

Call for Evidence on mutual recognition with non-EE jurisdictions
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Introductory

We thank CESR for taking up the important issue of mutual recognition in relation to non-EU jurisdictions. This is not only important to again move forward the transatlantic dialogue in this matter, in which UBS AG has been participating as a member of the relevant trade associations, but also in relation to other major financial centers, such as Switzerland.

UBS AG is one of the leading financial firms worldwide and one of Europe's largest universal banks, offering services in the area of investment banking, wealth management and asset management. As a firm headquartered in Switzerland, which is not a Member State of the European Union, and thus not qualified for an EU-passport to offer investment services throughout Europe from its Swiss base, UBS AG has a keen interest in the topic of mutual recognition.

Questions & Answers

General.

Q1: Do you believe that other relevant topics should be added in the regulatory areas above? In the affirmative case, please explain the reasons why the specific topic deserve attention together with costs and benefits of mutual recognition associated to the area of interest

Answer:

- In addition to the topics of mutual recognition addressed in the questionnaire, one of the lessons learnt in the financial crisis is the deep integration of financial markets across the globe. This strengthens the need for increased levels of regulatory cooperation in the supervisory area. UBS's main regulators, the FINMA, the FSA and the FED already form a supervisory college of regulators under which information exchange is occurring and supervisory actions are coordinated. We believe that it is important that such international cooperation across the globe is taken into account when new regulation is introduced in the EEA. Thus, the role and position of large financial institutions headquartered outside of Europe but having significant operations within Europe should be taken into account appropriately.
- Apart from the supervisory angle, regulatory priorities have changed as a result of the financial crisis, and gave rise to similar regulatory initiatives in the US, in the EU and at national levels, including in Switzerland. In order to make those initiatives effective, those activities should be coordinated and a level playing

field should be achieved to avoid regulatory arbitrage, but also to avoid increasing risk by increasing regulatory entry barriers into each others' markets.

This concerns the areas of

- various initiatives to create new central counter parties, e.g. in the area of derivatives
- regulation of remuneration practices

Actual mutual recognition is addressed in the draft directive on alternative investment funds. This could be further extended in relation to UCITs compatible regimes as well as the cross-border merger of investment funds.

Q2): Focusing the above areas and topics, would you expect benefits of mutual recognition frameworks for your own business (e.g. in terms of cost savings and business opportunities). Please provide any evidence/data/market statistic to support your view and indicative prioritization of the major regulatory and market segments?

Answer:

- Within the EEA, MiFID has and should further contribute to allow full use of economies of scale to the extent to which the harmonized rules are effective and implemented by the Member States in a harmonized fashion (Level 3). As long as the latter is not fully the case, the potential advantages of mutual recognition can not fully be developed either, as complexity would remain due to differences in specific national regulations for the relevant products and services.
- Assuming Level 3 implementation will be successfully achieved, mutual recognition would have similarly positive effects as the MiFID harmonization if a clear set of rules for a Europe-wide equivalence test were introduced. This would allow to further use of economies of scale by our firm, which should increase liquidity in certain markets and products, result in lower costs and thus be beneficial to the investor. We believe such a regime would ultimately strengthen the European financial markets, to the benefits of the consumers of such financial services.
- Pre-requisite would be that the requirements of the equivalence test are not set at such a level that effectively new entry barriers are created. Those would have the opposite effect and thus the desired result of increasing the product offering, its quality whilst lowering costs for end users, could not be achieved.

Q3): What rules and regulations could cause the most severe distortion of competition in the field of cross-border activity with respect to a system of mutual

recognition? Are there other potential risks that could result from a system of mutual recognition between Europe and third-countries? Differentiate according to third countries, where necessary

Answer:

- Supervisory standards, capital and liquidity requirements as well as remuneration principles should be harmonized so as to avoid regulatory arbitrage, which would allow offering services into the EEA at lower cost for doing business. In all of those areas, Swiss regulations tend to be stricter and we thus do not see such potential for regulatory arbitrage if mutual recognition were granted between Switzerland and the EU.
- That also applies in the area of UCITs, where Swiss capital requirements for fund managers are usually stricter than for EU UCITs.

Q4): How could possible risks be mitigated

Answer:

- Seeking harmonization in those areas mentioned above through increased international cooperation between regulatory and supervisory bodies.

1. Trading venues

Our answers focus on 2: Intermediaries and 3: Products including collective investment schemes.

