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CESR consultation paper on the level 2 measures related to the UCITS management company passport (CESR/09-624)

Dear Mr. Comporti,

BVI¹ is grateful for the opportunity to submit its views on the proposals for implementing measures setting out a new operational framework for UCITS management companies.

General remarks

We support the general concept of the UCITS IV Directive requiring greater harmonisation of organisational and conduct of business rules for UCITS managers in order to facilitate the functioning of the management company passport. In this regard, we also share CESR's view that the MiFID regime stipulating acknowledged high standards for the activities of investment firms should be treated as a benchmark also for the regulation of management companies.

¹ BVI Bundesverband Investment und Asset Management e.V. represents the interest of the German investment fund and asset management industry. Its 88 members manage currently assets in excess of EUR 1.5 trillion both in mutual funds and mandates. For more information, please visit www.bvi.de.

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In this context, however, it is important to notice that for smaller UCITS managers who focus on the services of collective portfolio management and hence, have not yet been obliged to follow the MiFID rules, implementation of organisational and conduct of business standards alongside the MiFID regime presents a serious challenge both in operational and financial terms. In order not to inappropriately increase this burden, it is very important for CESR to keep in mind the specificities of the fund business and the position of UCITS managers as product providers when considering alignment of UCITS rules with MiFID which was designed for the investment services sector. Also from the viewpoint of cross-sector competition, MiFID standards must not be exceeded by the UCITS regime where such extension is not justified by peculiar features of the fund business. UCITS management companies are already subject to very high standards of regulation as compared to MiFID firms. Thus, any modification of organisational or conduct of business rules must be discussed on a broader basis in order to avoid competitive distortions between financial sectors and to keep in line with the generally provider-neutral concept of MiFID.

Furthermore, we would like to note that the UCITS IV Directive allows for different national approaches to the allocation of duties between the management company and the depositary. For example, in some Member States the duties of fund valuation or handling of issuance and redemption orders are assigned to or may also be performed by the depositary, whereas in other Member States these are core functions of the management company itself. Hence, we request CESR to pay attention to these divergences in regulatory models when formulating its final advice to the Commission in order to avoid unnecessary restrictions to the general UCITS framework carved out at level 1.

Specific comments

Concerning specific issues for consultation raised by CESR, we will abstain from commenting on the details of supervisory cooperation suggested in section V of the consultation paper. In respect of the remaining proposals, we would like to comment as follows:

Section I: Organisational requirements and conflicts of interest

Q1: *Do you agree with the general approach proposed by CESR?*

In reference to the general statement above, BVI agrees with the suggestion to treat MiFID level 2 provisions as the primary regulatory model for UCITS as this step should enhance consistency in the EU financial market regulation and facilitate business set-up of management companies offering MiFID services alongside of UCITS management.

Q2: *In your view, does aligning the organisational requirements for UCITS management companies with the relevant MiFID requirements in the areas of*

- *general organisational requirements;*
- *compliance;*
- *internal audit;*
- *responsibility of senior management;*
- *complaints handling;*
- *personal transactions; and*
- *electronic data processing and recordkeeping*

impose additional costs on UCITS management companies? If so, please specify which areas are affected. If possible, please provide quantitative cost estimates of the additional costs for UCITS management companies.

For German UCITS managers not yet subject to MiFID requirements (e.g. smaller management companies offering solely services of collective portfolio management), costs of compliance with the new organisational rules would be quite considerable. Should the suggestions on recording of subscription and redemption orders in Box 8 be maintained, however, all management companies would incur extensive (and in our view, useless) expenses.

Q3: *In your view, what are the benefits of aligning the organisational requirements for UCITS management companies with the relevant MiFID requirements?*

Cf. our reply to Q1.



Q4: *Do you agree with CESR's proposals on organisational procedures and arrangements for management companies? If not, please suggest alternatives.*

We agree with the proposals for general organisational requirements in Box 1 as in our view they reflect the already valid and efficient organisational standards of the fund business.

Q5: *Do you agree with the above CESR proposal on the responsibility of senior management of management companies? If not, please suggest alternatives.*

We consent to the principles on allocation of organisational responsibilities proposed by CESR in Box 2.

Q6: *Do you agree with the above CESR proposal on the remuneration policy of management companies? If not, please suggest alternatives.*

BVI members acknowledge the intention to establish general principles on remuneration in the financial sector in order to countervail short-term financial incentives and to promote consistency with sustainable risk management and interests of investors.

