

THE ASSOCIATION OF GLOBAL CUSTODIANS

The Bank of New York
Bankers Trust Company/Deutsche Bank A.G.
Brown Brothers Harriman
N.W.
The Chase Manhattan Bank
Citibank, N.A.
Investors Bank & Trust Company
Mellon Trust/Boston Safe Deposit
& Trust Company
Northern Trust Company
State Street Bank and Trust Company

Counsel to the Association:
Baker & McKenzie
815 Connecticut Avenue,
Washington, D.C. 20006
Telephone: 202/452-7013
Facsimile: 202/452-7074

Some Frequently Asked Questions Concerning the Depository Questionnaire Project

November, 2000

1. What is the Association of Global Custodians?

The Association is an informal group of nine U.S. banks that are major providers of custody services to U.S. institutional investors. The members of the Association are listed on the letterhead above. The Association primarily seeks to address regulatory issues that are of common interest to U.S. global custody banks. The member banks are competitors, and the Association does not involve itself in member commercial activities or take positions on how members should conduct their custody businesses.

2. What is SEC Rule 17f-7 and What Does It Require?

The genesis of the depository questionnaire is the recent adoption by the U.S. Securities and Exchange Commission ("SEC") of Rule 17f-7.¹ Rule 17f-7 sets forth

^{1/} The SEC explained the background and purpose of Rule 17f-7 in Investment Company Release No. 24424 (April 27, 2000), 65 FR 25630 (May 3, 2000). You may review a copy of this release on the Commission's web site (<http://www.sec.gov>).

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the circumstances under which U.S. investment companies may hold securities through the facilities of non-U.S. securities depositories. The key requirement of Rule 17f-7 is that an investment company must receive from its "Primary Custodian" an analysis of the custody risks associated with maintaining assets with each depository it uses.

Rule 17f-7 does not provide specific guidance concerning the content of these analyses of depository custody risk. However, in the release announcing the adoption of the rule, the SEC stated:

"As a general matter, we expect that an analysis will cover a depository's expertise and market reputation, the quality of its services, its financial strength, any insurance or indemnification arrangements, the extent and quality of regulation and independent examination of the depository, its standing in published ratings, its internal controls and other procedures for safeguarding investments, and any related legal protections."²

3. What is the Purpose of the Association's Depository Questionnaire?

The purpose of the questionnaire is to gather basic, factual information concerning depositories and similar facilities. The Association believes that the information sought by the questionnaire will be needed to prepare the analyses required under Rule 17f-7. However, some custodians may draw on additional sources of information in the preparation of an analysis. Each Association member bank will decide for itself whether to gather additional information and how to synthesize the information available to it regarding a particular depository into the required risk analysis.

4. How Does the Association Define the Term "Depository" For Purposes of the Questionnaire?

²/ Investment Company Act Release No. 24424 at 10-11 (notes omitted) (April 27, 2000).

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The Association looks to the SEC's definition of the term "securities depository." Rule 17f-7 describes the depositories to which it applies by referring to another SEC rule, Rule 17f-4. Rule 17f-4 provides that a securities depository is "a system for the central handling of securities where all securities of any particular class or series of any issuer deposited within the system are treated as fungible and may be transferred or pledged by bookkeeping entry without physical delivery of the securities."

The SEC has provided only limited guidance concerning how this definition applies to nontraditional depositories, such as banks that operate a book entry system to record ownership of sovereign debt, or other certificateless securities. Therefore, in some cases, it is not clear whether or not the SEC would regard a particular facility that performs some of the functions of a securities depository as falling within the definition in Rule 17f-4.

5. Has the Association Determined That All of the Institutions That Received the Questionnaire Are Securities Depositories Under the SEC's Definition?

No. The Association has not, as a group, made any formal determinations concerning which entities would be regarded as depositories within the meaning of Rules 17f-4 and 17f-7. Because of the limited SEC guidance available and the ambiguity in some of the SEC's statements on this issue, we do not believe that it is appropriate for the Association to attempt to make such determinations. Individual Association members, in consultation with their clients, are, of course, free to decide whether they believe that a particular facility is or is not a "securities depository" under the SEC definition.

Instead of making a legal determination, the Association sent the questionnaire to institutions that perform some or all of the types of functions described in Rules 17f-4 and 17f-7. As a practical matter, the Association believes that most of the entities that received the questionnaire would be deemed depositories. In those cases where the application of the definition is less clear, we believe that many institutional investors are likely to wish to receive the type of risk analysis information required by Rule 17f-7 with respect to the institution in question, regardless of whether or not it is technically a securities depository.

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6. By Responding to the Questionnaire, Has an Institution Conceded That It Is a Securities Depository?

No. For the reasons stated in response to the prior question, the Association does not view an entity's willingness to respond to the questionnaire as indicating that the entity is necessarily a securities depository under the SEC definition.

7. Will the Association Treat Depository Questionnaire Responses as Confidential?

No. As explained in the June 13, 2000 letter by which the questionnaire was transmitted, the information provided in response to the questionnaire will be used in compiling Rule 17f-7 risk analyses and may also be furnished by members of the Association to U.S. investment companies. In addition, the information may be furnished to other types of institutional investors, or to other parties who have an interest in the securities markets of various countries.

