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European Commission
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Brussel
Belgium

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Reply to the European Commission “Working Document of the Commission Services – Consultation Paper on the UCITS Depositary Function”

Assogestioni¹ welcomes the opportunity to comment on the European Commission “Working Document of the Commission Services – Consultation Paper on the UCITS Depositary Function”. We deem particularly important to consult intermediaries and other stakeholders on the definition of measures that, once adopted, will have significant consequences on the provision of the collective portfolio management service and on a adequate protection of investors’ interests.

Preliminary to our comments, we wish to express our appreciation for the aim of the Consultation Paper. In fact, we fully support an effective harmonisation of investor protection level across Member States; therefore, we agree with the need to adopt all the initiatives that the European Commission will consider necessary, through a legislation which rules depositary function in a sufficiently detailed manner, in order to face all the critical issues raised during the recent crisis.

I. DEPOSITARY’S DUTIES

A. Safe-keeping duties

Question 1) Do you agree that the safe-keeping (and administration) duties of depositaries should be clarified?

¹ Assogestioni is the Italian association of the investment fund and asset management industry and represents the interests of over 160 members who currently manage assets whose value exceeds 800 billion euro.



Question 2) Do you agree these duties should be clarified for each class of assets eligible to the UCITS portfolio

Question 3) Are there any other appropriate approaches?

Question 4) Do you agree to a common horizontal and functional approach of the custody duties on the listed financial instruments, to be applied to UCITS depositaries?

Question 5) Is there some specificity that may be applicable to the custody functions of a UCITS depositary that should be taken into account?

We agree with the need to clarify what safe-keeping means; however, we believe that safe-keeping should be identified with the custody activity, without differentiating this concept depending on the different type of assets that could be kept in custody. For the assets that cannot be kept in custody (for example, OTC contracts), we deem important that the European Commission defines the specific duties of the depositary.

Custody obligations should include the duty of the depositary to hold financial instruments, in which the fund is invested, in books/registers where those instruments are indicated, in such a way that guarantees the segregation between financial instruments pertaining to a fund/compartment from those pertaining to another fund/compartment; furthermore, the custody activity should ensure the segregation of the assets of each fund from those of the depositary.

Therefore, we deem preferable to identify what safe-keeping means and implies in terms of depositary duties in a general manner, as described above; differentiating safe-keeping duties having regard to the type of assets that are kept in custody could be not consistent with the specific operational procedures that are already in place, in practice, in Member States and could generate unjustified burden for depositaries and, indirectly, for asset managers.

B. Supervisory duties

Question 6) Do you agree that the existing supervisory duties of the UCITS depositary should be clarified?

Question 7) If so, what clarification do you suggest?

Question 8) To what extent does the list of supervisory duties need to be extended?

The UCITS Directive rules the depositary's supervisory duties and already defines the content of such duties, harmonising the main principles to which they should aim. However, some of those duties should be better clarified in details. In particular, the



UCITS Directive provides in Article 22, paragraph 2, that *“the depositary shall: [...] (b) ensure that the value of the units is calculated in accordance with the applicable national law and the fund rules”*, without specifying how such result should be reached. To this reference, we deem coherent with the nature of the activity of supervisory that the depositary should simply control the calculation done by the management company, without recalculating the NAV. As a consequence, the European Commission should adopt a specific provision in order to clarify the content of the abovementioned article 22.

Question 9) Do you agree that the 'only one depositary' requirement should be clarified?

In order to guarantee an adequate investor protection, we deem important that the UCITS assets can be entrusted to only one depositary, as suggested by the European Commission. Therefore, we support the principle of “only one depositary”, which is already effective in Italy.

II. RESPONSIBILITY REGIME

A. Liability regime in case of improper performance

1. Identification of the associated risks

Question 10) Do you think that the risks related to improper performance have been correctly identified?

We believe that the European Commission has correctly defined the risks associated to the improper performance of depositary's duties and the main critical issues concerning the cases described.

Question 11) Do you foresee other situations where a risk associated with improper performance of the depositary duties might materialise?

We would like to bring to the European Commission attention a further issue which, in our opinion, is very important for an effective and correct functioning of the asset management structure in case of market crisis. The Consultation Paper takes into account the risks linked to the sub-depositary's bankruptcy, but analyses the effect of the depositary's default only with respect to a possible amendment to the scope of the Investor Compensation Scheme Directive (Directive 1997/9/EC).