However, we have certain objections against endorsing such principles by means of binding legislative measures only for UCITS management companies. The excessive use of short-term oriented bonuses has become particularly visible in the banking sector which we would expect to be at the centre of respective regulatory actions. Measures for other market participants should be modelled after these requirements in order to avoid competitive distortions by way of diverging standards of remuneration.

Q7: *In your view, should the requirements set out above in relation to senior management be extended to cover all employees of UCITS management companies?*

We deem it disproportionate to extend the suggested remuneration requirements to the entire staff of UCITS management companies. In order to stay in line with the Commission's recommendation of April 2009, the



remuneration principles should apply only to “those categories of staff whose professional activities have a material impact on the risk profile of the management company”. Such limitation of scope should be evident from the wording of CESR’s advice to the Commission laid down in Box 3.

Q8: *Do you agree with the above CESR proposal on the compliance function of management companies? If not, please suggest alternatives.*

In general, we support CESR’s suggestion to extend MiFID standards on compliance to the UCITS management. In practice, however, it must be ensured that the responsibility of the compliance function for ensuring observance of the UCITS regime is limited to the oversight of effectiveness of applicable policies and procedures and clearly distinguished from the management companies’ operative functions.

Q9: *Do you agree with the above CESR proposal on the internal audit of management companies? If not, please suggest alternatives.*

We agree with the proposed approach to internal audit.

Q10: *Do you agree with the CESR’s proposal on complaints handling procedures for management companies? If not, please suggest alternatives.*

The language requirement in Box 6, last sentence, should apply only to Member States in which a UCITS is notified for marketing. This would be in line with Art. 15 of the UCITS Directive which is designed as specification of the general provision in Art. 92.

Furthermore, neither MiFID nor the UCITS Directive requires establishment of a “complaints handling policy” as a formal documentation of procedures for complaints’ handling which should be provided to investors free of charge. This additional requirement suggested by CESR in para. 43 must be rejected as it would further enhance the bureaucratic burden placed upon UCITS management companies. In order to ensure appropriate investor information, however, details on available means of filing complaints could be provided on the management company’s website and communicated to investors via a general reference in the KID.

Q11: *Do you agree with CESR's proposals on personal transactions? If not, please suggest alternatives.*

We agree with the transposition of MiFID provisions in relation to personal transactions.

Q12: *Do you agree with CESR's proposals on electronic data processing and recordkeeping requirements? If not, please suggest alternatives.*

We reject the suggestion in Box 8 para. 1 letter h) to make records on reasons behind a potential revocation of order as such requirement goes beyond MiFID provisions on record-keeping and is of no discernible value to the authorities.

Moreover, we decisively oppose the extensive provisions on recording of subscription and redemption orders. For the German model of unit order handling, the proposed requirements could at the most be fulfilled by the depositary who is under the obligation to conduct subscriptions and redemptions of fund units according to § 23 InvG. Management companies are involved in the subscription and redemption process only in the (rare) case of direct distribution. But even the depositary is generally not able to identify the ultimate unit-holder as, in most cases, it receives subscription orders from intermediaries like banks who sell units of UCITS on own account and keep them in custody accounts for investors. Identification of unit-holders is further complicated by the fungibility of fund units which are issued as bearer notes in Germany and hence, can be resold or otherwise transferred to a third party without involvement or knowledge of the issuing management company.

Therefore, from the viewpoint of the German fund industry, the recording requirement would be only workable if it were addressed at the depositary and limited to recording of directly received orders (from intermediaries / from clients in case of direct distribution).

Nevertheless, we do not see how such recording requirements could be of any help in terms of preventing malpractices such as late trading or market timing as identification of individual unit-holder and monitoring of its investment behaviour is virtually impossible. In Germany, moreover, it is very easy (and quite common with sophisticated investors) to buy fund units on secondary platforms and to redeem them with the depositary. In this case,



the depositary has definitely no means to control the holding period of the respective investment.

In addition, details of order execution cannot possibly be recorded “immediately after receipt” of an order, but require successful order execution. The relevant information stipulated in Box 8 (p. 29, para. 2 (iii)) is definitely not available before the transaction note has been generated.

Lastly, we definitely do not agree with the suggestion in para. 57 of the explanatory text to facilitate appropriate access to IT systems and databases between the management company, the depositary and the distributors. Such allowance would be blatantly contradictory to the applicable standards of data protection and confidentiality of information and would disregard the still valid principle of banking secrecy.

