THE INVESTMENT ASSOCIATION

FINAL RESPONSE TO CAPITAL MARKETS UNION GREEN PAPER

1) Beyond the five priority areas identified for short term action, what other areas should be prioritised?

We agree with the 5 priorities set out, given that CMU for the benefit of the whole EU can most pragmatically be developed as an incremental set of measures. Our only concern is that some other, bigger or more challenging tasks could also benefit from groundwork sooner rather than later, notably in relation to optimal distribution of investment products. In other words, we believe i) that the Commission should seek a balance between 'quick wins' and projects that require a longer lead time; and ii) that there should be close co-ordination between objectives relating to the operation of wholesale markets and those relating to the experience of the end, retail customer, even if these latter objectives are also to be the focus of a separate, later work stream. It is retail customers who will ultimately bring new money to the table, as well as mobilising any relatively unproductive part of their bank deposits. We recognise that this puts the spotlight on investment management.

A second area where we see early groundwork as important is greater legal certainty over securities holdings. Similarly, it is important to begin to measure the impact of existing pieces of legislation on secondary market capacity in securities and on derivatives, especially as this impact appears increasingly likely to be negative where MiFIR and the capital/solvency rules are concerned. This is a matter of growing concern for Investment Association members.

Having said all of which, we agree that it is pragmatic to build up some momentum for CMU by means of an initial focus on the five areas mentioned. We would only note that, within this list, the first three lend themselves most readily to early, concrete measures, ie. streamlined processes for prospectuses (but no loss of material content); SME information dissemination; and sustainable securitisation. On the other two areas – ELTIFs and private placements – more time may be required to assess market evolution.

The only other prefatory comments relate to systemic risk. In particular, we flag the considerable conflict between CMU and the possible designation of funds or asset managers as 'Systemically Important Financial Institutions (or SIFIs). It takes a peculiar and in practice very rare combination of circumstances for any fund or manager to even approach systemic significance, notably involving significant leverage in combination with size. We therefore urge great caution in allowing the SIFI agenda to undermine the potentially powerful role of asset management in CMU.

The real systemic dangers in fact now lie in CCPs and particularly in plans to instigate their recovery at any cost. Once a CCP exhausts its resources – which are set at extraordinarily high levels, whose depletion would require events that are themselves already systemic – it cannot command the confidence of the market, making recovery a futile exercise. So, even though there would undoubtedly be considerable costs associated with the winding down of a CCP, the uncertainty that would be created in the wider financial system by what amounts to unlimited liability for end-users in attempts at recovery would only worsen a crisis. For funds and institutional investors, of course, derivatives remain important risk-management tools and, at the same time, ones they have little choice but to clear. CCP collapse may in practice be very unlikely, as it would entail the failure of multiple bank clearing members, which is itself less likely in the new regulatory regime and as a matter of underlying public policy. But, assuming collapse is not impossible, it is essential to then be realistic about the conditions that would bring this about and the dangers of leaving investors, small and large, in an uncertain position as to their liabilities.

2) ***What further steps around the availability and standardisation of <u>SME credit information</u> could support a deeper market in SME and start-up finance and a wider investor base?***

We support measures to pull together and disseminate effectively information about SMEs, though we caution that, as things currently stand, collective funds may not be the most likely buyers of SME assets. There is however some interest and action, on both the institutional and the funds side, in 'direct lending'. Information flow could be helpful in developing this more widely.

Even this, however, may not suffice. We believe it will also be important to allow non-banks to invest cross-border on essentially the same terms as banks – a concept sometimes referred to as an 'asset passport'. (We cover this in more detail in our answer – *to question 3, below* – on ELTIFs).

As regards the information to be made more widely available, we believe that this should 'look through' any credit scores, to the underlying information, notably data on incidence of default and levels of loss given default.

3) ***What support can be given <u>to ELTIFs</u> to encourage their take up?***

ELTIFs have great potential in the long-run and the Investment Association believes that their take up will in practice depend primarily on greater awareness among the wider public of the clear advantages of longer-term investment. (Even though ELTIFs are only available to those retail investors with significant amounts to invest and limited need for liquidity, there remains the opportunity to channel funds into them indirectly, via other institutional investors that themselves aggregate retail savings.)

