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Dear Sirs

Response to UCITS Consultation on product Rules, Liquidity Management, Depositary, Money market Funds, Long-term investments

NatWest TDS provides depositary services to over 850 UCITS funds with a total value of around 280 billion euros.

We are pleased to provide our thoughts on the European Commission's consultation and in particular welcome the fact that the Commission is asking for comments on the potential for a Depositary Passport. We are in favour of the passport as it remains the only area in the UCITS domain that has not been harmonised (as passports for the product and manager have been). Such a development would provide for increased competition and would have the added benefits of economies of scale for depositaries. There is no reason, once some areas of regulation are harmonised, why a passport should not be available at the earliest available opportunity.

Our responses to the points in the boxes as well as some questions are set out below.

Chapter 2 Eligible Assets

At present asset eligibility rules for UCITS are quite detailed, and interpretations are encapsulated in both the Eligible Assets Directive and the associated guidance issued by CESR. We do not feel it necessary to limit the scope within the Directive, it should be for ESMA to issue revised guidance on eligibility.

As regards the eligibility of certain types of derivative, we again consider ESMA are best placed to provide guidance and clarity of what should be permitted. Our opinion however is that a great part of the eligibility test should focus on liquidity. This would mean there may be less emphasis on whether a derivative is linked to a commodity index.

Chapter 3 Efficient Portfolio Management

In this area ESMA have issued Guidance (Guidelines on ETFs and other UCITS issues). In consideration of this and the current consultation it should be borne in mind that the EAD definition of EPM is drawn wider than securities lending and repos / reverse repos, and include the use of derivatives for hedging purposes. Once again the most appropriate route for clarifying aspects of EPM is via ESMA and we note that in the recent ESMA Guidelines advice is given on costs and revenues for EPM techniques, as well as the quality, valuation and diversification of collateral required .

Chapter 4 OTC Derivatives

Whilst there will undoubtedly be merit in clarification of risk measurement techniques covering counterparty risk and frequency of calculation we do not feel it necessary to amend the Directive in this regard. Such clarification could for example be provided as an update to 'CESR's Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS'.

Further, most issues on OTC derivatives will depend on the application of both the EMIR regulation and the revision of MIFID/MIFIR that will profoundly impact derivative markets. We feel therefore any further regulation within UCITS in this area should not be effected until EMIR and revisions to MIFID/MIFIR are in place.

Chapter 5 – Extraordinary Liquidity Management Tools (Box 4)

Q1: What type of internal policies does a UCITS use in order to face liquidity constraints? If you are an asset manager, please provide also information specific to your business.

Current tools include suspension or deferral of redemptions however managers do have a requirement to ensure they manage their portfolio in as prudent a manner to avoid liquidity bottlenecks other than in the most exceptional of circumstances.

Q2: Do you see a need to further develop a common framework, as part of the UCITS Directive, for dealing with liquidity bottlenecks in exceptional cases?

A common framework would be desirable, however we do not feel there is a requirement for it to be in the Directive. Indeed, any new framework should be both practical and allow for flexibility in terms of the tools available and take account of varied circumstances which can create liquidity bottlenecks, and take full account of the guidelines issued by other global organisations. In this regard note should be taken of the recent guidelines issued by IOSCO on suspension of redemptions and their consultation on 'Principles of Liquidity Risk Management for Collective Investment Schemes'.

Q3: What would be the criteria needed to define the "exceptional case" referred to in Article 84(2)? Should the decision be based on quantitative and/or qualitative criteria? Should the occurrence of "exceptional cases" be left to the manager's self-assessment and/or should this be assessed by the competent authorities? Please give an indicative list of criteria.

We do not consider there is a need for new rules to define exceptional circumstances and such assessment should be left to the manager in conjunction with the depositary. The current regulatory framework in the UK allows for this approach.

Q4: Regarding the temporary suspension of redemptions, should time limits be introduced that would require the fund to be liquidated once they are breached? If yes, what would such limits be? Please evaluate benefits and costs for all stakeholders involved.

We do not consider time limits should be imposed here. Decisions should be taken in the best interests of unitholders. Once again the UK framework provides for regular review of any suspension and a requirement to keep investors informed of the status. We recommend this approach.

Q5: Regarding deferred redemption, would quantitative thresholds and time limits better ensure fairness between different investors? How would such a mechanism work and what would be the appropriate limits? Please evaluate benefits and costs for all the stakeholders involved.

One option would be to align the deferred redemption rules with the dealing frequency of the fund to take account of those funds which do not value on a daily basis.

Q6: What is the current market practice when using side pockets? What options might be considered for side pockets in the UCITS Directive? What measures should be developed to ensure that all investors' interests are protected? Please evaluate benefits and costs for all the stakeholders involved.

Side pockets not used in the UK. These could potentially be considered as a tool, giving unitholders access to the liquid part of the fund, however the complexities need to be carefully considered such as the conversion of assets into a separate vehicle and ensuring an appropriate spread of risk is maintained.

Q7: Do you see a need for liquidity safeguards in ETF secondary markets? Should the ETF provider be directly involved in providing liquidity to secondary market investors? What would be the consequences for all the stakeholders involved? Do you see any other alternative?

This issue is addressed in 'ESMA's guidelines on ETFs and other UCITS issues' and we agree that investors should have the ability to redeem with the UCITS / manager in the circumstances envisaged.

Q8: Do you see a need for common rules (including time limits) for execution of redemption orders in normal circumstances, i.e. in other than exceptional cases? If so, what would such rules be?

