

Cross-border distribution of investment funds

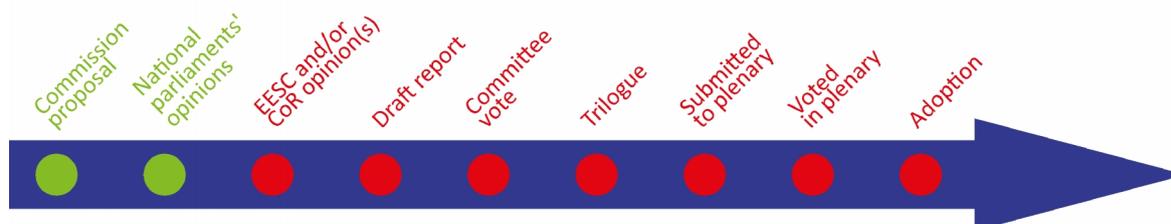
OVERVIEW

Investment funds are products created to pool investors' capital and to invest it in a collective portfolio of securities. In the European Union, the characteristics of a range of different types of investment funds have been established in Union law, and most funds on the market are categorised as one of these types. The market in the EU is smaller than in the United States, despite there being far more funds in the EU. This is the reason why the European Commission has adopted two legislative proposals: one for a regulation aligning national marketing requirements and regulatory fees and harmonising the process and requirements for the verification of marketing material by national competent authorities, and the other for a directive harmonising the conditions under which investment funds may exit a national market and allowing European asset managers to engage in pre-marketing activities.

Proposal for a directive of the European Parliament and of the Council amending Directive 2009/65/EC of the European Parliament and of the Council and Directive 2011/61/EU of the European Parliament and of the Council with regard to cross-border distribution of collective investment funds;

Proposal for a regulation of the European Parliament and of the Council on facilitating cross-border distribution of collective investment funds and amending Regulations (EU) No 345/2013 and (EU) No 346/2013

<i>Committee responsible:</i>	Economic and Monetary Affairs (ECON)	COM(2018) 92
<i>Rapporteur:</i>	Wolf Klinz (ALDE, Germany)	COM(2018) 110
<i>Shadow rapporteurs:</i>	Alain Lamassoure (EPP, France)	12.3.2018
	Mady Delvaux (S&D, Luxembourg)	2018/0041 (COD)
	Syed Kamall (ECR, UK)	2018/0045 (COD)
	Matt Carthy (GUE/NGL, Ireland)	Ordinary legislative procedure (COD)
<i>Next steps expected:</i>	Publication of draft report.	(Parliament and Council on equal footing – formerly 'co-decision')



Introduction

[Investment funds](#) are investment products created with the sole purpose of pooling investors' capital and investing that capital collectively through a portfolio of financial instruments such as stocks, bonds and other securities. In the EU, investment funds can be categorised as [undertakings for collective investment in transferable securities \(UCITS\)](#) and [alternative investment funds \(AIFs\)](#) managed by alternative investment fund managers. UCITS are covered by Directive 2009/65/EC and AIFs are covered by Directive 2011/61/EU. Directive 2011/61/EU is complemented by four fund frameworks:

- [Regulation \(EU\) 345/2013](#) on European Venture Capital funds (EuVECA),¹
- [Regulation \(EU\) 346/2013](#) on European social entrepreneurship funds (EuSEF). Both the aforementioned regulations were amended by [Regulation \(EU\) 2017/1991](#).
- [Regulation 2015/760](#) on European long-term investment funds (ELTIF)² and
- [Regulation 2017/1131](#) on money market funds (MMF).³

These rules share the aims of protecting investors and making cross-border distribution easier.

Existing situation

The current EU legislative framework provides banks and financial service companies established and authorised in one EU country with the possibility to open branches or provide certain services in other EU Member States, with a few authorisation requirements. This is known as 'passporting'.⁴ Despite the existence of such a regime and the rapid growth of EU investment funds (with a total of €14 310 billion in assets under management in June 2017), the EU investment fund market is still predominantly organised as national markets: according to the European Commission, 70 % of all assets under management are held by investment funds registered for sale in their domestic market only. Only 37 % of UCITS and about 3 % of AIFs are registered for sale in more than three Member States. Compared with the USA, the EU market is smaller in terms of assets under management. In addition, while there are considerably more funds in the EU (58 125 in the EU compared with 15 415 in the USA), they are on average smaller. This has a negative impact on economies of scale, the fees paid by investors and the way in which the internal market operates for investment funds.

Parliament's starting position

The Parliament had not called for specific action in this area.

Preparation of the proposal

This proposal, which was already mentioned in the [action plan](#) on building a capital markets union and its [mid-term review](#), was scheduled in the [Commission's 2018 work programme](#). It aims to help address fragmentation in the capital markets, by removing regulatory barriers to the financing of the economy and increasing the supply of capital to businesses.

