CONSULTATION

AFG RESPONSE

Facilitating cross-border distribution of investment funds

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afg
association française de la gestion financière

The Association Française de la Gestion financière (AFG) represents and promotes the interests of third-party portfolio management professionals. It brings together all asset management players from the discretionary and collective portfolio management segments. These companies manage at end 2017 €4,000 billion in assets, including €1,950 billion in French funds and €2,050 billion in discretionary portfolios and foreign funds.

The AFG's remit:

- Representing the business, financial and corporate interests of members, the entities that they manage (collective investment schemes) and their customers. As a talking partner of the public authorities of France and the European Union, the AFG makes an active contribution to new regulations,
- Informing and supporting its members; the AFG provides members with support on legal, tax, accounting and technical matters,
- Leading debate and discussion within the industry on rules of conduct, the protection and economic role of investment, corporate governance, investor representation, performance measurement, changes in management techniques, research, training, etc.
- Promoting the French asset management industry to investors, issuers, politicians and the media in France and abroad. The AFG represents the French industry – a world leader – in European and international bodies. AFG is of course an active member of the European Fund and Asset Management Association (EFAMA), of PensionsEurope and of the International Investment Funds Association (IIFA).

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Response to the Better Regulation consultations on the proposals on cross-border distribution of funds

Executive Summary

AFG welcomes the European Commission's endeavour to foster cross-border distribution of investment funds in the EU as part of the Capital Markets Union initiative.

However, in light of the practical solutions that are needed, AFG believes that ESMA would be better placed and would have the right instruments to achieve this objective. Therefore, AFG calls on the co-legislators to focus their work on the areas already identified by the European Commission.

Overall, AFG believes that some of the proposed changes (in particular those set out in the proposal for a Regulation) are to be welcome, while others (in particular those set out in the proposal for a Directive) would be counterproductive and would lead to restricting cross-border distribution due to new regulatory constraints.

Part 1. Proposal for a Regulation

I. Marketing communications

Harmonisation at EU level of rules applicable to the review of marketing communications by the National Competent Authority (NCA), as well as the removal of their notification as prior condition to the marketing of funds, are considered as positive developments.

However, some barriers remain.

In Art. 2(2), the wording "*or diminishes its significance*" lacks clarity. In the case of a broad interpretation by a Member State, the perfect concordance between the legal documentation and the marketing documentation would create additional costs for funds, lead to legal uncertainty, and hamper the cross-border commercialisation of funds. The requirement to avoid contradiction in information transmitted via the prospectus and the KID – as it is currently the case – should be sufficient.

Article 2(2)

Commission proposal	AFG proposal for amendment
UCITS management companies shall ensure that no marketing communication that contains specific information about a UCITS contradicts the information, **or diminishes its significance**, contained in the prospectus referred to in Article 68 of Directive 2009/65/EC and the key investor information referred to in Article 78 of that Directives	UCITS management companies shall ensure that no marketing communication that contains specific information about a UCITS contradicts the information, ~~***or diminishes its significance***~~, contained in the prospectus referred to in Article 68 of Directive 2009/65/EC and the key investor information referred to in Article 78 of that Directives

Harmonisation at EU level of marketing communication rules review by NCAs is justified when marketing communications target retail investors only and when host NCAs require marketing communications to be notified to them. Indeed, professional investors already have the required financial knowledge, and they can access information if needed. Local regulators already apply such lighter requirements regarding professional investors.

Article 2(5)	
Commission proposal	AFG proposal for amendment
ESMA shall issue guidelines, and thereafter update those guidelines periodically, on the application of the requirements for marketing communications referred to in the first paragraph, taking into account on-line aspects of marketing communications	ESMA shall issue guidelines, and thereafter update those guidelines periodically, on the application of the requirements for marketing communications referred to in the first paragraph ***when addressed to retail investors***, taking into account on-line aspects of marketing communications

Some regulators do not require the notification to be "*systematic*" but ask to review some commercial or marketing documentation on a case-by-case basis, adopting a risk-based supervision approach (as it is the case for the French supervisor Autorité des Marchés Financiers – AMF). The word "*systematic*" should therefore be removed at each occurrence in Article 5 of the Regulation.

