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11 August 2017

Central Bank of Ireland
New Wapping Street
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Re: Response to Discussion Paper on Exchange Traded Funds

Dear Sir/Madam,

The Irish Funds Industry Association ("Irish Funds") is the representative body of the international investment funds community in Ireland, representing fund managers, custodian banks, administrators, transfer agents, professional advisory firms and other specialist firms involved in the international fund services industry in Ireland.

Irish Funds welcomes the opportunity to input and comment on the Central Bank's Discussion Paper on Exchange Traded Funds. In addition to providing answers to specific questions we acknowledge the level of interaction the paper has generated, including much positive feedback on the proactive approach taken by the CBI. We note from our membership that there has been a positive reception to the paper and it has generated a strong level of interest. We welcome the open tone and approach of the questions asked and believe it is beneficial for the industry in Ireland and, more broadly, in Europe, to have a regulator that is actively engaged in global thought leadership on ETFs.

The broader global ETF industry has grown in the past decade towards the well-developed and evolved model we see today. The ETF industry participants, represented by our members, support this continued evolution of a positive, investor focussed model and we welcome the desire of the Central Bank to foster a "…robust, but enabling, regulatory framework". In this context, it is important to note that, while ETFs have some distinctive features relative to other funds, at their core they are regulated investment funds most of which are authorised as UCITS, regulated as UCITS and adhere to the UCITS requirements. The alternative could risk damaging the UCITS brand and impose unnecessary complications for investors and costs for promoters.

It is important to note that all the benefits of investment in UCITS (diversification, regulated product, safekeeping of assets, transparency on fees etc.) apply to those holding in the secondary market as they would any other investor and our members see the functionality of ETFs as bringing additional benefits to investors in traditional UCITS funds.

ETFs remain a growing percentage of overall funds market and stock market activity. We would welcome continued dialogue on these topics as our interests are aligned in providing a robust and functional regulatory framework.

Section I Questions

A. Is public disclosure of the identity of APs and OLPs of an ETF of benefit and should regulators have a clearer view of the interconnectedness of the AP / OLP ecosystem? Should remuneration models of OLPs (and if relevant APs) be disclosed?

Many ETF promoters disclose key liquidity providers on their websites and this transparency is seen as another benefit of ETFs. However, public disclosure is not necessarily of benefit as on-exchange liquidity providers do not necessarily need to have any contact with an ETF platform other than to seek inventory from APs. With this in mind, we believe that requiring publication of a list may be misleading as it may not be possible to cover all the relevant market participants.

We certainly agree that regulators should have a clearer view of the interconnectedness of the AP / OLP ecosystem. We note that the Central Bank recently carried out an information gathering exercise and think it important that there is greater understanding as to how the market operates and benefits investors.

Remuneration terms between ETF issuers and Liquidity Providers are private commercial arrangements. There is no discernible benefit from public disclosure and our understanding is, that such fees are decreasing as the volume of exchange activity increases. Investors have complete visibility on the price which they will pay for their shares.

B. Transparency is described as the feature which enables a tight secondary market price (by comparison to net asset value) to be maintained. It also provides certainty to investors in terms of exposure achieved through the ETF. It might be the case that there are other mechanisms which achieve the same goal as transparency? If ETFs are not transparent does this have unintended consequences?

Increasing transparency has been a key feature of the ETF industry in Europe. Transparency has helped maintain tight pricing between ETF shares and the relevant exposures. It is not a given, however, that general transparency over all aspects of an ETF's operation to all stakeholders is a material benefit. For certain Active ETFs it is in the interests of investors to limit disclosure to APs and OLPs who are under a duty of confidentiality. Many liquidity providers, even if not privy to the exact holdings, will be able to trade competitively by constructing an effective hedge on the underlying securities of the ETF. Indeed, we believe that competition among APs and OLPs is also a very significant mechanism for keeping secondary market prices tight when compared to the net asset value. In many cases, there will be a number of parties trading the same ETF and the competition to have the "tightest spread" will lead to the secondary market prices being close to the NAV. Certain stock exchanges also set out regulations as to the spreads APs and OLPs may charge when dealing ETFs in the secondary market.

