association française de la gestion financière

Mr Charlie McCreevy
Commissioner for Internal
Market and Services
European Commission
1049 Brussels
Belgium

SJ/PB - 2069/Div.

Paris, 15 November 2005

Dear Commissioner,

Thank you for offering us the possibility to provide the European Commission services with comments regarding the Green Paper on investment funds.

Before any development of AFG members' views on the Green Paper, let us first stress the quality of the work carried out by the team of Niall Bohan under the leadership of David Wright. The vast majority of current issues regarding investment management have been precisely identified, and their analysis was undertaken by DG MARKT services very carefully, with frequent consultation of market participants.

As you are aware, AFG represents the France-based investment management industry, both for collective and discretionary (mandate-based) individual portfolio managements.

AFG members' clients are both retail and institutional investors (including insurers and pension funds).

Our members include management companies and investment companies (SICAVs). They are entrepreneurial or belong to French or foreign banking, insurance or asset management groups. AFG members are managing around 2000 billions euros in the field of investment management - making the France-based industry a leader in Europe (for collective investment in particular, with more than 1100 billion euros i.e. 20% of EU investment funds assets under management) and one of the first at global level.

For your convenience, a list of the nearly 400 management companies that belong to AFG is attached in **Annex 2**.

The majority of the funds managed by the France-based management industry are domiciled in France but a significant part is also domiciled in other EU Member States or in the rest of the world.

In the field of collective investment, our members' activity covers – beside UCITS – products such as employee saving schemes, among which those which are specifically dedicated to retirement (the PERCOs), regulated hedge funds and a significant part of private equity funds.

The large size as well as the pan-European and global activity of the management industry based in France explain to a very large extent why AFG members follow very closely all the current debates at European level regarding any possible improvement of the existing European legislation.

Therefore, we hope that AFG can provide with a helpful contribution to the European Commission, based on our members' experience.

Being an active member of the European Fund and Asset Management Association (EFAMA) - along with many corporate members and other national associations, we clearly support EFAMA comments. Consequently, AFG's own contribution will concentrate on certain subjects that appear of particular importance to us.

1. AFG is very grateful to the European Commission for having acknowledged the importance of asset management industry

Two years ago, we highly appreciated the initiative from DG MARKT to set up four post-FSAP professional expert groups in order to assess the progress and existing limits of European financial integration in relation to specific financial fields, in particular investment management. Asset management for third parties has become a major activity on European financial markets today, and our members welcome the importance DG MARKT recognised to our industry through the setting up of both a dedicated expert group and a dedicated and well staffed new unit in the Financial Markets Directorate.

The France-based management industry strongly supports such actions which will reinforce and speed up the process of building up a Single Market in the field of financial services, as it is for the common profit of investors, issuers, and asset managers.
AFG strongly wishes that the Commission continues to take new initiatives which will lead to this Single Market in practice.
In order to get the largest consensus, these initiatives will clearly require avoiding over-regulation of the asset management industry, in order not to deter innovation and not to stifle competition. Indeed, the creation of new management companies and the development of new management techniques and products should be encouraged. Beyond regulatory impact assessments, cost-benefit analysis should become the rule.
This being said, we must refrain from the temptation to equate any new European initiative with cost – as the building of a Single Market for investment management, driver of creative competition and economies of scale, does require legislative action more often than not.
Moreover, AFG shares your view of stressing the urgent need for the European Union to tackle the financing of retirement as a top priority.

This very positive consideration of the asset management industry by the European Commission is also reflected in the Green Paper. In particular, the European Commission agrees that the UCITS Directive was a way in 1985 to make important progress to build a strong European investment funds industry through a Single Market together with the appropriate balance between industry needs and investor needs. Thanks to that Directive, the European pattern became a reference at global level and UCITS became a worldwide label, synonymous of *good regulation*.

Obviously the implementation of the existing European legislative framework can be improved. CESR is already working on these aspects.

But the true implicit question of the Green Paper is: *is there a need for changing such a "good" regulation?* This question leads us to two complementary questions. *Isn't there a risk in changing it? Isn't there a risk in* ***not*** *changing it?*

In order to try to get out of this apparent dilemma, let us recall that, as stated by John F. Kennedy some decades ago: "*Change is the law of life. And those who look only to the past or present are certain to miss the future*"[1]. Our industry is in permanent innovation: regarding products, regarding strategies, regarding architecture. Good regulation for yesterday is maybe acceptable regulation for today but very probably it will mean bad regulation for the (near) future. Thus, we support completely the position you took at the Commission Hearing on Investment Funds on 13 0ctober 2005 when you stated[2]: "*The industry cannot afford to be held back by fragmented markets or outdated legislation (...). We cannot rest on our laurels (...). Financial markets have not stood still since 1985 or indeed 2001. Regulation needs to respond to these changes (...). Otherwise, UCITS law risks becoming a strait-jacket rather than a facilitator. We need to start engaging with some of these issues if the European industry is to remain in the global vanguard.*" One of the main findings of the survey carried out by the Bank of New York in July 2004 among senior executives of European investment managers, banks and other financial institutions[3] reveals that more than 50% of the respondents were considering that reforming supra-national regulation would be important to regain trust.

So, how is the dilemma to be solved? The answer is quite clear for us: upgraded regulation does not mean over-regulation, creating additional constraints for the investment funds industry. We agree with your statement: "*I would rather be accused of being timid than rush to badly prepared legislation which generates unforseen consequences.*"[4] But we also think that an excessive shyness would entail paralysis by analysis.

To be more specific, our members agree with the European Commission that **significant improvements can be done to facilitate the successful development of the fund industry in Europe by building on existing legislation. But** they also strongly believe that **several truly important issues for our industry will require significant modifications of the current legislation in the near future.** We urge the European Commission to start considering them *immediately* – as even medium term deliveries require immediate action to launch the work. The real question to raise and to answer positively to is: *do not worldwide investors, European industry and regulators need* <u>*to keep*</u> *a good regulation in Europe* – which means <u>modernising</u> it when needed, which entails in our view the necessity that it becomes more flexible and more innovation-friendly?

Apart from this AFG request to the Commission on undertaking work for modernising legislation as soon as today (including for medium term deliveries), we wish to underline that four issues, which are crucial to the healthy development of our industry, are not as developed in the Green Paper as they could have been:

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[1] John F. Kennedy, Frankfurt, 25 June 1963

[2] Your speech "*The EU framework for investment funds: a facilitator – not a strait-jacket*", Commission Hearing on Investment Funds (UCITS), Brussels, 13 0ctober 2005

[3] "*Restoring broken trust – a pan-European study of the causes of declining trust in the European financial services industry and analysis of the actions needed to rebuild investor trust*", Bank of New-York, July 2004

[4] see footnote 2

- The necessity to promote occupational pensions and create a real Single Market for them;
- The need to work on taxation issues, such as the existence of different tax treatment for competing savings products and the largely counterproductive Directive on taxation of savings, both creating/reinforcing barriers for a Single Market for financial services;
- The need to take into account the development of alternative investments in a wider way (including real estate funds and private equity funds beside hedge funds);
- The need for considering the competitive situation of the European fund industry vis-à-vis the rest of the world.

The two latter aspects imply that we will most probably need in due time **a lighter and more flexible (principle-based) European regulation** to ensure a level playing field of the European industry both vis-à-vis substitute products (e.g. certificates, structured notes) and vis-à-vis non-European competitors. Obviously, upgrading and making European legislation more flexible cannot solve every issue, but it is a prerequisite.

We will come back to each of these issues following the structure of Commission's Green Paper in the **Annex 1** of this letter.

2. Two general concerns regarding investment management

In the field of investment management, our members share two general concerns.

First, **the existing regimes remain very different from a Member State to another one**. When these regimes cover issues already dealt with by European Union legislation (for instance the UCITS Directive), some Member States take an over-lax approach for *interpretation* of the provisions of the Directive while others take the opposite position by sticking too rigidly to the letter of the text or even by applying stricter rules. When there is no European Union legislation, the divergence in *national regulations* is logically even bigger. In both cases, it creates prejudice to our members which wish a Single Market in practice, in order to be able to develop their activities at European level. It also creates a prejudice to investors, including institutional investors such as defined benefit retirement plans, which cannot benefit from an increased innovative and yet properly regulated competition.

In this view, it appears to AFG that the European Commission should take action towards CESR in the following way. We consider that the European Commission should ensure that the work of CESR for harmonising national interpretations is fully consistent with the provisions of the UCITS Directive – in order to avoid any legal risk to distort the letter or the spirit of these provisions. And if it appears that some potential improvements of harmonised practice would not fit with the UCITS Directive, then the European Commission should make clear to CESR that these improvements are not currently possible following the UCITS Directive provisions. It is important that we make sure both that CESR work is, once approved by competent EU authorities, fully implemented by national regulators and that we do not assign to CESR objectives that it cannot reach given the current state of the UCITS Directive.

This latter consideration leads to **the second general concern of our members: it appears that for several topics the existing Directive needs modernisation**, and the Commission should recognise it.

In practice, how to tackle this difficult issue of modernising some elements of the existing Directive?

AFG members consider that we have obviously to start from the real world.

In this view, **work should start without delay also on the changes that will take a longer time to be devised and implemented**. **The works for short term deliveries and those for medium term deliveries must be undertaken in parallel**. Such an approach seems realistic, considering the significant size and excellent staffing quality of the DG Markt unit in charge of asset management, and the will expressed by the European Parliament during the UCITS 3 adoption debate that a review of this text, with the view of tackling unsolved issues, should be undertaken by February 2005.

Once again, the crucial point is to **avoid wasting a precious time, increasing the gap between the market needs and the current legal framework**. We all know that implementing any initiative is quite long, not less than five years, which delays the positive effects of any European action after any decision. In that sense, it is pretty sure that some time will be required to take any new initiative. But if no work on improving the European regulatory framework is undertaken as soon as today, the asset management industry will be at risk for the future, in the two following ways. First, the lack of modernisation of the regulatory framework will prevent to develop a competitive regional industry able to face non-European competitors in the same field, as well as competitors from other saving product industries considering the existing lack of level playing field. Second, the industry will be at risk for any possible market scandal leading - as we saw in the United States with the Enron, mis-selling, market timing and late trading scandals – to a '***scandal-driven over-regulation***' which would impact negatively the whole industry.

<u>3. Three directions for action</u>

For AFG members several actions have to be launched by the European Commission in parallel (even if the deliveries might occur at different times depending on the specificities of the related subject). This series of actions can be undertaken following three directions: cost efficiency, innovation and commercialisation.

a) *Actions to be undertaken to* ***promote cost efficiency***

- The first topic relates to **<u>cross-border registration</u> of UCITS for cross-border marketing**. The vast majority of professionals active in Europe share the view that there is a <u>need for simplifying the process, considering the costs implied by the existing procedure</u>. Some improvements can be surely managed under the existing European legal framework. We wish to laud CESR for the impressive work they have carried out on this issue and wish the advice it will soon make to be quickly endorsed by national regulators. However, a full improvement in practice for the cross-border process will require reinforcing the scope of power of the Home Member State vis-à-vis the Host Member State – in line with the 'country of origin' principle of the Treaty. It would imply a change in the existing European legislation (Article 44 and following of the UCITS Directive). It would also imply that <u>national regulators build more trust among themselves and that an efficient mechanism to solve discrepancies between them is put in place</u>. It would, finally, be made easier if we move toward a really unified simplified prospectus.
  But beyond improving cross-border registration of the UCITS, some <u>structural actions</u> are needed to develop economies of scale – even though in some specific cases the "*small is beautiful*" principle makes sense (e.g. regarding specialised management 'niches' developed at national level, for instance domestic sectorial equity funds).

