



Securities

The Gold Standard – Guide to choosing the right Gold Tracker

Introduction

This factsheet aims to provide existing and potential investors with a due diligence guide comprising of an extensive list of criteria for benchmarking whether a specific gold ETF/ETC structure is “best of breed”.

A strict due diligence process should encompass five key areas:

- **Track record**
- **Security**
- **Transparency**
- **Cost efficiency**
- **Physical holdings quality**

Track Record

Physically-backed gold ETFs and ETCs are unique in the exchange traded products world; unlike all other financial products they involve the management and the custody of a physical asset: gold bullion.

It is essential that investors carefully study the track record of the issuer and assess whether it perfectly understands the mechanics and the need for security of the precious metals market.

The robustness of the structure and processes that governs the physically backed gold ETF / ETC are key to selecting a vehicle that is meant to provide exposure to the so called “safe haven asset” that is gold.

Therefore it is crucial that all the participants involved in the management of the product such as custodian, registrar, and trustee are independent from each other and possess a proven track record fulfilling their respective roles.

In addition, for any exchange traded product, liquidity is paramount. A competitive product should be supported by a network of liquidity providers (Authorised Participants and Market Makers) to ensure tight bid/offer spreads and an efficient creation/redemption processes which can provide depth for the largest institutional capital flows. Products with single or limited APs should be avoided.

Security

The ETF/ETC must be 100% bullion backed at all times.

To fulfil their function as safe-haven investments, physically-backed ETCs and ETFs need to be backed by 100% physical LBMA “Good Delivery” gold bullion held in an Allocated account for which the Issuer has full legal title. The Bullion is therefore owned by the Issuer.

- The account should hold physical LBMA “Good delivery Bullion” sufficient to cover 100% of the securities outstanding
- Neither cash nor certificates representing the right to receive Bullion should substitute for physical Bullion
- Neither the issuer, the Custodian nor any other counterparty should be lending, leasing, trading or pledging as collateral Bullion held in the allocated account

- Audits and Bar list should be verifiable against the LBMA “good delivery” list
- Bullion should be kept in fortified, high security vaults specifically designed for bullion storage

Investors should not be exposed to any credit risk towards the Issuer or the Custodian or any other counterparty:

- Issuers should be a separate, bankruptcy remote entity (segregated from the issuer’s other assets and liabilities)
- Bullion should be identified as owned by the Issuer held in allocated form, and as a result segregated from any other assets held by the Custodian (both physically and in its books and records)

Transparency

Bullion holdings and clearly identified parties are essential.

Independent Counterparties:

Physically-backed ETFs and ETCs should have independent Authorised Participants, Market Makers and Custodians. Such independence has long been a hallmark of good corporate governance for the fund management industry, increases transparency and reduces any potential conflicts of interests.

Transparent Pricing:

The ratio of the security’s Net Asset Value to the London Gold PM fix should be stable (reflecting only the historical cost) and easy to calculate to allow Market Makers to efficiently trade the product and provide best prices and execution to the market.

Easily understandable fee structure:

Fees should be clearly identified, broken down and their impact on the Net Asset Value should be easy to calculate.

Reliable audit procedures:

For greater transparency and to insure that the ETF/ETC is effectively backed at all time by physical bullion, the issuer’s allocated account should be audited by both the Custodian’s own rigorous internal audit procedures and by an independent LBMA approved, independent Bullion assayer.

The Audit procedure should consist of semi-annual audits, at least one of which should be random and encompass both a physical inspection of the vault and a reconciliation of the bullion with both the Custodian’s and the Issuer’s records .

Daily Bar List

Both the Issuer and investors should receive updated account statements of the Bullion backing the ETF/ETCs.

- The Custodian should provide the Issuer with a bar list, updated daily for creations and redemptions, showing recognisable identifiers for each bar held. These generally comprise: brand name, serial number, weight and assay. These should be available to investors.
- Bar list allows investors to perform independent checks (to confirm there are no duplicates and that bars are LBMA good delivery) against the LBMA approved list.



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Cost efficiency

Product structure should be as cost efficient as possible

Multiple Authorised Participants:

The structure should allow for multiple APs to reduce tracking error. Products with only one AP may trade at a premium as there are no independent arbitrageurs ensuring that prices remain consistent with the underlying physical gold price.