We see a range of transparency levels across the broader ETF market and we are not aware of any of the different transparency models causing concern or otherwise impacting investors.

C. Is the idea of secondary market investors dealing directly with an ETF when the AP arrangements breakdown unworkable in practice or unnecessary? Is there a better way of enabling secondary market investors to dispose of their ETF shares

at a price close to the next calculated net asset value when secondary market liquidity is impaired?

Increasingly we see ETF providers moving to a multi-AP model for their ETF ranges. This is, in part, driven by on-exchange liquidity providers wanting direct access to inventory without having to trade via an AP. The types of liquidity providers currently in the market include banks, investment banks and proprietary trading firms, across a variety of jurisdictions and they increasingly want and receive direct access to the fund. Multiple APs can, for larger platforms, enhance the ability of ETFs to refund assets to clients in a number of different ways thereby reducing the risk of a break down in secondary market access and reinforcing the robustness of the ETF towards investors.

We note with interest the focus by the Central Bank on the challenges posed by modern settlement systems. Our members who have ETFs have to deal with multiple layers of settlement due to the fragmented nature of the European ETF landscape. Whilst the identification of beneficial owners is operationally complex for ETF issuers, most providers have already prepared and stress tested models for the acceptance and processing of redemption orders outside the AP community in the event of a catastrophic market event impacting APs' ability to trade. It is also important to note that secondary market investors seeking to access direct dealing with an ETF in the event of an issue with the secondary market would be legally required to go through anti-money laundering / know your customer processes with the ETF before a trade could be accepted from them.

It is also entirely possible that, as happened with respect to ETF products with Greek exposures after closure of the Athens exchange, that the ETF will continue to trade on its intrinsic liquidity.

D. Should ETFs warn investors that the ETF may temporarily become a closed-ended fund in certain market conditions? Would requiring an ETF to remain open-ended in a stressed market be disadvantageous to existing investors or have other unintended consequences?

It is important to note that liquidity issues and stressed markets impact all funds. We have seen global events that have led to the application of gating to non-exchange traded UCITS. As such any discussion of stressed markets should be viewed in the context of impacting all fund types and not simply ETFs.

We echo the view of other stakeholders that the ETF structure is designed to provide intra-day liquidity often when the underlying market is closed. For example, a European domiciled ETF that holds Asian equities will continue to trade throughout European market hours even though the underlying market is closed. We also see examples where underlying markets are closed for extended periods of time because of national holidays. In those circumstances, ETFs continue to trade in the secondary market. Market Makers use sophisticated hedging techniques in order to mitigate their risk during these periods. It is important to recognise that providing liquidity when underlying markets are closed carries a greater risk to liquidity providers and spreads will reflect this.

In our opinion the suspension of the primary market should not automatically result in suspension of trading in the ETF on the secondary market. The secondary market in that ETF should be orderly with spreads and depth commensurate with the level of dislocation in the market. An effective surveillance tool is important in assessing market quality.

A key facet of the primary market process is that the AP creating or redeeming in the fund has to bear the cost and implied liquidity cost of that transaction. The costs may include but are not limited to the bid-offer spread in the underlying securities, taxes, settlement charges and commissions. This mechanism ensures that parties actively trading the ETF requiring primary market liquidity do not impact investors in the fund. ETFs are therefore not subject to "run risk" or "first mover advantage". This mechanism works effectively in all market conditions, even in extremely volatile market conditions. Notwithstanding this, extreme liquidity concerns or market suspensions may necessitate primary market suspension.

A lack of liquidity does not in itself change the structure of an ETF from an open-ended fund to a closed-ended fund. Just as with any open-ended mutual fund a suspension of dealing is a liquidity management tool (albeit of last resort) the implementation of which does not change the structure of a fund. The risk of suspension of dealing is something highlighted in the risk warnings section of the ETF's prospectus and is a risk inherent when investing in all open-ended funds.

