

# Clearstream

## AIFMD & UCITS V

### Service information

#### Key benefits

##### Reduced risk

- Highly secure custody for all international bonds, German and Luxembourg securities where Clearstream is the issuing CSD
- Secure safekeeping for securities held by Clearstream's over 25 direct CSD links
- Stringent selection of sub-custodians for Clearstream's indirect links which is subject to regulatory oversight
- As a market infrastructure provider, Clearstream is strictly regulated regarding the restitution of securities

##### Transparency

- Complete information about where assets are held under custody by Clearstream
- Regulatory compliant asset segregation "one level down" from the depositary bank
- Extensive reporting on network of over 1,000 transfer agents (TAs)

##### Efficiency gains

- Significantly reduced need for bilateral requests to TAs
- Support for agent bank assessments



The Alternative Investment Fund Manager Directive (AIFMD) and the fifth Undertakings for Collective Investment in Transferable Securities (UCITS V) directive are reshaping the operational landscape of the European investment funds market. The joint objective of these two directives is to implement a clear and consistent framework for the regulation and supervision of both European fund classes and to ensure greater investor protection.

Market participants, in particular those appointed as depositary banks, are facing significant operational and legal challenges which may affect their current operating model, including their use of market infrastructure providers. Clearstream has developed innovative solutions to help market participants respond to these challenges.

##### Impact on depositary banks

Under AIFMD, all AIFMs are obliged to appoint a depositary bank for each AIF and the safekeeping of assets<sup>1</sup> of the AIF. Depositary banks will mainly be impacted by strict liability and oversight provisions. For example, the depositary bank will be held liable for the loss<sup>2</sup> of any assets they directly hold in custody on behalf of the AIF and those they hold in sub-custody accounts with a third party agent they have appointed.

The AIFMD provisions result in three key responsibilities for depositary banks:

##### - Safekeeping of assets

Depositary banks become responsible for the restitution of financial instruments in the event of loss

##### - Due diligence

The depositary bank needs to provide a general oversight of the fund's investment activities to ensure compliance with governing documents and to keep custody risk in a market or a sub-agent under control

##### - Cash monitoring

The monitoring of all cash movements between the AIFM, its funds and all of its counterparties becomes an essential requirement for depositary banks.

<sup>1</sup> Specifically financial instruments that can be held in custody as defined in the AIFM Directive 2011/61/EU [Article 21 (8)] and Article 88 and 89 of the Level 2 AIFM Regulation.

<sup>2</sup> Provided the loss is not the direct result of an event beyond the reasonable control of the depositary bank.

# We are the right partner

Clearstream is the natural partner of choice for depositary banks seeking to take on their responsibilities and manage their risk profile for the safekeeping of assets under AIFMD and UCITS V. We provide a highly compatible and secure infrastructure to support financial institutions in the new regulatory environment. As an (International) Central Securities Depository ((I)CSD) and Securities Settlement System (SSS), our business is subject to the strictest regulatory oversight.

## The right tools in place

We are in a position to assist depositary banks to fulfil their requirements with regards to:

- Asset monitoring and due diligence
- Asset safekeeping in a stable and secure regulatory environment
- Segregation of assets and streamlined account opening in our books
- Segregation “one level down” from the depositary bank in line with CSSF Circular 14/587
- Extensive cash reporting tools to facilitate balance monitoring.

## SSS within AIFMD and UCITS V standards

As per both directives<sup>3</sup>, the use of a SSS is not to be considered as a delegation of the custody function by the depositary bank. However, through our close contact with regulatory authorities and alongside our customers, we are working towards further clarifying this position and assessing any impacts it may have on the delivery of our products and services. Regardless of any future assessment, depositary banks can make use of our reliable and secure environment to deposit their assets and our low risk profile as a market infrastructure.

Notwithstanding this exemption, we further recognise that depositary banks may require additional support for the financial instruments they hold via

Clearstream and it is on this basis that Clearstream has already been working to put in place services and is looking at further ways to support them.

## Assessment

Under AIFMD and pursuant to Art. 21 (12) of AIFMD and Art. 101 of the Level 2 regulation, the depositary bank will not have to provide immediate restitution of the lost asset if it can also demonstrate that the event was external and beyond its reasonable control and that its consequences were

unavoidable despite all reasonable efforts to the contrary. Art. 101 of the Level 2 regulation states the conditions that need to be met for an event to be regarded as external and unavoidable. Similar provisions are also referenced in UCITS V.

In all such cases, depositary banks will need support to be able to demonstrate that they have taken reasonable measures to avoid a loss event and have acted in the best interests of the fund with the appointment of the agent or SSS.



<sup>3</sup> AIFMD: Article 21 (11); UCITS V: Article 22(a), paragraph 4.

# Coverage of assets

For the vast majority of our customers' assets we provide the most secure custody environment currently possible. In view of AIFMD and UCITS V, Clearstream holds assets in the following way:

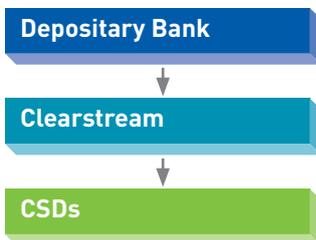
## Assets issued through Clearstream as place of issuance



We provide the most secure custody environment for assets where Clearstream is the place of issuance and deposit – namely international

bonds and ETFs as well as domestic German and Luxembourg securities.