Q13: *Do you agree with CESR’s proposals on UCITS accounting principles? If not, please suggest alternatives.*

We agree with the proposed substantial standards for UCITS accounting. As regards the allocation of responsibilities, however, it must be ensured that the different models of asset valuation and calculation of NAV which have evolved under the UCITS Directive can be maintained and in particular, that the responsibility for these functions can be entrusted to the UCITS depositary. For details, cf. our comments on Q1 in section II.

Q14: *Does this proposal lead to additional costs for UCITS management companies? Please quantify your cost estimate. What are the benefits of this proposal?*

We do not expect additional costs for UCITS management companies as a result of CESR’s proposals in terms of UCITS accounting.

Q15: *Do you agree with CESR’s proposals on investment strategies? If not, please suggest alternatives.*

In our view, the difference between “general investment policy” as specified in the KID and “investment strategies” is unclear and needs further elaboration. The explanatory sentence provided in para. 1 of Box 10 does not lead any further as “general indications on strategic asset allocation”,



and applicable “investment techniques” are usually considered part of the investment policy laid down in the fund prospectus. Within these limits, decisions on specific investment strategy applied to a UCITS portfolio are taken by the portfolio management team on a daily basis and thus, cannot be approved or verified by the senior management. In any case, we think that the respective responsibility of the senior management should be clearly reduced to organisational aspects of ensuring compliance with the “general investment policy” and the applicable risk limits of a UCITS.

Q16: *Does this proposal lead to additional costs for management companies? If possible, please quantify your estimate. What are the benefits of this proposal?*

Due to the uncertainty regarding the meaning of “investment strategies”, it is at this stage not possible to make estimates concerning additional costs. However, as such strategies shall apparently be laid down in writing and reviewed on a regular basis, they will certainly have financial implications on the UCITS management.

Q17: *Do you agree on the proposed requirements relating to the exercise of voting rights? If not, please suggest alternatives.*

Divergences in voting behaviour adopted for specific UCITS should be avoided whenever possible in order to prevent conflicts of interests. For that purpose, management companies should be granted more flexibility in interpreting the “exclusive benefit of unit-holders” by amending the wording of Box 11, para 2 letter b) in the following manner:

*“evaluate timing and modalities for the exercise of the votes **in accordance with** the investment objectives and policy of the relevant UCITS”*

Moreover, there should be no general obligation to report to investors on details of the exercise of voting rights.

Q18: *What are the additional costs of this proposal for management companies? If possible, please quantify your estimate. What are the benefits of this proposal?*



BVI members already make available to investors summary information on their voting rights policies. Depending on specific requirements in this respect, extension of such information to implementation aspects can generate additional costs.

Q19: *Do you agree with the proposed approach? Is there any additional adaptation you would suggest?*

In general, BVI members agree with the proposed alignment to MiFID standards as regards management of conflicts of interest. However, we have certain reservations against the “holistic” approach to conflict management suggested by CESR. As with MiFID provisions, the obligation to manage conflicts of interests should in case of UCITS management companies be clearly limited to the provision of the relevant service which is collective portfolio management.

Q20: *In your view, does aligning the requirements for conflicts of interest for UCITS management companies with the relevant MiFID requirements impose additional costs on UCITS management companies?*

- *procedures for conflict identification and management,*
- *independence of the persons managing conflicts,*
- *recordkeeping for collective portfolio management activities, and*
- *management of non-neutralised conflicts.*

If so, please specify which areas are affected.

If possible, please provide quantitative cost estimates of the additional costs for UCITS management companies.

Implementation of new rules on conflict of interest management will impose considerable costs on German UCITS managers not yet subject to MiFID provisions. More generally, additional costs should be expected from the reporting duty on non-neutralised conflicts suggested in Box 16, para 1.

Q21: *In your view, what are the benefits of aligning the requirements for conflicts of interest for UCITS management companies with the relevant MiFID requirements?*



The probable benefits are reduction of distortions in the financial sector regulation and a consistent set of rules for management companies engaging in both UCITS management and MiFID services. However, there is also the imminent danger of UCITS regulation becoming too tied to the MiFID regime and thus, unable of dynamic self-evolution.

