European Association of Co-operative Banks
Groupement Européen des Banques Coopératives
Europäische Vereinigung der Genossenschaftsbanken

EACB answer to the consultation of the European Commission on the UCITS depositary function

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The **European Association of Co-operative Banks** (EACB) is the voice of the co-operative banks in Europe. It represents, promotes and defends the common interests of its 28 member institutions and of co-operative banks in general. Co-operative banks form decentralised networks which are subject to banking as well as co-operative legislation. Democracy, transparency and proximity are the three key characteristics of the co-operative banks' business model. With 4.200 locally operating banks and 63.000 outlets co-operative banks are widely represented throughout the enlarged European Union, playing a major role in the financial and economic system. They have a long tradition in serving 160 million customers, mainly consumers, retailers and communities. The co-operative banks in Europe represent 50 million members and 750.000 employees and have a total average market share of about 20%.

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General remarks

1. The European Association of Co-operative Banks (EACB) would like to thank the European Commission for the opportunity to contribute to important issues around the UCITS depositary function that were revealed recently by the Lehman default and the Madoff fraud.

2. The EACB fully shares the view of the European Commission that the UCITS regulatory model is a great success of European harmonisation and regulation. It made of UCITS a respected label in all relevant capital markets around the world.

3. From the perspective of European co-operative banks the safe-keeping and supervisory duties carried out by depositaries contributed to the success of the UCITS model.

4. Three principles are important for us: the transparency of the investments, the accountability of the players involved and a balanced as well as fair treatment for all parties.

5. The end-investor should have access to all information allowing him the assessment of the risks associated with his investments. Every participant involved in the chain, from the investor to the asset management company, must know the precise nature of its duties and responsibilities, and be in a position to fulfil them. In addition it needs to be ensured that risks are clearly identified and properly controlled in order to be matched with a fair risk/reward remuneration all along the chain.

6. You can find our thoughts and comments on the UCITS depositary consultation in the following paragraphs:

Questions

(1) Do you agree that the safe-keeping (and administration) duties of depositaries should be clarified?

7. We would like to highlight that a standardisation of the business of depositaries is desirable especially with respect to the further expansion of the European single market. However the measures as proposed in the working paper of the DG MARKT go beyond a standardisation of the depositary business (with its special supervisory duties) but would touch also the custodian business in general and therefore a much wider field of financial services in the area of securities. This correlation should be taken into account by European legislators when elaborating further regulatory measures for depositaries.

8. The key issue in this respect is the need for a European uniform definition of “safe-keeping”. Indeed, recent events – mentioned in paragraph 1 – enlighted the differences of local interpretations between member states of the “safe-keeping” function and the consequences on the level of protection for UCITS investors.

(2) Do you agree these duties should be clarified for each class of assets eligible to the UCITS portfolio?

9. No answer.

(3) Are there any other appropriate approaches?

10. No answer.

(4) Do you agree to a common horizontal and functional approach of the custody duties on the listed financial instruments, to be applied to UCITS depositaries?

11. It is not clearly defined with which approach we are dealing with in this question. If it is a *same business, same rules* approach than we would welcome it, provided that the depositary business – carried out by credit institutions – is compared accordingly and regulated the same way. A horizontal equal treatment can only refer to the same functional services that are carried out within the same regulatory framework. Depositaries that are not a credit institution have significant cost benefits which would lead to a distortion of competition.

(5) Is there some specificity that may be applicable to the custody functions of a UCITS depositary that should be taken into account?

12. The investment in different classes of assets – with corresponding limitations and constrains as imposed by local markets – have an impact on the safe-keeping and supervision of assets.

(6) Do you agree that the existing supervisory duties of the UCITS depositary should be clarified?

13. We welcome a clarification of the existing supervisory duties of the UCITS depositary in order to achieve the objective of the European Commission of an harmonization of the depositary function. This would allow for more transparency and a level playing field between depositaries in the European Union and enhance investor protection.

(7) If so, what clarification do you suggest?

14. No answer.

(8) To what extent does the list of supervisory duties need to be extended?

15. We are against an extension of the supervisory duties currently in place. In case European legislators are considering this step we call for an intensive cost-benefit-analysis beforehand.

(9) Do you agree that the 'only one depositary' requirement should be clarified?

16. The ‘only one depositary’ principle is of utmost relevance and deserves to be reaffirmed. The depositary should be entrusted with an unrestricted view on all fund’s assets. This condition is a key element to ensure the maximum level of investor protection.

(10) Do you think that the risks related to improper performance have been correctly identified?

17. Yes.

(11) Do you foresee other situations where a risk associated with improper performance of the depositary duties might materialise?

