the UCITS directive. In the case of non-UCITS ETFs, for instance US ETFs, there are many cases in which they would not comply with requirement 3 ("*3. The rules on investment arrangements, asset segregation, indebtedness, leverage and uncovered sales are similar to those of the Spanish legislation contained in Section 1 of Chapter I of Title III.*") and would therefore not be eligible for investment pursuant to Article 50(1)(e) of the UCITS directive. Add to that the fact that neither are they considered eligible within Article 50(2)(a), which only allows for Closed-Ended Funds, remaining outside the investment realm of UCITS despite being financial instruments with a very similar operation (regarding liquidity and daily valuation) to that of securities traded in secondary markets.

This makes it necessary for:

i) These requirements to be changed/relaxed to allow for investment in non-EU ETFs by being considered listed transferable securities, in the same manner as that foreseen in the Eligible Assets Directive for closed-ended funds, as indicated in the general comments; and
ii) These requirements to be harmonised.

Consequently, **it is proposed that ETFs traded in certain non-EU regulated markets (e.g., the US) that do not comply with the criteria of Article 50(1)(e)(ii) (diversification and leverage), may be considered eligible assets** of Article 50(1)(a) of the UCITS Directive or, at least, included within the 10% of Article 50(2)(a).

Q16: How would you propose modifying the Eligible Assets Directive[20] to improve investor protection, clarity and supervisory convergence regarding the issues related to **Efficient Portfolio Management** (**EPM**) identified in following ESMA reports:

(1) Peer Review of the ESMA Guidelines on ETFs and other UCITS issues[21];

(2) Peer Review of the Guidelines on ETFs; and

(3) Common Supervisory Action on costs and fees.

[20] In particular, Article 11 of the Eligible Assets Directive.
[21] In particular, the recommendations stated in section III.

In this context, ESMA is also interested in collecting examples and opinions on the best way to tackle divergent market practices with regard to fees for securities lending described in the aforementioned ESMA reports in order to better protect investors against excessive charges.

Awaiting the corresponding regulatory development, this operation is not permitted in Spain.

Q17: Would you consider it useful to link or substitute the **notion on EPM techniques** set out in the UCITS Directive and the Eligible Assets Directive to/for the **notion on securities financing transactions (SFT)** set out in the SFTR[22]? Beyond the notions on EPM and SFT, are there other notions or issues causing any worries in terms of transversal consistency between the UCITS and SFTR frameworks?

No comments in this regard.

Q18: Apart from the definitions and concepts mentioned, are there **other definitions, notions or concepts used in the Eligible Assets Directive** that may require updates, clarifications or greater consistency with the definitions and concepts used in other financial legislation acts of the EU, for example, MiFID II[23], EMIR[24], Benchmark Regulation[25] or MMFR[26]?

If so, please provide details on the problems you may have observed and your proposal on how to clarify or link the pertinent definitions or concepts.

The review of the Directive should take the chance to align the definition of concepts such as regulated market or financial instruments with those set out in Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (MiFID II), acknowledging the possibility of investing in Emission allowances consisting of units recognised for the purposes of compliance with the requirements of Directive 2003/87/EC (Emissions Trading Scheme).

On the other hand, although the UCITS Directive sets out a series of requirements regarding the use of benchmarks by UCITS, with the inclusion in the European financial legislation framework of the Regulation which seeks *to ensure the accuracy and integrity of indices used as benchmarks in financial instruments and financial contracts, or to measure the performance of investment funds in the Union*, in those cases in which the administrator and/or index are authorised or registered in accordance with the Benchmark Regulation, the removal of additional charges regarding their governance and transparency (e.g., Articles 9(b) and (c) EAD[27]) should be considered whenever exceeded by the specific regulations set out that are directly applicable.

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[22] Regulation (EU) 2015/2365 of the European Parliament and of the Council, of 25 November 2015, on transparency of securities financing transactions and of reuse.
[23] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.
[24] Regulation (EU) 648/2012 of the European Parliament and of the Council of 4 July regarding OTC derivatives, central counterparties and trade repositories.
[25] Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June on indices used as benchmarks in financial instruments and contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) 596/2014.
[26] Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on Money Market Funds.
[27] Article 9 EAD:

Article 19(1)(g) of Directive 85/611/EEC Financial indices

1. The reference in point (g) of Article 19(1) of Directive 85/611/EEC to financial indices shall be understood as a reference to indices which fulfil the following criteria:

Q19: Are there national rules, guidelines, definitions or concepts within the **national regulatory framework** going beyond ("overregulation"), diverging from or being more detailed than that set out in the Eligible Assets Directive? If so, explain *whether they pose recurrent or significant problems or practical challenges*.