Q22: *Do you agree with CESR's proposals on the criteria for identifying conflicts? If not, please suggest alternatives.*

We agree in general, but would like to suggest more stringency in terms of wording, especially regarding the scope of application of conflict of interest measures. To this effect, the first sentence of Box 12, para. 1 should be aligned with the requirement in Box 13, para 2 letter a) and require identification of conflicts of interest *"that arise in the course of providing collective portfolio activities"*.

Q23: *Do you agree with CESR's proposals on the identification and management of conflicts? If not, please suggest alternatives.*

The requirement in para. 17, 2nd sentence of the explanatory text to identify circumstances giving rise to potential conflicts of interests in relation to each single UCITS is too far-reaching. In order to warrant consistency with the text in Box 13, para. 2 letter a), it should be sufficient to demand identification of conflicts on the basis of specific portfolio management activities carried out by or on behalf of the management company.

Q24: *Do you agree with the CESR's proposals on the independence of the persons managing conflicts? If not, please suggest alternatives.*

We agree with the proposed transposition of MiFID standards regarding the relevant persons' independence to UCITS management companies.

Q25: *Do you agree with CESR's proposals on records of activities giving rise to conflicts of interest? If not, please suggest alternatives.*

We agree.

Q26: *Do you agree with CESR's proposals on management of non-neutralised conflicts? If not, please suggest alternatives.*



In principle, we support the proposed approach to management of non-neutralised conflicts in the course of collective portfolio management. As regards reporting to investors, however, the explanatory text in para. 28 should be reworded in order to make clear that disclosure in periodic reports is deemed sufficient for compliance with the departing duty stipulated in Box 16, para. 1, 2nd subparagraph. As it stands, the passage might be read as implying that periodic reporting shall take place in addition to some other form of more immediate disclosure ("this solution shall be without prejudice to the duty...").

Moreover, the extension of standards for management of non-neutralised conflicts to individual portfolio management and investment advice suggested in para. 31 of the explanatory text should be deleted as it contradicts the MiFID provisions and discriminates against UCITS management companies versus MiFID firms authorised for the provision of those services.

***Q27:** Are there any other issues you feel should be considered in addition to those already mentioned in this paper?*

We do not have any further requests in this regard.

Section II: Rules of conduct

***Q1:** Do you agree with CESR's proposals on the duty of management companies to act in the best interest of UCITS and their unitholders and on due diligence requirements? If not, please suggest alternatives.*

We have several reservations against the requirements proposed in Box 1 and 2.

Pricing models and valuation systems for UCITS (Box 1, para. 3)

In terms of valuation of UCITS portfolios, **due account must be taken of valuation models in jurisdictions allowing for allocation of respective responsibilities with the depositary.** Under the German Investment Act, for instance, the obligation to value portfolio assets and to calculate the fund's NAV may rest either with the management company or with the



depository in which case involvement of the management company is required (cf. § 36 para. 1, 2nd sentence InvG). This implies the possibility of vesting the depository with the original responsibility for valuation which is very common with German fund managers. This approach is also covered by the UCITS Directive, according to which the depository is held responsible for ensuring proper valuation of UCITS (Art. 22 para. 3 letter b)).

Thus, in order to account for the outlined valuation model, the provision in Box 1 para. 3 should be reworded in the following terms:

*“3. Without prejudice to specific national law requirements, management companies should **ensure that** fair, correct and transparent pricing models and valuation systems **are applied to the UCITS they manage in order to comply with the duty to act in the best interest of the unit-holders. Management companies should be able to demonstrate that the UCITS portfolios have been accurately valued.**”*

Prevention of undue costs (Box 1, para 4 and para 2. of the explanatory text)

It is common understanding that the fiduciary duty of fund managers to investors applies throughout the conduct of their business activities (cf. Art. 14 para. 1 letter a) UCITS Directive). Thus, while acknowledging that management companies are bound by the fiduciary duty to avoid undue costs in terms of fund management, e. g. concerning order execution or appointment of third parties, we definitively reject the notion of requiring management companies to act in the best interest of investors when defining their own fees charged to the fund. If consequently applied, the fiduciary duty should lead to the management fee being fixed at the necessary level to cover operating expenses of a management company but allowing for no generation of profits, which is an absurd outcome. In our understanding, **definition of charges is a purely commercial decision of a management company and must remain unhampered by regulatory intervention** in order to allow for fair and dynamic competition.

