

15 October 2019

## Circular on Self-Assessment on potential Closet Indexing by Collective Investment Schemes targeting retail investors

Reference is made to the MFSA's [Circular](#) dated 11 July 2018 concerning the evaluation of potential closet indexing practices adopted by UCITS and Retail AIFs, with the initial deadline of submission of the self-assessment certificate on 28 September 2018. The above-mentioned Circular contains an in-depth explanation of what shall be understood as closet indexing and provides methodology for the UCITS Management Companies and Alternative Investment Fund Managers ('AIFMs') to conduct a relevant self-assessment in relation to the investment strategy which they are undertaking.

### Scope

This self-assessment exercise applies to: (i) Self-managed Undertakings for Collective Investment in Transferable Securities ('UCITS') licensed in Malta; (ii) Management Companies managing UCITS licensed in Malta; (iii) Self-managed Retail Alternative Investment Funds ('Retail AIFs') licensed in Malta; (iv) Maltese AIFMs managing Retail AIFs licensed in Malta (for the purpose of this Circular, collectively referred to as 'Fund Managers')<sup>1</sup>.

The following Schemes remain *excluded* from the scope of the self-assessment exercise:

- have an NAV of less than €10,000,000<sup>2</sup>; or
- are charged an Investment Management fee of less than 0.8% of the NAV<sup>3</sup>; or
- have already disclosed in the Offering Documentation the tracking of a benchmark, including but not limited to, volatility returns, geographical focus, i.e. approved index-tracking Schemes.
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### Results of Self-Assessment Exercise

Following the Authority's analysis of self-assessment certificates submitted by Fund Managers between July and October 2018, for which exercise a 100% response rate was received by the Authority, it transpired that (according to the self-assessment questionnaires) none of the actively-managed Schemes licensed by the MFSA, nor their sub-funds, showed signs of being potential

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<sup>1</sup> UCITS Schemes and Retail AIFs are collectively referred to as 'Schemes' for the purpose of this circular.

<sup>2</sup> Total of NAVs of all Sub-Funds.

<sup>3</sup> Each Sub-Fund shall be treated separately.

closet indexing. Nonetheless, the Authority expects that Licence Holders report to the MFSA any instances of Closet Indexing as soon as they are aware of such instances.

### **Updates to Applicable Regulatory Framework**

Following a Public Statement [\[ESMA/2016/165\]](#) on potential closet index tracking in February 2016, the European Securities and Markets Authority ('ESMA') updated its questions and answers on the application of the UCITS Directive [\[ESMA34-43-392\]](#) in March 2019. In its update, ESMA provided a clarification on the benchmark disclosure and past performance obligations for UCITS Schemes. Such clarification included the following:

#### **- *Benchmark disclosure***

1. Schemes should clearly indicate, in the Key Investor Information Document ('KIID'), whether their strategy is 'active' (or 'actively managed') or 'passive' (or 'passively managed');
2. A Scheme managed in reference to a benchmark is one where the benchmark plays a role in the management of the Scheme, for example, in the explicit or implicit definition of its portfolio composition and/or performance objectives and measures<sup>4</sup>; and
3. A Scheme should provide its investors with an indication of the degree of active management in comparison to its reference benchmark index.

#### **- *Past performance***

1. Where Schemes name a target in their investment objectives and policies, the performance should be disclosed against the target, even if the comparator is not named a 'benchmark'; and
2. The performance disclosed in the KIID regarding a benchmark index should be consistent with performance disclosure in other investor communications.

Licence Holders are required to fall in line with the above requirements as soon as possible and in any event by not later than **30 November 2019**.

### **Amendment to submission deadline of the next self-assessment certificate and submission format**

Fund Managers, as referred to in the second paragraph of this circular, are requested to conduct an on-going self-assessment involving, as a minimum, all three (3) mandatory metrics explained in Section 7 of the Circular dated 11 July 2018 and provide relevant details of the findings of the assessment to the MFSA. Fund Managers are further being reminded that the frequency at which the self-assessment certificates are to be submitted to the MFSA, is as follows:

- (a) Annually for Schemes with NAV between €10,000,000 and €100,000,000; and

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<sup>4</sup> This clarification led to the repeal of previous ESMA Q&As on past performance.

(b) Semi-annually for Schemes with NAV higher than €100,000,000.

**The Authority notes that the next self-assessment shall cover the entire period from the date of the submission of the last self-assessment certificate up until the submission date of the upcoming Annual Audited Financial Statements and supplementary regulatory reporting pack of the Scheme, in line with the applicable rules:**

- (i) [UCITS Schemes](#) – within four (4) months from the end of the reporting period concerned in terms of SLC 12.8 of Part BII of the Investment Services Rules for Retail Collective Investment Schemes; and
- (ii) [Retail AIFs](#) – within six (6) months from the end of the reporting period concerned in terms of SLC 5.06 of Part B of the Investment Services Rules for Alternative Investment Funds.

Going forward, the self-assessment certificate should be submitted to the MFSA in line with the above-mentioned submission periods. In addition, Schemes which are subject to semi-annual reporting, as referred to in point (b) above, shall submit the self-assessment certificate within two months from the end of the reporting period concerned *i.e.* within two months from the end of the interim period.

The Investment Services Rules applicable to UCITS Management Companies, AIFMs, UCITS Schemes and Retail AIFs will shortly be updated in order to reflect the inclusion of the self-assessment certificate in the regulatory reporting pack.

The above-mentioned updates will require Fund Managers and Schemes to, *inter alia*, submit the self-assessment certificate in a timely manner and to store any information used for the analysis conducted for the purpose of the self-assessment for a period of two (2) years following the date of the submission of the Annual Audited Financial Statements and supplementary regulatory reporting pack.

The Authority is in the process of requiring the submission of all regulatory reporting through the LH Portal. The self-assessment certificate referred to in this circular shall form part of the additional information to be provided within the annual audited financial statements pack. Further information on the regulatory reporting procedure will be communicated under separate cover.

## **Contacts**

Any queries or requests for clarifications regarding this Circular are to be addressed in writing to the Securities and Markets Supervision within the MFSA via e-mail on: [indextracking@mfsa.com.mt](mailto:indextracking@mfsa.com.mt).