2. Intermediaries

Q11): Which third country's financial market is of interest to your businesses? What benefits/costs would you expect for your business from the market opening to specific third countries? (Please provide any evidence/data/market/ statistic to support your view)

Answer:

- Key markets in Europe are: Italy, Spain, France, Austria, UK, Germany and Be-Ne-Lux. Some of these jurisdictions already offer explicit exemptions from local licensing requirement to conduct cross-border business. While this is already a great advantage compared to jurisdictions where such an exemption regime does not hold, a general mutual recognition regime would be based on the home state conduct of business rules and could generate the advantages the introduction of MiFID had within the EU.
- It would allow for standardization of products and services, products and services documentation, standardization of compliance procedures and processes, etc.

Q12): What are currently the main regulatory obstacles that EU banks/investment firms face when providing financial services located in third countries (differentiate according to countries). Can these obstacles in the current regulatory environment be overcome (via cooperation arrangements with third country firms)?

Answer:

- We do not have any major restrictions for EU firms to do such business in Switzerland, and effectively EU firms are effectively offering from abroad into Switzerland

Q13): How important is the provision of cross border financial services provided to third countries (in terms of volume, generated profit) for your business? Please differentiate according to third countries and provide evidence/data if possible. How would you expect the development of this business after the implementation of a Mutual Recognition Agreement?

Answer:

- Cross border business is material for any global player. To build up and run different legal entities and infrastructures is extremely expensive. Thus, under a mutual recognition scheme we do not expect a material increase in business volumes per se but rather a significant decrease in operating costs as a firm could focus on a single operating platform and thus better leverage existing infrastructure (driving down marginal production costs). Thus, as outlined above, a mutual recognition regime could be beneficial to end users of financial services in the EEA.

Q14): What would you consider to be the effects, in terms of cost and benefits, on:

a) EU intermediaries, if non-EU brokers are allowed to do business with EU professional investors regarding listed securities of the country of the non-EU broker?

Answer:

- The effects should be basically the same in both cases: Competition and quality of services should increase, whereas cost for products and service offerings in the relevant areas should decrease, both for the benefit of the end users.
- Specifically in this case, the cost of cross-border transactions in the relevant securities should decrease. The offering for professional investors should increase; the intermediary chains should become shorter, to the extent that professional investors can deal directly with the foreign broker in those securities (where they could not do so under current requirements).

b) Non-EU intermediaries, if EU brokers are allowed to do business with non-EU professional investors regarding listed securities of the EU?

Answer:

- EU intermediaries would not have to establish subsidiaries in non-EU countries to get into the foreign market (passporting). They could potentially increase volumes and cost of cross-border transactions should decrease.
- Competition and quality of services would increase in the foreign jurisdiction.

c) *EU investors if non-EU brokers are allowed to do business with EU professional investors regarding listed securities of the country of the non-EU broker?*

Answer:

- More diversification
- Competition and quality of services would increase

Q15) Do you consider that a mutual recognition arrangement could reduce the fees in cross border investment services (due to increased cross border competition)? Would the reduction of cost make up a reduction of fees? Would the volume increase enough to match any differences?

Answer:

- Yes, reduction of costs and increased competition should result in a reduction of fees. However, some of the barriers identified by the Giovannini reports, such as in the fiscal area, would still remain.

3. Products including collective investment schemes

Q16) Do you consider the topic of collective investment schemes to be of primary relevance? Do you believe that other relevant topics should be considered and analysed first in the “products” regulatory area? Please provide reasons

Answer:

- We believe that not only collective investment schemes should be considered in such analysis, but also structured products as for their distribution different rules and regulations apply in different markets. This is also warranted as for professional investors, the product categories are often alternatives. Making the cross-border offering possible of one type only could result in unwarranted and artificial competitive distortion.

Q17) In what third countries do European asset management companies distribute shares in collective investment schemes? Please provide information on the (estimated) volume of distributed shares in collective investment schemes, distinguishing between different types of collective investment schemes (UCITS,

non-harmonized investment funds) as well as different types of investors (wholesale, retail).