Due diligence requirements (Box 2 and para. 10 of the explanatory text)

While technical due diligence of investments is already common standard with management companies, the proposed requirements for legal scrutiny with regard to more complex investments such as underlying funds are at



this level of detail a relatively new issue. Indeed, the question arises whether it is proportionate to demand such meticulous analysis for each underlying fund or whether in certain circumstances it might be allowable to rely upon proper authorisation and/or supervision of the product or its manager (e.g. in case of funds authorised in the EU or in other jurisdictions applying equivalent standards). Otherwise, application of such detailed due diligence criteria for each and every underlying fund would result in cost explosion at the fund of fund level which would render these vehicles less attractive to investors or possibly, promote investments in target funds belonging to the same financial group.

The requirement to keep records of due diligence assessment for every single investment decision imposes very high bureaucratic burden upon management companies and is entirely disproportionate in view of the mass investment business taking place in the area of fund management. Rather, **it should be sufficient for the underlying reasons of an investment to be reproducible** on the basis of the management company's due diligence policies and procedures as well as general investment policy of the relevant fund.

Q2: *What are the additional costs of this proposal for management companies? If possible, please quantify your estimate. What are the benefits of this proposal?*

The proposed due diligence standards will lead to high additional costs for UCITS management companies due to the requirement to implement written policies and procedures on due diligence and extensive operational efforts with regard to selection and monitoring of more complex investments such as target funds (cf. our answer to Q1 above).

Q3: *Do you agree with this general approach proposed by CESR for conduct of business rules relating to direct selling? If not, please suggest alternatives.*

In general, we deem it appropriate to extend MiFID rules to direct distribution of UCITS by management companies. However, Box 7 relating to execution of orders should not apply to direct sales by management companies which are effectuated by issuance and redemption of fund units. Apart from that, we will abstain for the time being from commenting on detailed requirements



proposed in Boxes 4 to 6 as they appear to adequately reflect the contents of the corresponding MiFID provisions.

Q4: *What are the additional costs of this proposal for management companies? If possible, please quantify your estimate. What are the benefits of this proposal?*

We do not expect significant costs in this area. Potential benefits are, clearly, alignment of distribution standards applicable to UCITS.

Q5: *Do you agree with CESR's proposals on conduct of business rules relating to direct selling? If not, please suggest alternatives.*

Q6: *What are the additional costs of this proposal for UCITS management companies? If possible, please quantify your estimate. What are the benefits of this proposal?*

No comments so far.

Q7: *Do you agree with CESR's proposals on direct execution of orders by management companies? If not, please suggest alternatives.*

Q8: *What are the additional costs of this proposal for UCITS management companies? If possible, please quantify your estimate. What are the benefits of this proposal?*

Q9: *Do you agree with CESR's proposals on the placement of orders with or transmission to other entities for execution? If not, please suggest alternatives.*

Q10: *What are the additional costs of this proposal for UCITS management companies? If possible, please quantify your estimate. What are the benefits of this proposal?*

We agree with the principles on direct and indirect execution of investment decisions on behalf of the managed UCITS and in particular, welcome the proposed flexibility in terms of the relative importance of factors for obtaining best execution results.

However, prior consent of a UCITS to the direct execution policy requested in Box 7, para. 3, is definitely not feasible in case of common funds without legal personality. If deemed necessary, such requirement should be restricted to UCITS in the form of investment companies.



Moreover, it would be helpful for CESR to clarify that access of unit-holders to information on the best execution policy and on any material amendment thereof suggested in Box 7, para. 3 and Box 8, para. 3 can be granted by means of publication on the management company's website, and that disclosure towards individual investor is not required.

Q11: *Do you agree with CESR's proposals on the handling of orders? If not, please suggest alternatives.*

Q12: *What are the additional costs of this proposal for UCITS management companies? If possible, please quantify your estimate. What are the benefits of this proposal?*

The delivery of financial instruments or cash amounts to the account of the appropriate UCITS represents a duty of the depositary in accordance with Art. 22 para. 3 letter d) of the UCITS Directive.

Q13: *Do you agree with CESR's proposals on inducements? If not, please suggest alternatives.*

In our opinion, MiFID standards for inducements render justification of a management company's payments to distributors a very difficult task. It is common practice in Germany as well as in other European countries to remunerate advice and distribution in terms of fund units by forwarding of generally the entire entry fee and parts of the annual management fee to the distributing entity. Such payments are meant to compensate distribution efforts and to ensure high standards in the quality of advisory services performed by intermediaries. Thus, they can be only indirectly deemed to enhance the quality of the collective portfolio management activity as required in BOX 11, para. 1, letter b) ii).