One indirect means of supporting ELTIFs could be to promote a more developed EU approach to retirement provision, since pension schemes are prominent among the natural holders of long term assets.

It would also be helpful to explore the 'asset passport' concept, whereby non-banks can invest (across border or otherwise) on largely the same basis as banks, ie. subject to the same withholding tax treatment, access to credit data and seniority in insolvency, yet without having to hold a banking licence.

4) Is any action by the EU needed to support the development of <u>private placement</u> markets other than supporting market-led efforts to agree common standards?

We believe that the well documented market efforts to promote greater use of private placements constitute the most appropriate approach. Ideally, more might be done on the tax incentives relating to private placements but we do recognise the challenge of making progress on tax harmonisation at EU level.

5) ***What further measures could help to increase access to funding and channelling of funds to those who need them?***

In order to raise awareness of infrastructure projects and to support investors' ability to assess them, we support the principle of a European Investment Project Pipeline.

Even before getting this pipeline working, however, and as noted in our response to question 12, the priority will be to ensure proportionate capital calibration for long-term investors (notably Solvency II for insurance companies).

In addition, if the EU wishes to develop investment in infrastructure even further, some tax incentives could be considered.

6) Should measures be taken to promote greater liquidity in corporate bond markets, such as standardisation? If so, which measures are needed and can these be achieved by the market, or is regulatory action required?

We do not believe that standardisation should be promoted, but left to markets to develop where appropriate (in essence, in relation to information provided to investors). While some degree of economic standardisation may be feasible and even helpful in relation to some larger debt issuers, for most (and particularly the smaller issuers for whom CMU arguably matters more), the advantages of flexibility will suit their idiosyncratic funding needs much better. As regards the financial system, care would also need to be taken in concentrating 'rollover' risk, if maturity dates were standardised. This would suggest that, at most, any potential benefit lies in aligning coupon dates for some issuers, which could bring some marginal benefits in terms of meshing with the most liquid parts of the hedging market.

In any case, it would seem sensible to rely on the market to determine where greater standardisation is viable (as it has in relation to derivatives on interest rates and credit, where there are benefits in terms of clearability that simply do not apply to the world of bonds). This could cover standardisation not so much in relation to economic terms but to some legal/credit considerations (eg. bond covenants, which market groups periodically review and discuss). The most productive measures here are likely to arise in relation to prospectuses, which we address in the parallel consultation on the Prospectus Directive. (Our preferences on the PD review relate to the isolation of salient points and earlier delivery thereof to prospective investors.)

To be absolutely clear, we view the greatest impact on liquidity as arising from the operation of the capital regime and the impending rules on pre- and post-trade transparency. This has led inter alia to the well documented decline in market-maker inventories, at the same time as bond issuance has increased, encouraged by the return of loose monetary policy.

7) Is any action by the EU needed to facilitate the development of standardised, transparent and accountable ESG (Environment, Social and Governance) investment, including green bonds, other than supporting the development of guidelines by the market?

We support the existing market initiatives in this area. The appeal of green bonds (for example) may grow over time but it is conceivable that other 'labels', beneficial to the cause of CMU, may also develop and there does not seem to be any barrier or market failure in this regard. This, therefore, is an area where we see the Commission's role as limited to the encouragement (most likely via Communications or Recommendations, as opposed to Directives or Regulations) of standards that can evolve over time, in line with developing market practice.

8) Is there value in developing a common EU level accounting standard for small and medium-sized companies listed on MTFs? Should such a standard become a feature of SME Growth Markets? If so, under which conditions?

Small and medium-sized companies that raise capital through listing on unregulated markets need to provide high-quality financial information to enable investors to assess their performance and prospects. We would prioritise market integrity, meaning that the same accounting standards should apply to each and every listed company. Our preference is for international consistency, which is achieved by adherence to IFRS, rather than EU-specific standards. IFRS reporting is widely understood by investors and it is generally accepted that, while not perfect, IFRS provides relevant and comparable information. This is important for our members investing internationally and for small and medium-sized companies accessing international finance. For unlisted companies, we accept that different standards could apply

and arguably should, in the interests of developing businesses (which could of course eventually translate into listed companies).