Furthermore, in the case of indirect dealings, the intermediary is in relation with the investor. It should therefore be specified "*in their dealing with **end**-investors*".

Regarding the time period, in practice, French asset managers wait for feedback from the host country regulator before marketing their funds, even if it is not mandatory, to avoid having to re-do marketing documentation and apply changes according to this feedback. This time period should be aligned with the one already in place with the product passport under UCITS (10 business days for the home country NCA, + 5 business days after notification to the host NCA).

It should also be specified that marketing communications are considered as usable, unless there the

host NCA requires them to be modified within 5 working days.

Article 5	
Commission proposal	AFG proposal for amendment
1. For the sole purpose of verifying compliance with this Regulation and with national provisions concerning marketing requirements, competent authorities may require systematic notification of marketing communications which the UCITS management companies intend to use directly or indirectly in their dealings with investors. The **systematic** notification referred to in the first subparagraph shall not constitute a prior condition for the marketing of units of UCITS. Where competent authorities require notification of marketing communications referred to in the first subparagraph, they shall, within 10 working days, starting on the working day following that of the receipt of a notification, inform the UCITS management company of any request to amend its marketing communications. 2. Competent authorities that require **systematic** notification of marketing communications shall establish, apply, and publish on their websites, procedures for the **systematic** notification of marketing commun ications. The internal rules and procedures shall ensure transparent and non discriminatory treatment of all UCITS, regardless of the Member States in which the UCITS are authorised. […] 4.Competent authorities that require **systematic** notification of marketing communications as referred to in paragraph 1 shall, by 31 March of each year, report to ESMA on the decisions taken in the preceding year rejecting or requesting adaptations to marketing communications. […]	1. For the sole purpose of verifying compliance with this Regulation and with national provisions concerning marketing requirements, competent authorities may require ~~***systematic***~~ notification of marketing communications which the UCITS management companies intend to use directly or indirectly in their dealings with ***end***-investors. The ~~***systematic***~~ notification referred to in the first subparagraph shall not constitute a prior condition for the marketing of units of UCITS. Where competent authorities require notification of marketing communications referred to in the first subparagraph, they shall, within ~~***10***~~ ***5*** working days, starting on the working day following that of the receipt of a notification, inform the UCITS management company of any request to amend its marketing communications. ***In the absence of any request upon expiry of the 5 working days period following the receipt of a notification by the host competent authority, the relevant marketing communications are deemed as being authorised*****.** 2. Competent authorities that require ~~***systematic***~~ notification of marketing communications shall establish, apply, and publish on their websites, procedures for the ~~***systematic***~~ notification of marketing commun ications. The internal rules and procedures shall ensure transparent and non discriminatory treatment of all UCITS, regardless of the Member States in which the UCITS are authorised. […] 4.Competent authorities that require ~~***systematic***~~ notification of marketing communications as referred to in paragraph 1 shall, by 31 March of each year, report to ESMA on the decisions taken in the preceding year

	rejecting or requesting adaptations to marketing communications. […]

II. Fees or charges

During the first year of registration of the fund, the invoice must be sent upon receipt of the passeport notification (« *initial registration fee* »). Following this, the invoice is sent every year (« *maintenance fees* »).

Article 6(2)	
Commission proposal	AFG proposal for amendment
Competent authorities shall send an invoice to the registered office of the AIFM or UCITS management company. The invoice shall indicate the fees or charges referred to in paragraph 1, the means of payment and the date when payment is due.	Competent authorities shall send an invoice ***upon receipt of the passport notification and then for the subsequent financial year*** to the registered office of the AIFM or UCITS management company. The invoice shall indicate the fees or charges referred to in paragraph 1, the means of payment and the date when payment is due.

Part 2. Proposal for a Directive

I. Local facilities

The removal of the requirement to establish local facilities (paying agent / representative agent / information agent…) in the host country is considered to be a good step forward.

However the possibility to establish such local facilities should stay as an option for asset managers, in particular when it is relevant to facilitate access to countries where information channels are less developed.