If there is no liquidity available in the secondary market then it is not possible to "require" an ETF to remain open in stressed market conditions and furthermore any such requirement would not be in the best interest of all investors. The manager of an ETF will generally allow dealing where possible and where this will not cause prejudice to investors, because to do otherwise would be contrary to the open-ended nature of ETFs and the UCITS Regulations. Our opinion is that it is not of particular benefit to provide for any additional elements to the UCITS liquidity regime.

Risks, such as potential issues with liquidity or liquidity risk management tools, should be clearly disclosed to investors in relevant fund documentation.

We would note that the manner in which firms deploy the tools at their disposal can result in different outcomes for clients.

E. Is it correct to permit share classes to be structured having regard to the operational concerns of APs and the impact this may have on secondary market pricing? Are there factors (other than those noted above) that could be relevant to ETF structuring?

As long as such operational concerns do not prejudice investors (including secondary market investors), then in our opinion it makes sense to make alterations where a better operational process is available. Altering the dealing cut off between classes should be permitted, for example, in order to reflect the operational challenges (e.g. hedging) which may benefit from a revised process. Differential cut offs are currently permitted for cash versus in kind deals, so there is no logical reason why this approach could not be extended to other scenarios, such as hedged versus non hedged classes dealing cut off. As far as share classes of UCITS are concerned, ESMA guidance is clear on what features and differentiators are permitted. We believe there is no reason why UCITS ETFs should be treated any differently in this respect.

We are aware of a number of bespoke dealing arrangements on ETFs to tailor trading to suit the operational needs of a wider variety of market makers and APs (e.g. differences with respect to trading cut-offs). Ultimately this should improve the end investor experience, again as long as the variety in approaches does not prejudice the interests of those investors as we have outlined previously ETFs are predominantly structured as UCITS and are therefore subject to UCITS requirements in respect of the use of share classes.

F. What are the benefits or disadvantages of permitting listed and unlisted share classes within the same investment fund? Do listed and unlisted share classes create unfairness as between investors in the same investment fund and if so, can these be mitigated or addressed?

In our opinion there is no public policy reason why a UCITS ETF could not offer both listed and unlisted share classes, there is no prohibition on having such classes. The ESMA Guidelines on ETFs and other UCITS issues acknowledge that some classes may trade and others not:

> *"A UCITS ETF is a UCITS at least one unit or share class of which is traded throughout the day on at least one regulated market or Multilateral Trading Facility with at least one market maker which takes action to ensure that the stock exchange value of its units or shares does not significantly vary from its net asset value and where applicable its Indicative Net Asset Value."*

We believe that the key to understanding listed and unlisted share classes is to acknowledge the role of investor expectation. At a UCITS ETF level both classes operate on the same basis. If, at a class level, one class is listed, the holder of such a class will have bought it for that express purpose and understands, in part through the disclosure in the offering document, both the advantages and disadvantages of holding it in such a manner. It is important that investors have optionality and that mechanisms are found to deliver solutions to investors that are both operationally and cost effective for the end user. The classes will share a common net asset value but those trading on exchange may have a different price point due to movements of the iNAV and associated trading costs. In the same way as for listed classes in an ETF which only offers such classes, we think it unlikely that material differences will arise

In this context, it should be established that "fair" treatment does not necessarily equate to "equal" treatment – in other words, it is perfectly possible for consequences to be fair on all parties without them being equal in all respects. Provided there is adequate disclosure on the risks and consequences of opting for a particular class, in the event that they arise, there should not be an issue regarding fairness of treatment – perhaps the appropriate test is whether a result is detrimental to investors compared with investors on a standalone basis and not in comparison to another class. An unlisted class, therefore, would not suffer detriment by virtue of it being in a fund with a listed class - the result is no worse than if the investors were in an unlisted standalone fund. An unlisted share class is inherently different from a listed share class and one of the key differences is the trading mechanism – to align the trading mechanism would reverse/undermine the justification for a separate class.

Finally, we believe that it is worth noting that a product issuer in the USA has successfully run ETF classes on their passive mutual fund ranges and our understanding is that this has functioned well to date.