- Second, in the numerous existing cases of the same fund pattern currently offered locally under different national domiciles, we consider that **<u>cross-border mergers of</u>**

funds should be eased in the Union. At domestic level, mergers of funds have already been tested successfully (e.g. around 600 fund mergers in France since 2003). This success shows the need for mergers. First, mergers provide economies of scale. Second, mergers offer an opportunity to rationalise the range of products, making it easier to be understood by investors.

- Third, from a pragmatic point of view, the easiest and hence quickest measure for cost efficiency would be to authorise European **cross-border master-feeders**. The master-feeder architecture does not collide with Commission's and Member States' legitimate concerns on investors' protection, because both the master fund and the feeder funds will have to be UCITS managed by UCITS management companies. Master-feeders lead to a reduction of costs and, at the same time, ease the access to harmonised products by investors. Lastly, still from an investor protection perspective, master-feeders are totally transparent and easier to explain than other pooling techniques (in particular, virtual pooling – which might raise questions about the operational risks involved, the need for complex contractual arrangements and valuation processes). In France, domestic master-feeders have been a very significant success: less than five years after being authorised domestically, the French master-feeder fund market represents more than 7% of general UCITS AuM, through 577 master funds/696 feeder funds and 72 billion € (for feeder funds) at end 2004.

- Fourth, as the common aim for the Commission and professionals is to make the Single Market a reality, we have to build together a complete set of *functions which can be ensured at pan-european level*. A very crucial point would be to authorise management companies from one Member State to launch UCITS funds under the law of another Member State: the so-called '**management company passport**'. In particular, such a passport would delete the various costs related to the existing requirement from the UCITS Directive to set up local management companies to manage locally-domiciled funds. Such a costly step should not be made mandatory anymore.

- **A cross-border passport for depositaries** would be a valuable additional improvement as a way to increase competition among depositaries and to complete the 'open architecture'. However, an obvious prerequisite would be a clear European definition of the status and of the related functions to be passported, and these questions will obviously have to be discussed with representatives of this industry.

- **As a conclusion, AFG members warmly welcome the setting up of a dedicated expert working group** by the European Commission regarding 'cost-efficiency' and will be happy to contribute to the work to be carried out by this group in early 2006.

b) *Actions to be undertaken to **promote innovation***

- Work seems required as soon as today to find an appropriate European legal framework for **non-UCITS funds**: regulated hedge funds (at least for funds of hedge funds), real estate funds and some types of private equity funds. One of the reasons is that these funds are more and more oriented towards retail investors as well as these institutional investors transferring the risks and obviously the benefits to retail investors ('*instividuals*', such as pension funds for instance). Another reason is that non-European institutional investors wishing to invest in the European Union would benefit (and therefore the European industry as well) from minimum harmonised standards throughout Europe, avoiding wasting time in assessing all the local specificities of national regimes.

Such European regimes for non-UCITS funds would obviously not prevent Member States to keep their national regimes in place: they would constitute **additional and facultative** regimes beside the purely national ones.

On the approach to be followed, we fully agree with you that "*there is no need for a heavy-handed legislative intervention.*"[5] A solution might be :

- to acknowledge that the aim is not to regulate all these funds but to create new, additional, European regimes offering the opportunity to those who wish it to obtain a passport;

- to keep the general principles currently applicable today for UCITS and to extend them to non-UCITS, *but* to adapt the details **very differently** for UCITS and non-UCITS, in order to fit with the specificities of the funds, which would become specific funds covered beside existing UCITS by the same framework-directive – with a lighter regime of course. Thus, the existing 'UCITS label' would stay intact for the 'traditional' funds, without preventing the development of a similar label in parallel for the 'non-UCITS'. This approach would fit the Lamfalussy approach well, by clearly differentiating Level 1 provisions (essential principles common to all players in the value chain in relation with investment funds) from Level 2 provisions (technical details, including on the detailed features/limits/thresholds of products, differentiated between UCITS and non-UCITS). The idea would be to concentrate rules more on the **players in the value chain** (for instance through *'programmes d'activité'* such as those successfully introduced in France for asset managers wishing to create hedge funds or private equity funds) than on the products themselves - to depart from the existing product-based UCITS Directive the borderlines of which are tested regularly these days;

- A preliminary step for accessing non-UCITS funds might be to work on a common definition of the notion of European private placement. Private placement is currently very heterogeneous from one Member State to another one. Harmonisation of the notion would help developing a Single Market for such products, but with two caveats. First, it remains to be demonstrated that this goal can be reached in the short term as we all know that even at domestic level in Member States, private placement rules are not harmonised for different savings products. Second, we would still face the necessity to determine which types of funds would benefit such a 'private placement' regime;

- The setting up of a **dedicated expert working group by DG MARKT services** at the beginning of 2006 is an excellent initiative in this complex context, to which AFG members will be pleased to participate. However, we wish the European Commission to include **real estate funds** in the scope of the group. Our analysis on the need to tackle real estate funds as well is reflected for example by the global annual studies regularly published by Russell since 1992 on alternative investing[6];

- However, the features of the three categories of alternative investments are different from the ones to the others. Therefore, the approach to be followed will have to be differentiated to some extent from one category to another one.

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[5] see footnote 2

[6] '*2005-2006 Russell Investment Group Survey on Alternative Investing*', Russell Investment Group, 12 September 2005

- Not in the substance but on the legislative approach, in order to provide a European legislative framework flexible enough to ongoing innovation, it appears necessary to put the UCITS Directive under **a '<u>Lamfalussy' format</u>'** (i.e. a framework Directive defining the '*essential principles*' – level 1 – complemented by several implementing Directives on some '*technical details*' where necessary – level 2):

  - This would <u>ensure a better updating and upgrading of the Directive in a field where innovation is key</u>. In this view, we share your opinion that "*a brand is a storehouse of trust and [that] we need to be careful to ensure that we achieve the right balance between maintaining that trust and providing the necessary degree of flexibility to maintain competitiveness.*"[7] This latter aspect of flexibility can be fulfilled through a true Lamfalussy Directive

  - A first priority task will be to make it possible to <u>update and complete the list of eligible assets</u> for UCITS, which is today strictly limited by the Directive.

c) *Actions to be undertaken in relation with **commercialisation***

- In the interest of the investor, there is a need for the **clarification of responsibilities between the manager and the distributor vis-à-vis the customer**, in particular as open architecture is currently developing in the whole Union. The linkage between the current finalisation of the MiFID implementing measures and the forthcoming work on investment funds should be made clearer by the European Commission in the coming months. In particular, many management companies will have to comply with both sets of measures (i.e. UCITS 3 plus MiFID), which might be contradictory and very burdensome in some cases. Furthermore, France-based management companies making use of external distributors wish to recall that those management companies are legally responsible neither for the delivery of information documents nor for the advice delivered by the external distributor to the investor. Generally speaking, the responsibility of information delivered to the investor and of the knowledge of this investor (e.g. regarding the origin of assets to be invested, in the context of anti-money laundering actions) should rely in the hands of the distributor.
  Beyond the debate on the respective responsibilities between the manager and the distributor, AFG Members, as management companies, wish to be authorised to market other financial instruments than UCITS – in particular the other financial instruments they manage (such as CDOs for instance). The list of authorised activities by fund management companies will need some brushing up.

- It is important to ensure <u>a regulatory **level playing field** between investment funds and so-called 'substitute products'</u> (in particular some financial instruments listed on regulated markets and passported through the Prospectus Directive). We welcome competition, but on an equal basis (in particular through a lighter regime for UCITS - including guaranteed structured funds). In particular, let us recall that already today too many requirements (such as for the prospectus for instance) apply to the asset management industry that do not exist for competitors offering products which are similar but are out of the scope of the UCITS Directive. In this view, the main aim should not be to increase the load of paperwork for UCITS even more, but on the contrary to ensure a level playing field with substitute products (in particular for transparency standards). Ensuring such a level playing field would benefit the investor: investors need standardisation on the minimum information delivered to them.

[7] see footnote 2

- In relation with the level playing field, the last topic, but by no means the least, relates to the **simplified prospectus**. The recommendation of the European Commission on the subject did not really provide positive effects until today. The same UCITS registered simultaneously in different Member States leads to various prospectuses depending on the local regulator. Even worse, in some jurisdictions the so-called simplified prospectus became even longer as compared to the former one and TERs are not defined in the same way in the different Member States. There is no reason for that**. This document should be harmonised at European level**, dedicated both to investor information and cross-border marketing, along the following line: the simplified prospectus should be a short notice allowing investors to compare product features across borders through a harmonised document informing investors in an easily understandable language about the key features of a fund, thus enabling them to make well considered investment decisions, but also a marketing document simplifying cross-border distribution and benefiting therefore from the Single Market. It might be helpful to assess to which extent the example of the so-called Prospectus Directive (for issuers) might be used in this regard.

Last, we want to mention **two specific topics which are related to investment funds but are currently assessed at the European level in a wider context.** Those two topics will have to be considered by the European Commission in the medium term as well.

First, in order to ensure investor protection and to guarantee a full open architecture, we consider that fluid circulation of funds in Europe without undue risks is crucial, including regarding **clearing and settlement processes**. On these last processes, we consider that some aspects of them should be tackled through a Directive, such as segregation of functions for instance.

Second, our industry will have to be involved in developing European defined contribution schemes, building up on the good progress made through **the IORP Directive**, which fits mores the defined benefit and insurance based schemes – which will of course continue to play a prominent role in the European funded retirement schemes market.

You will find below **(Annex 1)** our answers to the detailed questions raised by the Green Paper.
If you wish to get more details or comments on any point of this letter, please do not hesitate to contact me (a.leclair@afg.asso.fr, phone: 00 33 1 44 94 94 01), our CEO Pierre Bollon (p.bollon@afg.asso.fr , phone: 00 33 1 44 94 94 14 or 00 33 6 12 30 40 00) or our Head of International Affairs Division Stéphane Janin (s.janin@afg.asso.fr, phone: 00 33 1 44 94 94 04).
Yours sincerely,

Alain Leclair

ANNEX 1: DETAILED ANSWERS FOLLOWING THE GREEN PAPER'S STRUCTURE

1. PRIORITY ACTIONS

By monitoring the consistent and efficient implementation of existing rules, the Commission carried out or intends to carry out:

- *Publication of an interim report on how national authorities have implemented the CESR guidelines on transitional provisions regarding UCITS III;*

- *Encouragement to CESR to adopt by the autumn of 2006 guidelines on how to simplify notification procedures;*

- *Publication of an assessment of how Member States have implemented the Commission's two Recommendations of April 2004 on the use of derivatives and the simplified prospectus*[8]*;*

- *Adoption by summer 2006 of implementing legislation on eligible assets of UCITS. This issue is currently dealt with by CESR, which will deliver its advice to the Commission in early 2006.*

Q.1: *Will the above initiatives bring sufficient legal certainty to the implementation of the Directive?* **The answer is: Unfortunately, No**

- We strongly support the series of actions already undertaken by the Commission and CESR to find a path for more consistent and harmonised implementation of the UCITS Directive. We are already grateful to the Commission and CESR for these restless efforts. And we would be extremely pleased if we were able to notice that they reached their goals. Unfortunately, our diagnosis is that, although progress has been and can still be made, many difficulties have their roots in the wording of the Directive itself but also in the system it has devised.