9) Are there barriers to the development of appropriately regulated crowdfunding or peer to peer platforms including on a cross border basis? If so, how should they be addressed?

We have no particular insight on these types of platform, but suspect that the issues will be relevant, mutatis mutandis, to investment products more generally. In other words, without letting investor-protection standards slip, it would be attractive to accommodate distribution via electronic means, supported by guidance that provides some basic orientation as to the characteristics of the investment. This will, of course, be more feasible for investment products that are themselves regulated as to their content, notably UCITS and other EU-branded vehicles.

10) What policy measures could incentivise institutional investors to raise and invest larger amounts and in a broader range of assets, in particular long-term projects, SMEs and innovative and high growth start-ups?

While (new) tax incentives might help, particularly to encourage long-term investment, we also believe much could be achieved by simply ensuring the existing tax regime works properly. We go into detail on this below.

We do also note the pernicious effect of accounting standards that can turn what would otherwise be natural long-term holders of assets into forced sellers, or tilt them more towards bonds than equities in the first place, when the underlying economics might more naturally suggest equity holdings as beneficial to investors and companies. We view this as unhelpful, especially when there is an incentive to issuers in many countries (in the form of tax deductibility) to fund themselves through debt rather than equity. This latter phenomenon is not necessarily bad in itself (as some assume), though we agree that it should be analysed as part of this broader picture of incentives.

Any consideration of ways forward here should take account of indirect routes into asset classes. For example, the ability of institutional investors to invest in private equity vehicles should, wherever relevant, be subject to favourable regulatory treatment and fair tax treatment.

Institutional investors often fail to get the same tax treatment on cross-border dividends and interest when investing through pooled arrangement as they would if they invested directly. In recent times, and in particular in the context of the OECD's work on combating tax avoidance through base erosion and profit shifting (BEPS), this problem has been accentuated because tax authorities too often view investment pooling vehicles as existing for the purpose of avoiding tax through treaty shopping. In fact these alternative funds exist only to pool investment into capital markets from a variety of sources.

The risk of incurring additional tax liabilities (particularly cross-border withholding tax) and the surrender of fair tax treatment by investing in fund structures acts as a disincentive to investment. In order to achieve the aims of CMU we believe that it is vitally important to arrive at a settlement on the correct cross-border tax treatment for investors in pooled vehicles.

Finally, it is important to check that the capital requirements for SME investments are appropriate (as is increasingly recognised to be the case with securitisations). While SME investments may be more risky than those in well established companies, the advantages to the economy of encouraging such businesses mean that capital requirements should, if anything, be slightly lower than what is implied by the risks. They certainly should not be higher. This would apply most obviously to lending – which is where we believe there is the greatest demand from SMEs – but also if less obviously to equity stakes, notwithstanding the continuing anecdotal evidence of unwillingness of SME businesses to open up to outside shareholders.

11) What steps could be taken to reduce the costs to fund managers of setting up and marketing funds across the EU? What barriers are there to funds benefiting from economies of scale?

The Commission should look at the possibilities afforded by electronic media for reaching a wider range of customers. Current distribution costs may conceivably be justified – at least they might be if they allowed significant customer support – but it is nonetheless striking and hard to explain why distribution costs for the same investment product vary widely across member states.

Meanwhile, other issues are of more immediate concern, including the lack of a common rule book for what constitutes leverage; for financial promotions (assuming that opening this debate would not lead to *more* barriers), or for conduct (which is set at national level on matters such as requirements for daily dealing). First, the rules on master-feeder structures need correcting. Second, there are issues – particularly on the tax front – with fund mergers. Also on the tax front, the application of withholdings goes against: EU Treaty principles; related ECJ findings; and established bilateral treaty benefits. Separately, we question the requirement to publish daily prices in a national newspaper, when other media are available. Finally, there should be:

i) a streamlining of procedures relating to cross-border marketing – with no registration requirement and with the only obligation being notification (by means of sending a KIID, and with the option to send that to the home-state supervisor for transmission to in the host-state supervisor) ;
ii) the removal of the requirement for a local paying agent, which is redundant.

