

## THE ASSOCIATION OF GLOBAL CUSTODIANS

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26 June 2007

Mr. Jean-Michel Godeffroy  
Director General Payment Systems and Market Infrastructure  
European Central Bank  
Postfach 16 03 19  
D-60066 Frankfurt am Main  
Germany

Dear Mr. Godeffroy:

We write on behalf of the Association of Global Custodians (the "Association")<sup>1</sup> with regard to the European Central Bank's ("ECB") "T2S Consultation Paper: General Principles and High-Level Proposals for the User Requirements", issued 26 April 2007 (the "Proposals Paper"). This letter follows up the Association's earlier comments regarding anticipated T2S features,<sup>2</sup> and it continues members' discussions with you and other ECB officials on 16 April 2007 concerning T2S.

The Association reaffirms members' keen interest in the ECB's efforts to create a cost-effective, efficient and harmonized securities settlement system for a pan-European market. At this date, our comments are general -- focused on certain key

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<sup>1</sup> The Association is an informal group of ten global custodian banks with extensive business in Europe through European offices, branches and affiliates that provide securities safekeeping services and related asset-servicing functions to cross-border institutional investors, including pension funds, insurance companies and investment companies. Through their intermediary activities, Association members play a critical role in enabling the flow of investment capital from market to market and facilitating investments in European securities. The Association members are listed on the letterhead above.

<sup>2</sup> Association Letter to Jean-Michel Godeffroy, 7 February 2007.

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design issues -- given the high level of the information in the Proposals Paper. As the work of the T2S technical groups leads to greater functional and operational detail, we expect to provide more detailed commentary. In addition, as you know, member representatives would be pleased to meet with you and others involved in the T2S initiative to continue discussions on open issues as the initiative evolves.

### **General Comments.**

- T2S should be designed to ensure that settlement operations are effectively synchronized with asset-servicing functions and operations. Principle 3 in the Proposals Paper confines the scope of T2S to "settlement" and indicates that T2S will not engage "in any asset-servicing businesses". Given this principle, we remain concerned that the technical design of T2S may not take fully into account the significant interdependencies between asset servicing and settlement, thus limiting the opportunity to generate meaningful net savings and efficiencies for market participants.

On this topic, we ask the ECB to recognize that core asset-servicing operations of Central Securities Depositories ("CSDs"), including features such as process timelines and funding, are -- and need to be -- closely linked with the settlement functionalities envisioned for T2S. As we noted in our earlier comments, absent close and careful synchronization of functions, intermediary users (such as custodians) and investors will continue to pay for multiple, fragmented systems and non-harmonized processes. Although we appreciate the need to avoid over-extending the scope of the T2S user requirements, the Association continues to encourage the ECB to actively work with CSDs and market participants to develop an efficient and workable solution in this regard.

- The introduction of T2S requires careful consideration of the collateral impacts on systemic risks and competitive fairness. Removal of core settlement functionalities from CSDs as a result of implementing T2S will likely encourage further CSD expansion into commercial value-added services generally performed by intermediaries. During the design and implementation of T2S, we urge the ECB to be careful not to promote incentives for CSDs to re-position their operations into non-traditional lines of business in ways that expose market participants to increased systemic risks (e.g., by conducting activities that involve taking credit risks) or that create anti-competitive effects in the environment in which added-value services are currently performed (e.g., by leveraging their dominant market infrastructure position).

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- Intermediary users should have maximum flexibility to access T2S directly if they so choose. Principle 11 of the Proposals Paper suggests that users will be allowed direct technical access to the T2S platform, albeit such access can only be obtained from participating CSDs. We believe it is likely that a number of intermediary users, including global custodian banks, will seek direct access in order to assure they have timely and accurate information needed to perform their role. The Association realizes at this early stage that the exact details of the relationships and dependencies between direct CSD participants and indirect/direct bank participants in T2S are not fully formed. As the user requirements are developed and clarified further, we ask the ECB to ensure that resultant participant configurations and attendant procedures afford intermediary users seamless and unhindered opportunities to access T2S directly.

- The guiding objective of harmonization should be systemic efficiency, not necessarily "minimal market impact". Principle 3, Principle 5, and Proposal 67 of the Proposals Paper suggest that the ECB's guiding standard for the design effort is a T2S that "minimizes overall market impact." Although the Association agrees that the ECB must consider the development requirements and cost impacts of T2S on the various markets, we firmly believe that attention to such factors should not create a long-term dilutive effect on market standardization efforts, such as progress on the removal of the Giovannini barriers. Indeed, we believe the ECB's guiding principles should remain centered on contributing to the realization of a cost-effective, efficient and harmonized infrastructure across the euro area.

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We appreciate the opportunity to provide the ECB again with the Association's views. We look forward to further discussions with you and to delivering more detailed comment as the project gains definition. If you have questions or would like additional information, please contact the undersigned.

Sincerely yours,



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