- Regarding *simplification of notification procedures*, the current Articles 44, 45 and 46 of the UCITS Directive prevent a 'true' product passport. Even if CESR were able to find an agreement among regulators on the process to follow regarding cross-border notification, the UCITS Directive leaves some significant powers of interpretation of the relevant Articles in the hands of the host Member State, in particular as marketing and advertising have not been harmonised by the Directive. A true product passport is not possible in practice as long as the existing wording of the relevant Articles of the Directive remains. Our members need a lighter and shorter (two months being too long for a real product passport) regime for notification procedure through lighter powers for the Host Member State authorities (in line with the general 'country of origin' principles of the Treaty). This can be achieved only if the Directive does not allow national regulators to reject funds domiciled in another Member State on the ground of the existing Directive provisions. Moreover, the list of documents to be submitted should be shortened (e.g. annual report).

[8] Recommendations 2004/383/EC on the use of financial derivatives and 2004/384/EC on the simplified prospectus
A first report on the implementation of these Directives was published by CESR on 7 July 2005.

- Regarding *transitional issues and Commission's Recommendations on derivatives and the simplified prospectus*, consistent implementation across Europe is crucial. The absence of consistency in implementation will unavoidably lead to new cross-border barriers. In this context we would like to point out that the Commission should – pro-actively – accompany implementation with a more precise advice <u>and</u> in a text of binding nature (as compared to the non-binding Recommendations it adopted).
  In particular, we can already acknowledge today that the Recommendation on the Simplified Prospectus - because of its non-binding nature notably - fell short of achieving its goal to create a fully harmonised marketing tool to the benefit of European household investors and the fund industry. In assessing the implementation of its Recommendation, the Commission should reconsider it and remember that the simplified prospectus was aimed at both:
    - easing cross-border distribution in using a European single harmonised document on the basis of which units of UCITS may be purchased without any possible request by the host country's competent authority for additional information;
    - providing European investors for simple, reliable and comparable information (including an harmonised TER) about the essentials of a fund before investing in this fund.

  In practice, simplified prospectuses are often as long as the full prospectus, look very different from one country to the other and include more or less diverging information. TERs in particular do not have the same scope and hence differ for the same fund.

  In some Member States, the so-called simplified prospectus became even longer than its predecessor document, without any added value for the investor. It was recognised by some national regulators which have now to consider setting up 'super-simplified' prospectuses.

  Due to the lack of legal certainty coming notably from the non-binding nature of the Recommendation on the simplified prospectus, cross-border distribution has become more complicated and more expensive than before. The Commission should reconsider the approach taken by the UCITS Contact Committee, which ended in the above-mentioned Recommendation and consider returning to the way shown by the FEFSI/EFAMA model for instance.

  A European harmonised simplified prospectus becoming mandatory in a precise format through a European binding text (European Regulation) following the principle of <u>maximum harmonisation</u> would solve the issue.

- Regarding *eligible assets*, it seems too soon to draw conclusions from the final CESR advice, which cannot be known yet. However, in our reply to CESR's first consultation, we stressed the fact that a clear-cut had to be made between Level 2 and Level 3 – as this lack of differentiation between the two Levels were generating potential legal uncertainty for our members. However, in spite of CESR current efforts to widen the list of eligible assets as far as possible, AFG members consider that the existing provisions of the Directive do not allow for a sufficient upgrading. The result is that UCITS could become 'outdated' in the future by competing, less regulated financial saving products.

Q2: *Are there additional concerns relating to day-to-day implementation of the Directive which need to be tackled as a priority?* **The answer is Yes**

At the current stage of progress on MiFID level 2 implementing measures, our members are concerned about the linkage between the UCITS Directive and MiFID.

The positive aspect of the MiFID could be that the Commission might use the section on distribution and suitable advice to improve the single market for investment funds. This approach might also help to solve two core issues raised by the Asset Management Expert Group under the auspices of the Commission in 2003/2004: how to improve the quality of distribution and advice on the one hand; how to create a level playing field between funds and other retail saving products at the point of sale (see additional comments in the next section).

However, our members have difficulties in understanding the potential linkage in practice between the two Directives on these aspects. Moreover, other aspects of the MiFID might impact negatively the activities of the large majority of AFG members (those who both manage collective investment and portfolio management), regarding organisation requirements and conflicts of business rules, as two different sets of rules would cover them.

Another additional concern is the discrepancies of tax treatments between European investors and funds and the lack of tax consistency between Member States. Our members consider that taxation is a key issue and that it can become a barrier to the development of their industry. Therefore, the tax issue must be tackled in line with the general ‘Single Market’ principle.

2. MAKING BETTER USE OF THE CURRENT FRAMEWORK

This section of the Green Paper deals with two issues: the management company passport and the question of distribution and advice. Both are very important issues, but which cannot be solved under the current regulatory framework unfortunately.

- THE PASSPORT FOR THE MANAGEMENT COMPANY

Q3: *Would an effective management company passport deliver significant additional economic advantages as opposed to delegation arrangements (please indicate sources and likely scale of expected benefit)?* **The answer is Yes**

There is a clear need for a management company passport. This '*ability for a management company to establish and manage a UCITS constituted in another Member State - regardless of the legal structure of the UCITS – by means of a branch or under the freedom to provide services*' will constitute a necessary complementary tool to the product passport. Even if the current difficulties encountered in UCITS cross-border registration are solved, there will still be good reasons to set up local funds (local investor preferences, type of client, tax regulation). This is why the "real" management company passport is one of our top priorities.

The product passport aims at disseminating the same product from one Member State to the whole European Union - such a product appearing as a pure pan-European product. On the contrary, the principle of a management company passport will not be to 'export' the product but the company management services: the company will be able to provide for (potentially) the same product through *local domiciliations* in order to address *local customers* (not only retail investors but also institutional investors which invest in local products preferably). Therefore, the first advantage of the management company passport will be to offer a potential of growth in sales at the European level through the easy/non-expensive use of a local branch or free provision of services.

By contrast, what is the situation today? The Green Paper mentions delegation arrangements as an existing solution. In general, the faculty of delegation arrangements constitutes an opportunity and can generate cost savings if decided for economic reasons. But if put in place for the single reason of mending the lack of management company passport, delegation has some significant drawbacks.

First, through the need for setting local management companies in *each* Member State where it is wished to domicile a UCITS, it creates obviously a related cost in capital, staff and administration:

- **Capital**: up to 10 M€ per Member State, to be multiplied by the number of Member States where the management company wishes to offer the product. Among our members, either there are France-based global players which have then to set up six or seven different local management companies to be able to offer locally domiciled products to local (retail and institutional) investors. Or there are France-based medium-sized or 'entrepreneurial' players which have difficulties facing such local investments in setting up local management companies

- **Staff and administrative costs**: according to real cases reported to us, the cost of those is around 500 000 € per year for AuM around 35 M€ under management in one case. In another case, for each compartment, the related staff and administrative costs amount to around 100 000 € per year for 50 M€ of AuM.

Second, in order to answer the question of the Commission on **delegation arrangements**, let us mention that:

- As a general principle, the faculty of delegation of functions constitutes a progress for the industry as soon as it is determined for cost savings reasons (which is usually the case)

- However, in the context of the lack of management company passport, delegation arrangements are not motivated by cost savings but by the wish to cope with the obligation of setting a local management company in the Member State where the UCITS is situated. In this specific case, delegation is a source of cost which could be saved by a true management company passport.

- Furthermore, it appears that some functions - such as fund administration - cannot be delegated across borders.

- All things being equal, these legislation-driven costs impact negatively the management fees to be paid by the investors.

In addition to the question raised by the Commission, AFG wishes to add that the management company passport is not only a question of costs. It is also a question of **better transparency for the customer**: the knowledge by the customer of the identity of the ‘real’ management company is easier in the case of a passport, contrary to the case of delegation, where this delegation (and possibly sub-delegation) dedicated to cope with the requirement of the UCITS Directive can introduce opacity in terms of management chain (as well as in terms of related costs).

Q4: *Would the splitting of responsibility for the supervision of the management company and the fund across jurisdictions give rise to additional operational risks or supervisory concerns?* **The answer is: Not necessarily**. *Please describe sources of problem and steps that would have to be taken to manage such risks effectively.*

Interestingly, already today such management company passport is already possible in one Member State. In Italy, the Consolidated Finance Bill (Legislative Decree 58/98) has been modified in 2003 to grant SICAVs the right to designate as management companies “*harmonised management companies*”[9] authorised in other Member States. Although there are no practical examples of such arrangements yet, it seems to be a good example for a future management company passporting mechanism. Such a mechanism also appears to be possible in the UK.

Following the Italian model, the fund would remain under the supervision of the regulator of the Member State where the fund is established, while the authorisation and supervision of the “*harmonised management company*” is left to the supervisor of the Member State where the management company is registered. The supervisor of the Member State where the fund is located shall supervise the compliance with fund rules by the management company and could have the right of inspection and review of fund documentation, based on national regulation. As a result, the management company will be subject to the supervision of two regulators, one concerned with the fund (as the product), and one concerned with the fund manager.

[9] “*Harmonised management company*” is a company having its registered office and head office in a Member State other than Italy and being authorised under the UCITS Directive to provide the service of collective portfolio management (as per Legislative Decree 58/98 and following amendments).

In any case, with the current system of delegation arrangements, in the specific context of lack of management company passport, supervisors have to agree on and try to monitor delegation schemes which are much less straightforward than management company passports. The company management passport will increase transparency in management structures to the benefit of investors, and will ease the work of regulators as well in terms of monitoring: higher transparency will make the work of supervisors more efficient and timely. Furthermore, the decrease in the number of management companies to be supervised by the supervisors would ease their workload.

In the medium term, co-operation between regulators of the management company and of the fund would help making the network of regulators a reality (as mentioned by CESR)[10].

Last but not least, some national securities regulators (UK FSA for instance) clearly stated in recent fora that such an approach for a real management company passport was realistic from their point of view. The current UK Presidency of the Council supports such an approach as well.

- DISTRIBUTION, SALES AND PROMOTION OF FUNDS

For the Commission Asset Management Expert Group, quality distribution and good advice were two key points in the asset management value chain. AFG thanks the Commission for taking this issue on board. In this context, the Green Paper and the Background Paper raise a number of issues.

Q5: *Will greater transparency, comparability and attention to investor needs in fund distribution materially enhance the functioning of European investment fund markets and the level of investor protection? Should this be a priority?* **The answer is Yes to the first question. Regarding the second question, AFG's opinion is that it should be considered as a priority in the wider context of a need for ensuring a level playing field with substitute products – and also in relation with the clarification of responsibilities of distributors**

As already pointed out above, quality distribution and good advice are key issues for the investment funds industry not only in Europe, but worldwide. However it must be underlined that speaking in this context only about investment funds is unfair and does not take into account the environment in which fund distribution takes place.

In fact regarding distribution, investment funds are competing with an increasing number of other savings/investment products, which often can operate under less onerous conditions with respect to taxation, investment regulation, supervision and disclosure. The product range is very broad, covering regulated products such as pension products, certificates, securitized derivatives and structured notes. Some of them are so similar in content and purpose to investment funds that it is often difficult for the normal retail investor to distinguish them from a UCITS. In most cases the transparency and investor protection requirements applied to those 'substitute' products are less burdensome than those applied to UCITS (for more details, see later under "*Competition from substitute products*").