Section II Questions

G. Are conflicts of interest rules effective for dealing with concentrations of activities within an ETF provider's financial group (e.g. group entities could act as promoter, investment manager, AP and swap counterparty or SFT counterparty)? Are other approaches worthy of consideration?

The regulation of UCITS already provides for the identification and management of conflicts of interest. ETF providers are able to manage their conflicts of interests where group entities act in

multiple capacities and such potential conflicts and relevant resulting risks should be appropriately disclosed to investors so that investors can make an informed decision. Some of the risks associated with group entities acting in multiple capacities are acknowledged by providers and generally ETFs have multiple APs or counterparties to help manage that risk.

ETF providers are typically more open about conflicts and how they are managed than traditional UCITS. Nevertheless, it should be up to ETF providers, as regulated entities, to manage the benefits versus costs of having multiple APs and counterparties and to work out an effective balance. We do not think that regulations should stipulate any minimum or maximum number; ultimately, the economics differ between ETFs. We would note that more regulated financial services group entities or constituent part of group entities are already subject to well established rules on conflicts of interest.

H. Are multiple counterparties necessary, or appropriate for ETFs? Could multiple counterparties expose ETFs to unintended risks and consequences?

We do not believe there is a necessity for ETFs to appoint multiple counterparties.

Equally, if the counterparty risk is properly managed and the disclosure of the investment technique is clear to investors, then the addition of multiple counterparties should not expose ETFs to unintended risks or consequences. This comment is consistent for all investment funds – whether established as a UCITS and/or as a UCITS ETF.

Multi-counterparty models are generally built for the purpose of reducing single counterparty risk and improving the ability of the ETF to mitigate and, where necessary, transfer counterparty positions in a distress scenario. We also note the reduction in risk due to the requirement for initial (threshold dependent) and variation margin applying to each counterparty in accordance with the EMIR requirements. The management of FDI exposures is clearly well regulated and ESMA's 2014 review did not conclude that any meaningful changes were required.

I. Some academic research suggests that if a synthetic ETF experiences counterparty default, the synthetic ETF is more likely to be able to deliver the performance of its underlying index if the collateral received is correlated to that index. Should collateral received (where a funded model is used) or securities purchased (where an unfunded model is used) be correlated to the index being tracked? Is this practical, particularly for example where the index tracked by an ETF is comprised of securities which may be relatively expensive to access? Is collateral quality sufficiently regulated and disclosed?

No, we do not believe that mandating correlation of investments is of benefit. Ultimately the manager picks the collateral they think appropriate to the asset class. A manager has a stronger vested interest, but one that is aligned with the investor, in ensuring his collateral is of a similar or better quality in the event of a market movement causing a dramatic loss to a fund holding. Collateral quality is a consideration for all UCITS, not just UCITS ETFs and the current regime has proved both robust and workable. Requiring an unfunded model to purchase securities, or a funded model to receive collateral, that are correlated to the underlying index may not be practical in a number of scenarios. For example, this may not be practical for certain types of index constituents, e.g. commodities futures, or a manager may take the view that a volatile emerging market exposure is best collateralised with a liquid asset such a US treasury bills. As with all

UCITS it is for the manager to determine the collateral profile in accordance with relevant regulatory guidance, trading requirements and general risk.

Section III Questions

J. Are active strategies appropriate for "housing" in an ETF structure and if so, is there a limit to the type of strategy that would be appropriate? If the ETF structure provides opportunities for managers to achieve scale is there a downside to this where the strategy is active (or, if scale is achieved, its potential impact is not otherwise capable of being ascertained)?

Yes, if the definition is "alpha-generating", active strategies are compatible with ETF structures. Put another way, Active ETFs are ETFs which do not track an index. All UCITS, in one form or another, can to a degree be described as employing "rules-based investment strategies", given the detailed investment restrictions and diversifications that they operate under, so this may not be a useful determinant of whether a UCITS ETF is "active" or not.

