



COMMITTEE OF EUROPEAN SECURITIES REGULATORS
THE CHAIRMAN

Commissioner Charlie
McCreevy
European Commission
Rue de la Loi 200
B-1049 Bruxelles,
Belgique

Date: 28 September 2009
Ref.: CESR/09-845

**RE: CESR's response to the European Commission's consultation on the UCITS
depository function**

Dear Mr McCreevy,

Please find enclosed CESR's response to the Commission's consultation on the UCITS depository function.

Since late 2008, CESR has been working on a number of issues related to UCITS depositories. At the outset, the focus was on assessing the impact of the Madoff fraud on the fund industry; this work was then widened to include consideration of the duties and responsibilities of UCITS depositories. In this context, CESR carried out a mapping exercise to establish how the various rules on depository obligations have been implemented in Member States. A summary of this mapping exercise is included as an annex in CESR's response.

Meanwhile, in February 2009 CESR was requested to advise the European Commission on the measures to be taken by a depository in order to fulfil its duties in the case of cross-border management situations (Articles 23 and 33 of the modified UCITS Directive). For that purpose, CESR created a technical group which is chaired by the French market authority (AMF). This group was also tasked by the CESR Members with establishing whether further clarity is needed on an EU-wide basis on the status, role and liability of UCITS depositories and, if so, to prepare a recommendation for CESR's Investment Management Expert Group with a view to advising the European Commission on the legislative proposals or modifications that would be required.

In the meantime, the Commission launched its public consultation on UCITS depositories. Since the scope and topics of this consultation are very similar to the ones on which the CESR technical group had worked with a view to making suggestions to the Commission, CESR considered that it should provide a response to the public consultation.

As a general response to the consultation as whole, CESR expresses support for greater clarity, legal certainty and harmonisation in the duties and responsibility of UCITS depositories. These entities play a key role in the UCITS framework, particularly in the promotion of investor protection. As such, the design and implementation of a robust and transparent legal framework is to be encouraged.

In its response, a key area on which CESR makes specific recommendations is on the definition of safekeeping. CESR's proposal is for a definition composed of two broad elements: overall control of assets and segregation. On the former, a key requirement would be that the assets could not be transferred by the manager/management company without prior knowledge or consent of the depository. On segregation, meanwhile, CESR sees merit in imposing explicit controls on re-hypothecation and clarifying that the sub-custodian should also be obliged to put in place proper



segregation arrangements. In this context, CESR also highlights the possibility of providing further clarification and harmonisation via level 2 measures and elaboration of CESR guidelines at level 3.

There is wide agreement within CESR that depositaries should have the possibility to delegate certain functions, including custody. Similarly, Members agree that the liability of the depositary is not affected by delegation of custody functions. However, the mapping exercise mentioned above has made clear that Member States take diverging approaches to the liability attaching to a depositary in case of loss of assets by the sub-custodian. CESR is of the view that this situation is not acceptable and that particular focus should be put on developing a harmonised approach. As a first step towards an improved legal framework, almost all CESR Members suggest that the priority should be to clarify and harmonise the duties and functions of UCITS depositaries.

Consequently, the key issue regarding liability of the depositary relates to the conditions under which a depositary may delegate its custody functions to a sub-custodian. CESR believes that these conditions should be clarified and strengthened by introducing due diligence requirements in relation to the selection, appointment and periodic review of the sub-custodian. CESR makes a number of suggestions on the criteria that should be satisfied before a UCITS can entrust the UCITS' assets to a third party. These include that the third party be subject to supervision by a public authority in its own jurisdiction; that the presence of the relevant assets be verified on a regular basis by an independent auditor; that the sub-custodian have an adequate and proportionate organisational structure; and that the depositary itself be required to keep adequate records and documentation of its delegation.

Finally, I would like to highlight that CESR has a number of concerns regarding the Commission's stated desire to apply certain elements of the Alternative Investment Fund Managers (AIFM) Directive to the UCITS sphere as regards depositaries. CESR Members do not feel that the AIFM provisions as currently drafted, and which are in any case subject to change, represent a sound basis for the requirements that should apply to UCITS depositaries. In contrast, CESR sees the proposals in its consultation response as a good starting point for an improved legislative framework for depositaries.

Should you have any questions on the content of our response, please do not hesitate to contact me or Carlo Comporti, Secretary General of CESR.

Yours sincerely,

A handwritten signature in blue ink, appearing to be 'Eddy Wymeersch', written in a cursive style.

Eddy Wymeersch