

**FREQUENTLY-ASKED QUESTIONS ON  
REVISED GUIDELINES ON EXCHANGE-TRADED FUNDS  
(Date of Issuance: 26 November 2018)**

**1.0 APPLICATION OF THE GUIDELINES**

**1.01 When will the revised *Guidelines on Exchange-traded Fund (Guidelines on ETF)* issued on 26 November 2018 take effect?**

The revised Guidelines on ETF is issued on 26 November 2018 to enable the industry to familiarise itself with the new requirements. This approach is in line with the current practice for the issuance of revised guidelines. Based on the feedback received from the industry during the familiarisation period, an amendment to paragraph 6.42(a) has been made to the Guidelines on ETF. Full compliance with the requirements of the Guidelines on ETF will take effect on 2 January 2019 (Effective Date).

**1.02 Apart from the Guidelines on ETF, are there any other guidelines or requirements which are applicable to persons involved in the offering of ETFs?**

Yes. In addition to the requirements provided under the *Capital Markets and Services Act 2007* (CMSA), any person involved in the establishment and offering of an ETF should refer to, among others, the *Licensing Handbook*, *Prospectus Guidelines for Collective Investment Schemes* and *Main Market Listing Requirements* issued by Bursa Malaysia Securities Berhad.

**1.03 What are the requirements applicable to persons undertaking secondary listing of a foreign ETF in Malaysia?**

Any persons undertaking secondary listing of a foreign ETF in Malaysia must comply with the requirements under the *Guidelines for the Offering, Marketing and Distribution of Foreign Funds*. Prior consultation with the SC is encouraged for added clarity and understanding.

## **2.0 TRANSITIONAL ARRANGEMENT**

### **2.01 What is the transitional treatment for applications to establish and list an ETF prior to the Effective Date, i.e. 2 January 2019?**

Applications to the SC can still be made based on the existing guidelines up to 31 December 2018. However, applicants are encouraged to comply with the requirements under the Guidelines on ETF for applications made prior to the Effective Date. From the Effective Date onwards, all applications must be made based on the Guidelines on ETF.

For a deed or prospectus that needs to be amended to comply with the Guidelines on ETF, the applicant should consult the SC on the timeframe for the registration of a supplementary deed or prospectus.

### **2.02 Does a management company need to immediately comply with the requirement to maintain a website incorporating information specified in Schedule A of the Guidelines on ETF?**

A management company must ensure that its website contains the minimum information specified in Schedule A within six months from the Effective Date. However, if the management company chooses to revise the prospectus to remove the information specified in Schedule A, then the management company must ensure that its website is updated to reflect such information, before submitting supplementary or replacement prospectus to the SC for registration.

## **3.0 EXCHANGE-TRADED FUNDS**

### **3.01 What are the key requirements and amendments in the Guidelines on ETF?**

<b>Requirements</b>	<b>Remarks</b>
Definitions	Definitions of commodity ETF, futures-based ETF, inverse ETF, leveraged ETF, synthetic ETF and physical commodities.
Paragraph 3.03	Additional requirement on acceptability of a management company intending to establish futures-based ETFs or synthetic ETFs.

<b>Requirements</b>	<b>Remarks</b>
Paragraphs 3.10, 3.13, 3.14, 3.15 and 3.16	Requirements on management company's oversight duties on the operation and management of an ETF following the removal of the requirement on appointment of an investment committee.
Paragraph 3.12	Requirement on the management of conflict of interest where the index is constructed by an index provider which is a related corporation of the management company.
Paragraphs 3.26, 3.27 and Schedule A	Requirements on maintenance of a website by the management company.
Paragraph 5.05	Requirement on naming conventions in relation to leveraged ETFs, inverse ETFs, futures-based ETFs and synthetic ETFs.
Definition, paragraphs 5.02, 5.04, 5.06, 9.05, 9.13, 10.07, 11.02, 11.17 to 11.21, Schedule F: paragraph (5), Schedule C: paragraph (4)	Requirements to allow the establishment of multiple classes of units within an ETF.
Paragraph 6.09(c)	Requirement to allow synthetic replication as one of the strategies that may be adopted.
Paragraph 6.11	Requirements on acceptable indices are expanded for better clarity in relation to diversification of an index and the index to be developed by a reputable agency.
Paragraphs 6.18 and 6.19	Requirements on the methodology of commitment approach to calculate an ETF's global exposure to derivatives.
Paragraphs 6.20 to 6.24	Requirements on netting and hedging arrangements in relation to an ETF's exposure to derivatives.
Paragraphs 6.25 to 6.31	Requirements on counterparty exposure for an ETF's investment in derivatives.
Paragraphs 6.32, 6.33 and 6.34	Requirements on collateral management to address an ETF's exposure to a counterparty.
Paragraphs 6.35, 6.36 and 6.37	Requirements on reinvestment of collateral.
Paragraphs 6.59, 6.60 and 6.61	Requirements on notification of breaches in relation to investments of an ETF.