This problem is due to MiFID taking the view of intermediaries maintaining direct contacts to clients. The UCITS Directive, on the other hand, is focused on product manufacturing and targets management companies who need to appoint intermediaries in order to sell fund units to the retail public. This practice is common also with other investment products such as e.g. unit-linked insurance contracts, but shall be subjected to the MiFID standards on inducements only with regard to UCITS. Such punctual extension of MiFID provisions to the production side might not only have adverse effects on distribution and growth of UCITS, but would also privilege other "substitute"



products which would compete with UCITS for investors' assets on more than ever unequal terms.

Thus, having regard to para. 46 of the explanatory text, **we urge CESR to make proper allowance for the characteristics of UCITS and their distribution practices when transferring the MiFID inducement standards into the UCITS regime.** As the receipt of payments by the intermediary is already covered by MiFID, we basically regard it as sufficient to limit the scope of UCITS rules to the receipt of payments by the management company. To accomplish this, any reference to payment of a fee or commission, or provision of non-monetary benefit by a management company should be deleted from Box 11.

As a second-best solution, it could be contemplated to introduce appropriate variations in the applicable standards for payments to third parties. Payments should be allowed if their receipt by the intermediary is permissible according to the MiFID rules and the respective potential for conflicts of interests is clearly disclosed in the conflict of interest policy of the management company. Stricter criteria for justification of distribution remuneration are in our view not acceptable.

Q14: *What are the additional costs of this proposal for UCITS management companies? If possible, please quantify your estimate. What are the benefits of this proposal?*

The extent of financial implications for UCITS managers will clearly depend upon the solution provided to the above mentioned problem.

Section III: Measures to be taken by a depositary of a UCITS managed by a management company situated in another Member State

Q1: *Do you agree that no additional requirements should be imposed on a depositary when the management company is situated in another Member State?*

Q2: *What will be the costs of imposing such a requirement for the industry? What would be the implementation difficulties for regulators?*



We consent to CESR's suggestion to extend the requirement for a written agreement governing the relationship between the management company and the depositary to domestic situations. As such agreement is already common standard with German fund managers, we do not expect additional costs in this regard.

Q3: *Are the proposed requirements appropriate?*

Q4: *Are the information flows exchanged in relation to the outsourcing of activities by the management company or the depositary relevant?*

Q5: *Is it appropriate to indicate in the written agreement that each party may request from the other information on the criteria used to select delegates? In particular, is it appropriate that the parties may agree that the depositary should provide information on such criteria to the management company?*

We do not agree with the extensive inquiry measures suggested for the depositary in the second last paragraph of Box 2. Inquiries into the management company's conduct of business by means of on-site visits imply an oversight in terms of reasonability (Zweckmäßigkeitprüfung) which is not the remit of a depositary. Indeed, a depositary is neither qualified nor equipped for performance of such substantive control function which, therefore, should remain with the auditors and the competent supervisor. In case of suspected violations of legal or contractual rules, the depositary should request written representation from the management company and if that proves dissatisfactory, should report the incident to the authorities.

Therefore, we suggest deleting the first sentence of Box 2, second last paragraph, and rephrasing the second sentence in a manner allowing for reciprocal application, e.g.:

"The agreement shall include a provision regarding the possibilities and procedures for the review of the depositary by the management company and vice versa."

Moreover, we agree with the suggestions regarding information flows on outsourcing as long as their application is left to the discretion of the contractual parties. In general, the ongoing information obligations on delegation arrangements and their details should be limited to the level which is necessary for both the management company and the depositary to meet their mutual obligations.

Q6: *Is the split between suggestions for level 2 measures and envisaged level 3 guidelines appropriate?*

Q7: *Do you see a need for level 2 measures in this area or are the level 1 provisions sufficiently clear and precise?*

Q8: *Do you consider that the proposed standard arrangements and particulars of the agreement are detailed enough?*

Q9: *What are the benefits of such a standardisation in terms of harmonisation, clarity, legal certainty etc.?*

Q10: *What are the costs for depositaries and management companies associated with the proposed provisions?*

We deem the level of detail proposed for level 2 provisions appropriate. Moreover, we do not see the immediate need to elaborate upon level 3 guidelines on the content of the depositary agreement.

