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Launched in 1960, the European Banking Federation is the voice of the European banking sector from the European Union and European Free Trade Association countries. The EBF represents the interests of almost 5000 banks, large and small, wholesale and retail, local and cross-border financial institutions. Together, these banks account for over 80% of the total assets and deposits and some 80% of all bank loans in the EU only.

ESMA's draft technical advice to the European Commission on possible implementing measures of the Alternative Investment Fund Managers Directive in relation to supervision and third countries

Key Points

- The EBF considers that there must be a **level playing field** between the depositaries located in the EU and the depositaries located in third countries.
- For the purpose of interpreting the level 1 text, the EBF believes that “Effective” is **results driven** and requires as the Directive specifies the achievements of the **same effects**.
- As long as the same effects are realized in the end, **operating conditions** should not have to be equivalent in the sense of being identical in design per se, but geared towards achieving the same effects. Different legal systems and structures can just as well result in the same effects being achieved.
- Another standard under the AIFMD for the purpose of recognizing the regulation for credit institutions as equivalent should be avoided where equivalence has already been accepted by CEBS and EBA under the **Capital Requirements Directive**.

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Related document : <http://www.esma.europa.eu/popup2.php?id=7702>

INTRODUCTION

The European Banking Federation (EBF) welcomes the work carried out by ESMA in providing this consultation paper on draft advice on possible implementing measures for the Alternative Investments Fund Managers Directive in relation to supervision and third countries.

The EBF trusts that ESMA will find value in this contribution. If necessary, further comments can be provided.

EBF INTEREST & APPROACH

The EBF's perspective is manifold, including that of distributors of both hedge funds and other types of funds; investors in funds; prime brokers to hedge funds; and depositaries.

In line with its recent response to the ESMA consultation on draft technical advice to the European Commission on possible implementing measures of the Alternative Investment Fund Managers Directive, the EBF has concentrated on responding to the questions concerning depositary issues in this consultation regarding supervision and third countries.

In brief, the EBF would also add that it sees Chapter III on delegation as being crucial and considers it very important that ESMA should actively help provide the necessary cooperation arrangements.

DEPOSITARY (ARTICLE 21(6))

Box 2

1. For the purposes of the assessment provided for in Article 21 (6) the following criteria should be met:

- a. The entity should be subject to authorisation and on-going supervision by an independent competent authority with adequate resources to fulfil its tasks;
- b. The local regulatory framework should set out criteria for the eligibility to act as depositary that are equivalent to those set out for the access to the business of credit institution or investment firm;
- c. The capital requirements imposed in the third country should be equivalent to those applicable in the EU as set out in Article 21 (6) (b) depending on whether the entity is equivalent to a credit institution or to an investment firm;
- d. The operating conditions are equivalent to those set out for credit institutions or investment firms within the EU depending on the nature of the entity;
- e. The requirement on the performance of the specific duties as AIF depositary established in the third country regulatory framework are equivalent to those provided for in Article 21 (8) to (15) and in the relevant implementing provisions;
- f. The local regulatory framework provides for the application of sufficiently dissuasive sanctions in cases of violations by the depositary;
- g. The liability to the investors of the AIF can be invoked directly or indirectly through the

AIFM, depending on the legal nature of the relationship between the depositary, the AIFM and the investors.

3. Do you agree with the above proposal? If not, please give reasons.

The EBF agrees with most of the above proposal as long as it ensures a level playing field between the depositaries located in the EU and the depositaries located in third countries. In this respect, we would recommend for the sake of legal clarity and legal accuracy that **the implementing measures proposed by ESMA be strictly based in their formulation on the results/objectives-driven approach adopted by the AIFMD level 1 text and not on new equivalence-based approach not provided for in the AIFM Directive**. Thus, in accordance with article 21.6 last paragraph of the AIFM Directive, the implementing measures proposed by ESMA in relation to the appointment of depositaries in third countries should aim to ensure that the prudential regulation and supervision of the third countries concerned **have the same effect** as the Union Law as regards the duties and liabilities of the depositary and are effectively enforced.