In general regarding transparency, AFG wishes that a **level playing field** be ensured between all competing financial products. Therefore, regarding **product transparency** of UCITS, AFG opposes to further disclosure beyond the information that fund managers must already

[10] It might also contribute to the building of a single securities and/or asset management regulator (as requested by AFG, in particular in AFG's response to CESR '*Himalaya Report*' in early 2005)

today provide under the existing UCITS Directive and in particular in the simplified prospectus.

Regarding the **distribution fee transparency**, it should, if necessary, be let to the distributor. Indeed, these fees and costs can only be properly expressed with respect to a particular sales offer and to an individual client taking into account fee-defining elements such as size and type of investment for instance[11].

Q6: *Will clarification of 'conduct of business' rules applying to firms which (distribute) retail funds to investors contribute significantly to this objective? Should other steps (enhanced disclosure) be considered?* **Yes to the first question: to a large extent through MiFID. No to the second question.**

The relationship between the distributor/advisor and the final investor, in particular regarding advice, is regulated by MiFID. Under this approach, MiFID will probably solve one of the main problems raised in the report of the Commission's Asset Management Expert Group, i.e. 'the provision of quality distribution and good advice'.

However, in order to ensure a level playing field with substitute products, no further disclosure should be considered for UCITS.

Q7: *Are there particular fund-specific issues that are not covered by ongoing work on detailed implementation of MiFID conduct of business rules?* **Yes. Self-regulation should tackle these non covered issues to a large extent. Moreover, the linkage between the UCITS Directive and the MiFID (in particular the responsibility of the distributor) will have to be examined carefully by the Commission – as well as the impact of the e-commerce and distance marketing Directives. Lastly, anti-money laundering monitoring by the distributor should be dealt by the European Commission.**

Neither the UCITS Directive nor MiFID define the relationship and the sharing of responsibilities between the management company and the distributor. This gap must be filled in and the most adequate way to do so would be by establishing industry best practices. The EFAMA Board of Directors has just agreed on such *Industry Best Practices*, including a set of rules on "*policies as to selection, use and monitoring of distributors*". EFAMA is going to start discussion with the European Commission and CESR on these rules and how to implement them.

To conclude this section, AFG wishes to stress that the Commission will have to ensure that both perspectives of the current UCITS Directive and of the MiFID regarding investor protection (through product harmonisation and disclosure in the UCITS Directive; through distribution/suitable advice in MiFID) are consistent with each other. But the Commission will have also to be aware that trying to achieve investor protection on the production side mainly through product regulation is too restrictive and inhibits innovation.

Furthermore, it must be noted that the complexity of the regulatory environment regarding public distribution of investment funds was significantly increased by two other regulatory initiatives by the Commission: the e-Commerce and Distant Marketing Directives. In particular, it seems that thanks to these directives, distribution of non-harmonised products via internet is possible even if their distribution is officially restricted or even prohibited in the Host Member State. Some adaptation/clarification of the relevant directives on the topic by the Commission or the European institutions at large would be welcome.
Lastly, regarding anti-money laundering measures, let us recall that contrary to the management company (as a producer), the distributor knows the identity of the client and is better placed to know the origin of the assets to be invested.

[11] Reference to MiFID draft implementing measures should be made in this matter

3. LONG-TERM CHALLENGES

The issues raised in this last section of the Green Paper are those which go beyond the existing regulatory framework and which, by definition, need new regulation to be solved. From the industry's point of view, **some of these issues are first priorities**, as they are closely linked with its efficiency – even though deliveries might be in the medium term only.

Notwithstanding a significant number of critical comments to be made, it must be underlined and welcomed that the Commission recognises that the industry is currently undergoing profound structural changes and that the environment in which it acts is becoming increasingly competitive. The Commission has understood that a single market in investment management is to be achieved through the creation of a level playing field not only among funds across borders, but also between funds and other retail savings/investment products. The Commission also recognises that any future regulatory framework for the fund industry must be '*capable of representing a viable basis for the successful development of the fund industry over the longer-term while assuring a high level of investor protection*'.

Regarding the five main issues the Commission is focussing on, we agree that before starting significant changes of the current regulatory framework, one must discuss what is needed in order to achieve the above-mentioned goal. We also agree with the Commission that in many cases progress cannot be achieved within the existing framework and that regulatory adjustments might be necessary.

- ENHANCING THE COST-EFFICIENCY OF THE INDUSTRY

Enhancing the cost-efficiency of the industry is crucial for AFG members. We agree with the Commission to take the four issues of *cross-border fund mergers, fund pooling, passport for the depositary and fund processing* on board. From AFG's point of view, fund mergers and pooling are of particular importance and should be considered among the first series of priorities mentioned in the first part of this letter. In particular, mergers of funds have already been tested successfully in France, with around 600 mergers since 2003.

Q8: *Is there a commercial or economic logic (net benefits) for cross-border fund mergers? Could those benefits be largely achieved by rationalization within national borders?* **The answer is Yes to the first question and No to the second one.**

Q9: *Could the desired benefits be achieved through pooling?* **The answer is Yes, through master-feeders. But it does not mean that cross-border mergers are not necessary.**

Cross-border mergers of funds and domestic mergers of funds have the same goal, i.e. mainly:
- rationalising a range of funds for commercial purposes, and/or
- cutting unnecessary costs or making substantial economies of scale for economic purposes.

However, their strategy and use are totally different: one is used to merge funds domiciled in two different Member States within a pan-European range of products and the other one is used to merge funds domiciled in the same Member State within a national range of products. As a consequence, we do not believe that the commercial effects and economic benefits of fund mergers could only be achieved within domestic fund mergers only.

As a general comment on cross-border fund mergers and pooling, we would like to underline that their relative usefulness will depend on the specific investment company strategy, geographic presence, history (in case of past mergers or firm acquisitions), as well as national specificities. It is therefore totally inappropriate to think of pooling necessarily as an alternative to mergers. The industry needs all of these tools (along with the management company passport) because "one size does not fit all".

For the France-based investment funds industry, both cross-border mergers of funds and cross-border pooling (under the form of 'entity pooling', i.e. cross-border master-feeders) are of highest priority.

The subjects of cross-border mergers of funds and of pooling are very complex. Preparatory work has already been carried out and very helpful data on these issues have been collected at French and European levels this year:

- *Regarding cross-border fund mergers*:

In France, the domestic experience of fund mergers was very successful. Around 600 fund mergers took place in France since 2003.

At the EU level, one of AFG members, Invesco, published a study in January 2005, which clearly shows the economic need for action by the European Commission.[12]. Another study, from Lipper Fitzrovia[13] on actively managed equity funds domiciled in Luxembourg, clearly shows that bigger funds have a significantly lower average TER. While the TER of funds with up to $25 Million Assets under Management amounts to 2.01%, the TER for funds with up to $100 Million AUM decreases to 1.75%.

Making cross-border mergers of funds possible would constitute an important step towards the consolidation of the European fund industry, resulting in significant economies of scale and therefore benefits for investors.

A possible regulation of fund mergers could be based on the principles of the Directive on cross-border mergers of companies with share capital and on the recently modified Directive on taxation of mergers, taking into account the special features of the fund industry.

The following principles should be introduced:

- Technical mechanisms for cross-border mergers: a merger should be possible through either a "*pure merger*" where two entities merge to build one continuing or new entity, without a shell remaining, and/or "*transfer in specie*" (redemption and subscription in specie, the remaining shell to be wound up);

- Voting requirements: it seems necessary to put provisions in place to ensure that voting does not become an insurmountable barrier for cross-border mergers. Vote casts (**actual votes**) should be taken as the basis for determining quotas, rather than referring to the total number of unit holders.

We recognise that taxation is a key issue, and that tax can become a barrier to cross-border mergers. Therefore, the tax issue must be tackled at three levels:

- Investor level: as regards taxation of investors in the case of a merger, a precedent was set to introduce a measure of legislation on this subject by the Taxation of Mergers Directive, which establishes the principle that a merger does not result in a taxable event for the investor. This principle should also be used as a solution for fund mergers;

[12] '*Benefits of an integrated European Fund Management – cross-border merger of funds, a quick win?*', January 2005

[13] Economies of Scale and Consolidation in Collective Funds (March 2005)

- Portfolio level: a merger of funds should not result into a taxable event at portfolio level – typically in the form of stamp duty or transfer tax on the sale of assets;

- Fund level: a merger of funds should not incur tax at fund level throughout the Member States.

The same taxation problems can arise from domestic mergers and are of particular importance if fund investors reside in various countries. This situation shall arise even more in the future, as more funds are sold cross-border. Ideally, any future merger regulation should cover cross-border as well as domestic mergers, so as to ensure equal treatment of investors regardless of their country of residence and of the type of merger - in consistency with the Single Market principle.

- *Regarding "pooling" in the form of cross-border Master-Feeders*:

AFG supports the Commission proposal to examine the issue of pooling within a Working Group, as this subject deserves a high level of care. However, in spite of its complexity, we urge the Commission not to wait for a long term delivery on it, as the problem already arises today and as **at domestic level entity pooling (master-feeders) has already been tested very successfully**.

Entity pooling (master-feeder funds) and virtual pooling are two possible pooling techniques; the advantages and drawbacks of each form of pooling are different.

It is important to recall to the Commission that regarding the so-called master-feeder structures:

- domestic master-feeders have already been tested successfully in France and other Member States. Master-feeders offer a reduction in transaction fees (both custodian and broker commissions), operational costs as well as a reduction in administrative variable costs – to the benefit of investors. Still from an investor perspective, master-feeders are totally transparent and probably easier to explain than other pooling techniques (in particular virtual pooling – which might raise questions about the operational risks involved, the need for complex contractual arrangements and valuation processes)

- the advantage of master-feeders lies also in the benefit/interest for the investor to invest in a dedicated feeder

- on cross-border master-feeders, the European Parliament already agreed ten years ago on the necessity to introduce this option into the UCITS Directive and – following this opinion – the Commission had even made a proposal [14].

Thus, European cross-border master-feeders are for us a clear priority. On the contrary, AFG considers that the case for virtual pooling still remains to be made, in particular from an investor perspective, as contrarily to master-feeders it generates specific organisational risks, substantial IT and control investments as well as financial risks. Moreover, virtual pooling is less transparent: therefore, in case of virtual pooling, investor information (and thus investor protection) would be more complex and less efficient.

[14] As part of an amended proposal for UCITS II, which was withdrawn when UCITS III was launched [COM(94) 329, OJ C 242 of 30.08.1994, p. 5].

Q10: *Is competition at the level of fund management and/or distribution sufficient to ensure that investors will benefit from greater efficiency?*

Q11: *Which are the advantages and disadvantages (supervisory or commercial risks) stemming from the possibility to choose a depositary in another Member State? To what extent does delegation or other arrangements obviate the need for legislative action on these issues?*

The answer to Q10 depends on how the question is understood. At the level of management companies in particular, competition is already very high (e.g. in France where around 500 management companies compete), so any efficiency improvement or innovation benefits investors. The answer would be Yes then. But at the same time, we need improvements of the legislation to increase efficiency and facilitate innovation even more. In that sense the answer would be No.

The answer to Q11 is the following. Regarding the advantages and disadvantages of the cross-border depositary passport, this issue has been on the Commission agenda for years; it was already part of the 1993 UCITS II proposal, it came up again in the context of the discussion on UCITS III and culminated last year in the Commission's Communication on '*Regulation of UCITS Depositaries in the Member States: Review and possible developments*'.[15]

AFG Members will welcome the principle of the cross-border depositary passport, provided that core depositary functions, qualifications and eligible type of institutions are harmonised[16].