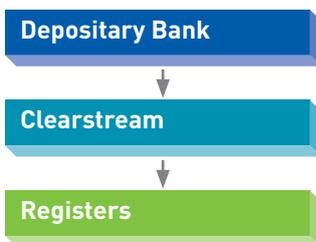
## Assets held directly via Clearstream at the domestic CSD



We provide an optimal custody environment for securities held by Clearstream via our extensive network of over 25 direct CSD links, many of which are assessed for Eurosystem monetary policy operations. This is Clearstream's preferred access model for domestic markets and it is being implemented whenever feasible or relevant. Clearstream will also extend its support to depository bank clients for managing their obligations under AIFMD as follows:

- Full transparency on the structure of the domestic market and Clearstream's link to the local CSD
- Monitoring of the local CSDs by Clearstream and reporting to the depository banks
- Monitoring of the local legal and regulatory framework by Clearstream and reporting to the depository banks
- Supports the TARGET2-Securities (T2S) settlement model.

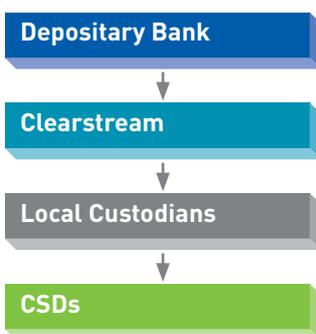
## Fund shares held via Clearstream in TAs, registrar or processing agent registers



Through its Vestima service, Clearstream offers a custody solution for international funds. The registrars used to hold the investment fund shares are not considered a custody delegation under AIFMD. Clearstream will also extend its AIFMD support to depository bank clients as follows:

- Full transparency on the structure of the Clearstream shareholder ownership chain
- Monitoring of the TAs or registrars by Clearstream and detailed reporting to the depository banks
- Monitoring of the local legal and regulatory framework by Clearstream and reporting to the depository banks.

## Assets held with Clearstream via an indirect local link



For certain domestic assets, Clearstream has indirect network links where access to the domestic market CSD is delivered via a local custodian or agent bank.

Clearstream will also extend its support to depository banks' clients for managing their obligations under AIFMD and UCITS V as follows:

- Full transparency on the structure of the domestic market and the Clearstream custody chain
- Monitoring of local CSDs by Clearstream and reporting to the depository banks
- Monitoring of the local legal and regulatory framework by Clearstream and reporting to the depository banks
- Further commitments to support due diligence and oversight tailored to customer requirements.

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# AIFMD/UCITS V-related service offering

Clearstream has developed two comprehensive reports to support depositary banks in effectively monitoring the performance of the underlying custody chain and in assessing the risks they could be exposed to in relation to TAs, registrars and processing agents:

- A Domestic Markets Monitoring Report (DMMR) on securities held through our extensive network of 55 domestic markets and more than 90 links to local CSDs as well as information related to its sub-custodian selection and review process.
- A specific Registrar Monitoring Report (RMR) for securities held in the fund's register kept by registrars and TAs.

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## Domestic Markets Monitoring Report

Customer demand has been the key driver for developing the DMMR to supplement the extensive information that is already available at Clearstream today. The reporting is helping depositaries to monitor the performance of their underlying custody chain and support their due diligence obligations.

The report shows the custody chain below Clearstream that is applied to safekeep securities in the domestic markets. In most cases, a significant volume of securities are held through direct links we have to CSDs, however, others go through

a more traditional custody chain with commercial banks as sub-custodians.

The DMMR supports depositary banks in reporting to AIFMs and for fulfilling the due diligence and regulatory obligations they face.

As part of this service, Clearstream is offering information related to the:

- Domestic market's specificities
- Structure of our direct and indirect custody links and indicators of our relationship with CSDs and/or sub-custodians
- Reports on risks at market, sub-custodian and CSD level.

Customers can subscribe to the report via the respective application form on the Clearstream website.

Subscribers can access the most recent version through a dedicated closed user access section on the website.

The form can also be requested from your Relationship Manager.

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## Registrar Monitoring Report

For assets recorded in shareholder registers, Clearstream has developed the RMR enabling depositary banks to assess the quality of TAs, registrars or processing agents, based on a profiling report.

This report contains key information on the holdings of Clearstream clients with the respective agent and provides ratings as well as relevant weighted scores based on extensive due diligence questionnaires.

The RMR provides depositary banks with a reliable and efficient tool for meeting their risk management obligations under AIFMD and UCITS V, related to their fund assets. The risk assessment is conducted by Clearstream's proven system, based on documentation and operational data sourced internally or externally via industry-defined questionnaires.

The monthly reports include:

- TA structure and turnover metrics
- Information about the auditor and control reports

- Regulatory compliance of a TA, details about the regulator and compliance structure
- Possible legal proceedings or investigations against the TA as well as its insurance coverage
- Operational information, such as system automation, business continuity planning and cash and security reconciliation
- TA records, such as efficiency of contract notes, statements and any significant unreconciled positions.

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## Contact information

For further information, please contact your Relationship Manager

[www.clearstream.com](http://www.clearstream.com)