Master-feeder structures are an effective way of boosting economies of scale in collective investment (allowing investors from a range of jurisdictions globally to come together, through 'feeder' funds, each of which then invests all of its funds in the 'master' fund).

The case for master-feeder structures was well made by the Commission in Staff Working Document SEC (2008) 2263 and enshrined accordingly in the UCITS legislation. Recital 50 of UCITS IV itself says: "Several Member States have enacted provisions that enable non-coordinated collective investment undertakings to pool their assets in one so-called master fund. In order to allow UCITS to make use of those structures, it is necessary to exempt feeder UCITS wishing to pool their assets in a master UCITS from the prohibition to invest more than 10% of their assets [...] in a single collective investment undertaking. Such an exemption is justified as the feeder UCITS invests all or almost all of its assets into the diversified portfolio of the master UCITS, which itself is subject to UCITS diversification rules."

But, through an incoherence in UCITS IV (Directive 2009/65/EC) and in spite of the UCITS legislation nominally accommodating master-feeder structures, they are rendered sub-optimal. This arises from a failure to 'switch off' the 10% rule for funds investing into feeders (Article 50(1)(e)(iv). The that measure generally prohibits UCITS to invest into collective schemes that may invest (in aggregate) more than limits to 10% the amount of its funds that any one UCITS may (in aggregate) invest in other such funds. The reason for this provision was to limit circularity of investment.

However, the necessary safeguards already exist. Any potential circularity is addressed by a provision (article 58.3) prohibiting the master from channelling money back into a feeder fund. Finally, the master will itself be limited (under article 50) as to how much it may in aggregate invest in other UCITS.

As such, we believe that a simple addition to article 50(1)(e) would solve the problem: "(v) in the case of investment in units of a feeder UCITS, there is no limit on the amount that the feeder UCITS can hold in units of the master UCITS."

It is also necessary to ensure that existing UCITS funds can easily be restructured into a master UCITS. Such fund restructuring tends not to be tax-neutral, especially for cross-border mergers. Clearly the crystallisation of tax payments can give rise to an administrative burden as well as direct tax costs, which we believe is sub-optimal, given the policy advantages of encouraging economies of scale in investment vehicles. So, while tax measures are inherently more difficult to harmonise, we believe this is one more targeted area that is worth considering. Also, we believe that, instead of requiring funds to write to all shareholders ahead of a merger, the emphasis should simply be on supervisory approval of the merger.

The current national investor tax reporting regimes required for cross-border sales of investment funds should be replaced by a single pan-European regime. Today, the diversity and

complexity of such national tax reporting requirements constitute a barrier to the cross-border offer of investment funds across Europe – harming competition, to the detriment of investors.

On withholdings, please see our response to Question 30.

12) Should work on the tailored treatment of infrastructure investments target certain clearly identifiable sub-classes of assets? If so, which of these should the Commission prioritise in future reviews of the prudential rules such as CRDIV/CRR and Solvency II?

The Investment Association believes that there should be a level playing field for long-term infrastructure investment as between banks, insurers and pension funds. Together with the removal of barriers to investment by insurers, this could greatly assist the level of investment by insurers in European infrastructure.

However, as currently drafted, Solvency II places insurers at a disadvantage relative to banks in terms of their ability to invest in infrastructure. This is because the current treatment of infrastructure debt under Solvency II overstates the risk and volatility of these assets and fails to recognise that:

1. There is a materially lower default rate for infrastructure investments compared to corporate bonds in the same rating category, because of the ability to manage directly and actively the relationship with the borrower and also greater granularity in covenants and control regarding the operation of the borrower's business, allowing the management of event risk to a greater extent than is possible in corporate bonds.
2. The average level of recovery for infrastructure loans is materially higher for infrastructure loans compared to corporate bonds in the same rating category, again due to the positive risk management characteristics and strong business profiles present in the infrastructure sector.
3. Data for infrastructure loans over the last 20 years shows that infrastructure-loan default rates are uncorrelated with the economic cycle. In contrast, for corporate debt, default rates are positively correlated with the economic cycle and, in any case, are generally at a significantly higher level than infrastructure default rates.

