

THE ASSOCIATION OF GLOBAL CUSTODIANS

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January 28, 2008

Via Electronic Transmission

Dr. Luis Correia da Silva
Reinder van Dijk
Oxera Consulting Ltd
40/41 Park End Street
OXFORD
OX1 1JD
United Kingdom

Re: Phone Conference of 18 January 2008 Concerning the Oxera Study on prices, costs and volumes

Dear Sirs:

On behalf of the Association of Global Custodians ("Association"),¹ thank you for meeting with Association representatives last Friday, 18 January, to discuss the Oxera Study on prices, costs and volumes of trading and post-trading services ("Study") and the current version of the Study's Pilot questionnaire for global custodians ("Questionnaire"). Association members appreciated your time and courtesy as well as the opportunity to begin a dialogue around the issues and concerns of Association members relating to the Study and the Questionnaire. We found the discussion and exchange valuable and informative.

¹ As you know, the Association is an informal group of eight global custodian banks that provide securities safekeeping services and related asset-servicing functions to cross-border institutional investors, including pension funds, insurance companies, and investment companies. Members are substantial users of sub-custodians and central securities depositories, either directly or indirectly, in all European markets. The Association regularly provides commentary to European regulators on matters of interest or concern to members and institutional cross-border investors. Members of the Association are listed on the letterhead above.

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As promised last Friday, this letter summarizes the points Association representatives conveyed to you during the meeting and includes additional suggestions regarding alternative approaches to the data-gathering focus. As noted during the meeting, certain of our points trace to Oxera's "monitoring methodology" paper prepared as background to the Study last July, and we understand that your thinking concerning the specifics of the methodology continues to evolve, including the nature of market-specific "user profiles" and the relevant "indicators" and other variables affecting costs and prices. We appreciate your invitation to develop more detailed commentary regarding the structure of global custodian services and the many variables affecting individual custodians' mix of services and prices to global institutional investors.

For your convenience, I have grouped the points we addressed during last week's meeting into four categories.

One: The Proprietary, Confidential and Competitively-critical Nature of Service-Price Information; Needed Assurances regarding Use and Safety of any Price and Service Specific Data Given to Oxera

- Service-specific and market-specific pricing data – even if not specific to identified clients – is strictly proprietary to individual custodians and is competitively sensitive. Disclosing details to any third party, including Oxera, about price-and-service mix may well breach custodians' service agreements with clients. Those agreements may require client consent, and consent from one or all clients may not be given.
- Assurances need to be provided by Oxera and the European Commission ("Commission") that any custodian-specific data will be kept secure and secret (1) during transmission to and handling by Oxera or its agents, and (2) when in safe storage and during destruction. Suitable procedures need to be confirmed and in place to ensure strict confidentiality and non-disclosure. These assurances and procedures should be included in confidentiality agreements. As we noted during the meeting, Association members would be pleased to review and provide comment on draft provisions.
- Due to the sensitivity of price information – and due to the critically competitive nature of such data – it is advisable if not imperative that such data be collected and reported to the Commission as anonymous. Assurances need to be provided that price

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data will not be used for any purpose other than Oxera's summary reports to the Commission.

- Price secrecy is particularly crucial at the custodian level, where competition for institutional investor business is robust. Confidentiality regarding each custodian's prices and pricing arrangements and approaches are central to the candid process of negotiating customer-by-customer specific terms of service. Moreover, an unfettered pricing mechanism is critical to free and effective competition among intermediaries. Therefore, in designing the data requests in the Questionnaire and in stating data aggregates or summaries or averages, care needs to be taken to avoid revealing competition-critical information publicly. In this regard, the "public domain report" that Oxera anticipates publishing must be closely reviewed to ensure that it does not impact market dynamics among intermediaries or negotiating freedom as between intermediaries and customers. The review should confirm that the report will not set out, or be perceived as setting out, "average" prices or pricing "guidelines."

Two: Data Production Burdens on Intermediaries; Timing Issues.