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[15] Communication COM(2004) 207 from the Commission to the Council and the European Parliament of 30 March 2004.

[16] Here are some possible ideas in this respect:

- *Core depositary functions:*
  - *Bookkeeping of Custody accounts:*
    - Accounting for cash accounts and securities accounts in the name of the UCITS
    - Safekeeping of assets and their transfer on demand of the UCITS according to the measures laid down by the market authorities.
    - Settlement of instructions from the management company
    - Clearing of derivatives instruments traded on regulated markets
    - Payment of dividends and income on assets held in the name of the UCITS
    - Processing corporate actions on these assets
    - Tax treatment linked to the UCITS
    - Centralizing the money flows related to purchases and redemptions when the UCITS is not listed on a market.
  - *Supervision:*

    The depositary should check the compliance with, and ensure the respect by the management company of, the
    - Investment policy set out in the relevant regulation or in the prospectus
    - Rules for calculating the value of UCITS units
    - Legal provisions.

- Eligible institutions:

With regard to the type of legal entity that should be eligible to exercise depositary functions, limiting eligibility to credit institutions might ease supervisors' acceptance of the passport, since credit institutions are already accepted everywhere as depositaries and their capital requirements are harmonised at EU level.

- Liability:

Art. 9 and 16 of the UCITS Directive state that a depositary shall be liable to the management company (or the investment company in Art 16) and to the unit-holders "*for any loss suffered by them as a result of its unjustifiable failure to perform its obligations or its improper performance of them*". These provisions point to an obligation of means by the depositary, not an obligation of results.

With regard to counterparty risk for specific transactions (such as OTC derivatives, fund-of-funds) the depositary should not be liable and the risk should borne by the fund except in cases where the management company did not exercise adequate care in the choice of counterparties.

- Investor protection

Investors would maintain the possibility to obtain legal redress in their country and might have access to a compensation scheme (depending on national regulation or industry agreements, particularly if the depositary is a credit institution).

- Conflicts of interest

Conflicts of interest can be effectively dealt with through adequate disclosure (e.g. in the Market Abuse Directive, there is an obligation of adequate disclosure of conflicts of interest for those persons providing investment recommendations such as financial analysts for instance) and/or Chinese walls (regulated for credit institutions by the Consolidated Banking Directive).

We must also once again underline that delegation (by the depositary) can only solve certain problems, in particular as rules on delegation differ from country to country. As compared with a depositary passport, it creates unnecessary costs, as these costs are not generated by a cost saving principle but by the wish to circumvent the lack of depositary passport.

Q12: *Do you think that on-going industry-driven standardisation will deliver fruit within reasonable time-frames?* **The answer is Yes.** *Is there any need for public sector involvement?* **The answer is No for direct public sector involvement, except if industry-driven standardisation cannot deliver in the medium term or proves to be impeded by national or European regulations. However, AFG wishes regulators to commit themselves on the acknowledgement, support and use of such standardized technical languages or processes set up by the industry.**

We agree with the Commission that common standards in fund processing would significantly increase the efficiency of the European investment funds industry, in particular regarding cross-border distribution. We also very much welcome the Commission's support for the industry's efforts to improve fund processing.

To address this issue, EFAMA's Fund Processing Standardisation Group (FPSG) has published a number of recommendations aimed to converge towards industry-wide standards. These standards would enable firms to communicate electronically, using messages constructed to international open market standards (ISO 20022) and referring to universally recognised unique identifiers for funds and the actors involved in back-office procedures. Fund managers should also summarise in a fully harmonised single pan-European document – the Fund Processing Passport – the essential information on their investment funds in order to facilitate funds processing.

We very much hope that these Recommendations will deliver fruit within a reasonable time frame. A clear endorsement by the fund management industry should give a clear signal to other market participants, especially fund distributors, that the fund industry is moving to a more harmonised and efficient system of fund processing. This will facilitate their decisions to adapt their back-office systems to the new standards, and this will result in more standardisation and automation of fund processing.

To encourage industry-wide endorsement by all players involved in fund processing, AFG members support the recent adoption by the EFAMA Board of Directors of a fourfold "*Fund Processing Action Plan*":

- To draft a "business case model" to facilitate the endorsement and implementation of the FPSG recommendations by fund groups, distributors, service providers as well as national associations;

- EFAMA members' associations will apply for identifier codes (BIC/BEI) for their members and encourage the use of ISIN codes to identify funds at the level of each individual share/unit class;

- EFAMA member associations will also encourage the formation of national market practice groups for fund processing (already existing in France, Germany, Italy, Luxembourg, Switzerland and the United Kingdom);

- EFAMA will organise a Round Table with all interested European/international organisations to discuss the case for standardisation in fund processing.

We are of the clear opinion that public sector involvement in the shaping of the work itself should be avoided. By nature, standardisation of technical languages or processes must be tackled by the professionals themselves. However, AFG wishes regulators to commit themselves on the acknowledgement, support and use of such standardised technical languages or processes set up by the industry.

- MAINTAINING HIGH LEVELS OF INVESTOR PROTECTION

Whilst recognising the high level of investor protection provided by the UCITS Directive, the Commission expresses concern that current regulation might not be sufficient to cope with emerging new risks and changing expectations in markets, and points out that CESR will work on a convergence among European supervisors regarding the prevention of conflicts of interest and the investor protection safeguards included in Article 5f and h of the new UCITS Directive.

Furthermore, in its Background Paper, the Commission staff mentions various industry self-regulatory initiatives, as well as the lack of a pan-European widely recognized industry code. It is suggested that "*appropriate regulatory intervention*" will be inevitable if self-regulation is not adequate and enforceable.

Q13: *Does heavy reliance on formal investment limits represent a sustainable approach to delivering high levels of investor protection?*

AFG fully agrees with the Commission that it is necessary to continuously maintain investor protection safeguards if investment funds should become the "vehicle of choice" for retail investors, in particular in the field of second and third pillar pension.

However, it also must be underlined that already today:

- UCITS are subject to more detailed investment rules than any other savings/ investment product

- The UCITS Directive provides through the simplified prospectus far more product information than any other savings/investment product and that UCITS are far more transparent regarding costs and fees than any other savings/investment product. In summary, UCITS provide already today a far higher level of investor protection than most of other savings/investment products.

We must repeat that over-regulation and gold-plating would hurt the industry and client interests unnecessarily as we are in competition with other savings/investment products which do not have such expensive investor protection rules.

The European investment funds industry, including of course the France-based one, always argued that it will take care of strengthening its integrity and already years ago, well before the scandals in US, the industry put this issue on the top of its agenda. Last year we agreed on a set of pan-European High Level Principles to be adopted by EFAMA and recently these High Level Principles were completed by pan-European industry best practices. AFG members are convinced that with these standards we can contribute to the prevention of conflicts of interest and to the implementation of the investor protection safeguards included in Article 5f and h of the new UCITS Directive. The industry is proposing to discuss this issue with both the European Commission and CESR.

We agree in principle with the Commission that the heavy reliance of the UCITS Directive on detailed investment limits and risk-spreading rules will be probably in the future no longer the right approach to protect investors, and we are prepared to discuss other approaches with both Commission and CESR. In any case, the conclusion drawn both by the Commission and AFG that reliance of the UCITS Directive on detailed investment limits and risk-spreading rules is probably no longer the right approach makes the case of the need for a Lamfalussy-formatted Directive - oriented to regulation of players of the value chain at Level 1 through essential principles and to regulation of products at Level 2 in order to adapt them rapidly if necessary in a fast changing environment.

Q14: *Do you think that safeguards – at the level of the management company and depositary - are sufficiently robust to address emerging risks in UCITS management and administration? What other measures for maintaining a high level of investor protection would you consider appropriate?*

We think indeed that the safeguards regarding management company and depositary in the UCITS Directive are robust to address emerging risks in UCITS management and administration. However a clearer definition of the depositary's responsibilities would strengthen investor protection.

Finally, we fully agree with the Commission that the corporate governance initiatives for listed companies should not be extended to funds without taking into account fund specificities.

- OPERATIONAL RISK, OUTSOURCING AND CAPITAL REQUIREMENTS – IN RELATION WITH THE BACKGROUND PAPER

In its Background Paper, the Commission staff seems to be of the opinion that operational risks are increasing, in particular those from outsourcing, and the Commission raises the question whether the current regime for capital protects investors sufficiently in an environment of changing risk patterns and against the background that an increasing number of management companies runs "more and more services".

- *Outsourcing*

Whilst recognising that the risks patterns in the industry are changing with the increased reliance on outsourcing, we must state that outsourcing does not by itself increase operational risks in asset management. On the contrary, outsourcing may permit management companies to access expertise and technology at a lower cost and/or higher quality and thus it can lead to lower overall operational risks.

We agree, however, that outsourcing poses a number of challenges both for management companies that choose to undertake such a strategy and for the regulators of such companies.

With respect to the management company, outsourcing is detailed and sufficiently regulated in Article 5g of the UCITS Directive, as it was discussed extensively in the run-up to the modernisation of the UCITS Directive. These rules today constitute an important "benchmark" and are widely accepted as best practice.

In summary, with respect to Article 5g, outsourcing arrangements should not diminish the obligations of the management company to investors and regulators and asset managers should be in a position to monitor effectively at any time the activity of the undertaking to which the mandate is given. This requires that asset managers maintain suitable oversight and control systems to be able to identify, assess, monitor and manage operational risks arising from outsourcing.

On the other hand, the increased reliance on outsourcing does not require higher minimum capital requirements as the most direct approach to limit operational risk is to implement carefully monitored risk management systems.

Regulators have also a special role to play to help cope with the challenges posed by outsourcing. As an integral part of their ongoing assessment of a regulated entity, regulators should watch to ensure that high standards of compliance and risk management systems are maintained. In order to be able to accomplish their mission, regulators should be able to obtain any relevant information pertaining to the outsourced activity.

Regulators should also be informed of the potential systemic risks posed by the concentration of outsourcing services within a limited number of service providers, and take steps to identify cases where a significant proportion of outsourcing firms use a common service provider. We are, however, convinced that the development of outsourcing activities in investment management in Europe has not yet reached the stage where it could pose a threat of systemic risk.

However, although being rather keen to the general principle of outsourcing, outsourcing must be motivated by economies of scale or cost cutting. It must not been motivated by the drawbacks of European legislation. In this view, the development of delegation arrangements in order to circumvent the practical impossibility of the Management Company Passport by the existing UCITS Directive creates in fact additional costs. It is one of the reasons why a Management Company Passport is necessary.

- *<u>Other changing risk patterns</u>*

We take note of the Commission's views that asset management companies "*run more and more services*" and that the capital requirements for asset management companies "*should be assessed in order to know if they are suitable with the new AM company patterns and still protect adequately investors*". Apparently, the widening of the permitted activities of management companies under UCITS III and the increased offering of complex investment products using derivatives instruments had become a potential source of concern for the Commission.

Whilst agreeing that the increased complexity of investment products require specific expertise and suitable risk monitoring systems on the part of management companies, an increase in minimum capital requirements would probably not be the most effective approach to monitor these new risk patterns. The Expenditure Based Requirement (EBR) included in the new Capital Requirements Directive (CRD) and the UCITS Directive remains appropriate provided that the risk management procedures are met and enforced. Through CRD Pillar 2 there are also mechanisms proposed to address any additional risks.