Therefore, we would encourage the Commission to prioritise Solvency II and welcome the:

- European Commission's call for advice from EIOPA on whether it would be appropriate to amend the Solvency II standard formula for the calculation of the solvency capital requirement regard investment in infrastructure; and
- work that EIOPA is doing in response to this call for advice, including, its efforts to:
  a. develop, for regulatory purposes, a definition of infrastructure investments that offer predictable, long-term cash flows whose risks can be properly identified and monitored by insurers; and
  b. explore possible criteria for this new class of long-term infrastructure assets covering issues such as standardisation and transparency.

We agree that infrastructure investments should be treated as a separate assets class under Solvency II. However, it is important that any work that is done on to define a separate infrastructure asset class should adopt a principles-based approach that would allow investments to be reviewed case by case, taking into account the nature of the risks (which are often project-specific rather than structure- or sector-specific. Adopting a detailed definition of infrastructure – or sub-classes thereof –would create a risk that some infrastructure investments would be excluded; and that the definition would become out of date as technology advances. In addition, a detailed criteria approach will not be helpful

unless it refers to the overall level of risk in the transaction and is based on appropriate risk mitigation and management methods.

For the avoidance of doubt, we would *not* say that a straight corporate bond or other security issued by an infrastructure provider counts as an infrastructure investment per se.

13) Would the introduction of a standardised product, or removing the existing obstacles to cross-border access, strengthen the single market in pension provision?

Arguably, the fundamental reason why there is limited cross-border pension provision relates to the profoundly national nature of pensions, ie. specificities in social, labour and tax rules. There is limited evidence as yet that a standardised product would in and of itself do much to change this reality. However, it is also clear that the ability to harness economies of scale on a cross-border basis could over time deliver significant benefits for European consumers. And long-term saving by individual citizens clearly has the potential to improve their financial security, while supporting longer-term company development, all to the benefit of economic growth.

As mentioned above (*in our answer to question 3*), we also believe that there could be mutually reinforcing benefit as between ELTIFs and a more developed system of retirement provision in the EU. To that extent, we support the debate about how a single market in pensions provision could be made more of a reality, whether through removing obstacles and/or creating a European pension product, possibly as a '29th-state' regime.

14) Would changes to the EuVECA and EuSEF Regulations make it easier for larger EU fund managers to run these types of funds? What other changes if any should be made to increase the number of these types of fund?

We support moves to remove the size limit on managers offering such funds. Venture capital and social entrepreneurship are clearly specialist areas but we see no reason why they should be subject to constraints on achieving economies of scale.

15) How can the EU further develop private equity and venture capital as an alternative source of finance for the economy? In particular, what measures could boost the scale of venture capital funds and enhance the exit opportunities for venture capital investors?

We have no specific comment on this.

16) Are there impediments to increasing both bank and non-bank direct lending safely to companies that need finance?

Please see our answers to questions 2 (SME credit information) and 3 (ELTIFs). As a general point, non-bank direct lenders should not be discriminated against, as compared with banks, particularly where they do not entail the same degree of leverage or deploy fractional-reserve banking, both of which cause 'run' risk.

By way of background, we stress two things:

1) that some of this direct lending is accessible as an asset class relatively widely, via funds (ie. not all is conducted by institutional investors).
2) Sometimes, this business focuses on long-term lending, in partnership with other financial institutions that provide shorter-term credit. This makes it particularly valuable, in CMU terms, and therefore especially important to treat fairly, as compared with banking.

By way of recap, our concerns in relation to the level playing field (as between non-banks and banks) revolve around withholding tax treatment, access to credit data, seniority in insolvency, and the redundancy of a banking licence for this business.

17) How can cross border retail participation in UCITS be increased?

We share the views of those who see digital media as being important to this issue especially if that brings distribution costs down. But other factors will also be important, including the passport that management companies can acquire and flexibility in terms of share classes within a UCITS. It seems likely, also, that the demand side cannot be stimulated in relation to the UCITS label per se, but to the asset class(es) wrapped within a given fund. In other words, the focus should be on greater consumer awareness of the role that fixed income, equity and other assets can play in a savings and investment strategy.

18) How can the ESAs further contribute to ensuring consumer and investor protection?