This section aims to evaluate the possible risks and advantages UCITS acquire from the exposure to asset classes on which there are diverging opinions regarding their eligibility as investments of the UCITS.

The inclusion of additional rules, together with the diverging interpretations of the regulations, are always detrimental to the existence of an adequate level playing field in the market and homogeneous investor protection throughout the Union.

Due to this, setting additional requirements in a common market that do not appear in the regulation works against those managers with the strictest rules (e.g., in the case of Spain dealing with financial indexes, the lack of development of securities lending).

To this effect, the proposal is that the revision serves for a full harmonisation by means of: (i) turning the Directive into a Regulation; or (ii) including an explicit forecast in the revision of the Directive that foresees that the Member States must not set additional requirements or more detailed rules than those foreseen in the Directive.[28].

Q20: Please fill in the following table on the **advantages of allowing direct or indirect exposure of UCITS** to the asset classes listed, taking into account the additional instructions provided in the footer.

Evaluate and provide examples on the advantages of such exposures in the light of their **risks and benefits**, taking into account the **characteristics of underlying markets** (for example, available of reliable valuation information, liquidity, custody).

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a) they are sufficiently diversified, in that the following criteria are fulfilled:

i) the index is composed in such a way that price movements or trading activities regarding one component do not unduly influence the performance of the whole index;
ii) where the index is composed of assets referred to in Article 19(1) of Directive 85/611/EEC, its composition is at least diversified in accordance with Article 22a of that Directive;
iii) where the index is composed of assets other than those referred to in Article 19(1) of Directive 85/611/EEC, it is diversified in a way which is equivalent to that provided for in Article 22a of that Directive;

b) they represent an adequate benchmark for the market to which they refer, in that the following criteria are fulfilled:

i) the index measures the performance of a representative group of underlyings in a relevant and appropriate way;
ii) the index is revised or rebalanced periodically to ensure that it continues to reflect the markets to which it refers following criteria which are publicly available;
(iii) the underlyings are sufficiently liquid, which allows users to replicate the index, if necessary;

(c) they are published in an appropriate manner, in that the following criteria are fulfilled:

(i) their publication process relies on sound procedures to collect prices and to calculate and to subsequently publish the index value, including pricing procedures for components where a market price is not available;
(ii) material information on matters such as index calculation, rebalancing methodologies, index changes or any operational difficulties in providing timely or accurate information is provided on a wide and timely basis

[28] An example of this limitation is included in Recital 99 of Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market.

Asset classes	Arguments for direct investment	Arguments for indirect investment	Current exposure	Additional comments
1 Loans		(1) Via another open-ended or closed-ended CIS/AIF: Allows investment by means of professional management; (2) Access to unconventional assets that allow for diversification and negative correlation of the portfolio;		Review the restrictive interpretation and allow for the inclusion in at least Article 50(2)(a) of the UCITS Directive, of both open-ended and closed-ended AIFs.
2 Catastrophe bonds ("cat bonds")	(1) Allow only when the manager has the capacity and the means to value the investment in this type of asset.	(1) Via Funds: Allows investment by means of professional management; (2) Access to unconventional assets that allow for diversification and negative correlation of the portfolio;		Indirect investment via Funds would require the revision of Article 50(2)(a) of the UCITS Directive.
3 Contingent convertible bonds ("CoCo bonds")	(1) Issuers with high credit rating (2) good profitability, (2) There are risk management teams capable of valuing and managing them. (3) Assets with market maturity.			
4 Distressed securities		(1) Via another CIS (AIF): Allows investment by means of professional management; (2) Access to unconventional assets that allow for diversification and negative correlation of the portfolio;		(1) the restrictive interpretation and allow for the inclusion in at least Article 50(2)(a) of the UCITS Directive, of both open-ended and closed-ended AIFs.
5 Non-marketable securities	(1) Portfolio diversification; (2) Exposure to non-traditional assets.	(1) Portfolio diversification; (2) Exposure to non-traditional assets.		Harmonise the criteria for investment in unlisted securities
6 Crypto-assets		(1) Via other closed-ended and open-ended CISs/AIFs: (1) Allows for investment via professional and specialised risk management; (2) Portfolio diversification; (3) Exposure to non-traditional assets. b) Via ETPs:		(1) Deemed financial instruments by MiCA; (2) Specific risk management; (3) Specialised depositary; (4) Allows for inclusion in the 10% of Article 50(2)(a) of the UCITS Directive.

