# Towards a deepening of the single market for asset management in the context of an ambitious Capital Markets Union

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Almost half of the European investment funds are distributed in several countries. However, the boundaries between Member States have not been completely abolished in the asset management sector. The new Capital Markets Union Action Plan aims to accelerate this momentum,with a view to financing the energy, social and digital recovery and transition.

The creation and deepening of a single European market which promotes the free movement of persons, goods, services and capital, and benefits both the citizens and businesses of the Union, has always been one of the essential objectives of European integration. This is a long-term undertaking whose practical implementation is facing many obstacles, of a political, cultural, fiscal or regulatory nature, but whose realisation is now more necessary than ever, if not urgent, in the context of the economic crisis linked to the COVID-19 pandemic.

In a September 2020 Communication presenting its new Action Plan for a Capital Markets Union (CMU), the European Commission underlines how essential the CMU is to the achievement of all the EU's key economic policy objectives, including the post-COVID recovery and the transition to a more inclusive, digital and sustainable economy. As the Commission rightly points out, *'only efficient, deep and integrated capital markets can provide support of sufficient magnitude to emerge from the crisis and carry the transition'.* [1]

The investment funds and asset management sector, as a leading player in the financial market,[2] has a crucial role to play in achieving the objectives of the CMU, which it fully supports. In practice, what measures can be taken to further reduce the obstacles to the development of more integrated capital markets and, in particular, to the cross-border distribution of investment funds? We are talking here about a few avenues.

### *Cross-border distribution of funds: constantly increasing*

Let us start by recalling a fact: the cross-border distribution of investment funds, both within the EU and to the rest of the world, is doing better and better. The share of cross-border fund assets has grown substantially over the last decade and now accounts[3] for 4-8% of total funds outstanding (compared to only 41% in 2010).[4] This success is, of course, largely due to the international recognition of the legal framework put in place by the UCITS and AIF directives, as well as to the creation of European distribution passports allowing these funds to be marketed throughout the European Union on the basis of the sole authorisation of the country

[1]Communication of the European Commission of 24 September 2020, "A Capital Markets Union at the service of people and businesses – a new action plan" (link)
[2] At the end of 2020, investment funds accounted for about 23% of the overall capitalisation of the financial markets (source: EFAMA Fact Book 2021).
[3] Defined as funds marketed in at least one country (inside or outside the EU) other than their country of domicile.
[4] During the2018, 2019 and 2020 years sales outside the EU accounted for almost half of cross-border fund sales (source: EFAMA Fact Book 2021).

of domicile. In the same way, the introduction of the 'management company' passport within the frameworks of the above-mentioned directives has made it possible to create European centres of excellence for the management and administration of investment funds, also making it possible to achieve economies of scale. The combination of these factors translates for investors into access to a wider choice of products and increased competition between fund managers, resulting in a significant reduction in the costs associated with their investments.[5]

### *The regulation on cross-border distribution: a further step in the right direction*

Despite this success, there are still many obstacles to the cross-border distribution of funds. In addition to linguistic or cultural obstacles, they relate in particular to the imposition of specific national provisions on marketing, fees to be paid to local supervisory authorities, administrative formalities and notifications. All this entails significant costs, the added value of which for investors is often questionable.

Fortunately, the adoption in 2019 by the EU (as part of the first CMU Action Plan) of a package of regulatory measures to facilitate the[6] cross-border distribution of investment funds – the bulk of whose provisions will enter into force on 2 August 2021 – should help to resolve some of the problems mentioned above, by limiting the possibilities of 'gold-plating' (or 'over-regulation' or divergent application) by Member States of the European rules in force. For example, the introduction of a harmonised definition of the concept of 'pre-marketing' in the framework of the AIFM Directive should avoid divergent interpretations between Member States and increase legal certainty for fund managers wishing to test the interest of investors in a given country before proceeding to its actual marketing. Similarly, the increased transparency regarding their fees and other fees charged by the supervisory authorities of the various countries for supervising the funds is also welcome.

### *European long-term investment funds (ELTIF)*

As part of the creation of a capital markets union, the European asset management industry is also supporting the proposed revision of the regulation applicable to European long-term investment funds (ELTIF). So far, this type of investment vehicle has not been as successful as expected, with just over fifty ELTIF registered to date (some of which have not yet been marketed), due to a regulatory framework that is too corseted and poorly adapted to the needs of investors.

Subject to substantial adaptations to the existing regime, which would make it possible to increase supply as much as[7] demand, ELTIF could position themselves in the future as a complement of choice to UCITS, giving individual investors access to new, less liquid asset classes, such as unlisted companies, listed SMEs, social infrastructure, sustainable energy or transport projects, etc. This would allow them to diversify their investments as part of a pan-European vehicle while contributing more directly to the financing of these projects aimed at the real economy and essential for a sustainable recovery of the European economy.

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[5] The cost of UCITS invested in equities and bonds decreased by 11% and 18% respectively between 2016 and 2020 and this downward trend is likely to continue in the future (source: EFAMA Fact Book 2021).
[6] Directive (EU) 2019/1160 and Regulation (EU) 2019/1156 to facilitate the cross-border distribution of investment funds (published in the Official Journal of the EU on 12 July 2019).
[7] See on this subject the Recommendations by EFAMA.

This is one of the recommendations of the European Commission aimed at increasing the participation of retail investors in the financial markets, which represents one of the priority objectives of the CMU. Indeed, contrary to what is observed in the United States, for example, and despite particularly low interest rates for several years, retail investors prefer to keep their savings in their bank accounts rather than invest them on the markets (either directly or through collective savings products such as investment funds), preferring security at the price of a negative return after inflation.[8]

***Tax barriers: reduction of withholding tax***

Finally, how can we conclude this brief overview without mentioning the tax barriers which constitute a major obstacle to cross-border investment? The procedures currently in place to allow the refund of withholding tax and to prevent double taxation of income when taxes on yield have to be paid both in the Member State of the investment and in the Member State of the investor, are particularly tedious, slow and costly. They are a real brake on cross-border investment.

The proposals put forward by the European Commission in its new action plan for a CMU are aimed at the introduction of a common and standardised system at Union level which would facilitate and speed up the reimbursement of withholding tax. They are therefore particularly[9] welcome, even if they still meet with the reticence of a number of Member States which are taking advantage of the current situation. We are proposing, however, to go a step further by simply abolishing withholding tax on payments (of coupons, dividends, etc.) made to UCITS and AIFs.

***Conclusion***

While the principle of the single market is already a reality in the field of asset management more than in other sectors, many obstacles to cross-border investment still remain. The European Commission's new action plan for the establishment of a CMU should help to improve the situation. The rapid and effective implementation of this action plan is essential and will require strong political support from the Member States and the European Parliament in the coming months.

[8] For a detailed study, see EFAMA Report: Household participation in capital markets, September 2020 (link)
[9] Inspired in particular by the TRACE model developed by the OECD (link)