ESAs can play a significant role in this area, even though national competent authorities (NCAs) will naturally tend to be in the front line. ESMA should, in particular, monitor the extent to which incentives built into product-distribution models can and do affect consumer outcomes.

In the EU, funds distribution to retail investors is fragmented along national lines, which in some MS is concentrated among very few large entities. Such entities are in a powerful position to promote their own, 'home-grown' funds at the expense of those offered by third parties, reducing choice for investors and incentives for managers to register UCITS cross-border. The Commission should, in our view, facilitate and promote 'open architecture' for funds distribution, maximising choice and competition while increasing the potential for cross-border investment.

19) What policy measures could increase retail investment? What else could be done to empower and protect EU citizens accessing capital markets?

Tax is, of course, a powerful driver but difficult to harmonise across the Union. Investor literacy is also vital, even if difficult to change quickly and unlikely even then to lead to immediate benefits. What is essential, in our view, is to ensure that a truly level playing field exists in terms of product information and other protection measures, including those relating to inducements (which are looking likely to be lighter in relation to insurance products than those sold under MiFID).

It may be too early for conclusive judgement as to the effects of the UK 'Retail Distribution Review (RDR)', which attempts to align incentives better as between financial advisers and end-consumers. But, in the absence of a system of broad guidance on savings and investment, it is far from clear that the impact has been positive in terms of motivating individuals to invest productively, rather than keep cash on deposit or tied up in property.

20) Are there national best practices in the development of simple and transparent investment products for consumers which can be shared?

National experience in the UK has been mixed, especially in relation to longer-term saving. Tax incentives have proved helpful in relation to the 'ISA' product, but the 'stakeholder' pensions label was insufficiently attractive, hence the need for 'auto-enrolment' (effectively putting the onus on individuals to opt out of workplace-based schemes for occupational retirement, rather than assuming they are out unless they decide to opt in). It is, therefore, hard to conclude that there is any identifiable best practice.

21) Are there additional actions in the field of financial services regulation that could be taken ensure that the EU is internationally competitive and an attractive place in which to invest?

We encourage the Commission to do everything possible to ensure that no transaction tax is introduced. Even if it was possible to introduce a transaction tax on a global basis (which is clearly unlikely, given that it is not viable even as an EU-wide measure), it would remain a counter-productive measure that penalises investors.

Additionally, given the constructive role that investment management can play in CMU, we encourage the Commission to take advantage of the CRD review that is scheduled for this year and refocus capital requirements for investment managers on the relevant risk, ie. operational risk. Imposing a capital regime devised for banks will, at the margins, make investment managers in the EU less competitive.

22) What measures can be taken to facilitate the access of EU firms to investors and capital markets in third countries?

This requires a culture of open access. It may even be necessary for the EU to take the lead, opening up access to EU consumers for third-country investment products and providers. We view this as an acceptable approach, given: the existing strength internationally of the EU's UCITS brand; the more recent inclusion of AIFs in the suite of regulated investment products; the promise of the ELTIFs structure; and more generally the benefits to EU-based savers of being able to access an internationally competitive range of products and providers. If the EU does erect barriers to third-country services providers, then it should be with an eye to the effect this will have on market access for EU-based providers and with the flexibility to remove those barriers promptly in the future.

There is clearly a risk of fragmentation of financial markets globally, beginning with derivatives but extending to other sectors. Consolidation within the EU can counter this but by definition only up to a certain point, hence our preference for openness at a global level. Ideally this will be reinforced through IOSCO and in trade treaties, though we recognise that this is a topic that is beyond the remit of the current consultation.

Ultimately, the competitiveness of EU firms will attract savings from outside the EU.

23) Are there mechanisms to improve the functioning and efficiency of markets not covered in this paper, particularly in the areas of equity and bond market functioning and liquidity?

We believe there are measures that would be helpful.

For equity IPOs, we advocate eliminating the research blackout period that applies prior to publication of a prospectus. Such 'blackouts' are arguably unnecessary, in a world of improved Chinese walls. Moreover, in practice they perpetuate information asymmetry at the expense of investors, thereby hampering price discovery and a sustainable post-listing price.

