

ACSDA General Assembly
Issues for Depositories Managing Risk in the Post-Crisis Environment

J.P. Morgan on behalf of the Association of Global Custodians

Depository Information Gathering Process and the 17f-5 package 2009 - 2010

- The Tenth year of the consolidated AGC effort
 - 123 Depository Submissions received as of Mid February
- The Process has NOT changed significantly – because the legislation has not changed
 - Mutual Funds were not the problem
- The client reaction has changed
 - Not at all a perfunctory process this year
 - **Many questions about insolvency of counterparties and or systems**

So, What has Changed?

Introduction of a New Risk Classification - and Global reaction to it

The change of address of one individual has had more immediate impact on the custody business than any other aspect of the crisis:



"Madoff Risk"

So, What *has* Changed?

Europe:

The EU directive on Alternative Investment Fund Managers (AIFM),

An effort to create a regulatory and supervisory framework for AIFMs; which proposes to place the depository bank directly in the chain of liability for insolvent agents. Among other things, the proposal calls for a strict liability standard of care, which is a significant departure from the current standard under UCITS, and reverses the burden of proof in cases where assets are "lost". There is a strong possibility that new rules will result, which will shift at least some liability for the insolvency of subcustodians or the actions of criminals onto depository institutions.

The EU consultation on the Undertakings for Collective Investment in Transferable Securities (UCITS) depository function,

Which proposes that there should be additional requirements for depositories/custodians where assets are entrusted for safekeeping through a network of subcustodians. As with the AIFM Directive above, there is similar concern that a strict liability standard and liability to return assets immediately, notwithstanding a subcustodian insolvency, could be applied to all UCITS funds.

So, What *has* Changed?

United States:

SEC Amended Rule 206 Custody by Investment Advisors,

Registered Investment Advisors deemed to have custody as defined in the rule must observe 3 main requirements :

- Have quarterly statements sent directly to their clients from the Qualified Custodian
- Be subject to a surprise exam from a public accountant (annual Custody account statement)
- Obtain a SAS70 or equivalent report when the Qualified Custodian is related

Thank You!

For more information:

www.TheAGC.com

The **Association of Global Custodians'** members are:

- The Bank of New York Mellon Corporation
- Brown Brothers Harriman & Co.
- Citibank, N.A.
- HSBC Securities Services
- JPMorgan Chase Bank, N.A.
- Northern Trust
- RBC Dexia Investor Services
- Standard Chartered Bank
- State Street Bank and Trust Company

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