Asset management II

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The Committee on Economic and Monetary Affairs adopted the own-initiative report by Wolf **KLINZ** (ALDE, DE) on asset management in response to the European Commission's white paper on enhancing the single market framework for investment funds.

Non-harmonised retail funds: the report invites the Commission to examine future extension of the UCITS III Directive on eligible assets to open-ended real estate funds (OREF) and funds of hedge funds (FoHF). The report states that consideration should be given to the establishment of a single market framework for OREF, FoHF and other non-harmonised retail funds as regulated products at EU-level underpinned by an impact assessment and taking full account of diversification, liquidity and valuation issues. Lastly, the report underlines that this shall not interrupt the currently ongoing revision of UCITS III.

Private Placement Regime (PPR): the committee calls for a harmonised framework for private placement at EU-level in order to enhance the single market integration. MEPs believe that a PPR should apply to all open-ended investment funds, including EU-regulated funds, nationally regulated funds as well as funds regulated in third countries. The Commission is called upon to negotiate such agreements with third countries, in particular with the United States, and requests the Commission to address this issue within the Transatlantic Economic Council. The committee is convinced that European PPR framework should only apply to cross-border private placement and in this case override the existing national rules, it should, however, not replace national rules that apply to domestic private placement.

Distribution and fees: the report notes that that the use of commission payments is an acceptable means of remuneration. It points out, at the same time, that investor information including fee disclosure is crucial to empowering investors to take more informed decisions and to increase competition. The committee believes that cost and fee disclosure requirements at the point of sale as well as information requirements on risk and performance on an ongoing basis should not only apply to UCITS but equally to all competing products (i.e. certificates, notes, unit-linked life insurance). It requests, in this context, a review of the legislative framework on the marketing and sale of all retail investment products by the end of 2008 at the latest, in particular the upcoming Solvency II Directive, the Insurance Mediation Directive and the UCITS III Directive.

Acknowledging that tracking of commissions, in particular retrocession fees, is a time-consuming and costly process, MEPs call on the industry to examine whether common standards across the European Union for appropriate position keeping are necessary such as standards for identifying distributors or providing data, such as data file formats, data transmission protocols, reporting frequency. The Commission is also invited to propose how the appropriate provisions, e.g. capital requirements, at the EU level for these funds can be achieved in order to ensure effective consumer protection.

Taxation of cross-border fund mergers: the committee invites the Commission to prepare a taxation of fund mergers directive following the principle of tax neutrality set out in Directives 90/434/EEC and 2005 /56/EC in 2008. It stresses that the objective is not to harmonise tax but to determine that domestic and cross-border mergers should be tax-neutral if the investor keeps its investment in the fund before and after the merger or withdraws its investment as a result of the intended merger, before the latter takes place.

Fund processing: initiatives at national level to increase the efficiency of fund processing have been welcomed. According to the report, the Commission believes that the Commission should take action if the industry does not substantially progress in greater use of electronic and standardised fund processing

by the end of 2009. The idea of setting up a standardised process to facilitate access to reliable and standardised data on cross-border funds is noted.

Depositary: MEPs regret that not all Member States allow the branches of EU credit institutions to act as depositary even though they are regulated at the EU level in accordance with EU financial services legislation. Therefore, they call on the Commission to take the necessary legislative steps in the 2008 UCITS III revision to allow such credit institution branches to act as depositary and to clarify ways for an effective supervisory cooperation. The harmonisation of a definition of depositary functions could contribute to better understanding and cooperation between regulators and ensure a consistent level of investor protection across Europe. However, the difficulty of overcoming national differences, in particular with regard to property law, terms of liability and insolvency protection rules could be problematic.

Further analysis is needed of the legal barriers that would have to a be removed in order to achieve a harmonisation of depositary functions taking into account the already existing research on the different roles and responsibilities of depositaries across EU Member States.

Lamfalussy: the report highlights the importance of ensuring the choice of implementing instruments on the basis of the content and objectives of the underlying Level 1 legislation. The Commission is asked to propose a legal basis at Level 1 for the use of both implementing directives and implementing regulations at Level 2. It points out that the new regulatory procedure with scrutiny must be applied to all Level 2 measures.

Hedge Funds: MEPs point to the evidence showing that alternative investments such as hedge fund activities often result in higher market liquidity, dispersion of risk, in particular for traditional portfolios, and enhanced competition among market makers and intermediaries as well as in beneficial propriety research contributing to more information and more efficient pricing. The report considers transparency and disclosure for investors and supervisors of utmost importance and expects the forthcoming IOSCO proposals to bring more clarity in this respect. The industry is urged to agree on a code of conduct on portfolio valuation, risk management systems, transparency of fee structures and enhanced insight in investment strategies and the Commission is urged to play a more active role in this discussion (e.g. within G8). MEPs believe that hedge funds could help strengthening corporate governance practices by increasing the number of investors that make active and informed use of their shareholder rights.

Private Equity: MEPs consider private equity as an important source of start-up, growth and restructuring capital, not only for large listed companies, but also for SMEs. However, they are also aware of cases in which an increased level of indebtness brought considerable risks for companies and their employees when their management was no longer in the position to fulfil the repayment obligations.

The importance of transparency towards the investors as well as towards supervisory authorities concerning fees and raising funds is stressed. The committee believes that regulation of the counterparties exposure is crucial as well as clear criteria of eligibility of investors to limit the retail investors' exposure to private equity.

MEPs are convinced that a more in-depth analysis is needed to better understand the impact of alternative investments such as hedge funds on the one hand and private equity on the other on financial stability, corporate governance, consumer choice and protection as well as employment. They look forward to examining these in the forthcoming parliamentary reports on hedge funds and private equity, based on the outcome of the studies commissioned in August 2007 should include among others an examination of:

- whether an industry-driven code of conduct is sufficient to enhance financial stability and investor protection or is there a need for more action by the legislator and supervisory authorities in terms of disclosure requirements through minimum reporting standards and regulation of relevant players;

- whether there is an interest in or even a need for a European label for alternative investment instruments and if so, what could be the criteria to distinguish different asset classes that would be covered by such an EU framework;

- under which conditions retail access to these asset classes could be permitted.