There are two key elements to an assessment of appropriateness in this context: liquidity; and transparency. As with any fund, asset managers need to ensure that the liquidity profile of the underlying assets or investment strategy match that of the fund and that the liquidity profile of the fund in turn matches the needs of the target investor. There should be little liquidity mismatch and it is the job of the asset manager to ensure that this is constantly monitored. If the liquidity profiles are matched then the strategy may be suitable for housing in an ETF structure. However, we believe that the question of this suitability is one that the managers are best placed to assess and determine.

The merits of passive and active products have been well debated. The flexibility of UCITS to accommodate both forms of investing has been key to the development of the UCITS brand. The application of both to ETFs should be no different. Given the advantages that an exchange traded open-ended vehicle brings to investors; we believe that Active ETFs are broadly in the interest of investors. The Active ETF model can be attractive to investors and asset managers alike for the following reasons:

- Outperformance: an Active ETF seeks to outperform an index rather than align performance as with a passive ETF.
- Cost: Active ETFs involve lower client servicing and fund administration needs than non-ETF Funds, there are also tax efficiencies inherent with the use of ETFs.
- Flexibility of trading: it is possible to trade ETFs multiple times during the course of a day, so an Active ETF may be more appealing than a non-ETF version of the same active strategy.

Further, a key reason for a manager launching an active strategy in an ETF is to gain access to a broader distribution reach. From this point of view, it should be noted that wrapping an active strategy in an ETF should be seen as a positive, as it brings additional choices to investors, can help to deliver more efficient investment solutions for them and can also bring additional levels of transparency to the investors when compared to other vehicles providing access to this strategy.

We firmly believe that all UCITS ETFs are UCITS from the point of the eligibility of investment strategies and are subject to regulation on that basis. There does not appear to be any evidence that investors choose to invest in ETFs because they are "simple" and in fact, it is important for the future development of the ETF industry that ETFs are not labelled as simple.

The "concept" of ETFs as simple is already very much open to question: (i) there are a large number of ETFs that are not active but are equally not simple, and transparent either because of the smart beta indices that they track or because of their use of synthetic replication; and (ii) existing ETFs may still lack transparency in respect of their use of techniques like stock lending or collateral. It is important to remember that investors needs will evolve over time and regulatory structures must allow product development to evolve too: UCITS have moved a long way since 1985 but are still the standard bearer for retail funds around the world and this is in large part because of the flexibility of the regulatory framework first created over thirty years ago to evolve to continue to meet investors' needs to this day.

In terms of the potential concerns raised about investor understanding of the product, we do not see a significant difference here between ETFs and other UCITS and, if there is a potential for lack of understanding, we believe that disclosure and investor education are the answer.

K. Similar to the question posed in Section I, is portfolio transparency fundamental to the nature of an ETF or are there are other mechanisms which achieve the same goal as transparency? In the context of an active ETF, is transparency essential in order to achieve a liquid market and to facilitate efficiency in pricing?

Portfolio and pricing transparency is relevant to a successful ETF and is a principle underpinning the success of the product to date. Without appropriate levels of transparency, an ETF may be unattractive to Market Makers, as they will not be able to manage their risks in providing a market for the ETF accurately. This, in turn, will result in the prices that they are prepared to offer to the market diverging further from the NAV of the ETF to reflect the spread that they feel is necessary to build in to protect them from movements in the NAV which they cannot foresee, which may consequently make ETFs unattractive to investors.

One alternative option which may be open to Market Makers is to model pricing and risk on an underlying benchmark index, however, where, as with an Active ETF, there is no such index, this will not be an option.

In this respect, it is worth remembering that ESMA reviewed this issue less than five years ago and did not find it necessary to impose portfolio transparency requirements on ETFs, consequently a majority of EU regulators do not require this. Equally, again as pointed out in the Discussion Paper, many of the exchanges on which ETFs are traded have reviewed and revised their disclosure policies in recent years, with very few determining that full portfolio disclosure was necessary to protect the integrity of their markets.

