

Set up in 1960, the European Banking Federation is the voice of the European banking sector (European Union & European Free Trade Association countries). The EBF represents the interests of some 5000 European banks: large and small, wholesale and retail, local and cross-border financial institutions.

The EBF is committed to supporting EU policies to promote the single market in financial services in general and in banking activities in particular. It advocates free and fair competition in the EU and world markets and supports the banks' efforts to increase their efficiency and competitiveness.

Response to CESR's Consultation on its draft technical advice to the European Commission on level 2 measures relating to mergers of UCITS, master-feeder UCITS structures and cross-border notifications of UCITS (CESR/09-785)

Key Points

- In defining appropriate Level 2 measures for depositaries under the UCITS Directive, it must be borne in mind that depositary obligations are not currently harmonised across Member States. At this stage the Level 2 measures must therefore remain sufficiently generic and flexible to accommodate all possible situations and applicable home country depositary rules.
- Going forward, the EBF reiterates its support for the clarification and harmonisation of depositaries' responsibilities across Member States, on the basis of a thorough understanding of the current situation in different Member States.
- Depositaries should not have to perform different and/ or additional duties to those required by their local regulation when management companies are located in different Member States. In particular, the feeder fund depositary should not have to control the master fund depositary through an indirect look-through approach.
- It must also be borne in mind that feeder funds are often just one of a larger number of investors in a master funds. Care must be taken to ensure that all investors are treated alike.

Contact Person: Uta Wassmuth, u.wassmuth@ebf-fb.eu

Related documents: CESR consultation document: <http://www.cesr-eu.org/popup2.php?id=6042>

General remarks

The European Banking Federation (EBF) has been following the negotiations of UCITS IV and the related implementing measures over the past several years. Besides distribution issues, it takes a particular interest in the requirements related to depositaries. The below response therefore focuses on master-feeder structures and specifically, the agreement to be concluded between depositaries and the reporting requirements imposed on master depositaries in the case of detected irregularities.

As a general principle, the EBF wishes to underline the need to ensure that depositaries' responsibilities are the same for all UCITS under their supervision, regardless of the location of the management company. Furthermore, it must be borne in mind that feeder funds are often just one of a large number of investors in a master fund. In this case, care must be taken to ensure that all investors are treated alike.

Finally, the EBF **supports the harmonisation and clarification of depositaries' responsibilities across Member States, in line with the detailed suggestions it made in this respect to the European Commission¹**. As long as important differences in depositaries' responsibilities persist in different Member States, Level 2 requirements pertaining to depositaries must remain principles-based and flexible and refrain from imposing overly detailed rules which would likely conflict with national law and with the requirements of specific circumstances.

Specific responses to CESR's questions

Agreements between depositaries in the case of master-feeder structures (Section 2.4 of CESR's consultation document)

21. Do you agree with CESR's proposals for defining the content of the depositaries' agreement?

The EBF believes that the focus of the Level 2 measures on the agreements between depositaries should be to ensure that the information exchanged between the depositaries, or between their respective management companies, allows the feeder fund or its management company to communicate to the depositary all information needed by the feeder fund depositary to duly fulfil its oversight obligations, in compliance with its local rules.

As there is currently no harmonisation of the roles or obligations of depositaries in different Member States, care must however be taken to avoid any contradictions with local law and to refrain from imposing any additional obligations on depositaries. **The regulatory guidance for the agreements to be concluded between depositaries must therefore remain sufficiently principles-based and flexible to allow for a range of different situations and involved countries.**

Specifically, the level 2 measures should be limited to defining the general framework of the agreements in a level of detail sufficient to ensure a consistent approach across EU Member

¹ Cf. EBF response to the Consultation Paper of the Commission Services (DG Markt) on the UCITS Depositary Function: <http://www.ebf-fbe.eu/content/Default.asp?PageID=238>

States. Should further details be required for the content of the agreements, they should be defined through level 3 measures.

European banks would furthermore suggest that the content of the agreements to be concluded between depositaries be based on the following principles:

- **The two involved depositaries should agree between them, and on a case-by-case basis, on the documents or pieces of information to be exchanged between them** in order to ensure that the depositary of the feeder fund will be able to discharge its obligations. Parameters such as the existence of only one or two different management companies, the domicile of each fund involved and cases where each depositary has to report to its national regulator should be considered when defining the scope of the agreement and the nature of documents or information to be shared.
- The depositaries should at the same time **retain the freedom to agree on the most appropriate way and timing** for the transmission of these documents or information.
- Information to be communicated by the depositary of the master fund on its own initiative to the depositary of the feeder fund should be the same as that sent to the master fund's regulator when the depositary of the master fund has identified irregularities at the master fund level in the course of its oversight obligations; and when the master fund or where applicable, the management company of the master fund, has not taken the appropriate measures to solve these irregularities in a reasonable time.

However, it must be borne in mind that a feeder fund might be just one of many investors in a master fund and that investors must be treated alike. It would not be appropriate to grant the feeder fund's depositary access to information that is not available to other investors.

22. *Does Box 7 cover the right issues? Should other issues be addressed?*

23. *Which option do you prefer in relation to the national law and jurisdiction applicable to cross-border agreements? Would you prefer the law of the master depositary's home State to be applicable in every case?*

The EBF has the following comments on the elements proposed by CESR in Box 7:

- **Elements 1 and 2:** The EBF agrees with these points, provided that depositaries have enough flexibility to identify the corresponding documents on a case-by-case basis and to define the most appropriate way to exchange information between them, according to their respective organisation, location and set-up.
- **Element 3a:** Depositaries' specific responsibilities in NAV calculation, if any, vary widely according to the legal nature and the domicile of the fund. The EBF would therefore advise that this point should not be part of the Level 2 measures on the standard agreement to be signed between depositaries.