Answer:

- Switzerland is one of the biggest financial services centers for wealth management. Accordingly, there is demand for services and products in that area also from European offerors. This concerns all type of funds, UCITs and alternative investment funds.
- As of 31 December 2008, below are the AuM figures in CHF mn for the EEA on a client domicile basis from the Global Distribution view. Fund assets are not reported under the country of fund domicile but rather at the investing client's domicile:

Total AuM:	143,556mn
Institutional:	74,557mn
Wholesale:	68,999mn
Actively Managed:	126,742mn
Passively Managed:	16,814mn

Q18) What are the most significant obstacles for the European asset management industry in respect to efficient cross-border marketing of collective investment schemes in third countries? What are the (estimated) costs caused by these obstacles? Please distinguish between countries.

Answer:

- As a CH-based firm we are not in the best position to answer this question. However, in terms of cross-border marketing the following obstacles are the most significant:
- Passporting
- Different local CIS regulations
- Restrictions to investigation and surveillance of CIS by foreign regulatory authorities
- (Obstacle if CIS are to be regulated by the home regulatory authority where the CIS is based, rather than by the foreign regulatory authority)
- Some jurisdictions prohibit a foreign regulatory authority from conducting an investigation or surveillance of a foreign CIS in its jurisdiction. E.g. Switzerland, France and Luxembourg, do not allow a foreign regulatory authority to conduct investigations or inspections neither alone nor in association with the home regulatory authority.
- Some jurisdictions, allow a foreign regulatory authority to conduct an investigation in its jurisdiction, if there's a reciprocal agreement in place only (e.g. Germany) or they permit a joint inspection where the foreign regulatory authority has a clearly identifiable interest only (e.g. UK). (->Sovereignty issues)

Examples from different countries:

- Belgium: Distribution Agreements that contain Public Distribution; Pricing Grids have to be disclosed to the Belgian Authorities (CBFA); Any marketing material about a Fund for an end-client (every registered fund) must be approved by the CBFA before it may be distributed; Prospectus must have an extra Addendum that is approved by the CBFA in E or in F/Dutch
- France: French Authorities may request Marketing Material for approval before a Fund can be registered; This is done more often in the recent past
- Italy: Italian Authorities request an additional Appendix to each Prospectus, containing further details for subscription/redemption of the Fund (e.g. costs for paying agent; generic information on distributor, etc.)

Q19) What kind of products (UCITS, non-harmonized investment funds) should be covered by a mutual recognition agreement between EU and third countries? In terms of non-harmonized investment funds, please describe what kind of funds should be included in respective considerations (regarding investment policy, degree of regulation/supervision, right of redemption). Please distinguish between countries

Answer:

- As the offering is to professional investors, the product range should be broad enough and not be limited to harmonized investment funds, i.e. include both UCITs as well as alternative instruments. This is particularly true in light of the proposal for a directive for alternative funds and private equity. Further, it should also extend to other products such as investment products (equities, bonds, structured products, derivatives, etc.) and commercial lending .

Q20) What decisive benefits and effective gains would a mutual recognition agreement between EU and third countries bring for the EU asset management industry? Please distinguish between countries

Answer:

- EU Regulators will be disburdened regarding the administration effort and costs originating from cross-border business with non-EU jurisdictions
- Mutual recognition increases the legal certainty
- Faster and more efficient evaluation of potential new distribution countries
- More (taxable) foreign assets would flow into the EU
- A mutual recognition agreement between EU and Switzerland would strengthen Europe's intercontinental position
- Faster and more efficient evaluation of potential new clients
- Faster and more efficient client attention and contract management
- Diversification would increase
- Competition and quality of services would increase

- Cooperation between EU and 3rd party country companies would be meliorated and more efficient; mutual asset management would be less complicated (e.g. outsourced fund management; structures of financial products; asset managers; etc.)
- Crossborder concern structures would be more transparent as non EU companies would not have to set up affiliates or subsidiaries in EU countries for passporting reasons

Q21) What kind of asset management companies would benefit from a mutual recognition agreement between EU and third countries (small and medium size companies, bigger companies)? What size if the share of those asset management companies in the European asset management market? Please distinguish between countries

Answer:

- All asset managers would benefit but smaller companies benefit more through a reduction in regulatory costs which tend to weigh more on the smaller players

Q22) Are there other potential risks that could result from a system of mutual recognition between EU and third countries? How could possible risks be mitigated? Please distinguish between countries

Answer:

- The main risk would be that instead of simplification a harmonized regulation and mutual recognition could lead to more complexity and restrictions and that based on such regulations it will become more difficult to distribute collective investment schemes or structured products to clients in other countries
- Arbitration of AML risks. Mitigation could be achieved through distinction between FATF/non-FATF member countries