- *<u>Further work to be done</u>*

Looking forward we are very much prepared to contribute to the study that the Commission has commissioned to understand better the trends and risks in our industry. This is indeed an important topic for our industry that we are following very closely. We could in particular help collect the asset management related data relevant to the studies and we could also contribute to achieve a better understanding of the current trends by sharing our views on specific issues and questions that would emerge in the course of the preparation of the study.

- COMPETITION FROM SUBSTITUTE PRODUCTS

Q15: *Are there instances resulting in a distortion of investor's choice that call for particular attention from European and/or national policy-makers?* **The answer is: Yes.**

AFG welcomes the fact that the Commission started looking at the regulatory framework for UCITS in a wider context.

Although in the Green Paper the topic is discussed under the heading "*Competition from Substitute Products*", a more appropriate title for this issue should be: "*Level Playing Field*" (as used in the Background Paper). At issue is not the protection from competition for UCITS products, but rather the removal of differences in regulatory and tax treatment to the benefit of investors and of the asset management industry in equal measure. The achievement of a Level Playing Field in the financial services industry would greatly increase competition, lead to the creation of a truly efficient Single Market with higher growth rates, and directly benefit investors through lower costs and better products.

How to define "*substitute products*"? We define as such any products giving exposure to the capital markets which look very similar to UCITS for investors. For example, structured products are often presented as alternatives to UCITS – in spite of different credit and investment risk profiles: UCITS invest directly in underlying assets while structured products are usually bonds issued by a financial institution - therefore the risk exposure is linked to the solvency of that issuer, which in turn makes use of complex derivative structures to pursue a specific investment strategy. Also, in many cases, structured products have specific risks (e.g. issuer risk – even if guaranteed) and often they might be more complex than UCITS.

Transparency is without doubt the most important factor ensuring investor protection. In that regard, we should distinguish between transparency at production level (information to investors to be provided by the producer) and at distribution level (information to be provided by the distributor). At production level, UCITS are a very transparent product, thanks to the provision of the prospectus (full and simplified), the annual and semi-annual fund reports, and to the frequent (mostly daily) publication of fund NAVs. UCITS offer a very demanding level of disclosure regarding costs (TER, portfolio turnover rate, entry and exit commissions), as well as investment objectives, risk and performance.

At distribution level, some substitute products are subject to a lighter regime than UCITS and other financial products which are subject to MiFID requirements[17]. In spite of MiFID, however, it is questionable whether comparable transparency of costs can be achieved[18], since pricing for structured products is subject to liquidity conditions and spreads can vary significantly, and the cost of derivatives as well as the lack of dividends might be excluded from the calculation.

In this context, the point is that the UCITS Directive approach to product regulation is <u>too restrictive and outdated</u>, and investors' interests could be effectively protected while granting more flexibility to the industry (e.g. regarding eligible assets).

Home Member State authorisation for new products is once again much more burdensome for UCITS: while some substitute products receive authorisation for an entire product class, and a prospectus can be filed for a whole programme with just supplements for individual issues,

[17] Unless Member States choose to exempt the reception and transmission of orders and advice related to UCITS, as provided in Art. 3 of MiFID (but as far as we know, only one Member State has chosen this option for the moment)

[18] Simply due to the fact that the point of sale does not know the cost structure

each new UCITS has to be authorised at national level and each amendment to the prospectus as well. UCITS are therefore faced with long delays in bringing products to market as compared to some substitute products.

Regarding Host Member States when a UCITS is notified cross-border, UCITS have to comply with local languages for documentation in a more burdensome way than substitute products. This situation generates an uneven playing field in two ways. First, it generates a delay in offering the relevant product as compared to a substitute product. Second, it also generates directly related administrative costs of translation and publication.

We are aware that to achieve a Level Playing Field for financial services, significant changes in lightening UCITS regulation would be required - both at production and at distribution levels. However, we strongly encourage the Commission to consider taking the necessary steps towards such a new regulatory framework.

- THE EUROPEAN ALTERNATIVE INVESTMENT MARKET

Q16: *To what extent do problems of regulatory fragmentation give rise to market access problems which might call for a common EU approach to a) private equity funds; b) hedge funds and funds of hedge funds?* **The lack of European regulation constraints the marketing development of many alternative investment funds (including real estate funds beside hedge/funds of hedge funds and private equity funds) both vis-à-vis European investors (lack of European passport, lack of tax harmonisation) and vis-à-vis non-European investors (lack of reassuring European regulation – in spite of wish for diversification of investments by those non-European investors). However, considering the specific features of each of the three types of alternative investments, any analysis and consequent action should be differentiated from one type of alternative investment to another one in order to fit with each of the three specific cases. It is also important that nationally regulated products are not forced to follow any future European rules, if they do not want to benefit from a passport and provided that they are managed by professional entities.**

The Green Paper itself discusses the alternative investment market in terms of hedge funds and venture capital funds, but does not consider other non-harmonised types of funds. What is the situation, for instance, regarding **real estate funds**, which today represent about 3% of all European investment funds?

In its Background Paper, the Commission quotes the conclusions from the FEFSI Real Estate Fund Workshop in November 2004, but does not make own suggestions. Instead the Commission plans to establish a working group to study whether harmonisation of alternative investments can help the development of the market for them. It is an undertaking, which we would, of course, strongly support as long as the **three** main categories of non-harmonised funds, i.e. including real estate funds beside hedge funds and private equity funds, are tackled.

More generally, the three pillars of alternative investments have to be taken into account by the European Commission in the context of the forthcoming expert working group on the issue of alternative investment.

For instance, the global annual survey by Russell on alternative investments has always taken into account real estate funds as well as the two other pillars of alternative investment.

Moreover, in its latest survey published in September 2005, it appears that the still growing development of alternative investments applies to real estate funds as well[19]:

- **Real estate represents the largest share of alternative investments in Europe at 60%**. In North America and Europe, respondents' use of real estate in allocation strategies remained virtually unchanged since 2003, with 55% of North American institutions and 66% of their European counterparts investing in real estate.

  Institutional investors in all regions except Australia anticipate raising the percentage of their total assets invested in real estate in 2007. In North America, the forecast rises from 6.7% in 2005 to 7.3% in 2007. For European and Japanese institutions, these numbers are expected to rise from 9.8% to 10.5% and from 3.4% to 6.1% respectively.

  The director of real estate at Russell even stated: "*Investors have historically been attracted to real estate for its competitive rate of return, ability to diversify a portfolio of financial assets, inflation-hedging attributes and income-generating capability. Although some regional differences exist, global allocations to real estate remain strong and are generally expected to increase by 2007. This is not an unexpected result given the longer period of experience and familiarity many investors have with real estate*".

  In our opinion, it makes the case for including real estate funds in the scope of the forthcoming working group of the European Commission.

- Regarding **hedge funds and private equity funds**, the Russell survey shows clearly the development of those alternative investments as well, at global level and particularly in Europe:

  - Compared to 2003, **hedge funds** have captured a growing share of allocations to alternatives in North America and Europe, where hedge funds now account for 10% of the overall allocation to alternatives, roughly double of the 6% and 5% levels found in 2003 respectively. "*Still mindful of the precipitous three-year market downturn that began in 2000, institutional investors are relying on hedge funds for absolute returns with low correlation to the traditional asset classes*," said Victor Leverett, director, hedge funds, Russell Investment Group. Between 2003 and 2005, the percentage of institutional investors using hedge funds grew from 23% to 27% in North America, **from 21% to 35% in Europe**. By 2007, institutional investors in North America expect to dedicate 9.1% of their portfolio to hedge funds, an increase from 7.7% for 2005. Similar changes are anticipated in Europe, where this figure is forecasted to rise to 7.2% from 5.3%.

  - Allocations to **private equity** are forecast to reach new highs in all markets in 2007, with European markets that have traditionally had lower allocations to private equity showing the largest expected increases. European tax-exempt institutions currently allocate 4.5% of their investment portfolios to private equity and are planning to increase to 6.1% in 2007.

But beyond the common development of the three types of alternative investments, it seems necessary to adapt the analysis for each of the three types, in order to avoid a 'one size fits all' approach.

Regarding **private equity funds** in particular, the following approach is asked by AFG members:

[19] '*2005-2006 Russell Investment Group Survey on Alternative Investing*', Russell Investment Group, 12 September 2005

- regulatory fragmentation has to be tackled in its two different dimensions:
  - the investor has difficulties to chose private equity funds in which to invest throughout Europe, because of very different national regimes
  - the asset managers have difficulties to orientate their investments (knowledge of the types of targets; eligibility…).

- The issue of possible European regulatory provisions on private equity funds must be differentiated depending on the type of investor**. Institutional/professional/qualified investor private equity funds** need some minimum regulatory and fiscal standards across the European Union in order to offer a European pattern for some private equity funds (the national regimes might stay in place and therefore this European regime would be a facultative one for investors). These standards must be understood as 'minimum' in the way that they would just define the general lines to be respected but would leave significant space for contractual arrangements between the investor and the manager. However, in spite of being minimum standards from this point of view (i.e. they will be complemented by contractual arrangements), the contents of these standards should be considered as maximum from a regulatory perspective in their transposition from one Member State to another one (i.e. Member States should not be authorised to introduce additional regulatory requirements beyond those European requirements).

Regarding **hedge funds/funds of hedge funds**, our members have expressed to us their following views on the situation:

- *Funds of hedge funds cannot be distributed de facto – even to qualified investors – across Europe today. Practical examples include the following ones*:

  - In some Member States, the regulator prohibits by principle any active marketing of EU foreign funds of hedge funds, including those registered by the regulator in another Member State

  - Some other Member States prohibit the marketing of funds of hedge funds registered by the regulator in another Member State when they are not listed on an EU exchange

Q17: *Are there particular risks (from an investor protection or a market stability perspective) associated with the activities of either private equity or hedge funds which might warrant particular attention?*

In its Background Paper the Commission is concerned that investor protection at Member States level might not be sufficient. Regarding Hedge Funds and Funds of Hedge Funds, the role of the prime broker and its relationship to the depositary are also discussed, without making specific recommendations.

The recent survey on Hedge Funds carried out by EFAMA under the chairmanship of Assogestioni and to which AFG participated very actively, proposes the harmonisation of hedge funds regulation either through new regulation or amendment of the UCITS Directive. It does not mean that all hedge funds have to be harmonised but that the possibility of creating harmonised hedge funds, and in particular funds of hedge funds, should be offered to European asset managers.

From a French perspective, let us recall that the risks of funds of hedge funds have been widely taken into account by the domestic regulation. For instance, 13 criteria have been set up by the regulator in order to be applied by the fund regarding underlying assets.

Q18: *To what extent could a common private placement regime help to overcome barriers to cross-border offer of alternative investments to qualified investors? Can this clarification of marketing and sales process be implemented independently of flanking measures at the level of fund manager etc.?*

Regarding hedge funds, in the short term, private placement (and thus a harmonisation of private placement rules) and/or a definition of the professional/qualified investor might appear an appropriate first step. Still, such an approach on private placement should ensure that it would not ease the placement of non-EU funds in Europe beside EU ones.