The recent crisis raised the attention to the fact that important institutions faced major difficulties, which could have caused their default; in this case, a full segregation of UCITS assets would have not been sufficient to protect the asset



management industry and investors, because it would have not been ensured a quick and effective restitution of the UCITS assets. Such event would have frozen the UCITS liquidity and the UCITS ability to continue to operate, with the consequence to jeopardise the asset management industry.

Therefore, we deem extremely important that the European Commission examines the effects of such risk in order to define, in addition to the suggested amendment of the Directive 1997/9/EC, any further measure necessary to guarantee the ability of the UCITS to continue to perform its activity where such event occurs.

Question 12) Do you agree that safeguards against the risk associated with the improper performance of depositary duties, such as requiring that UCITS assets be segregated from the depositary's and sub-custodian's assets, should be introduced?

We share the European Commission position concerning the need to introduce a segregation obligation through all the value chain, both at level of depositary and sub-depositary. With this respect, we also deem necessary that the segregation principle applies between: (i) the assets of a UCITS and the ones of the depositary and sub-depositary; (ii) the assets of a UCITS and the ones of another UCITS; (iii) the assets of a UCITS and the assets which the depositary keeps in custody in relation to other investment services or activities performed.

This should become an essential principle of an harmonised discipline of the duties of the depositary and of the sub-depositary, given that it would increase the level of protection ensured by European legislation to face events, such as the depositary or sub-depositary default, which, otherwise, could compromise, where relevant, the assets restitution to the UCITS.

2. Liability regime: Unconditional performance vs. obligation of means

Question 13) Do you agree there should be a general clarification of the liability regime applicable to the UCITS depositary in cases of improper performance of custody duties?

Question 14) What adjustments to the liability regime associated to the custody duties of the UCITS depositary would be appropriate and under what conditions?

We deem that the alternative between unconditional performance vs. obligation of means should necessarily be referred to safe-keeping duties only, given that supervisory duties are duty of control and, as such, should certainly be qualified as obligation of means. We believe that the concepts of “unconditional performance” and of “obligation of means” are clearly understood in most Member States; therefore, the qualification of the depositary's safe-keeping duties in terms of



unconditional performance or of obligation of means should be considered as the first step for an effective harmonisation in this respect. Therefore, we strongly support the introduction of an harmonised European legislation, in order to avoid, across Member States, an unlevelled protection of investors.

In our opinion, due to the fact that, as we said, safe-keeping duties should be identified, where possible, with the custody activity, those duties should be qualified as unconditional performance (even when the assets can not be kept in custody). As a consequence, the improper performance of the depositary's duties should imply, where applicable, the right of the UCITS to an immediate restitution of its assets. The same approach should be adopted even when the depositary entrusts to a sub-depositary the assets of the UCITS and the sub-depositary does not perform its obligation of safe-keeping; in this case, article 22, paragraph 2, of the UCITS Directive should apply: *"A depositary's liability as referred to in Article 24 should not be affected by the fact that it has entrusted to a third party all or some of the assets in its safe-keeping"*.

Furthermore, we support the European Commission position on the inversion of the burden of proof because it is consistent with the depositary's function and, at the same time, does not introduce a "strict liability"; compared to the actual liability regime of the depositary, the proposed approach will exempt the UCITS from the burden of proving – in case of loss of its assets under custody – the improper performance of the depositary and, at the same time, gives the latter the chance to demonstrate that it could not have avoided the loss which has occurred.

B. Liability regime of depositaries in cases of delegation

Question 15) Do you agree that the conditions upon which the UCITS depositary shall be able to delegate its duties to a third party should be clarified?

Question 16) Under which conditions should the depositary be allowed to delegate the performance of its duties to a third party?

Question 17) Do you agree that the depositary should be subject to additional on-going due diligence requirements when delegating the performance of its duties to a third party?

We deem important that the delegation of depositary's functions to a third party is ruled at a European level, both in terms of conditions that should be fulfilled in order to delegate and in terms of requirements with which the third party should comply in order to be delegated.

In particular, we share the European Commission's proposals on this topic, except for the suggestion to limit the type of functions/activities that the depositary can delegate. The depositary should be allowed to delegate at least safe-keeping,



without any limits, provided that the choice of the sub-depositary is made after an accurate due diligence. This approach guarantees that the UCITS is not influenced in its investment policy by the activity that can be delegated to the sub-depositary. In any case, the depositary's liability regime shall remain that defined in Article 22, paragraph 2, of the UCITS Directive.

Furthermore, we share the need to impose, on the depositary, ongoing due diligence obligations in cases of delegation of functions to a third party; such requirement is consistent with the aforementioned article, which does not state any limitation of the depositary's responsibility.

