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Ihr Zeichen, Ihre Nachricht vom	Unser Zeichen, Sacharbeiter	Durchwahl	Datum
	BSBV 64/Dr. Priester/Sc	3132	24 October 2014

Re: ESMA Consultation regarding UCITS V; corrected version

Please regard this version as the final one. The one submitted earlier today contains one error.

Advice on the insolvency protection of UCITS assets when delegating safekeeping (Art. 22a(3)(e)[1] and 26b(e) UCITS V)

Q1: Do you agree that the steps to be taken by the third party are ultimately intended to ensure that the level of segregation foreseen under 22a(3)(d) of the UCITS Directive is recognised in the context of an insolvency proceeding involving the third party?

Yes.

Q2: Do you consider that the level of segregation foreseen under Art 22a(3)(d) of the UCITS Directive should protect UCITS assets from claims by creditors of an insolvent third party which had been delegated the safekeeping of the assets by the UCITS' depositary?

Yes. Such protection will however depend on the local insolvency laws, which will affect at least securities issued in such jurisdictions.

Q3: Are there other measures which could also help achieve this objective?

No.

Q4: Do you agree with the steps to be taken by the third party as identified above? If not, please explain the reasons.

Yes.

[1] Article 22a(3)(d) in the text of UCITS V published in the Official Journal.

Q5: Do you consider that there are any specific difficulties that may arise in verifying the applicable insolvency regime that makes the proposed rules difficult to be complied with? In particular, do you consider the requirement for the third party located in a jurisdiction outside the Union to obtain independent legal advice could give rise to specific issues?

Yes, if the legal advice obtained is subject to qualifications, i.e. that no clean legal opinion can be obtained.

Q6: Do you expect a significant increase in terms of costs that would be faced by the third party delegated entities located in jurisdictions outside the Union in order to obtain independent legal advice on the applicable insolvency regime? If yes, please provide any available data and/or estimation.

If the third party provides the legal advice, no cost will accrue; otherwise estimated EUR 200,000 will accrue upon implementation.

Q7: Would you suggest requiring the third party to take any further steps which are not foreseen in the draft advice?

No.

Q8: Should any specific consideration be given to the scenario where the third party further sub-delegates the safe-keeping of the UCITS' assets in accordance with Article 22a(3), last sub-paragraph of the UCITS Directive (as inserted by UCITS V)? Should the third party take any additional/different steps or measures in this case?

No.

Q9: Do you agree with the steps to be taken by the depositary as identified above? If not, please explain the reasons.

Yes. However, it is well understood that the depositary does not guarantee the insolvency-remoteness. In case of jurisdictions where an impact of third-party insolvency on the UCITS assets cannot be avoided, a mitigating action may be the disclosure of the risk to the investment company/management company, who shall provide for divestment of the UCITS in such jurisdictions after appropriate risk evaluation.

Q10: Do you expect any significant one-off and ongoing compliance costs for depositaries in order to take the steps identified above? If yes, please provide any available data and/or estimation.

Yes, estimated 300,000 p.a.

Q11: Would you suggest requiring the depositary to take any further steps which are not foreseen in the draft advice?

No.

Q12: Which measures do you think should be taken by the depositary and/or the investment company/management company in the best interest of the investors once the depositary has informed the investment company or the management company on behalf of the UCITS that the segregation of the UCITS' assets in the event of insolvency of the third party is no longer guaranteed in a given jurisdiction located outside the Union? Would the transfer of the relevant UCITS' assets held by the third party in a non-EU jurisdiction to another (EU or non-EU) jurisdiction which recognises the segregation of the UCITS' assets in the event of insolvency of the third party/depositary be a possible measure?

Normally the assets of an UCITS (securities) are held by a third party in the jurisdiction of the issuance of the securities. Therefore, transfer to a third party in another jurisdiction will not mitigate the risk, as such third party will again have to hold such assets through a fourth party in the jurisdiction of issuance of the securities. A mitigating action may be the disclosure of the risk to the investment company/management company, who shall provide for divestment of the UCITS in such jurisdictions after appropriate risk evaluation.

IV. Advice on the independence requirement (Art. 25(2) and 26(b)(h) UCITS V)

Q13: Do you agree with the identified links that may jeopardise the independence of the Relevant Entities? If not, please explain the reasons.

We disagree with the definition of cross-shareholdings and group inclusion as identified links that may jeopardize the independence of the Relevant Entities. Many financial groups have developed asset management as well as depositary bank businesses. This is common practice in the European Member States, where financial groups are active in both asset management and depositary activities, thus putting their know-how to the best use for their customers.

Not allowing management companies and depositaries to be included within a group of undertakings heavily breaks with very common historically grown forms of organization which have been proven and tested for over more than half a century throughout the EU.