In the medium term, if we wish to develop the marketing of alternative investments towards both retail investors and a wide range of institutional investors requesting for 'retailised' products, there will be a need either for European legislation – preferably on the management companies (e.g. through the equivalent of the so-called '*programme d'activité*' in France); and/or through a European legislation on the product itself (as the practical examples shown in answering Question 16 above show that some national regulators could still have some domestic room for manoeuvre at the level of rules to be imposed on the imported product). Whichever the way followed, both ways would perfectly fit with a true Lamfalussy-formatted directive.

Moreover, the lack of tax harmonisation will have to be solved through harmonisation. In some Member States, some constraints on tax reporting prevent to a large extent the marketing of funds of hedge funds from other Member States.

Last, AFG wishes to raise the attention of the Commission on the opinion expressed by fund managers regarding regulation of hedge funds, according to a comprehensive global survey carried out by KPMG in 2005[20]. Here are some of the major findings of the survey:

- Fund managers welcome the regulation of hedge funds:
  with a majority of positive or neutral opinions both in the UK and in continental Europe

- This position is shared to a large extent by managers of hedge funds and fund of hedge funds:
  "*outside North America, more than two in three hedge funds or fund of hedge fund managers believe that the impact will be a net positive at best, or neutral at worst.*'

- Fund managers are diversifying into hedge fund type strategies:
  More than one third of fund managers are already involved in hedge funds or funds of hedge funds and anticipate major growth

- Worldwide, pension funds interest in hedge funds or fund of hedge funds is growing. Over the next three years, for example:
  - One in every three pension funds are likely to invest in single strategy funds – up from one in five in the past three years
  - Two in five will invest in multi-strategy funds – up from one in five in the past three years
  - One in two will invest in fund of hedge funds – up from two in five in the past three years.
- Moreover, pension funds consider that regulation will professionalize the industry and attract a new breed of investors.

[20] '*Hedge funds: a catalyst reshaping global investment*', KPMG, 2005

- MODERNISATION OF THE UCITS DIRECTIVE

Q19: *Does the current product-based prescriptive UCITS law represents a viable long-term basis for a well-supervised and integrated European investment fund market? Under what conditions, or at what stage, should a move toward principle-driven, risk-based regulation be contemplated?*

‘*General Overhaul or Repairing?*’ This is Commission’s succinct summing up of the issue.

Bearing in mind Commission’s long-term challenges and the fact that a satisfactory harmonised definition of what constitutes an eligible asset will probably be difficult to reach under the current ‘product approach’ of the Directive, many in the industry are of the opinion that **only a new and ‘Lamfalussy-conform’ approach would create a competitive regulatory framework for the European investment management industry**.

There can be no doubt that this would require a careful preparation and a co-decision procedure, a point highlighted by the Commission. This also means that the Commission would probably be happy if such new regulation were to be adopted by the end of its current term, that is in 2010. But the advantage would be that the heavy co-decision process would occur **only once for a significant period of time**, by concentrating only on '*essential principles*' (as stated by the Lamfalussy Report) which are more stable in duration than ‘*technical details*’.

The alternative is ‘*repairing*’. Here a step-by-step-approach is possible, but each step would mean modification of non-Lamfalussy legislation anyway and, therefore, systematic use of the co-decision procedure which ever the importance (in size or content) of needed changes and without proposing more flexible regulatory approach for the future.

4. PENSIONS

The reference in the Staff Working Paper (section 4.2.) to the industry's views on the role investment funds can play in occupational pensions is a positive step forward towards a level playing field for financial services. When we think about the Single market for investment management in the post-FSAP phase, the issue of using retail funds in occupational pension schemes cannot be neglected.

- ADVANTAGES OF FUND BASED PENSION SCHEMES

For both institutional investors and beneficiaries of pension schemes, investment funds are a perfect pension savings product. In many respects, they offer the qualities that were identified by the European Financial Services Round Table in June 2002 for a standard for Single Market pensions[21]: security, efficiency, flexibility, transparency, information provision, portability, mobility and user friendliness. Furthermore, they are also cheaper than most competing products.

We strongly believe that fund managers should contribute to bridge the pension funding not only by offering investment funds but also by operating directly as institutions proposing and managing pension schemes. Their distinctive expertise in product design, asset allocation and investor services make them ideal operators in both the second and third pillar pension markets.

The move in many countries from defined benefit (DB) to defined contribution (DC) schemes also calls for an important role of investment managers in retirement savings.

Indeed, DC schemes have much in common with investment funds. Above all, their providers invest assets they hold on behalf on their stakeholders, without taking in general any investment-linked liabilities. This is fundamentally different from the specific expertise required from DB schemes promoters that should ensure that their future pension liabilities are sufficiently covered by suitable assets by using appropriate asset liability management practices.

We are convinced that fund managers could contribute to the emergence of a solid and efficient market for DC schemes in Europe, as they would propose new solutions for financing pensions and offer increased choice for individuals. By way of illustration, they would be well placed to offer a new pension concept that EFAMA has proposed earlier this year – the so-called European Personal Pension Account, in line with the French PERCO and other similar defined-contribution national vehicles – into which employees could build up pension saving making choices among various investment funds and other investment options.

- THE FAILURE OF THE PENSION DIRECTIVE TO ESTABLISH A LEVEL PLAYING FIELD

We therefore regret that 2003 *Pensions Directive*[22] seems to limit the access to the occupational pension market to traditional pension funds (most often managing DB schemes only) and life-insurance companies, excluding investment managers and other institutions such as investment firms and banks. Neither the Commission nor the Council was at that time apparently willing to extend this possibility to other financial entities, with the consequence of

[21] *„One Europe, One Pension – Affording the Future“*

[22] Directive 2003/41/EC of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision (IORP Directive)

restricting the choice of occupational pension schemes and making the structure of second-pillar pension market less competitive.

Against this background, we very much welcome the Commission's new approach expressed in the Background Paper and we feel encouraged by recent remarks made by you at the IAPF Conference on 22 September 2005 where you stated: "*My objective is to enable private pension providers to fairly compete on a pan-European basis. Efficiency gains should in turn lead to better and cheaper pensions. These providers should of course also respect adequate and harmonised prudential and conduct-of-business rules*."

- WHAT SHOULD BE DONE?

The Commission should first take very seriously what is stated in Recital 12 of the IORP Directive "*... it is important that this Directive does not lead to distortions of competition ..... the Commission should carefully monitor the situation in the occupational pensions market and assess the possibility of extending the optional application of this Directive to other regulated financial institutions*". When drafting a new working program, this must not be forgotten.

Secondly, the Commission should promote a cost-effective interpretation of the IORP Directive to allow institutions for occupational retirement provision to operate without legal personality and outsource management functions to financial institutions to benefit from their expertise and existing infrastructures[23].

[23] as proposed in the EFAMA report on the European Personal Pension Account EPPA

5. TAXATION ISSUES

The forthcoming updated study on tax issues, in particular tax discrimination, carried out by EFAMA together with PriceWaterhouseCoopers[24] is going to conclude that the most significant tax cases of tax discrimination were solved. However what becomes more and more clear is that there are a number of other inefficiencies making taxation one of the biggest obstacles to the single market for investment funds:

- Onerous administrative requirements
- Taxation issues in the context of fund mergers and pooling
- Withholding taxes

6. ACCOUNTING ISSUES

Regarding the implementation of IFRS in the European Union, the domestic interpretations of IFRS standards diverge from the US one on *'dedicated funds'*. In the US, mutual funds won the exemption of deconsolidation of dedicated funds in the accounts of the relevant institutional investors. By contrast, in the EU, the industry did not get any similar exemption in the European relevant provisions.

We therefore ask the European Commission to assess the case urgently, as this lack of level playing field with US legislation might harm the activity of investment management industry in its relation with institutional investors in the years to come.

7. CONCLUSION

The European Commission's initiative in publishing this Green Paper is to be welcomed and its staff congratulated for the very hard work in putting it together. For the first time in the history of European investment management regulation, the industry was involved in the preparatory work. Asset management is now accepted as a profession in its own right. This is a very positive signal. It also shows that the Lamfalussy procedure is at work.

The Green Paper on the enhancement of the EU framework for investment funds opens wide the window of opportunity. With these comments the European investment management industry, including AFG members, takes up the challenges aiming to contribute to the realisation of a real Single Market for investment management (including the creation of a level playing field among competing savings/ investment products) with a more modern, simpler and more flexible regulatory environment.

[24] *'Tax discrimination against foreign funds: light at the end of the tunnel'*, PriceWaterhouseCoopers/EFAMA, 7 November 2005

ANNEX 2: LIST OF AFG MEMBERS AND MEMBERS OF THE BOARD OF DIRECTORS

(AFG members belonging to the board of directors are indicated in bold)

123 VENTURE
A PLUS FINANCE
A2 GESTION
AAZ FINANCES
ABC ARBITRAGE ASSET MANAGEMENT
ABN AMRO CAPITAL France
ACER FINANCE
ACOFI GESTION
ACTIGEP SA
ADDAX ASSET MANAGEMENT
ADEQUATION FINANCE
ADI - ALTERNATIVE INVESTMENTS
AESOPE GESTION DE PORTEFEUILLES
AFORGE GESTION
AGF ALTERNATIVE ASSET MANAGEMENT
AGF ASSET MANAGEMENT
AGF PRIVATE EQUITY
AGICAM
AGILIS GESTION S.A
AGRICA EPARGNE
ALBION ASSET MANAGEMENT SAS
ALCIS GESTION
ALCYONE FINANCE
ALIS CAPITAL MANAGEMENT
ALTERAM
ALTERNATIVE LEADERS France SA
ALTIGEFI
ALTIVIE ASSET MANAGEMENT France
ALTO INVEST
AMIRAL GESTION
ANTELMA ASSET MANAGERS
AQTIS - Advanced Quantitative Technical Investment Services
ASSET ALLOCATION ADVISORS
ATHENA GESTION
ATLAS GESTION
AUREL LEVEN GESTION
AUREUS CAPITAL
AVENIR FINANCE INVESTMENT MANAGERS
AVIVA GESTION D'ACTIFS
AXA GESTION FCP
AXA INVESTMENT MANAGERS PARIS
AXA INVESTMENT MANAGERS PRIVATE EQUITY EUROPE
BANQUE D'ESCOMPTE ASSET MANAGEMENT
BARCLAYS ASSET MANAGEMENT FRANCE - B.A.M.F.
BAREP ASSET MANAGEMENT
BARING ASSET MANAGEMENT France
BBR ROGIER
BBS FINANCE
BDF-GESTION
BDL CAPITAL MANAGEMENT
BFT GESTION
BFT GESTION 2
BLC GESTION
BMG ASSET MANAGEMENT
BNP PARIBAS ASSET MANAGEMENT
BOISSY GESTION
BOOMERANG ASSET MANAGEMENT
BORDIER GESTION PRIVEE
BOUSSARD & GAVAUDAN GESTION
BOUVIER GESTION
BPSD GESTION
BRYAN GARNIER ASSET MANAGEMENT
CAIXA GESTION SNC
CAP WEST EQUITIES
CAPITAL FUND MANAGEMENT
CARDIF ASSET MANAGEMENT
CARDIF GESTION D’ACTIFS
CARMIGNAC GESTION
CAVA GESTION
CCR ACTIONS
CCR CHEVRILLON PHILIPPE
CCR GESTION
CDC ENTREPRISES VALEURS MOYENNES
CEDEFONDS
CEREA GESTION
CFD CAPITAL MANAGEMENT
CFM : CORTAL CONSORS FUND MANAGEMENT
CHAMPEIL ASSET MANAGEMENT
CHAUSSIER GESTION
CIC NORD OUEST GESTION
CIC OUEST GESTION
CITCO FUND ADVISORS
CLARESCO FINANCE
CLARESCO GESTION
CM - CIC ASSET MANAGEMENT
COGEFI GESTION
COMGEST SA
CONSEIL PLUS GESTION -CPG
COPAGEST FINANCE
COSMOS GESTION PRIVEE
CPR ASSET MANAGEMENT
CRAIGSTON FINANCE
CREDIT AGRICOLE ALTERNATIVE INVESTMENT PRODUCTS GROUP - CA AIPG
CREDIT AGRICOLE ASSET MANAGEMENT (CAAM)
CREDIT AGRICOLE PRIVATE EQUITY
CREDIT AGRICOLE STRUCTURED ASSET MANAGEMENT (CASAM)
CREDIT LYONNAIS EUROPEAN FUNDS - C.L.E.F
CREDIT MUTUEL OCEAN GESTION
CREDIT SUISSE (France) GESTION PRIVEE
CREDIT SUISSE ASSET MANAGEMENT (France) SA
CREDIT SUISSE ASSET MANAGEMENT GESTION
CYRIL FINANCE AM
DELUBAC ASSET MANAGEMENT
DEXIA ASSET MANAGEMENT
DNCA FINANCE
DOLFI FINANCE
DORVAL FINANCE
DTAM
DUBLY DOUILHET GESTION
DWS INVESTMENTS
E.F.A.E.
ECOFI INVESTISSEMENTS