Article 92(2)	
Commission proposal	AFG proposal for amendment
Member States shall not require the UCITS management company to have a physical presence for the purpose of paragraph 1.	Member States shall not require the UCITS management company to have a physical presence for the purpose of paragraph 1. ***The necessity of a physical presence in the host***

	Member State shall be at the discretion of the AIFM or UCITS Management company.

Furthermore, translation requirements could greatly hinder cross border provision of funds, as this process would be costly in resources. English should therefore be the standard, except when funds (UCITS/AIFs) are aimed at retail investors, and when translation is required by regulation (i.e. UCITS KID for retail investors).

Article 92(3)(a)	
Commission proposal	AFG proposal for amendment
The UCITS Management company *(or the AIFM*) shall ensure that the facilities referred to in paragraph 1 are of the following types and have the following characteristics : (a) Their tasks are performed in the official language or official languages of the host Member States where the UCITS is marketed ;	The UCITS Management company *(or the AIFM*) shall ensure that the facilities referred to in paragraph 1 are of the following types and have the following characteristics : (a) Their tasks are performed ***in a language customary in the sphere of international finance or, where otherwise required by law for certain type of fund documentation***, in the official language or official languages of the host Member States where the UCITS is marketed ***to retail investors***;

II. De-notification of funds

The limitations imposed regarding de-notification of funds cause important barriers to the cross-border distribution of funds. Their implementation would make de-notification impossible for some asset managers, or would reduce the incentive and their capacity to commercialise funds in other EU markets.

Alternative criteria (thresholds or other reason accepted by the NCA) would be preferable to grant flexibility to asset managers while protecting existing investors (free repurchase and publication of information in English to remaining investors).

The cumulative criteria set by the Commission are extremely restrictive. The threshold of 10 investors or less, in particular, is very complicated to follow in practice, and virtually impossible to implement by the asset manager. To give further flexibility on those aspects, while harmonising regulatory practices on the EU level, we think these criteria should be removed and one the following criteria applied:

- A threshold in %; or
- A nominal threshold (for reasons related to the size of funds); or
- Any other reason that would be accepted by the NCA of the host country.

There is no incentive for abusive de-notification of funds to avoid regulatory costs, since other costs arising from distributing funds on a cross-border basis (e.g. transfer agent costs, translation and printing costs, lawyer fees) far outweigh these.

Furthermore, the wording "*discontinue marketing*" is not appropriate, as de-notification covers two situations:

- Deregistration of a fund in a host country, following a passport request notification but without marketing this fund.
- Termination of marketing activities in a host country. In France, even without active marketing by asset managers, if an investor invests in the fund it is considered as conducting marketing activities.

De-notification is therefore to be processed in two steps:

- Step 1: Blocking subscriptions to avoid entrance of new investors;
- Step 2: Effective de-notification in the host country.

Article 93a(1)	
Commission proposal	AFG proposal for amendment
1. The competent authorities of the UCITS home Member State shall ensure that UCITS may discontinue marketing its units in a Member State where it has notified its activities in accordance with Article 93, where all the following conditions are fulfilled: (a) no investor which is domiciled or has a registered office in a Member State where the UCITS has notified its activities in accordance with Article 93 holds units of that UCITS, or no more than 10 investors which are domiciled or have a registered office in that Member State hold units of the UCITS representing less than 1% of assets under management of that UCITS; (b) a blanket offer to repurchase, free of any charges or deductions, all its UCITS units held by investors in a Member State where the UCITS has notified its activities in accordance with Article 93 is made public for at least 30 working days and is addressed individually to all investors in the host Member State whose identity is known; (c) the intention to stop the marketing activities in the Member State where the UCITS has notified its activities in accordance with Article 93 is made public by means of a publicly available medium which	***The competent authorities of the UCITS home Member State shall ensure that UCITS may proceed to the passport de-notification of its units or shares in a Member State where it has notified its activities in accordance with Article 93, where no investor which is domiciled or has a registered office in a member State where the UCITS has notified its activities in accordance with Article 93 holds units or shares of that UCITS.*** ***1.The competent authorities of the UCITS home Member State shall ensure that UCITS may discontinue marketing of its units or shares in a Member State where it has notified its activities in accordance with Article 93, where all of the following conditions are fulfilled :*** **(a)** ***where investors which are domiciled or has a registered office in a member State where the UCITS has notified its activities in accordance with Article 93 holds units or shares of the UCITS representing less than X% of asset under management of that UCITS or, alternatively, where investors which are domiciled or has a registered office in a member State where the UCITS has notified its activities in accordance with Article 93 holds units or shares of the UCITS representing less than « nominal amount still to be determined » of assets under management of that UCITS or any other***

