Irish Stock Exchange

ISE Response to the Central Bank of Ireland Discussion Paper on Exchange Traded Funds 2017

The Irish Stock Exchange (ISE) welcomes the opportunity to respond to Central Bank of Ireland's (CBI) Discussion Paper on Exchange Traded Funds (ETF's). We believe this discussion paper is timely and is a very important initiative which will provide a comprehensive picture of the European ETF industry.

As you are aware, the ISE operates the regulated market (Main Securities Market) in Ireland on which equity securities, government bonds, collective investment undertakings (including ETF's) and debt securities are admitted. The ISE also operates three multilateral trading facilities, the Enterprise Securities Market, the Atlantic Securities Market and the Global Exchange Market. At the end of July 2017, the ISE had 1,532 funds and sub-funds listed on its markets. This includes 189 exchange traded funds and sub-funds.

The ISE has set out responses below to questions F and K.

Question 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 funds and if so, can these be mitigated or addressed?

ISE response

There are a number of issues to contemplate when considering whether listed and unlisted share classes should be permitted within the same investment fund.

An investment fund structure that accommodates both listed and unlisted share classes provides greater flexibility to investors, decreases costs for the manager with a resulting reduction in costs for investors and leads to economies of scale. Furthermore, there are mechanisms in place, such as the suspension of trading, if the market becomes disorderly or it is necessary to protect investors.

In our view there are number of factors which will influence the decision on how to structure an ETF offering including legal costs, tax, branding, marketing, distribution as well as the size of the asset manager and the network of relationships they have. The regulation of the issuer should not prevent listed and unlisted share classes provided there is a single pool of assets with one investment strategy and this structure complies with both the applicable regulatory requirements and listing rules of the relevant exchange. Any risks identified relating to how the investor accesses the fund will be highlighted in a prospectus. Provided all investors in the same class are treated equally then this would comply with the ISE listing rules for investment funds.

Full disclosure on the various features of each share class should be provided in the prospectus, including specific risk factors on subscriptions/redemptions in stressed market conditions. This will facilitate investors in making an informed assessment of which investment route is optimal for them.

A separate class of shares is often created for a different type of investor which may have different fees attached to it, different minimum subscriptions and even different redemption terms. The ISE listing rules permit this once all of the shareholders of the same class are treated equally. Investors therefore know there are different classes which have different features and can invest on an informed basis.

Although there are different mechanisms used in how the investment is made, the underlying exposure is the same and this remains a typical regulated UCITS product. If one investor group was of the view there was specific advantages to using a particular class of shares then there is always the option for a direct investor to redeem out and invest via the secondary market or vice versa.

The existence of both listed and unlisted share classes within a single fund is also in line with the high level principles detailed in the ESMA opinion on share classes issued in January 2017.

One final point is that the possibility of creating both listed and unlisted share classes is also permissible in other EU domiciles. Taking a similar approach in Ireland will ensure a consistent approach is taken across the EU. This will reduce any regulatory arbitrage and allow providers to focus on choosing the most suitable domicile for them for the right reasons.

Question K
Is portfolio transparency fundamental to the nature of an ETF or are there 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?

ISE response
The ISE believes that it is not necessary for active ETF's to disclose portfolio details publicly for the following reasons:

- The practice could be deemed commercially detrimental and anti-competitive;
- It heightens the risk of "front-running" and may enable other managers or investors to trade against the funds in question leading to undesirable market activity; and
- There is no similar requirement for non ETF funds pursuing active strategies.

The direct provision of portfolio details to the Authorised Participant (AP) would not appear to be problematic and would assist with liquidity and efficient pricing. Furthermore, the provision of portfolio holdings in this way, but not to the general public, would appear to be in line with applicable EU legislation as well as protecting the interests of both investor and the ETF provider.

In 2014, the ISE removed a listing requirement for daily portfolio disclosure for the reasons above and also to align our requirements with other EU markets where the ETFs may trade such as the London Stock Exchange and Borsa Italiana.

If you wish to discuss any matter covered above please contact:

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