Requirements	Remarks
Paragraph 7.01	Requirement to allow for both cash or in-kind creation or combination of cash and in-kind creation.
Paragraphs 11.10 and 11.11	Requirements on termination of an ETF.
Schedule B – Appendix I	Requirements on investment limits and restrictions for synthetic ETFs.
Schedule B – Appendix II	Requirements on investment limits and restrictions for futures-based ETFs, including leveraged ETFs or inverse ETFs.
Schedule B – Appendix III	Requirements on investment limits and restrictions for commodity ETFs.
Schedule D	Requirements on investment restrictions and limits for holding of collateral.

### 3.02 What are the Shariah requirements for Islamic ETFs?

Requirements	Remarks
Part B - Additional requirements for Islamic exchange-traded funds	Incorporation of the Shariah requirements for Islamic ETF based on gold and silver, which will supersede the <i>Shariah Parameters on Islamic Exchange-traded Fund Based on Gold and Silver</i> issued on 7 October 2014.
	Requirements that apply to Islamic ETFs are consolidated in Part B which include the appointment of Shariah Adviser, additional duties of the management company and trustee and investments of the Islamic ETF.

In addition to the existing requirements which are consolidated in Part B of the Guidelines on ETF, there is a new requirement on allowing ETF to participate in Islamic Securities Selling and Buying – Negotiated Transaction activities when the management company finds it appropriate to generate additional income.

There is also a requirement that an Islamic ETF must only use Islamic derivatives for hedging purposes. However, conventional derivatives may be used if Islamic derivatives are not available or are not commercially viable. To undertake this process, management company should seek prior consultation with the SC for endorsement from Shariah Advisory Council to ensure timelines are met.

**3.03 Would conventional ETFs be allowed to utilise Islamic Securities Selling and Buying Negotiated Transaction (ISSBNT)?**

Yes, conventional ETFs are allowed to utilise ISSBNT.

**3.04 Would the SC consider other equity-related securities that is not set out in the definition of `transferable securities`?**

The management company should consult the SC for any other forms of equity-related securities.

**3.05 What criteria should the management company be guided by in order to ensure persons undertaking oversight functions are fit and proper?**

The management company should be guided by the fit and proper criteria referred to in section 65 of the CMSA for the appointment of persons to undertake the oversight functions.

**3.06 Can the management company develop an index with a third party index provider for the ETF it manages or proposes to manage?**

Yes. While the management company is allowed to develop the index with a third party index provider which may include an affiliate of the management company, the management company is not allowed to be involved in the construction, maintenance or review of such index.

**3.07 For the purpose of compliance with paragraph 6.11(e) of the Guidelines on ETF, what are the methods that can be adopted by the management company?**

The management company may make available such information to investors via hyperlinks to the relevant websites.

**3.08 For the purposes of paragraph 6.30 of the Guidelines on ETF, what are the examples of acceptable calculation methods on the exposure to an OTC derivative counterparty?**

Example of an acceptable calculation method is shown below:

The calculation method of the exposure to a counterparty of an OTC derivative will be the sum of–

- (a) the current positive replacement cost of each OTC derivative by carrying out a valuation at market price; and
- (b) the 'add-on factor' by multiplying the notional principal amount or the market value of the underlying asset of the OTC derivative, whichever is more conservative, by the percentages in the following table to reflect the potential credit risk.

<b>Residual term</b>	<b>Equity derivative contracts</b>	<b>Other contracts</b>
1 year or less	6%	10%
> 1 year and ≤ 5 years	8%	12%
> 5 years	10%	15%

For total return swaps, the relevant percentage is 10% regardless of the residual term.

*Note: If a different calculation method that is deemed more appropriate is used, the result of the calculation from such method should be at least equivalent or more conservative from the method provided above.*

**3.09 In light of the introduction of collateral pursuant to the circumstances provided under paragraph 6.32, what is an example of ordinary shares that would be permitted?**

An example of such collateral involving ordinary share will be the constituents of the Kuala Lumpur Composite Index (FBM 30).

**3.10 What does the 'top 3 long-term credit rating' refer to?**

References to 'top 3 long-term credit rating' would include the sub-categories and gradations therein. For example, based on Standard and Poor's credit rating, it would be at least 'A'.

**3.11 Apart from the general requirements in the Guidelines on ETFs, what are the specific requirements applicable for the establishment of a futures-based commodity ETF?**

In addition to the general requirements, a futures-based commodity ETF must comply with the requirements prescribed under Schedule B, Appendix II. The term 'futures' must be included as part of the name of such ETF.

**3.12 Can an ETF be terminated for occurrences of the events other than those specified under the Guidelines on ETF?**

An ETF may be terminated for occurrences of events other than those specified in the Guidelines on ETF, if provided for in the deed of the ETF.