For all securities offerings, we favour automation of the new-issue process. This would entail increasing the use of electronic media to display offering documents and allowing electronic interactions, though whether legislation is required in order to achieve that remains to be seen. We also believe it would be helpful to draw out salient company-specific points better, instead of obscuring them in generic risk disclosure.

As regards securities already in issue, we believe it would be helpful to explore ways of setting deadlines for custodians to comply with their duties in relation to corporate actions, as these can easily leave investors with insufficient time to consider matters arising from such actions. (This issue highlights the practical impact of the cumbersome securities law regime, as regards holdings.) Facilitating electronic voting would help in this regard.

24) In your view, are there areas where the single rulebook remains insufficiently developed?

We believe that there is merit in reviewing and streamlining the various reporting requirements that attach to asset managers, taking into account not just EU-level obligations (including those coming under MiFID) but those that exist purely at national level. We do not, of course, object to reporting per se. But there is a clear obstacle to efficiency in the continuing proliferation of requirements (including electronic formats adopted nationally), especially when these are meant to address the same data.

25) Do you think that the powers of the ESAs to ensure consistent supervision are sufficient? What additional measures relating to EU level supervision would materially contribute to developing a capital markets union?

We do not see a need for significant additional powers per se for ESAs. We do, however, believe that it would be helpful for them to be present (in an observer capacity and only for dossiers on which they may later have to work) during the 'level 1' part of the legislative process.

As a more general point, legislation should be crafted with better consideration for how to 'switch off' provisions that prove problematic (or at least to recommend such swithcing-off), whether that (limited) power resides with ESAs, national authorities or some combination of the two.

26) Taking into account past experience, are there targeted changes to securities ownership rules that could contribute to more integrated capital markets within the EU?

As we say in our response to question 3: "It would also be helpful to explore the 'asset passport' concept, whereby non-banks can invest (across border or otherwise) on largely the same basis as banks, ie. subject to the same withholding tax treatment, access to credit data and seniority in insolvency, yet without having to hold a banking licence."

We do support targeted changes to the regime for securities ownership, reinforcing the Collateral Directive (Directive 2002/47/EC). In essence, the Directive should be properly implemented (to remove in any MS remaining formalities that act as obstacles to the perfection of collateral interests) and extended to all dispositions of securities as collateral.

27) What measures could be taken to improve the cross-border flow of collateral? Should work be undertaken to improve the legal enforceability of collateral and close-out netting arrangements cross-border?

We believe that improvements to legal certainty in relation to holdings of securities could reasonably be achieved – most likely through targeted amendments to the Financial Collateral Directive – to give users of collateral greater confidence in arrangements. We also believe that limits on rehypothecation (re-use) should be reviewed, as these will work against the free flow of collateral.

Close-out netting cross-border is not something that is generally directly material to our members, but we do acknowledge the financial stability benefits of having a broadly accessible netting regime. In fact, the broader the regime, in terms of instruments and participants accommodated, the better.

28) What are the main obstacles to integrated capital markets arising from company law, including corporate governance? Are there targeted measures which could contribute to overcoming them?

Corporate Governance and Company law regimes across the EU vary significantly. It is important that the EU continues to encourage and promote the best standards of corporate governance. We believe however, that this is best achieved through the comply-or-explain approach, rather than the harmonisation of governance or company-law regimes. We therefore, welcomed the European Commission recommendation on the quality of corporate-governance reporting and we believe that the Shareholder Rights Directive is the appropriate vehicle for any change. In that context, we continue to support rules relating to related-party transactions. We do not, however, see the need for further measures at this point in time.

29) What specific aspects of insolvency laws would need to be harmonised in order to support the emergence of a pan-European capital market?

While the harmonisation of such laws is in principle desirable, we recognise that, even as a long-term project, this could be very challenging. We do however believe this should be kept under review and that the following are the most promising aspects to focus on:

- a definition of 'centre of main interest' and 'relevant date for determination';
- rules standardising what constitutes the formal opening of insolvency proceedings;
- provisions to address cross-border or so-called 'secondary' proceedings;
- conflict-of-law rules, in the interests of co-ordination between jurisdictions and of avoiding long and costly insolvency proceedings (which can involve appeals to the ECJ and which reduce recovery rates for creditors).