The Association does not intend to release questionnaire responses directly to the general public and does not believe that most clients will request access to particular depository responses. However, the members of the Association cannot ensure that responses will be confidential. While Association members expect only a few clients to request copies of questionnaire responses, those clients that do obtain responses are unlikely to implement confidentiality procedures to prevent the possible release of such responses.

8. Will the Association Provide Participating Depositories, or the General Public, With Copies of Questionnaire Responses?

The Association does not intend to make responses available to other participating institutions or to release them to the general public. We recognize that, in most cases, the information sought by the questionnaire is publicly available. However, the Association is concerned that, if all responses are automatically disseminated to other depositories or to the general public, some institutions may be less likely to respond to the questionnaire, or to any subsequent Association requests for updated information. This could, in turn, hamper the

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ability of Association members to provide clients with the analysis required by Rule 17f-7.

At the completion of the project, the Association will ask each participant whether it will release its questionnaire response upon request, and, if so, to inform us how interested persons can obtain the depository's response. The Association will then prepare a list identifying all institutions to which the Association sent its questionnaire, indicating whether, in each case, the institution has responded and, if so, whether it will make its response available upon request. If an institution is willing to make its response public, we will include on our list the name and address of the person or web site from which the response is available.

9. May Respondents Make Their Own Questionnaire Public?

The Association encourages participants to make their own responses public. We understand that some depositories are considering posting their responses on their web sites. The Association has no objection to such posting, or to any other use that a depository wishes to make of its own response.

10. What Types of Judgments Does the Association Plan to Make Concerning Depositories?

The Association does not intend to issue ratings or make any other types of judgments concerning depositories. As explained above, the Association's objective is to gather basic, factual information. Each Association member will then decide for itself how to use that information in preparing a risk analysis under Rule 17f-7 or for other purposes. The Association will not take any position on this issue.

There is, however, one area in which the Association members will work together in evaluating questionnaire responses. Rule 17f-7 contains six eligibility standards. These standards provide that a securities depository is "eligible" as a securities depository" if it --

- (i) Acts as or operates a system for the central handling of securities or equivalent book-entries in the country where it is

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incorporated, or [as] a transnational system for the central handling of securities or equivalent book-entries;

- (ii) Is regulated by a foreign financial regulatory authority as defined under section 2(a)(50);³
- (iii) Holds assets for the custodian that participates in the system on behalf of the Fund under safekeeping conditions no less favorable than the conditions that apply to other participants;
- (iv) Maintains records that identify the assets of each participant and segregate the system's own assets from the assets of participants;
- (v) Provides periodic reports to its participants with respect to its safekeeping of assets, including notices of transfers to or from any participant's account; and
- (vi) Is subject to periodic examination by regulatory authorities or independent accountants.

The members of the Association intend to jointly review questionnaire responses in order to determine whether the information provided permits a determination concerning eligibility under these six criteria. In those cases where a questionnaire response is incomplete or unclear concerning eligibility, Baker &

^{3/} Section 2(a)(50) of the Investment Company Act of 1940 provides:

"Foreign financial regulatory authority" means any (A) foreign securities authority, (B) other governmental body or foreign equivalent of a self-regulatory organization empowered by a foreign government to administer or enforce its laws relating to the regulation of fiduciaries, trusts, commercial lending, insurance, trading in contracts of sale of a commodity for future delivery, or other instruments traded on or subject to the rules of a contract market, board of trade or foreign equivalent, or other financial activities, or (C) membership organization a function of which is to regulate the participation of its members in activities listed above.

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McKenzie, on behalf of the Association, may contact the respondent for clarification or additional information.

11. If Individual Association Members or Their Clients Wish to Obtain Additional Information, How Will Follow-Up Occur?

Once the responses have been disseminated to Association members, and eligibility issues have been resolved, the member banks will use their own judgment concerning whether particular responses require amplification or explanation and, if so, what sources should be used in obtaining further information. That process could include follow-up inquiries to particular depositories. In addition, the sources to which Association members may look could include published information concerning depositories, the views of local institutions that are depository participants, and commercial rating services, among others.

12. How Will the Results of the Questionnaire Be Presented To Clients?

Each member bank will use the questionnaire responses as it sees fit. Although it is certainly possible that some clients will request to see questionnaire responses, the questionnaire was not formulated with a view to routinely presenting the responses to clients. Instead, the questionnaire is intended to be a source from which member banks can draw in preparing Rule 17f-7 analyses. As noted above, the Association does not propose to amplify or analyze questionnaire responses, except in the area of Rule 17f-7 eligibility information. How individual Association member banks use questionnaire responses is a matter committed to their discretion and on which the Association has no position.

13. What is Baker & McKenzie's Role in the Questionnaire Project?

Baker & McKenzie's role is essentially ministerial. We have been charged with distributing the questionnaire, responding to inquiries from depositories, collating responses, and following up with depositories that do not respond. While we may seek clarification from depositories where responses are patently incomplete or inaccurate, we have not been asked to perform any type of substantive review or evaluation of depository responses. At the conclusion of the

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questionnaire process, we will provide each Association member bank with a set of the responses. The member banks will then proceed independently in gathering any further information they deem necessary and in preparing analyses for their clients.

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If you have further questions or comments concerning the questionnaire, please contact the undersigned at Baker & McKenzie, 815 Connecticut Avenue, N.W., Washington, D.C. 20006 (telephone: 202/452-7013; fax: 202/452-7074; e-mail: daniel.l.goelzer@bakernet.com).