ECUREUIL GESTION
ECUREUIL GESTION FCP
EDELWEISS GESTION
EDMOND DE ROTHSCHILD ASSET MANAGEMENT
EDMOND DE ROTHSCHILD MULTI MANAGEMENT
EFIPOSTE GESTION
EGP FONDS ET GESTION
EIM (France) SA
ELIGEST SA
EQUIGEST
EST GESTION
ETOILE GESTION SNC
EULER HERMES SFAC ASSET MANAGEMENT
EUROPANEL RESEARCH AND ALTERNATIVE ASSET MANAGEMENT
EUROPEENNE DE GESTION PRIVEE
EXANE STRUCTURED ASSET MANAGEMENT
FEDERAL FINANCE GESTION
FEDERIS GESTION D'ACTIFS
FI SELECT MULTIGESTION
FIDELITY GESTION
FINADOU - Financière de l'Adou
FINALTIS
FINAMA PRIVATE EQUITY SA
FINANCE SA
FINANCE SA GESTION PRIVEE
FINANCIERE ARBEVEL
FINANCIERE CENTURIA
FINANCIERE CENTURIA ASSET MANAGEMENT
FINANCIERE DE CHAMPLAIN
FINANCIERE DE L'ECHIQUIER
FINANCIERE GALILEE
FINANCIERE LAMARTINE
FINANCIERE VAN EYCK
FINCAPITAL
FININFOR & ASSOCIES MULTIGESTION
FINOGEST
FIVAL SA
FLINVEST
FONDS D'INVESTISSEMENT DE BRETAGNE
FONGEPAR GESTION FINANCIERE
FONTENAY GESTION
FORTIS INVESTMENT MANAGEMENT FRANCE
FRANCHE-COMTE PME GESTION
FRANKLIN TEMPLETON ASSET MANAGEMENT
GEA - GESTION EQUILIBREE ALTERNATIVE
GEFOLOR
GENERALI FINANCES
GENERALI GESTION
GEORGE V ASSET MANAGEMENT
GERER CONSEIL
GESMOB SA
GESTEPARGNE
GESTION BTP
GESTION FINANCIERE PRIVEE
GESTION PRIVEE INDOSUEZ
GESTION SA
GESTION VALOR
GESTOR FINANCE GESTION
GESTYS
GIFAO INVESTISSEMENT
GLOBAL GESTION
Go .Fx² ASSET MANAGEMENT
GPK FINANCE
GRIGNAN CAPITAL GESTION
GROUPAMA ALTERNATIVE ASSET MANAGEMENT
GROUPAMA ASSET MANAGEMENT
GROUPAMA GESTION
GSD GESTION
GSO FINANCE
GT FINANCE
HAAS GAIGNAULT ET ASSOCIES
HAREWOOD ASSET MANAGEMENT
HDF FINANCE
HF ALTERNATIVE INVESTMENTS
HGL GESTION
HMG FINANCE SA
HOGEP
HOSTA.FI
HR GESTION
HSBC FCP (France)
HSBC INVESTMENTS (France)
HSBC MULTIMANAGER EUROPE
I.DE.A.M
ING INVESTMENT MANAGEMENT (France)
INNOVEN PARTENAIRES SA
INTER EXPANSION
INTERNATIONAL CAPITAL GESTION
INVESCO ASSET MANAGEMENT
INVEST ASIA ASSET MANAGEMENT
INVEST IN EUROPE
INVESTISSEURS DANS L'ENTREPRISE
IRIS FINANCE
ISKANDER
IT ASSET MANAGEMENT
IXIS ASSET MANAGEMENT
IXIS PRIVATE CAPITAL MANAGEMENT
J. de DEMANDOLX GESTION SA
JCL FINANCE
JOHN LOCKE INVESTMENTS
JOUSSE MORILLON INVESTISSEMENT
JP KLEIN INVESTISSEMENT S.A.
JP MORGAN STRUCTURED FUND MANAGEMENT
KBL FRANCE GESTION
KEREN FINANCE
KMS GESTION
L2S CAPITAL
LA FRANCAISE DES PLACEMENTS GESTION PRIVEE
LA FRANCAISE DES PLACEMENTS INVESTISSEMENTS
LA MONDIALE GESTION D'ACTIFS
LAZARD FRERES GESTION
LEGAL AND GENERAL ASSET MANAGEMENT France
LILLE GESTION
LMBO
LOMBARD ODIER DARIER HENTSCH GESTION
LOUVRE GESTION
LYON GESTION PRIVEE
LYXOR ASSET MANAGEMENT
LYXOR INTERNATIONAL ASSET MANAGEMENT
MAAF GESTION SA
MACIF GESTION
MAGENTA PATRIMOINE SA
MALMY GESTION
MARIGNAN GESTION
MARTIN MAUREL GESTION
MARTIN MAUREL GESTION INSTITUTIONNELLE
MASSENA FINANCE GESTION
MATIGNON FINANCES
MCA FINANCE
MEESCHAERT ASSET MANAGEMENT
MEESPIERSON FORTIS PATRIMOINE
METROPOLE GESTION
MICHAUX GESTION
MIRABAUD GESTION
MMA FINANCE
MODELES ET STRATEGIES

MONAM
MONETA ASSET MANAGEMENT
MONTE PASCHI INVEST (France)
MONTPENSIER FINANCE
MONTSEGUR FINANCE
MULTIFONDS
MW GESTION
NATEXIS ASSET MANAGEMENT
NATEXIS ASSET SQUARE
NATEXIS EQUITY MANAGEMENT
NCI GESTION
NEUFLIZE ARBITRAGE
NEUFLIZE GESTION
NEUFLIZE PRIVATE ASSETS
NEVILLE GESTION
OBC GESTION
ODDO ASSET MANAGEMENT
ODYSSEE VENTURE
OFIVALMO CAPITAL
OFIVALMO GESTION
OFIVALMO PALMARES
OFIVALMO PATRIMOINE
OLYMPIA CAPITAL GESTION
OLYMPIA CAPITAL MANAGEMENT
OPPORTUNITE S.A.
OPTIGESTION
OPTIMUM GESTION FINANCIERE
ORSAY ASSET MANAGEMENT
ORSAY GESTION
OUDART GESTION
OVERLAY ASSET MANAGEMENT
PAI PARTNERS
PALATINE ASSET MANAGEMENT
PARIS LYON GESTION
PARUS FINANCE
PASTEL & ASSOCIES
PATRIMOINES & SELECTIONS
PATRIVAL
PERGAM FINANCE SA
PHILIPPE GESTION
PHILIPPE PATRIMOINE
PHITRUST FINANCE
PIM GESTION FRANCE
PLATINIUM GESTION
PORTZAMPARC GESTION
PRADO EPARGNE GESTION
PRAGMA CAPITAL
PRIGEST
PRIM' ALTERNATIVE INVESTMENT
PRIME CAPITAL
PROMEPAR GESTION
PROTIS GESTION
PROVALOR
PYTHAGORE INVESTISSEMENT BP
QUARTUS GESTION
QUILVEST & ASSOCIES GESTION PRIVEE
QUILVEST GESTION PRIVEE
RAYMOND JAMES ASSET MANAGEMENT INTERNATIONAL
RENE ABALLEA FINANCE SA
REYL et COMPAGNIE (France) SAS
RFS GESTION
RHONE ALPES PME GESTION
RHONE GESTION
RHONE LOIRE + X GESTION
RICHELIEU FNANCE GESTION PRIVEE
RIVOLI FUND MANAGEMENT
ROBECO A.M.
ROBECO GESTIONS
ROCHE-BRUNE SAS
ROTHSCHILD ET CIE GESTION
ROTHSCHILD GESTION
ROUVIER ASSOCIES
SAGARD SAS
SAINT OLIVE et CIE
SAINT OLIVE GESTION
SAPHIR CONCEPT SA
SARASIN EXPERTISE AM
SCHELCHER PRINCE GESTION
SEDEC FINANCE
SEI INVESTMENTS (France)
SERVEPAR
SGAM INDEX
SGI MANAGEMENT
SHANTI GESTION
SIGEFI NORD GESTION
SIGEFI PRIVATE EQUITY
SIGEFI VENTURES GESTION
SINOPIA ASSET MANAGEMENT
SINOPIA SOCIETE DE GESTION
SMA GESTION
SOCIETE D'ANALYSES ECONOMIQUES ET FINANCIERES (SAEF)
SOCIETE D'ETUDES ET D'ASSISTANCE - S.E.A.
SOCIETE GENERALE ASSET MANAGEMENT - S.G.A.M.
SOCIETE GENERALE ASSET MANAGEMENT ALTERNATIVE INVESTMENTS
SOCIETE PARISIENNE DE GESTION
SOCIETE PRIVEE DE GESTION DE PATRIMOINE
SOCIETE PRIVEE DE GESTION ET DE CONSEIL
SOGEPOSTE
SOMANGEST-VESIGEST
SORIA FINANCE
STATE STREET GLOBAL ADVISORS France
STELPHIA ASSET MANAGEMENT
STRATEGE FINANCE SA
SUD EST GESTION
SWAN CAPITAL MANAGEMENT
SWISS LIFE ASSET MANAGEMENT (France)
SYCOMORE ASSET MANAGEMENT
SYCOMORE GESTION PRVEE
SYSTEIA CAPITAL MANAGEMENT
TANGUY ACTIONS BOURSE
THIRIET GESTION
TOCQUEVILLE FINANCE
TRANSATLANTIQUE FINANCE
TRINOVA GESTION
TRUSTEAM FINANCE
TURENNE CAPITAL PARTENAIRES
UBS GLOBAL ASSET MANAGEMENT (France) SA
UI GESTION SA
ULYSSE PATRIMOINE
UNIGESTION ASSET MANAGEMENT (FRANCE) SA
UNION BANCAIRE GESTION INSTITUTIONNELLE (FRANCE)
VERMEER ASSET MANAGEMENT
VIVERIS MANAGEMENT SAS
VP FINANCE GESTION
YVES LEVEN CAPITAL
ZARIFI GESTION