

THE ASSOCIATION OF GLOBAL CUSTODIANS

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November 22, 2004

DG Competition
European Commission
B-1049
Brussels
BELGIUM

Dear Sirs/Madams:

This letter is submitted on behalf of the Association of Global Custodians ("Association") in response to the invitation of the European Commission (the "Commission") to comment on the report entitled, "Overview of EU25 securities trading, clearing, central counterparties, and securities settlement" (the "Final Report"), which was prepared for the Commission by London Economics. The Association is an informal group of nine banks, headquartered in North America, with extensive European branches and affiliates that provide securities safekeeping services and related asset-servicing functions to cross-border institutional investors, including pension funds and investment companies.¹

We think it is clear that the centralized safekeeping, settlement and transfer operations and activities of Central Securities Depositories and International Central Securities Depositories (collectively, "CSDs") comprise a fundamentally distinct line of business, particularly given the coupling of those activities with CSD's unique market-wide self-regulatory and risk-management responsibilities. That mix of CSD activities differs in a variety of material ways from custodian banks' provision of securities services to bank customers as part of a cluster of commercial banking activities.

¹

The Association members are listed on the letterhead above.

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operations. All custodian banks provide banking services in a commercially competitive environment in terms of price, range of services and flexibility.

In contrast to the individualized, often customer-specific, services delivered competitively by custodian banks, CSDs occupy an exclusive, central position in their respective markets, providing "one-size-fits-all" recordkeeping and related settlement and ownership transfer services to the full community of commercial intermediaries, including custodians. As the Final Report notes, market participants generally are obligated to use a particular jurisdiction's CSD (albeit indirectly in many cases). That requirement makes each CSD an "essential facility" and facilitates each CSD's mutualization of risk across the community of participants it serves (something custodian customers would never authorize at the custodian service level). In these various ways, CSDs, like their securities exchange counterparts, function as cooperative-style service utilities.

CSD risk-management, settlement and transfer activity thus serves the full community of intermediaries and issuers; and given their utility-style role, CSDs' activities and centralized safekeeping operations necessarily pose particular systemic significance and public policy considerations. In comparison, safekeeping activity at a custodian is one of several customer-specific banking services that enables individual customers to access markets and credit facilities economically, without, among other things, having to run a back office or meet market or CSD membership requirements. Custodian safekeeping activities for institutional investors are thus fundamentally different in function, purpose and character from the centralized risk-management and settlement-and-transfer activities of CSDs.

In the Association's view, the various differences between CSDs and custodian banks confirm their materially different functions and market roles. We believe these differences should be fully reflected in EU-level regulatory principles and policies, including policies concerned with matters of competition.

II. Conclusion.

The Association appreciates the Commission's invitation to comment and applauds its clear interest in factual precision. The development of increasingly safe and efficient cross-border clearing and settlement facilities and operations will be fundamental to sound EU securities markets, and continued thoughtful leadership and oversight by the Commission will be important to effective evolution. We believe that

I. Comments on Points of Fact and Underlying Assumptions in the Final Report and the Commission's Accompanying Press Release.

The Final Report, on page 6, sets out some of the differences between custodian banks as intermediaries, as compared to CSDs as infrastructure facilities, but then states that these "differing types of organizations provide similar clearing and settlement services...."² The Final Report then notes, on page 7, the development efforts being undertaken at the EU level by the ESCB-CESR working group to set "common standards" in the "clearing and settlement" area.³ These references and the underlying assumptions are not described or explained.

Similarly, the Commission's Press Release announcing issuance of the Final Report refers – again without explanation or description – to "international central securities depositories and banks at secondary level" as "infrastructures." In the absence of explanation, we assume that this reference is based on the statements and implications in the Final Report.

The foregoing references in the Final Report and Press Release suggest a general comparability between CSD operations and bank custodian activities that we think is overstated, and they create the impression that the Commission has adopted a broad view concerning the scope of infrastructure. As set out in brief below, the Association believes that CSDs and custodians have very differing core competencies and occupy differing segments of the securities services markets and, in so doing, perform different functions for different constituents. We would encourage the Commission to keep these differences closely in view as it develops policy in this area.

Custodians provide their institutional banking customers, including pension funds and mutual funds, with safekeeping, asset servicing, and related facilitative services as part of an array of flexibly-tailored, traditional banking services. *Global custodians* provide these services to customers that invest in multiple markets around the world and require the coordination and global custody management capabilities of a global custodian. *Local sub-custodians* serve as the point of connection for the global custodian and its institutional investors to the local market settlement facilities and

² Final Report at p.6.

³ Final Report at p.7.

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Careful and accurate use of terminology and effective recognition of functional distinctions are essential to refined policy decisions.

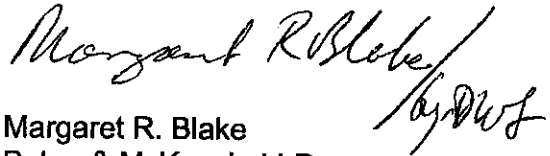
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On behalf of the Association, we express appreciation for the opportunity to comment on the Final Report. Questions can be directed to the undersigned.

Sincerely yours,



Dan W. Schneider
Baker & McKenzie LLP
Counsel to the Association



Margaret R. Blake
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Counsel to the Association