C. Default (bankruptcy)

Question 18) Do you share the Commission services approach to reviewing the ICSD, to allow UCITS to benefit from a compensation scheme where the depositary defaults?

Question 19) Do you agree that UCITS holders should also benefit from compensation if their custodian defaults and these assets are lost?

We share the European Commission's proposal to amend the Investor Compensation Scheme Directive (1997/9/EC Directive), in order to allow the UCITS to benefit of the compensation scheme in case of depositary's default. However, we would like to underline that the European Commission should take in due consideration the characteristics of the risks associated with the collective asset management activity, given that the latter are partially different from those linked to the provision of investment services, which are already included in the scope of the aforementioned directive.

III. ORGANISATIONAL REQUIREMENTS

Question 20) Do you agree that the general organisation requirements that are applicable to a UCITS depositary should be clarified?

Question 21) If so, to what extent?

Question 22) Do you agree that requirements on conflicts of interest applicable to UCITS depositaries should be clarified?

Question 23) If so, to what extent?

Considering the complexity and the nature of services and functions that the depositary should perform, we deem appropriate that organisational requirements



and conflict of interests rules applicable to the depositary should be fully harmonised. In this respect, we believe that the legislation applicable to credit institutions, which is already harmonised, guarantees, at the same time, the maximum level of protection for both UCITS and participants.

IV. ELIGIBLE DEPOSITARY INSTITUTIONS

A. Type of eligible institutions

Question 24) Do you agree that there is a need for clarifying the type of institutions that should be eligible to act as UCITS depositaries?

Question 25) Do you agree that only institutions subject to the CDR should be eligible to act as UCITS depositaries?

Question 26) If not, which types of institutions should be eligible to act as UCITS depositaries, and why?

The level of protection that the depositary's function ensures to UCITS and participants is strictly linked to the type of eligible institution; therefore, this aspect should be clarified and harmonised. We deem appropriate, as we said, that banks should be the only institutions entitled to act as depositaries, considering the strict supervisory to which they are subject.

V. SUPERVISION ISSUES

A. Supervision by auditors

Question 27) Do you agree that additional auditing requirements should be imposed, such as an annual certification of the depositary's accounts by independent auditors?

We deem appropriate that the depositary's auditor expressly certifies, within its ordinary audit activity, that the UCITS assets kept in custody by the depositary are duly segregated, on individual UCITS accounts. Such certification should be mentioned in the accounting documents of the UCITS.

B. Supervision by national regulators

Question 28) Do you agree that UCITS depositaries should be subject to a specific 'depositary' approval by national regulators?



Question 29) Do you believe that there is need to promote further harmonisation of the supervision and cooperation by European regulators of depositary activities? What are your views on the creation of an EU passport for UCITS depositaries?

We share the European Commission's proposal to require a prior approval by the competent authority for the provision of the depositary's function; in fact, the proposal prevents entities not able to perform such function from having access to it, significantly increasing the level of protection of UCITS and participants.

Finally, we deem appropriate that the introduction of a depositary's passport should now be taken into account, in order to increase the flexibility in structuring the collective portfolio management activity; the passport, however, should be introduced together with the measures necessary to guarantee the correct performance of the function and avoid any reduction of the level of protection ensured at present time.

VI. OTHER INVESTORS PROTECTION ISSUES

A. Calculation of the net asset value of the UCITS shares and units by an independent valuator

Question 30) As far as the UCITS portfolio and UCITS units or shares are concerned, do you agree that their value should be assessed by an independent valuator?

Question 31) If so, what should be the applicable conditions for an entity to be eligible to act as an UCITS Valuator?

As regards the valuation of the UCITS portfolio and the NAV calculation, we believe that the main issue, to this respect, is the independence of the function in charge to perform those activities. Therefore, we deem appropriate – in order to increase organisational flexibility– to allow that the NAV calculation could be done by an independent function of the management company; such solution implies also that the management company should be allowed to outsource such activity to a third party.

At the same time, however, the proposal to appoint an independent valuator can be agreed only if it is a further option to the two described above and not the only one allowed.

As a consequence, it should be clearly stated that if the NAV calculation is done by:

- (i) an independent function of the management company, the management company is responsible for such calculation;



- (ii) a third party delegated by the management company, the management company is responsible for such calculation, according to the general principles of delegation;
- (iii) an independent valuator, the independent valuator is responsible for such calculation, given that it is *ex lege* in charge of providing this activity. For example, the depositary could be appointed as independent valuator, given that it is an independent entity from, both, UCITS and management company, according to the UCITS Directive relevant provisions.

We remain at your disposal for any further information or clarification.

Best regards,

The Director General