		(1) No embedded derivative; (2) Portfolio diversification; (3) Exposure to non-traditional assets.		
7 Commodities		(1) Exposure via traded securities apart from delta-one e.g., ETFs; (2) Portfolio diversification; (3) Exposure to non-traditional assets. (4) Assets traded with a trading volume; (5) Via indices, in accordance with that stated in the ESMA Guidelines on ETFs and other UCITS issues.		(1) Settlement by differences; (2) Principle of commodity risk diversification; it is not acceptable for a UCITS to invest exclusively in different securities that are linked to the profitability of the same underlying asset; (3) Assets with market maturity.
8 ETCs	(1) Exposure to non-traditional assets via traded securities; (2) Portfolio diversification; (3) Traded securities with a high trading volume; (4) Reduction in replication costs.			As long as: (1) there is daily trading; (2) the market price is determined based on sale transactions performed by third parties.
9 Real estate		1) Exposure via traded securities; (2) Portfolio diversification; (3) Exposure to non-traditional assets.		
11 REITs	(1) They are traded securities; (2) Portfolio diversification; (3) Exposure to non-traditional assets.			
12 SPACs	(1) They are traded securities; (2) Portfolio diversification; (3) Exposure to non-traditional assets.			
13 EU AIFs	(1) Via another closed-ended or open-ended CIS/AIF: Allows for investment in professional and regulated management;	(		Review the restrictive interpretation and allow for the inclusion in at least Article 50(2)(a) of the UCITS Directive, of both open-ended and closed-ended AIFs.

	(2) Access to unconventional assets that allow for diversification and negative correlation of the portfolio; (3) Limited leverage; (4) Assets under custody; (5) Report to the supervisor.			
14 Non-EU AIFs	US ETFs (1) Traded securities; (2) Portfolio diversification; (3) Access and exposure to US market with high liquidity.			Allow foreign ETFs, when not fulfilling the criteria of Article 50(1)(e) of the UCITS Directive, inasmuch traded securities can be considered securities and not CIS.
15 Emission allowances		(1) Financial instrument according to MiFID II (Annex I, section C,11)); (2) Access to unconventional assets that allow for diversification and negative correlation of the portfolio.		The EU Emissions Trading Scheme is the main tool of the EU to reduce greenhouse gas emissions.
16 Delta-one assets	(1) They are traded securities; (2) No embedded derivative (3) They allow for portfolio diversification; (4) Exposure to non-traditional assets.			As long as: (1) there is daily trading; (2) the market price is determined based on sale transactions performed by third parties.
17 ETNs	(1) Exposure to non-traditional assets via traded securities; (2) Portfolio diversification; (3) Traded securities with a high trading volume; (4) Reduction in replication costs.			As long as: (1) there is daily trading; (2) the market price is determined based on sale transactions performed by third parties.
18 ABS and MBS				Relaxation of the requirements to encourage their appeal.
19 Other relevant assets	ADRs			Certificate representing a marketable security.

Q21: Please explain in further detail and provide examples of how indirect exposure to the asset classes mentioned (for example, via delta-one instruments, ETNs, derivatives) **increase or reduce the costs and/or risks** borne by UCITS and their investors when compared with direct investments.

Indirect investment allows for investment:

1. **Via open-ended or closed-ended AIFs**: access by means of professional and regulated management to unconventional assets, which allow for diversification, de-correlation of the portfolio and with limited leverage.
2. **Via derivatives**: as long as they are settled by differences and the diversification limits are respected, gaining exposure to unconventional assets (e.g., gold or oil futures) with market depth and volume, once again allowing diversification and de-correlation of the portfolio.
3. **Via indices**: financial instruments under regulation, investment in markets, commodities, other different financial instrument, as long as they respect the diversification limits.
4. **Via exchange-traded products (ETPs)**: exposure to non-traditional assets via traded securities, limits on portfolio diversification, without leverage and reducing the replication costs.