Article 21(6) of the Directive subparagraph b) expressly requires that the relevant entity is subject ‘to effective prudential regulation, including minimum capital requirements, and supervision which have the same effect as Union law and are effectively enforced’. As a matter of principle and in order to avoid regulatory arbitrage, prudential regulation and supervision applicable to a depositary established in a third country should not allow the depositaries established in third countries to circumvent the high standard of regulation applicable to European depositaries. The requirements of the local regulation applicable to the depositaries established in a third country should have the same effects and be effectively enforced as those provided in Article 21 (7)-(16) (Duties and liabilities applicable to a European depositary).

With this in view, the general criteria to be used by the Commission to assess third countries’ prudential regulation and supervision framework should allow ensuring that third countries’ different legal systems and structures have the same effects as the AIFM Directive (level 1 and 2 text), both as regards their requirements and enforcement.

In addition to our comments to question 3 above, the EBF has the following comments on Box 2 (taking each sub-paragraph in turn) :

- 1.(a) the EBF agrees with this criterion
- 1.(b) Criterion b should clarify in relation with explanatory text 6 that criteria to act as depositary should have the same effects and are effectively enforced as those set out for the access to the business of credit institution or investment firm applicable within the EU.
- 1.(c) The EBF agrees with this criterion

•1.(d) It should be clarified that “effective” is results driven and requires as the Directive specifies the achievement of the same effects. This means that the operating conditions (d), the requirements on the performance (e) etc. must result in the same results being achieved in terms of the duties and liabilities of the depositary.

•1.(e)The reference to article 21 should include (7) cash monitoring and (16) (information to the competent authority) .

•1.(f) The local regulatory framework should provide sanctions in case of violations by the depositary. **These sanctions shall have the same dissuasive effects as EU sanctions in order to ensure the effective enforcement of the requirements regarding the duties and liabilities of the depositary.**

•1.(g) This Criterion does not seem necessary as already included in criterion 1.(e) (Article 21 (15))

In view of the above mentioned concerns, the EBF would propose amending Box 2 as follows:

EBF proposed amendment to Box 2

1. For the purposes of the assessment provided for in Article 21 (6) the following criteria should be met:

a. The entity should be subject to authorisation and on-going supervision by an independent competent authority with adequate resources to fulfil its tasks;

b. The local regulatory framework should set out criteria for the eligibility to act as depositary that are equivalent to those set out for the access to the business of credit institution or investment firm **applicable within the EU**;

c. The capital requirements imposed in the third country should be equivalent to those applicable in the EU as set out in Article 21 (6) (b) depending on whether the entity is equivalent to a credit institution or to an investment firm;

d. The operating conditions are equivalent to those set out for credit institutions or investment firms within the EU depending on the nature of the entity;

e. The requirement on the performance of the specific duties as AIF depositary established in the third country regulatory framework are equivalent to those provided for in Article 21 ~~(8)~~ **(7)** to ~~(15)~~ **(16)** and in the relevant implementing provisions;

f. The local regulatory framework provides for the application of ~~sufficiently dissuasive~~ sanctions in cases of violations by the depositary. **These sanctions shall have the same**

dissuasive effects as EU sanctions in order to ensure the effective enforcement of the requirements regarding the duties and liabilities of the depositary.

~~g. The liability to the investors of the AIF can be invoked directly or indirectly through the AIFM, depending on the legal nature of the relationship between the depositary, the AIFM and the investors.~~

4. Do you have an alternative proposal on the equivalence criteria to be used instead of those suggested in point b above?

In line with our answer to question 3, we believe that there should be an effects test and not a test of equivalence, and that this test should be limited to the prudential side of the regulation, including capital requirements and supervision.

Where CEBS and EBA, respectively, have recognized the regulation for credit institutions as equivalent (e.g. as required under article 131a Capital Requirements Directive), the relevant requirement under article 21(6)(b) should be considered as being satisfied. Another standard under the AIFMD for this purpose should be avoided.