In the UK there are time limits prescribed in regulations. Redemption orders must be settled within 4 days of receipt of the required documentation from unitholders and we see no reason for changes in this area.

Chapter 6 – Depositary Passport (Box 5)

Q1: What advantages and drawbacks would a depositary passport create, in your view, from the perspective of: the depositary (turnover, jobs, organisation, operational complexities, economies of scale ...), the fund (costs, cross border activity, enforcement of its rights ...), the competent authorities (supervisory effectiveness and complexity ...), and the investor (level of investor protection)?

As regards advantages and drawbacks, we would expect the depositary passport to provide the same benefits of consumer choice and increased competition as is provided by the management company passport. Whilst there would be operational complexities to address we do not see these as, in principle, any different to the issues that faced the management companies in operation of their passport.

Q2. If you are a fund manager or a depositary, do you encounter problems stemming from the regulatory requirement that the depositary and the fund need to be located in the same Member State? If you are a competent authority, would you encounter problems linked to the dispersion of supervisory functions and responsibilities? If yes, please give details and describe the costs (financial and non-financial) associated with these burdens as well as possible issues that a separation of fund and depositary might create in terms of regulatory oversight and supervisory cooperation.

Yes, we encounter problems by the current restrictions on depositary location. If a firm who the depositary acts for in one jurisdiction wishes to launch an operation in another jurisdiction, it will be operationally more efficient to be able to do this seamlessly using the same depositary connection that already exists.

Q3. In case a depositary passport were to be introduced, what areas do you think might require further harmonisation (e.g. calculation of NAV, definition of a depositary's tasks and permitted activities, conduct of business rules, supervision, harmonisation or approximation of capital requirements for depositaries...)?

Whilst UCITS V will provide a significant degree of harmonisation of depositary duties there would need to be further study of matters that should be subject to increased harmonisation to enable the passport to operate effectively. We would encourage early ESMA work on that.

We observe however, that one of the examples given in the consultation is for harmonisation of the calculation of the NAV; depositaries do not calculate the NAV so the only element of harmonisation in this regard should be related to a depositary's duty of oversight.

Q4. Should the depositary be subject to a fully-fledged authorisation regime specific to depositaries or is reliance on other EU regulatory frameworks (e.g., credit institutions or investment firms) sufficient in case a passport for depositary functions were to be introduced?

Depositary authorisation should be provided for in the UCITS Directive but this should provide for the process of authorisation to be conducted as per individual practices of competent authorities. In this way for example the UK authorisation regime could remain but simply be recognised by the Directive.

Q5. Are there specific issues to address for the supervision of a UCITS where the depositary is not located in the same jurisdiction?

We do not consider there are any specific issues to address over and above those of a similar nature encountered on the onset of the management company passport.

Chapter 7 – Money Market Funds

Our comment relates to the operation of CNAV funds in light of the points raised in section 7.1 (Valuation and Capital) of the Consultation. We are not aware of any fundamental problems regarding the existence of such funds in the UK and see no need to adjust the Directive's treatment of them.

Chapter 8 - Long - Term Investments

We question whether investment of the type envisaged by the Commission in the Consultation are appropriate for investment by a UCITS fund. We would however recommend that a separate

regime be developed for retail investment in funds investing in such long term assets, where is no assumption of liquidity – an essential aspect of UCITS management.

Chapter 9 – UCITS IV improvement – (Box11)

Q1: Do you think that the identified areas (points 1 to 4) require further consideration and that options should be developed for amending the respective provisions? Please provide an answer on each separate topic with the possible costs / benefits of changes for each, considering the impact for all stakeholders involved.

Master / Feeder structures

We have no comment to make specifically on the requirements for a feeder that converts into a non feeder UCITS.

However, in relation to Master / Feeders, the main issue to address is the fact that in allowing for feeder funds in UCITS IV, an essential amendment to Article 50 of the Directive was not made. Article 50 includes a prohibition on a UCITS investing in other collective investment schemes, unless that scheme restricts its investment in other schemes to 10% of NAV. Consequently no fund can make use of the advantages afforded by investment into a master / feeder structure, as any feeder must invest at least 85% of its value in a master, therefore making the feeder ineligible for investment by another fund. We understand this to be of considerable concern to the funds industry and will severely restrict the growth of master / feeder structures. We therefore recommend a feeder fund is exempted from the 10% rule.

Fund mergers

In relation to notifications, our concern relates to the requirement for fund managers to notify all holders of a continuing fund within a merger in writing, of the prospective merger. This is without recourse to any test of materiality. In many cases a continuing fund in a merger could have a very large number of retail investors and the impact to them, in terms of value or investor protection, is likely to be minimal. The cost however to the fund managers could be considerable and we recommend the requirement should be amended to allow operators to apply a materiality test to establish what notifications are necessary.

Q2: Regarding point 5, do you consider that further alignment is needed in order to improve consistency of rules in the European asset management sector? If yes, which areas in the UCITS framework should be further harmonised so as to improve consistency between the AIFM Directive and the UCITS Directive? Please give details and the possible attached benefits and costs.

In terms of depositary requirements, alignment with the AIFMD is anticipated based on the recent proposals by the Commission (UCITS V). It is important to note at this stage that our view is that whilst it is important that the level of care and oversight for alternative funds should not be higher than that for UCITS, any alignment as regards depositaries does not 'raise the bar' further as regards liability and oversight duties.

Yours faithfully,

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