Q22: In accordance with the Eligible Assets Directive, should a look-through approach be demanded to determine the eligibility of assets? Please explain your position taking into account the aforementioned risks and benefits of UCITS acquiring exposure to asset classes in which they cannot invest directly, together with the higher or lower costs associated with such indirect investments.

This approach would aim at ensuring that the list of eligible asset classes set out in UCITS Directive level I is considered exhaustive and to reduce the risk of elusion by means of obtaining indirect exposure to non-eligible asset classes via instruments such as delta-one instruments, traded products or derivatives. As far as possible, please include opinions, data or estimates on the potential impact of this possible measure.

For greater legal certainty, it is necessary to determine the situations in which the Management Companies must look through the asset and when not.

Specifically:

- **UCITS**: Considering that the UCITS passport application consists in the located in a Member State UCITs to be able to market their units in the remaining Member States without the latter being able to submit these bodies or their units to any other provision (except for those which in these States do not depend on the same matters regulated by the Directive in question); the Management Companies should not have the obligation to perform an additional look through on the eligibility of these vehicles, beyond that required for diversification or investment policy issues**.**
- **Financial indices**
- **Delta-one without embedded derivative:** The Spanish supervisor's criteria seems appropriate, i.e. that when the following requirements are fulfilled: (i) daily trading; (ii) the market price is determined by third-party trading transactions, no look-through should be performed.

Q23: What are the risks and benefits of UCITS investments in **securities issued by securitizations**? Please share examples and experiences on current market practices and opinions on the possible need to make clarifications or legislation amendments.[29]

Only if the requirements for investment in securitizations, such as the originator having to permanently withhold an economic interest of at least 5% and others, imposing excessive due diligence, were relaxed, would it be appealing to invest in this type of security.

Thus, investments in securitizations involves performing due diligence, both beforehand and on an ongoing basis while the investment is maintained, allowing managers to obtain information and appropriate knowledge on the securitizations considered.

This is a complex and costly process, using up many resources within Management Companies, whose obligations have been intensely increased in the past years (by means of including ESG, ICT risks and other data intensive controls and actions) simultaneously to a continued trend of reducing management fees charged for the vehicles managed.

As a result of all this, relaxing these due diligence requirements is essential in order to reactivate the investments by Funds (both UCITS and AIF, since the AIFM Directive[30] is that which comprises these due diligence requirements) in this type of asset.

Another element which, to a lesser extent than the aforementioned due diligence requirements, hinders investment in securitizations is the valuation. In this way, the valuation procedures state that, in the absence of a representative market price, the entities will contrast the valuations by obtaining quotes from independent third parties. This service entails a cost for the entities which, without being the main reason for this, contributes to the lack of investor appetite for them.

Q24: What are the risks and benefits of allowing UCITS to **accumulate short positions** by using (embedded) derivatives, delta-one instruments or other instruments/tools? Please share examples and experiences on current market practices and opinions on the possible need to make clarifications or legislation amendments.

No comments in this regard.

Q25: Apart from the subjects dealt with in previous sections, have you observed **any other problem** in relation to the interpretation or consistent application of the Eligible Assets Directive?

If so, describe the problems and your proposal on how to review the Eligible Assets Directive or the UCITS Directive to improve investor protection, clarity and supervisory convergence.

In relation with the investment framework foreseen in the UCITS Directive, the following additional matters arise to improve the eligible assets framework:

i) The amendment of Article 50(2)(a), for this to act as a discretionary coefficient for investment in financial assets that do not comply with one of the requirements foreseen for each type of assets envisaged in Article 50(1), together with indirect investment in assets per se no eligible for UCITS.

[29] Taking into account Article 7 of the Eligible Assets Directive on the securitization vehicles which benefit from a banking liquidity line.

[30] Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on alternative investment fund managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) 1060/2009 and (EU) 1095/2010.

ii) The removal of the obligation to diversify into 6 issuances, when investing more than 35% in public debt of the same issuer, stated in the last paragraph of Article 54 of the UCITS Directive.

Both matters are extensively developed in section a) of the general comments.