Transparency of portfolio holdings can create a no win scenario for Active ETFs. In order for the ETF to be attractive to investors (low spreads) and efficient in its pricing (close to NAV), the Market Makers will typically look for full portfolio holdings, however active managers may not want to provide full details of their portfolio holdings because of the risks of compromising the large investments which they may have made in intellectual property, research and analysis that may have gone into the development of their strategies. In addition, as highlighted in the Discussion Paper, full disclosure of portfolio holdings can give rise to a significant risk of "front running" of investment strategies, which can have a significant, negative effect on investors who are invested in products which follow this strategy. It is important to note that such a negative effect would not be confined to investors in the Active ETF but would also impact investors in any other product offered by the manager which delivers an identical / similar strategy, e.g. through a non-exchange traded UCITS, which is not subject to any regulatory requirement to disclose its holdings outside of its formal financial reporting. We do not believe that it is appropriate for the same active strategy to have significantly different disclosure requirements just by virtue of how the different funds that are exposed to it trade.

However, these tensions, can in fact lead to a large degree of appropriate self-regulation of disclosure, whereby in order to encourage liquidity and tight spreads in their funds so as to encourage investment, Active ETF managers will be incentivised to limit transparency of portfolio holdings only where there is a genuine need for it (i.e. because of the threats that full disclosure poses to their investors or their own valuable intellectual property). For example, managers may determine that they would be happy to provide full portfolio transparency to Market Makers on a daily basis, to assist with liquidity and pricing, while limiting public access to this information to less frequent or time-lagged publication. Consequently, we believe it appropriate to permit a greater degree of flexibility in the determination of portfolio holdings disclosure policies, to enable market participants to assess where lines should be drawn for each particular ETF product between providing sufficient information to enable the exchange trading to function efficiently and fairly, while also protecting investors and managers' legitimate interests.

Furthermore, we are aware that this is very much a live issue for the ETF industry and are informed of managers which have felt compelled to re-consider preferences for domiciling ETF products in a particular jurisdiction, on the basis of the differing treatment of Active ETFs as between EU jurisdictions with respect to disclosure. We firmly believe that Active ETFs will have a big role to play in shaping the future of the regulated investment funds landscape and therefore think that it is important, given the levels of experience and expertise, in industry and regulation, which has been built up in this country in respect of ETFs, that Ireland remains at the forefront of this market.

Section IV Questions

L. Some commentators are concerned that ETFs are tracking indices of underlying stocks which are not sufficiently liquid to match the intra-day liquidity on the secondary market which the ETF offers. This statement is quite simplistic and does not, for example, reflect that there may be much secondary market activity but very little primary market activity. UCITS, including UCITS ETFs, are subject to general liquidity management rules which should ensure that ETFs track indices of underlying stocks that are sufficiently liquid to allow the ETF to meet creation and redemption requests. Is this sufficient? What liquidity practices do ETFs follow? Are there other practices that might be appropriate for ETFs?

The liquidity of an ETF will normally reflect the liquidity of the underlying assets.

There are a number of liquidity management tools available to managers of ETFs and UCITS and the decision to use these is generally agnostic to the listed structure. Fund managers should be well equipped to manage both market liquidity risk and fund redemption risk. The existing measures available to managers are wide-ranging and include both ongoing measures such as pricing mechanisms to reflect the cost of liquidity, market value adjustments, anti-dilution measures and exceptional measures such as in kind redemptions, deferrals and suspensions. We recommend that managers of ETFs are not constrained by limiting access to the current full flexibility to combine the full UCITS toolkit of measures in a way which allows them to react most effectively to a wide range of market circumstances and/or investor actions. The experience of recent market events shows the benefit of managers having the ability to choose from multiple tools when it comes to managing liquidity.

M. One of the potential impacts from greater investment in index-tracking ETFs is decreased informational efficiency of underlying securities as well as increased non-fundamental volatility of underlying securities. However, these may not be risks per se or, at any rate, may not be risks that ETF providers or regulators can mitigate, manage or eliminate. Is this assessment correct or could measures be taken to address this impact?