As regards concerns around market timing, European banks believe that it is the responsibility of the fund, or where applicable that of the fund management company, to establish operational models and procedures that protect against such practices. This

point should therefore not be imposed as an element to be included in the agreement to be concluded between the depositaries.

- **Element 3b:** The EBF believes that the feeder fund or where applicable, the feeder fund's management company, should be able to freely determine such aspects, as for any other UCITS fund. The Federation would indeed not perceive any added value in terms of investor protection from including this point in the agreement between the depositaries.
- **Element 4:** The EBF does not agree on the standard inclusion of the depositary report to unit-holders, as this document does not exist in some EU Member States. Furthermore, the Federation notes that the co-ordination of accounting period-end procedures might be included in the first element.
- **Element 5:** On this point, the divergences between EU Member States on how to report and monitor breaches need to be taken into consideration. In addition, it must be clearly specified that the feeder fund's depositary can only receive information transmitted voluntarily by the master fund's depositary, in accordance with law applicable to the master fund.
- **Elements 6 and 7:** The EBF agrees with these points, subject to a sufficient level of flexibility.
- **Elements 8a and b:** The EBF has a preference for the flexibility provided by Option B, as some of its members consider that the application of the master fund's law would facilitate the definition of the legal framework to govern this agreement, especially when there are several feeder funds for one master fund. Other members consider that the application of the feeder fund's law would guarantee a higher degree of protection for the feeder fund's investors. Flexibility, therefore, seems the most appropriate solution to address the lack of harmonisation.

24. <i>What would be the additional costs of the proposals in Box 7? Please quantify your estimate of one-off and ongoing costs. What would be the benefits of these proposals, compared to no prescription at level 2 on this issue?</i>
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As a Federation, the EBF cannot give an estimate of the costs expected to result from the requirements of Box 7. One-off costs as well as ongoing costs will vary between firms and will to a large extent depend on the final shape of the requirements.

However, firms expect little economies of scale given that different circumstances and the differences in according applicable national law strongly limit the potential for the harmonisation of the contracts. Costs are also expected as a result of the need to negotiate, in some cases, the agreements in different languages; or to translate them in other cases.

Depositaries expect in addition indirect costs in the form of the legal risks and divergences in national transpositions of the Directive; for example rules that might prevent the exchange of information with third countries as well as rules on professional confidentiality, data privacy, and others.

Reporting by the master UCITS depositary (Section 2.5 of CESR's consultation document)

25. Do you agree with CESR's proposals in relation to the irregularities to be reported by the depositary?

Upfront, the EBF would like to note that breaches with the master fund's objectives, policy or strategy as well as breaches of investment limits and borrowing limits do not currently have to be reported to the regulator in all Member States. Instead, it is often considered sufficient that they are reported to the fund auditor.

Apart from this, the EBF fully agrees with the important observation that the master fund depositary can be expected to report only on what it is required to oversee in accordance with its national law and regulation. The Federation considers that this principle should also apply for the types of irregularities to be communicated by the master fund depositary to the feeder fund depositary. European banks therefore agree with CESR's proposal in relation to the nature of irregularities outlined in Box 8.

Accordingly, Article 61 should **not imply any additional obligation on the master fund depositary to oversee, approve and report on the resolution of irregularities beyond what is required under the existing law of its home Member State**. Level 2 legislation should therefore not be prescriptive on the irregularities to be identified. It is important that the list of errors suggested in Box 8.2 is given by way of example and might not be applicable in some cases. Alternatively, such level of detail could be left to Level 3.

Regarding the scope of reporting, for any UCITS fund a depositary reports irregularities to its regulator after having informed the fund or its management company of the corresponding events, and when the fund or its management company has failed to properly solve these irregularities within a reasonable time. European banks believe that the same principle should apply to define those cases where the master fund depositary should inform the feeder fund depositary on irregularities at the level of the master fund. More frequent reporting to the feeder fund depositary on a wide range of irregularities, as proposed in point 2 of Box 8, would not add any value for the feeder fund depositary as the information would in most cases not be usable and could not be interpreted in terms of its impact on the feeder fund.

In addition, the EBF would recommend extending the requirement of such notifications to all other holders of units in the master fund to ensure equal treatment of shareholders.

26. Do you agree that the interests of other unit-holders in a master UCITS will be adequately protected under national laws if these proposals are implemented?

As noted above, the EBF believes that other unit-holders should be treated in the same way as the feeder fund, and specifically that they should have access to the same information as the feeder fund.

27. What would be the additional costs of the proposals in Box 8? Please quantify your estimate of one-off and ongoing costs. What would be the benefits of these proposals, compared to no prescription at level 2 on this issue?

European banks expect that the proposals made in Box 8 could potentially generate significant additional costs for both depositaries, especially as rules vary today across Member States as regards the irregularities to be reported by a depositary to its regulator.

Additional costs could be somewhat mitigated by introducing a general requirement on the master depositary to report irregularities observed to all unit-holders in the master fund, i.e. not only the feeder fund's depositary.

30. <i>Do you foresee that feeder UCITS will generally align their accounting periods with those of their master, or are there good reasons for having different accounting year-end dates?</i>

As noted above, it is the EBF's understanding that the feeder fund would not have to apply a look-through approach in its reporting duties. It would instead have to rely on the master fund's audited reports, including tax reports. The EBF would welcome that it is clarified that the feeder UCITS could re-use the master UCITS' statement of accounts in its own reporting obligations.