is customary for marketing UCITS and suitable for a typical UCITS investor	***reason that may be accepted by the relevant host Member State.*** **(b)** A blanket offer to repurchase, free of any charges or deductions, all its UCITS units or shares held by investors in a Member State where the UCITS has notifie dits activities in accordance with Article 93 is made public for at least 30 working days and is adressed ***directly or through financial intermediaries***, individually to all investors in the host member Stae whose identity is known ; **(c)** The intention to ***proceed to de-notification or*** stop marketing activities in the Member State where the UCITS has notified its activities in accordance with Article 93 is made public by means of a publicly available medium which is customary for marketing UCITS and suitable for a typical UCITS investor ».

As investors already have double protection (free repurchase and publication of information in English to remaining investors), it should not be required to translate this information.

Article 93a(5)	
Commission proposal	AFG proposal for amendment
Member States shall allow for the use of all electronic or other distance communication means for the purposes of paragraph 4, provided the information and communication means are available for investors in the official languages of the Member State where the investor is located	Member States shall allow for the use of all electronic or other distance communication means for the purposes of paragraph 4, provided the information and communication means are available for investors in the official languages of the Member State where the investor is located ***or in a language customary in the sphere of international finance upon a decision of the (AIFM or) UCITS Management company***

Lastly, there would be merit in clarifying (for instance at ESMA level) in relation to Art. 32a that agreements entered into by asset managers and local intermediaries & distributors can be complemented regarding the practicalities of what deregistration entails. Together with asset

managers, host-country intermediaries & distributors should share the responsibility of ensuring that deregistration is complete. There would be two ways to achieve this:

- Either model clauses with foreign host-country intermediaries & distributors, or
- By clarifying responsibilities during the transitory phase of deregistration as regards client support.

III. Premarketing

Premarketing rules as drafted in this proposal are too vague (e.g. investment strategies / investment ideas) and too restrictive in comparison with the rules already published by AMF (Position 2014-04), which overall suit our members as well as our European associations. This approach should be promoted at EU level.

Premarketing should therefore be extended to :

- UCITS provided to professional investors or high net worth individuals falling under the retail investors category (in line with the AMF position: minimum subscription of €100 000). The aim would be to avoid practical problems arising from having to handle two regimes (one for UCITS and one for non-UCITS), for instance when doing roadshows where both types of investors may be addressed for reasons of UCITS seeding.
- UCITS or AIFs already created to test the appetite of the local market before registering the fund.

Furthermore, the presentation of "*draft documentation*" should be authorised as it is in France.

Position AMF 2014-04 : The practice of management companies contacting up to a maximum of 50 investors (professionals or individuals whose initial subscription would be at least €100,000) to assess their interest prior to the launch of a UCITS or AIF does not constitute an act of marketing, provided that the investors are not given a subscription form and/or documentation containing definitive information on the fund's characteristics. However, any subsequent subscription by the investors contacted will be considered to constitute an act of marketing.