We note that indexing more broadly may potentially cause increased non-fundamental volatility of underlying securities. It is not clear to us that such an impact has been proven and it is very much a theory at this stage. As ETFs represent less than 3% of the global equity and fixed income markets it is hard to see how they, in and of themselves, could impact the global markets in a materially negative manner. We are of the opinion that continued vigilance is required but do not believe we are at the stage of having a defined ETF specific risk requiring mitigation, management or elimination. It is also worth noting that despite the increase in coverage ETFs receive in financial press and their increasing usage within clients' portfolios, they still make up a rather small percentage of overall traded volumes on exchange. In the US, the ETF market has grown substantially in the last five years, however, ETFs versus cash equities as a percentage of total exchange turnover has remained around, or below, 25% on average throughout this period. In Europe, whilst this number has grown in the last five years it remains at less than half of the total turnover versus cash equities seen in the US, currently around 11%. This illustrates that greater investment in ETFs does not necessarily result in decreased informational efficiency and/or increased non-fundamental volatility of underlying securities.

N. One of the key issues in the context of support by ETF providers is investor expectation. Investors' views about purchasing ETFs and their ability to sell may be informed by whether or not the ETF provider will support the ETF in the face of stress events. There are, however, divergent views amongst ETF providers as to whether they would support their ETFs. Is provider support a desirable objective?

Managers of all UCITS (not just ETFs) manage market liquidity risk and fund redemption risk constantly. We do not believe that potential issues of product support should be addressed in a narrow UCITS ETF context but rather, by means of a broader fund market disruption discussion. Concerns with respect to specific products or product types should be addressed at the authorisation stage. How would "support" be interpreted and would all UCITS managers/promoters be asked to provide similar support? Stress events impact all UCITS, of which exchange traded UCITS are just a sub-set.

Section V Questions

O. The Central Bank is primarily interested in risks associated with Irish authorised ETFs and European ETFs more generally yet much of the available academic literature, analysis and data relates to US ETFs. The concern is that any analysis of Irish authorised and European ETFs may be adversely affected by reliance on US-centric materials. Is this valid? Are Stakeholders aware of EU ETF specific information that might lead to different conclusions? Will MIFID II resolve these data issues?

It has certainly been useful to see this paper look at ETFs and related issues on a global basis and we do not think it has adversely impacted the quality of the analysis. Shares in ETFs are not currently MiFID instruments, which impacts on the accuracy of data on ETF trading volumes, as over-the-counter trades are not required to be reported and trading data is therefore incomplete for ETFs in Europe. When ETF shares are included as MiFID instruments on 3 January 2018, the expectation is that reported trading volumes will increase and that this will provide a more accurate picture of ETF liquidity. MiFID also prescribes enhanced data standards for trade reporting, which will improve the quality of ETF post-trade data. It should be noted that trade data will not be consolidated and the number of reporting venues will increase. As a result, obtaining a full picture of ETF liquidity will remain a fairly cumbersome process. It is also important to bear in mind that taxation rules in the US drive certain ETF investor behaviours that may not be mirrored in investor behaviour outside the US, making exclusive reliance on US-centric materials potentially misleading.

P. Does the nature of an ETF have peculiarities (and therefore risks) that neither the UCITS nor MiFID regulatory frameworks, either in isolation or in conjunction, address and which we have not examined here?

We do not consider that there are risks unique to an ETF which are not already addressed by the UCITS and MiFID frameworks

Conclusion

Irish Funds wishes to thank the Central Bank for the considerable effort in preparing this Discussion Paper. We believe that an ETF is simply a fund wrapper / distribution mechanism and, as such, any strategy that can be wrapped up in a daily dealing UCITS compliant mutual fund should be able to be offered in an ETF. One key feature of the ETF industry has been the continued strive towards the best in class product and increased efficiency. We expect this to continue and that ETFs will provide the gold standard for managing funds, expectations and investor outcomes.

We would be delighted to follow up with the Central Bank should additional thoughts or queries arise following completion of the review.

Yours Sincerely

Aoife Coppinger
Regulatory Affairs Manager