We also disagree with the interpretation of the scope of the mandate given by the European Commission to ESMA concerning the conditions for fulfilling the independence requirement referred to in Article 25(2) of the UCITS V Directive.

As it is clearly stated in the new article 26b (h) of the UCITS V Directive, which defines the scope of the Commission's empowerment to adopt delegated acts, the conditions for the independence of the depositary must be founded upon a legal basis laid down in article 25 (2) which provides that the management company and the depositary have to "act honestly, fairly, independently and solely in the interest of the UCITS and the investors of the UCITS […]".

Therefore we believe that the links identified, common management/supervision as well as cross-shareholdings/group inclusion, go beyond the objectives and the legal basis set out in the level 1 of the UCITS V directive

Instead the proposed option 1 with regard to shareholding structures of management companies and depositaries creates an automatic and, in our view, false link between a widely common form of organisation and the independence of the 2 entities.

We do not believe that the featured links make it possible to supply a useful guidance on how independence-criteria can be fulfilled. The negative point about this is that many entities will be forced to completely change the very fabric of their organisational structure in order to comply with the technical standard and remove a threat which has not been exerted by them. The prohibition of cross-shareholding (1st option) will therefore lead to substantial additional costs for the whole economy, as it would imply the separation of a large number of entities in most Members States such as France, Germany, Luxembourg, Belgium, Denmark, Sweden and Austria.

Thus we urge to propose final recommendations that are proportionate. The principle of proportionality is intended to ensure that regulatory measures go no further than required to achieve a set objective, which in this case is to ensure that both the management company and the depositary have specific safeguards against conflicts of interest to allow for the independent performance of its activities.

We are convinced that proposing recommendations based on the identified links (as mentioned above) will not achieve the final objective of higher investor protection but will rather lead to disproportionate costs and have a substantive impact on the existing shareholding structures of management companies and depositaries in Europe.

We believe that these long established market practices should not be restricted by any level – 2 measures for the following reasons:

1 The absence of evidenced market failure: recent events affecting UCITS, such as the Madoff scandal were not connected to circumstances where the asset management companies and funds depositories belonged to the same financial group. However, it was recognized that a better clarification and harmonization of depositary duties and liability regime were necessary. These issues were adequately addressed in the AIFMD. The AIFM level1 and level 2 establish strict requirements with regard to oversight duties, asset segregation, due diligence, and the liability regime for depositories. In addition AIFMD Article 21 4 (a) provides that an AIFM shall not act as a depositary. AIFMD does not impose additional requirements.

2 The new UCITS regulatory framework will already provide investors with a greater level of protection:

- The strict liability regime of the depository in UCITS V goes even further than AIFMD as the depositary's liability can, in no circumstances, be contractually waived.
- Depositaries are regulated entities; they must comply with stringent eligibility criteria and are subject to ongoing supervision. They have to comply with strict obligations as regards transparency requirements and reporting obligations to supervisors.
- Article 5 of the current UCITS IV Directive, requires that "The competent authorities of the UCITS home Member State shall not authorize a UCITS if the directors of the depositary are not of sufficiently good repute or are not sufficiently experienced also in relation to the type of UCITS to be managed (…….) . Directors shall mean those persons who, under the law or the instruments of incorporation, represent the depositary, or who effectively determine the policy of the depositary."

- Depositories are required to have in place and implement strict and detailed internal procedures for the prevention of conflicts of interest. They are also subject to a regular internal control process for the adequacy of resources and competences as well as to the supervision of internal audit, external audit and regulators.
- In addition MIFID reporting obligations include; on an annual basis, specific reporting on the safeguard of assets performed by an independent audit firm.

Q14: Do you consider that any additional links should be taken into account such as, for instance, the existence of any contractual commitment or other relationship which would affect the independence of the Relevant Entities? If yes, please provide details.

No.

Q15: Do you consider that the cumulative presence of all or some of the identified links is necessary to jeopardise the independence of the Relevant Entities or the presence of any of these links is sufficient to determine a lack of independence?

We are opposed to the cross-shareholdings/group inclusion links as it cannot pre determine a lack of independence of the Relevant Entities.

Q16: Do you agree with the proposed option to ensure the separation of the management bodies/bodies in charge of the supervisory functions of the Relevant Entities?

Do you have any alternative options to suggest, taking into account those identified under paragraph 47?

We agree with the proposed option with regards to members of management bodies; however we do not deem it necessary to include employees and members of the supervisory board in the prohibition to act as supervisory board members of the other entity.

Q17: Do you consider that the cap of one third of members of the body in charge of the supervisory functions of one of the Relevant Entities to also be members of the management body, the body in charge of the supervisory functions or employees of the other Relevant Entity is appropriate? Would you suggest any alternative percentage? If yes, please provide the reasons why.