Q11: *Do you agree that the agreement between the management company the depositary should be governed by the national law of the UCITS? If not, what alternative would you propose?*

Q12: *What are the benefits of such a proposal? Do you see costs associated with such a provision? In particular, is this requirement burdensome for the UCITS management company that will be subject to the law of another Member State regarding the agreement with the depositary?*

We agree with the proposed application of the national law at the UCITS domicile as this solution appears to warrant an appropriate level of investor protection.

With regard to the depositary, we do not see substantial additional costs associated with such a provision, as the depositary will be required to undertake the same duties that it currently performs in accordance with the law of the Member State in which the UCITS is established. This requirement will however have some impacts on management companies. The management company located in another Member State to the depositary will need to be aware of all the relevant laws of the UCITS national country and also the interpretations of such laws. This is however inherent and unavoidable in a situation where a management company uses the new passport. The provision will as well increase the legal and auditors fees for the management company.

Q13: *Do you agree that investment companies should not be treated differently from common funds in respect of CESR's proposals?*

Q14: *In your view, would such an approach impose unnecessary and/or burdensome requirements on investment companies? Would equal treatment improve the level playing field between different types of UCITS?*

We support CESR's suggestion for equal treatment of common funds and investment companies in their respective relationship with the depositary.

Q15: *Do you agree with CESR's proposal that equivalent rules should apply to domestic and cross-border situations? In particular, do you agree that depositaries should enter into a written agreement with the management company irrespective of where the latter is situated?*

Q16: *Do you think that such a recommendation would increase the level of protection for UCITS investors? Do you agree that a level playing field between rules applicable to domestic situations and those applicable to cross-border management of UCITS offsets potential costs for the industry?*

Q17: *What would be the benefits of such an extension in terms of harmonisation of rules across Europe? What would be the costs of extending rules designed for cross-border situations to purely domestic situations? In particular, would a provision stating that the management company and the UCITS depositary have to enter into a written agreement irrespective of their location add burdensome requirements to the asset management sector?*

We do not object to the universal application of the requirement for a written agreement between the management company and the depositary. However, we do not expect any significant implications for investor protection as such agreement is already common standard with German fund managers. Also, we would like to point out that the level 1 provisions of the UCITS Directive provide no legal basis for such an extension of rules.

Section IV: Risk management

Q1: *Do the proposals related to risk measurement for the purposes of the calculation of UCITS' global exposure (as set out in document Ref. CESR/09-489) lead to additional costs for management companies and self-*

managed investment companies? Please quantify your cost estimate. What are the benefits of this proposal?

The German fund managers already observe high standards of risk measurement when calculating the UCITS' global exposure to derivatives. Hence, we do not expect additional costs to be incurred by the German fund industry as a result of CESR's proposals.

Q2: *Do you agree with CESR's proposal on the scope and objectives of the risk management policy that should be adopted by the management companies? If not, please suggest alternatives.*

Q3: *Do the proposals related to identification of risks and risk management policy lead to additional costs for management companies and self-managed investment companies? Please quantify your cost estimate. What are the benefits of this proposal?*

Q4: *Do you agree with CESR's proposal on the organisational requirements which should apply to the risk management function? If not, please suggest alternatives.*

Q5: *Do the proposals related to the risk management function lead to additional costs for management companies and self-managed investment companies? Please quantify your cost estimate. What are the benefits of this proposal?*

Q6: *Do you agree with CESR's proposals on the organisational requirements and safeguards which should apply to the risk management function in case of arrangements with third parties? If not, please suggest alternatives.*

Q7: *Do the proposals related to performance of risk management functions by third parties lead to additional costs for management companies and self-managed investment companies? Please quantify your cost estimate. What are the benefits of this proposal?*

Q8: *Do you agree with CESR's proposals on the procedural and methodological requirements that should apply to the risk management process adopted by the management companies? If not, please suggest alternatives.*

Q9: *Do the proposals related to the measurement and management of risks, including liquidity risks, lead to additional costs for management companies and self-managed investment companies? Please quantify your cost estimate. What are the benefits of this proposal?*

Q10: Do you agree with CESR's proposals on the requirements concerning the responsibility and governance of the risk management process? If not, please suggest alternatives.

Q11: Do the proposals related to the responsibility of the board of directors and internal reporting lead to additional costs for management companies and self-managed investment companies? Please quantify your cost estimate. What are the benefits of this proposal?

No comments so far.