- Global custodians will incur substantial costs and require considerable resources to develop and cross-check the detailed, multi-market price and service data responsive to the Questionnaire. Data production in the form and detail anticipated will likely create duplications in effort within and among related service organizations or departments in large complex financial organizations. Even within a single custodian bank, there are uncertain implications of measuring the bank across multiple lines of business. Some banks may simply not be able to produce the data in the specific form or with the specific focus that Oxera seeks. For example, data collected will necessarily not take into account the wide variety of individual-customer service arrangements; will typically not be susceptible to correlation with individual markets; and will suffer from some double-counting across related entities or service departments. *These data-complexity problems are particularly acute for global custodians.*

- Data production during the first quarter of 2008 is particularly problematic. During this quarter, intermediaries in European markets, including Association members, are also being asked to review and comment on the 775-page consultative T2S papers (including for some participants the provision of cost assessments for the economic impact analysis); participate in monitoring the implementation of the Code of Conduct; manage the evolving implementation of the Euroclear Single Platform; and

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respond to the implementation schedule for the CRD and MiFID. Many of these resource demands involve duplicative efforts, and most will persist over the next several years. Moreover, all these demands will need to be serviced by the same individuals within each organization. On this issue point, we very much appreciate your indication of timing flexibility.

Three: Numerous variables inform and affect global custodians' individualized service/price packages to particular clients. Changes in those packages, negotiated periodically, often have nothing to do with European markets or market costs. Responses to the current iteration of the Questionnaire will necessarily be arbitrary, and individual custodians' responses and their many caveats will vary.

- It is particularly important to the efficacy of the Study that the Questionnaire solicit economically meaningful information. However, it is particularly difficult for global custodians, which provide cross-border investors with global services, to correlate market-specific costs with market-specific services/prices, as the current Questionnaire envisions.

- The costs of many local services purchased by global custodians are not, and cannot be, simply passed through to customers; nor can they be readily correlated with prices to customers. Some customers negotiate for an "all-in" fee, which necessarily applies without regard to volume of activity in any particular market. Other customers negotiate for a variety of client-care banking and related services, which make calculation of market-specific costs and prices infeasible. Further, some customers, including very large funds, demand services on a no-fee basis, and insist instead that the global custodian make its returns on asset-servicing functions, such as stock lending. The service benefits associated with such customer-specific, often blended pricing arrangements cannot be priced separately. Any attempt to state a price-per-service-per-market will necessarily be arbitrary and will vary from service provider to service provider, as the providers' methodology and price/service arrangements vary.

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Four: Oxera and the Commission should consider using less burdensome and less problematic alternative approaches to addressing the Commission's basic objective.

- It is not clear whether Oxera or the Commission have considered less burdensome approaches to studying the changes in prices over time, or approaches that pose less risk of harming competitive dynamics.
- As one alternative to the approach called for in the Study, data summaries for particular markets/services could be indexed to a base year, and data for subsequent years could be stated with reference to a positive or negative relation to the index. That approach would not pose the risk of publicly disclosing particular price averages, ranges or summaries.
- Another approach could involve publishing a summary of the structure of intermediary custodian services and a rundown of the types of variables that can affect pricing arrangements. That could be coupled with a set of periodic reports to the Commission from selected financial institutions indicating whether costs/prices have increased, decreased or stayed the same based on a stated methodology. This approach would achieve the same objective as the index approach, also without the risk of impairing custodians' service/price negotiations with customers.
- Finally, and perhaps optimally in terms of limiting the burden of producing data, the questionnaires at each targeted level of the value chain could confine data requests to costs incurred and services purchased, rather than pricing information. This approach would focus on the types of data now sought from global custodians in Part 3 of the current Questionnaire.

As discussed in our meeting, collecting and reporting to Oxera *data about costs* in particular markets is much more manageable at the global custodian level than is the problematic estimation or arbitrary stipulation of *price data* per service, per market. Indeed, it should be relatively easy at the global custodian level to generate such cost information for 2007 and 2006 as well. Furthermore, we believe this approach would provide Oxera with suitably comprehensive levels of data at the relevant points in the value chain, enabling it to give the Commission meaningful cost trend information year over year. Significantly, this approach would avoid the price confidentiality problems we have noted, and would reduce the potential that the published report of cost

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summations would misrepresent the actual correlation between global custodians' costs and prices.

* * *

In conclusion, the Association and its member representatives appreciate your willingness to discuss the Study candidly as well as your interest in members' views. We stand ready to work with you and the Commission to define an optimal review mechanism so that the Commission's effort to assess the impact of its policies can be carried out meaningfully. If you have questions, please contact the undersigned at 312.861.2620.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Dan W. Schneider", with a stylized, flowing script.

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