Multiple Market Makers:

The structure should allow for multiple market makers to provide liquidity, reduce spreads and to ensure the prices are made around NaV and not trading at a premium. Multiple market makers and APs also reduce operational risk in the event any one AP or MM is no longer able to participate in the Market.

Physical Delivery:

Physical redemptions should be within t+3 framework since the physical gold market settles within this timeframe.

For maximum security and liquidity the physical redemption should be in the form of London Good Delivery Bars delivered to an allocated or unallocated LBMA Account

Physical delivery should not be restricted or limited in quantity; investors must be able to redeem 100% of their physical gold holdings in a single transaction.

Cash redemption:

If allowed, this should not involve unnecessary costs

Physical holdings quality

LBMA approved "London Good Delivery" bars are paramount

Physically-backed ETCs and ETFs should provide access to Bullion with the security, reliability and strength of the London wholesale OTC Bullion market, therefore the bullion should be held in the form of London Good Delivery bars.

The custodian should be a member firm of the LBMA and the LPMCL

- Custodians that trade in these markets have vaults that are internationally recognized as meeting required standards for security and storage space.

Bullion should be LBMA good delivery bars

- These bars have a set number of ounces and a required fineness (purity) of 99.5%. They must bear the stamp of an LBMA-approved smelter/assayer.
- They are the only bars permitted for delivery in the London OTC market.
- Bullion held Loco London is the most liquid, If held anywhere else (e.g., loco Zurich), Bullion should be held with a Custodian or sub-custodian who is an LBMA/LPMCL member.
- Holding gold bullion outside London may result in metal trading at a premium or a discount to the London fixing price.
- Creating outside London may also require a loco swap with London; in the event of a shortage of metal, the swap price could increase dramatically. For example, loco Tokyo Bullion could trade 20bps either side of the London price (and can spike dramatically if demand outweighs available supply).



Due diligence checklist

		Yes/No
Track Record	Issuer has long operating track record under different market conditions	
	Partners are all highly experienced in their respective fields	
	Fund size is sufficient and reflects wide acceptance among investors	
Security	100% backed by physical Bullion held in an allocated account	
	No lending of or borrowing against Bullion	
	Bankruptcy remote issuer with segregated assets	
	No credit risk to the Custodian	
	Limited operational risk	
	No new ETCs/ETFs can be issued without the prior delivery of gold to the Issuer's gold account with the Custodian	
Transparency	All major counterparties are independent (APs, Custodian, Market Makers and Issuer)	
	Transparent and simple pricing	
	Easily understandable fee structure	
	Reliable audit procedures that are published, including at least one random audit of the Custodian's vault	
	Published bar lists with unique LBMA identifiers	
Cost-efficiency	Multiple APs to ensure arbitrage opportunities and limit tracking error	
	Multiple Market Makers to ensure maximum liquidity and reduce spreads	
	Tight spreads and minimal tracking error	
Physical Holdings Quality	LBMA Good Delivery bars	
	Held with a member firm of the LBMA and the LPMCL	
	Held by a Custodian who is a loco London clearer, in vaults that meet required standards for security and size	
Independence	Custodian, Trustee and Registrar must be independent from each other	
	Liquidity providers should be multiple and must be independent from the Issuer	
	Auditors and vault inspectors must be independent from the Custodian and the Issuer	
	Issuer is independent of the above functions	



For More Information

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About ETF Securities

ETF Securities is a provider of Exchange Traded Products (ETFs, Commodity ETCs and Currency ETCs). The management of ETF Securities pioneered the development of ETCs, with the world's first listing of an ETC, Gold Bullion Securities in Australia and London in 2003 and then the world's first entire ETC platform which was listed on the London Stock Exchange in September 2006.

ETF Securities now offers more than 180 Exchange Traded Products (ETPs). The ETPs provide investors with a wide variety of investment strategies, with ETPs offering access to asset classes such as equities, currencies and commodities with physical, long, forward, leveraged and short exposure.

ETPs are simple to access as they are traded in five currencies (EUR, USD, GBP, JPY and AUD) and listed on nine major exchanges globally including the London Stock Exchange, the New York Stock Exchange, the Tokyo Stock Exchange, NYSE-Euronext Paris, NYSE-Euronext Amsterdam, Deutsche Börse, Borsa Italiana, the Australian Securities Exchange and the Irish Stock Exchange.