Article 30a(1)	
Commission proposal	AFG proposal for amendment
Member States shall ensure that an authorised EU AIFM may engage in pre-marketing in the Union, excluding where the information presented to potential professional investors: (a) relates to an established AIF; (b) contains reference to an established AIF; (c) enables investors to commit to acquiring units or shares of a particular AIF;	Member States shall ensure that an authorised EU AIFM ***or an authorised UCITS management company*** may engage in pre-marketing in the Union, excluding where the information presented to potential professional investors: ***(a)*** relates to an ***authorised AIF or an authorised UCITS by the host Competent Authority;*** ***(b) [Removed]*** ***(c) [Removed]***

(d) amounts to a prospectus, constitutional documents of a not-yet-established AIF, offering documents, subscription forms or similar documents whether in a draft or a final form allowing investors to take an investment decision.	(d) amounts to a prospectus, constitutional documents of ***a not-yet-authorised AIF or a not-yet-authorised UCITS***, offering documents, subscription forms or similar documents ~~***whether***~~ in ~~***a draft or***~~ a final form allowing investors to take an investment decision.

To align this treatment with the UCITS directive, the time period for notification by NCAs should be reduced to 10 business days.

Article 32a(7)	
Commission proposal	AFG proposal for amendment
If, pursuant to a planned change, the AIFM's management of the AIF would no longer comply with this Directive or the AIFM would otherwise no longer comply with this Directive, the relevant competent authorities shall inform the AIFM within 20 working days that it is not to implement the change.	If, pursuant to a planned change, the AIFM's management of the AIF would no longer comply with this Directive or the AIFM would otherwise no longer comply with this Directive, the relevant competent authorities shall inform the AIFM within ***10 working days*** that it is not to implement the change.

Part 3. Tax issues

The report from the Commission to the Council and the European Parliament entitled "*Accelerating the CMU: addressing national barriers to capital flows*" mentions withholding tax (WHT) relief procedure as "a major deterrent to cross-border investment". The issues ranges from lack of access to tax treaties to difficulties in obtaining refunds of withholding taxes to discrimination of funds established in other Member States.

The report proposes a list of 9 "best practices" simplifying WHT relief procedures and one-member State particularly well placed to share its experience for each of them.

Member States are invited to "assess and confirm the relevance of the 9 WHT best practice" and make commitment on which of them they want to implement by 2019.

These 9 best practices are based on the pre-requisite that funds qualify for treaty benefits, either in their own name or on behalf of investors. The report states on page 10 *"To avoid double taxation of cross-border investment, most bilateral tax treaties provide for WHT refunds"*. Unfortunately this is seldom true in some European countries concerning funds like:

- A "Fonds commun de placement", which is a joint ownership of financial instruments,
- A "Société d'investissement à capital variable – SICAV" which is exempt from corporation tax.

A such, they are not considered as « resident » for international tax treaties purposes[1].

Some treaties signed by France (about 15 out of 120)[2] include specific provisions concerning SICAV and FCP whereby a French FCP or SICAV which invests in the other country may benefit from the reduced WHT provided by the treaty under condition:

- In certain treaties, the FCP/SICAV must demonstrate that a certain percentage of its investors are French tax residents[3]. The treaty advantage is generally limited to this percentage: e.g. treaties signed with Germany, Austria, Switzerland. In practice, French fund managers are not in a position to furnish the more and more detailed information requested by the foreign Revenue.
- In other cases, the FCP/SICAV must provide a certificate of residency to the Revenue of the other State (Belgium for SICAV only). As both FCP and SICAV are not liable to tax, the French Revenue does not accept to sign such a document but only an "attestation d'établissement".

Therefore, withholding taxes are currently applied at national level and the fact that in many cases investment funds do not have directly access to reduced withholding tax rates available under tax treaties acts as a barrier.

Two solutions should be considered:

I. The FCP/SICAV is considered as the beneficial owner (or a qualified person) and qualifies for treaty benefits on its own behalf

This solution, which is supported by the 2010 OECD CIV report, should be at least applied to all widely held open ended funds.

In France and some other European countries (Germany, Belgium …) most of the time the fund manager does not hold the fund's register: it is delegated to the custodian (a bank) or to Euroclear. In practice, the fund's manager just knows the name of the account holder. The KYC and AML requirements are carried out by the investor's account holder.

It means that the fund's manager is generally not in a position to certify that x% of the FCP/SICAV is held by French tax residents, let alone the exact number of French unitholders.