18. No.

(12) Do you agree that safeguards against the risk associated with the improper performance of depositary duties, such as requiring that UCITS assets be segregated from the depositary's and sub-custodian's assets, should be introduced?

19. We consider the mentioned requirements as self-evident. For credit institutions they are part of European law since the coming into force of the ISD.

(13) Do you agree there should be a general clarification of the liability regime applicable to the UCITS depositary in cases of improper performance of custody duties?

20. A general clarification in this field would lead to a long term harmonisation of the civil law in Europe since the liability regime complies with the national civil law. In case the European Commission wants to achieve this goal it should be aware of the very broad scope of this task.

(14) What adjustments to the liability regime associated to the custody duties of the UCITS depositary would be appropriate and under what conditions?

21. The current liability regime for depositaries complies with a very high standard. The depositary is fully liable for the accurate choice of foreign subcostodians. Further liabilities for possible failures of subcustodians would lead to immense costs which would not be affordable. We consider the reversal of the burden of proof – as foreseen for depositaries in the AIFM directive – as inconsistent with European law as applied until now, i.e. the liability has to be justified with a proof of negligence, fraud or failure.

(15) Do you agree that the conditions upon which the UCITS depositary shall be able to delegate its duties to a third party should be clarified?

22. The term "delegation" is not defined clearly enough. We would like to point out that depositaries are strictly supervised institutions. The regulations in place comprise also the outsourcing of duties to third parties. The depositary remains liable for the outsourced services. It is different in the case – already mentioned in paragraph 21 – of chosen subcustodians. Here the depositary is only liable for the selection process per se not for failures of the subcostodian.

(16) Under which conditions should the depositary be allowed to delegate the performance of its duties to a third party?

23. See paragraph 22.

(17) Do you agree that the depositary should be subject to additional on-going due diligence requirements when delegating the performance of its duties to a third party?

24. As outlined in paragraph 22 we consider the existing rules for depositaries as sufficient and do not agree with additional on-going due diligence requirements for depositaries when those delegate the performance of their duties to a third party.

(18) Do you share the Commission services approach to reviewing the ICSD, to allow UCITS to benefit from a compensation scheme where the depositary defaults?

25. No answer.

(19) Do you agree that UCITS holders should also benefit from compensation if their custodian defaults and these assets are lost?

26. No answer.

(20) Do you agree that the general organization requirements that are applicable to a UCITS depositary should be clarified?

27. The existing provisions regarding the depositary organisational requirements are in place and provide for adequate comfort. Depositaries are regulated entities in the European Union and subject to ongoing supervision by banking and securities regulators. Other types of institutions should therefore not be entitled to be a depositary.

(21) If so, to what extent?

28. See paragraph 27.

(22) Do you agree that requirements on conflicts of interest applicable to UCITS depositaries should be clarified?

29. We would like to highlight – once again – that depositaries already are strictly supervised credit institutions. Respective conflicts of interest are already covered by detailed compliance rules which are respected.

(23) If so, to what extent?

30. No answer.

(24) Do you agree that there is a need for clarifying the type of institutions that should be eligible to act as UCITS depositaries?

31. Yes, being a credit institution should be a mandatory prerequisite for UCITS depositaries. Those institutions are regulated by banking supervisors in order to ensure the highest possible investor protection.

(25) Do you agree that only institutions subject to the CDR should be eligible to act as UCITS depositaries?

32. Yes.

(26) If not, which types of institutions should be eligible to act as UCITS depositaries, and why?

33. See paragraph 31.

(27) Do you agree that additional auditing requirements should be imposed, such as an annual certification of the depositary's accounts by independent auditors?

34. No. Already today the activities of depositaries are intensively examined in detail by independent auditors on a yearly basis. There is no need for additional certifications.

(28) Do you agree that UCITS depositaries should be subject to a specific 'depositary' approval by national regulators?

35. In most European countries this is already the case.

(29) Do you believe that there is need to promote further harmonization of the supervision and cooperation by European regulators of depositary activities? What are your views on the creation of an EU passport for UCITS depositaries?

36. No answer.

(30) As far as the UCITS portfolio and UCITS units or shares are concerned, do you agree that their value should be assessed by an independent valuator?

37. No. The valuation functions should be linked to the depositary role and responsibilities. Introducing another party to the already complex chain may further blur the features of a product which calls for clarity.

(31) If so, what should be the applicable conditions for an entity to be eligible to act as an UCITS Valuator?

38. See paragraph 37.

Contact:

The EACB trusts that its comments will be taken into account. For further information or questions on this paper, please contact:

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