Fragmentation of European insolvency regimes and restructuring laws make it more complicated to engage in cross-border capital flows, even if marginally. Although the EU has made progress towards harmonisation of EU Insolvency laws, more could in principle be done. For example, the EU Insolvency Regulation does not provide uniform law provisions for members of the European Union. It merely establishes whether a Member State has jurisdiction to open insolvency proceedings. As a result, national courts are given the freedom to interpret the regulation quite differently. The regulation needs to go further in prescribing standardised national insolvency procedures for MS.

We advocate a review of the various EU measures: European Parliament resolution of 15/11/2011; Regulation No 1346/2000 on Insolvency proceedings; and Commission Recommendation C(2014) 1500.

Moreover, there are other measures in adjacent areas that could help, namely changes to securities law (relating to clarity as to ownership) and a levelling of the playing field as between banks and non-banks, when either is faced with the insolvency of an investee company.

30) What barriers are there around taxation that should be looked at as a matter of priority to contribute to more integrated capital markets within the EU and a more robust funding structure at company level and through which instruments?

We have provided comments on tax barriers in our responses to questions 10 and 11 above. In addition to these points we note the following three points on cross border withholding tax:

<u>Legal status of intra-EU withholding tax</u>
In recent years, the Court of Justice of the European Union has found consistently that it breaches EU Treaty principles of discrimination and free movement of capital if one Member State levies withholding tax on dividend payments to a recipient in another MS where no dividend withholding tax is levied domestically. However, most Member States have not introduced domestic legislation compatible with the findings of these cases and continue to

levy withholding tax on dividends paid to investors in other MS. In plain terms, the application of withholdings where there is no basis to do so is anti-common-market.

Administration of tax relief
Unless and until all Member States abolish dividend withholding tax on payments within the EU (which we would support), it is important that investors should be able to obtain bilateral treaty benefits. Claiming withholding tax relief under Double Taxation Agreements and/or a country's domestic tax laws is often cumbersome and time- and resource-intensive for governments, financial institutions, and investors. As a result, end-investors often are effectively forced to forgo the tax relief due them and this has adverse effects on capital markets. In our experience, the process for claiming withholding tax relief across the EU has deteriorated over recent years, resulting in increased costs and protracted delays for cross-border portfolio investors to collect the tax relief due them.

Without a harmonised and streamlined system for tax relief at source (such as that envisaged under the OECD's TRACE proposals), investors and intermediaries will continue to face the increasingly costly administrative burdens of varying domestic procedures; tax will often not only be inappropriately withheld but withheld in amounts exceeding the rate that would ever be applicable. The end result is that cross-border investment will be less attractive. Members States that continue to operate tax-reclaim systems will also continue to bear the costs associated with such a system, such as the stamping and certification of tax-reclaim forms and the processing of refund payments. The implementation of the EU Revised Directive on Administrative Cooperation in the area of automatic exchange of information could significantly reduce, and in some instances eliminate, many of the costs associated with implementing a pan-EU harmonised tax relief system.

Implementation of an EU financial transactions Tax
A financial transactions tax would be counterproductive, as it would demonstrably push up costs for all users of financial markets and reduce liquidity, which is already in decline. (Even the threat of an FTT is at the margins unhelpful.) In addition the implementation of a new tax in only a few member states plainly introduces distortions in the operation of capital markets across the EU.

31) How can the EU best support the development by the market of new technologies and business models, to the benefit of integrated and efficient capital markets?

Too often Level 2 technical specifications, particularly for reporting, transparency and disclosure are expressed in legal language and not in a language that system designers would see as unambiguous. An easy example is where an obligation states that the price of a share must be given, without specifying as a global standard whether that is to be expressed in euro and cents or cents or a decimal euro. If businesses are to offer technical solutions (including disruptive ones), there needs to be greater use of specifications that can implemented unambiguously and consistently. Mobile telephony and power industries will typically be given technical specifications in legislation, this must be done more for systems for financial services, even though that will require additional skill sets at the ESAs.

32) Are there other issues, not identified in this Green Paper, which in your view require action to achieve a Capital Markets Union? If so, what are they and what form could such action take?

We do not believe there are any issues not already covered under our responses to the questions above.