Q12: Do you agree with CESR's proposals on the link between the risk management policy and the valuation of OTC derivatives? If not, please suggest alternatives.

Q13: Do you agree with CESR's proposal to extend the application of the requirements set out in Box 3 (concerning the risk management activities performed by third parties) to the valuation arrangements and procedures concerning OTC derivatives (regarding both the valuation and the assessment of the valuation) which involve the performance of certain activities by third parties?

Q14: Do you agree with CESR's proposal to extend the application of the requirements set out in Box 6 to the valuation of other financial instruments which expose the UCITS to valuation risks equivalent to those of OTC derivatives? If not, please explain and suggest alternatives.

Q15: In cases where financial instruments embed OTC derivatives, do you consider it appropriate to apply the requirements referred to in Box 6 to the valuation of the embedded derivative element of the financial instrument? Should these requirements apply to the valuation of all such instruments? Please explain your answer and, where appropriate, suggest alternatives.

We urge CESR to take due account of valuation systems vesting the key role in the valuation process with the depositary as already explained in our reply to Q1 in section II. This approach is in line with Art. 51 para. 1, 2nd subparagraph of the UCITS Directive which requires management companies to employ processes "for accurate and independent assessment of the value of OTC derivatives". Indeed, the assessment by a management company may have the nature of verifying scrutiny suggested by CESR in Box 6, para. 1, letter ii). The requirements on initial valuation in para. 2, 4 and 5, however, should be phrased in a more neutral manner in order to allow for the UCITS depositary to assume responsibility for the valuation function. Also, the explanatory text would need to be adapted accordingly.

As regards determination of fair value of OTC derivatives, we would like to point out that under some framework agreements, quotes on OTC derivatives must be delivered by the respective counterparty. It remains an open question whether it would be feasible in such circumstances to deviate from such quotations for the purpose of internal valuation.

Moreover, we have some reservations in respect of the role assigned to the risk management function in para. 3. Generally, risk management and valuation units work on different premises, with the former aiming at identification of future valuation risks and the latter requiring determination of currently valid prices. Hence, requirement for the risk management function to perform independent assessment of valuation results might not always be appropriate, and we strongly advise CESR to change the wording of para. 3, 1st sentence in order to allow for more flexibility in this regard.

We have no general objections concerning extension of valuation principles for OTC derivatives to other asset types displaying similar valuation risks. In order to avoid practical problems in determining those asset classes, however, more specific regulatory guidance preferably by means of binding level 2 measures would be needed.

Q16: *Do the proposals related to the valuation of OTC derivatives in the context of risk management lead to additional costs for management companies and self-managed investment companies? Please quantify your cost estimate. What are the benefits of this proposal?*

We expect the proposals on valuation processes for OTC derivatives to generate additional costs at a moderate level. For German fund managers, however, the costs would be extensive if the provisions were not adapted to accommodate the depositary's responsibility for valuation.

Q17: *Do you agree with CESR's proposals on the supervisory framework that should apply to the risk management process adopted by the management companies? If not, please suggest alternatives.*

Q18: *Do the proposals related to authorisation processes and the supervisory approach of competent authorities lead to additional costs for management companies and self-managed investment companies? Please quantify your cost estimate. What are the benefits of this proposal?*

Q19: *Do you agree with CESR's proposals on the application to investment companies of the risk management requirements set out in this document? If not, please explain your position.*

The provision in Box 7 para. 2 can be valid only in domestic situations where the UCITS applying for authorisation shall be managed by a management company domiciled in the same Member State. In case of UCITS launches under the management company passport, oversight over risk management processes is assigned to the competent authorities of the management company's home Member State (cf. Art. 19 para. 1 of the UCITS Directive). Moreover, details of the risk management process do not form part of the cross-border UCITS authorisation under Art. 20 of the UCITS Directive, but shall be communicated to the host State supervisor only at the beginning of a management company's business activities in the relevant Member State (cf. Art. 18 para. 1 letter b)). Thus, CESR should not attempt to modify this allocation of responsibilities laid down at level 1 by means of subsidiary level 2 measures.

We hope that our suggestions will help CESR to adopt a conclusive and practicable approach to the operational framework for UCITS management companies and remain at your disposal for any further discussion of the consultation at hand.

Yours sincerely

BVI Bundesverband Investment und Asset Management e.V.

Signed:
Stefan Seip

Signed:
Dr. Magdalena Kuper