We consider that widely held FCP and SICAV regulated by the UCITS directive and authorized and controlled by the "Autorité des Marchés Financiers" (AMF) and marketed only in European countries should qualify for the treaties signed by France with the other European states without having to report information about the tax residency of its investors.

A widely held UCITS fund or SICAV cannot be used for treaty shopping purposes by its investors as the investors cannot interfere into the funds financial management: financial management is delegated to the management company ("société de gestion").

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[1] See the OECD Report "*The granting of treaty benefits with respect to the income of collective investment vehicles*" dated 23 April 2010 as well as the work of the Commission's Tax Barriers Business Advisory Group.

[2] In Europe the countries where specific provisions are included in the double tax treaty signed with France are the following: Austria, Germany, Spain, Switzerland, United Kingdom and Sweden.

[3] Unless this LOB clause further incudes "derivative benefits" for other EU investors, it should be regarded as discriminatory since investors who are resident of the other contracting state as well as all the investors who are resident of an European state should also be eligible.

This is for example the **approach adopted by Spain** where UCITS funds benefit from a reduced rate of WHT of 1% (instead of 19%) provided they demonstrate in a specific document signed by the national financial supervisory authority that they qualify as UCITS as defined by the directive. This approach seems particularly relevant.

This approach should be included into the best practices proposed by the report.

An alternative approach is to impose a EU-wide limit to the WHT-rate equal to the (maximum /minimum) WHT rate provided under double taxation treaties, such as 15%, like in Belgium, the Netherlands, and Germany from 2018.

II. WHT for payments made to UCITS and AIFs within the EU (and partner jurisdictions) should be abolished

The easiest solution to solve complex legal and practical WHT problems in Europe would be the abolishment of WHT on payments made to UCITS and AIFs within the EU and partner jurisdictions to the EU.

This solution was endorsed by the CJEU in the Santander (C-338/11 to 347/11) and Emerging markets (C-190/12) rulings. By relieving the cross-border tax barrier of withholding taxes on investment income, it best serves the free movement of capital and the purpose of creating a Capital Markets Union where investors and professional services firms are entitled to operate as they deem appropriate under the relevant legislation and regulations. At the same time, the professional intermediaries are accustomed to providing the relevant tax authorities with the information they require to effectively assess taxes upon the beneficial owners of investment income according to their tax status (see the experience of the EU savings directive, FATCA, etc.).

This is a less radical proposal than it may at first appear.

Indeed, due to specific problems for investment funds to achieve cross border treaty relief (unknown investor base), our favored solution to solve the problem - also presented as one possible option by the Commission - is to generally abolish withholding tax (WHT) on cross border dividend payments. The solution would also preserve the tax attributes of final investors such as the exemption of pensions funds, the availability of certain deductions for reserves in order to meet pension and other obligations (CJEU C-342/10), the possibility to capitalize income on a pre-tax basis, etc. These options should be considered in the context of the CMU initiative.

Further to the judgement of the ECJ on the principles of the free movement of capital (especially “Santander” C-338/11 or “Emerging Markets” C-190/12), some member states already abolished under certain circumstances WHT for certain types of foreign CIUs (France; Spain; Poland). Other member states do not levy WHT on certain type of income paid on the basis of their domestic legislation (e.g. UK on dividends and Luxembourg on interest). The Commission could thus consider a recommendation to member states to abolish the WHT for payments made to UCITS and AIFs in order to ensure a uniform and consistent application of the ECJ judgements.

As major source countries in Europe already followed that approach this would also help to create a level playing field for all countries within the EU and partner jurisdictions and to boost the competitiveness of the Single Market as a whole

Especially in this age of Automatic Exchange of Information, we are of the opinion that a WHT within

the EU and partner jurisdictions is not appropriate anymore. Where a WHT is triggered by cross-border investment income payments, it is a clear obstacle to the free movement of capitals. It is no longer required by the effectiveness of fiscal supervision since full information is now available to national tax authorities through reporting information by investment service providers. It is not required by the balanced allocation of taxing powers between Member States since less restrictive methods could be put in place (such as sharing the aggregate amount of taxes effectively collected by the State(s) of residence of the taxpayers with the State of source of the investment income).

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