We do not see the benefit of such a low percentage for entities with a dual structure. In addition to the fact that there actually are two separate bodies, various stringent rules and that the governance structure of the relevant entities already make an abuse of these positions very hard.

Q18: Do you have knowledge of any restructuring in the composition of the management bodies/bodies in charge of the supervisory functions of any Relevant Entities that would be triggered by the identified option? If yes, please provide data and an estimation of the one-off and ongoing costs that would be incurred.

No.

Q19: Which of the two identified options do you prefer? Would you suggest any alternative option? If yes, please provide details.

Since we do not believe that any of the links is a conclusive indicator for a threat of the independence of the relevant entities, we had rather not chose any of the two options. Since the set time frame is too short for the development of a new model and only two alternatives are given we have to state the following:

For the reasons set out in our response to question 13, we find the first option unacceptable and potentially destabilizing for the banking industry in the EU.

Option 1 contains new requirements which go beyond Level 1 and prevent the management company and depositary to be group related companies. We believe that this long established and well working market practice should not be restricted by any Level 2 measures.

The principle of proportionality is intended to ensure that regulatory measures go no further than required to achieve a set objective, which is to ensure that both the management company and the depositary have specific safeguards against conflicts of interest to allow for the independent performance of its activities. The limitation of solutions within the group inevitably leads to a restriction of the design and operating freedom for the affected investment firms and depositary banks.

We tentatively support the second option, which aims at harmonizing governance and organizational arrangements.

Notwithstanding the relative preference for option 2, we consider to demand the existence of at least one third of independent members of the management body of the management company/investment company and the depositary or at least one third of the members of the body in charge of the supervisory function. We also believe that independent directors should be allowed to be employees of any of the other undertakings within the group [except for the second relevant entity] [see our answer to Q21].

We believe that in this regard option 2 needs an extensive revision.

Q20: Under the second option, do you consider that it would be appropriate to require that – whenever the Relevant Entities are part of the same group – at least one third of the members of the management body of the management company/investment company and depositary should be independent? Would you suggest any alternative percentage? If yes, please provide the reasons why.

We do not support the requirement of at least one third of the members of the management body of both entities should be independent. This would raise many practical issues, (in particular for small structures and structures with joint or multiple shareholdings). An additional operational hurdle would also be the regulatory limits imposed on the number of directorships held by directors.

Should independent directors be imposed, we suggest limiting the number to 1 and the application only to the management company/investment company and not to the depositary.

This arrangement would allow reaching the same objectives without unnecessary constraints.

Q21: Do you agree that the concept of independence should be understood as requiring that independent directors should not be member of the management body or the body in charge of the supervisory function nor employees of any of the undertakings within the group?

No we do not deem it proportionate.

Q22: Do you have knowledge of the impact that each of the two options identified would have in terms of restructuring the shareholding of any Relevant Entities or finding alternative service providers? If yes, please provide data and an estimation of the one-off and ongoing costs that would be incurred.

The prohibition of cross shareholding, as envisaged in option 1 ("the management company company/investment company shall not be included in the same group...") may, if retained, lead to 2 types of consequences, both significantly detrimental to the investors:

- European-based diversified financial groups with a depositary arm will be compelled to limit their operations in asset management, thus depriving the market of a substantial part of the range of products available for investment for the retail market. A significant amount of UCITS would be closed and their assets could be transferred to other investment vehicles offering less protection.

- European-based diversified financial groups with an asset management arm will exit the depositary sector. Depositary service offering in the UE will therefore be reduced, be limited to fewer players, and is likely to be offered by banks somewhat away from the asset industry constraints.

Option 1 would entail huge costs and a complete transformation of the existing models with a chance to put at risk and to weaken the overall sector. These costs would ultimately be borne by UCITS investors with no added benefits in terms of protection given the absence of evidenced market failure.

But these costs would go far beyond the costs of transfer since option 1 would, in our view contradict, without any compelling grounds, the freedom of enterprise in the European financial and lead to a far reaching market restructuration detrimental to:
1) The employment in the financing sector
2) The financing of the economy
3) The stability and safety of the whole UCITS model
4) The stability of the banking sector.

Option 1 would provide undue advantage to a low number of market participants who exercise depositary business on the basis of a single business concept and thereby would lead to a market concentration.

Annex III

Cost-benefit analysis

Q23: Do you agree with ESMA's approach to discard the second and third options described above?

We could not disagree more with ESMA's approach to discard the second option. For the reasons given, we see option 1 as a grave mistake and believe that option 2 could be an acceptable option however still would need extensive revision.

Yours sincerely,

Dr. Franz Rudorfer
Managing Director
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