In the explanatory memorandum to its proposal, the Commission notes that regulatory barriers – namely Member States' marketing requirements,⁵ regulatory fees,⁶ and administrative and notification requirements⁷ – represent a significant disincentive to the cross-border distribution of funds. These barriers were identified in response to the [green paper on capital markets union](#), the [call for evidence on the EU regulatory framework for financial services](#) and the [public consultation on the cross-border distribution of funds](#).

The Commission's proposals were accompanied by an [impact assessment](#), of which EPRS is currently preparing an initial appraisal.

The changes the proposal would bring – the directive

Article 1 – amendments to Directive 2009/65/EC (UCITS)

The Commission – in article 1 – [proposes to amend](#) the following articles of the [UCITS Directive](#).

- In Article 17, it would delete paragraph 10, which empowers the European Securities and Markets Authority (ESMA) to develop draft regulatory technical standards (RTS); and insert a (new) paragraph 8a. According to this new paragraph, if – as a result of the change of any particulars referred to in paragraph 8 – the UCITS no longer complied with this directive, the relevant national competent authorities (NCAs) of paragraph 8 would inform the [management company](#) within 10 working days that it would not implement that change. If, despite the notification, the change was implemented, then the NCAs of the home Member State of the UCITS would take all necessary measures in accordance with Article 98 of the UCITS Directive (supervisory and investigatory powers). If, however, the change did not affect compliance of the management company with this directive, the NCAs of the home Member State of the company would inform the competent NCAs of the host Member State of the company of those changes, within 10 working days.
- In Article 18, the proposal would delete paragraph 5, which empowers ESMA to develop draft RTS.
- Article 77 – on marketing communications to investors – would be entirely deleted.⁸
- In Article 91, it would delete paragraph 3, which requires Member States to ensure that their national laws, regulations and administrative provisions governing cross-border marketing of UCITS within their territories are easily accessible from a distance, by electronic means and in a language customary in the sphere of international finance.⁹
- Article 92 would be replaced with an article that would specify the tasks to be performed by the facilities established in each Member State by the UCITS management company¹⁰ and add that Member States would not require the UCITS management company to have a physical presence for those tasks.
- In Article 93 (proposal from a UCITS to market its units in a Member State other than its home Member State), the proposal would replace paragraph 8. If the information in the notification letter of Article 93(1) changes or if share classes to be marketed change, the UCITS would notify the home Member State NCAs in writing at least a month before implementing the change. Similarly to the amendment in Article 17, if by implementing this change the UCITS no longer complied with the directive, the relevant NCAs would notify it, within 10 working days, not to implement it. If, despite this, the UCITS implemented the change, the home Member State NCAs would take all necessary measures in accordance with Article 98 of the UCITS Directive (supervisory and investigatory powers). If, however, the change did not affect the compliance of the UCITS with the directive, then the home Member State NCAs would inform the host Member State NCAs without undue delay of those changes.
- A new article 93a would be added, to complement the notification procedures with the conditions for UCITS that decide to stop their marketing activities in a Member State. These conditions would be: (i) a maximum of 10 investors who hold up to 1 % of assets under management of this UCITS having invested in this UCITS in an identified Member State; (ii) a blanket offer to repurchase all its UCITS units by investors in that Member State would be made public for at least 30 working days and would be addressed individually to all investors in the host Member State whose identity was known; (iii) the intention to stop the marketing activities in the Member State would be made public by means of a publicly available medium, which would be customary for marketing UCITS. The UCITS would further submit a notification

letter to the competent authority of its home Member State, comprising the previous information. The NCAs of the UCITS home Member State would transmit the notification letter within 20 working days of receipt to ESMA and to the competent authorities of the Member State where the marketing would be discontinued. They would further inform the UCITS of that transmission. As of that date, the UCITS would cease all marketing of its units in the Member State identified in the notification letter. It would continue, however, supplying the necessary information (articles 68 to 82 and 94) to investors who remain invested in it.

- Article 95(2), which empowers ESMA to develop draft RTS to determine the form and contents of the standard model of a notification letter to be used for the aforementioned notification, would be deleted.

Article 2 – amendments to Directive 2011/61/EU (AIFMD)

With regard to the Alternative Investment Fund Managers (AIFM) Directive (AIFMD), the Commission proposes, in article 2 of the proposal, to amend the following articles.

- In Article 4(1), on definitions, the proposal would insert the definition of 'pre-marketing', i.e. 'a direct or indirect provision of information on investment strategies or investment ideas' by the AIFM or on their behalf 'to professional investors domiciled or registered in the Union in order to test their interest in an AIF which is not yet established'.
- The proposal would introduce a new article 30a relative to the conditions under which an AIFM could engage in pre-marketing activities in the Union.
- Article 31(5), which empowers ESMA to draft implementing technical standards to determine the form of a model for the notification letter and the form of the written notice (both referred to in the article), would be deleted.
- Article 32 would be amended to reflect more specifically what 'without undue delay' refers to in the second and fourth subparagraphs of paragraph 7 ('20 working days' and 'one month' respectively). In addition, paragraph 8 – which empowers ESMA to develop draft ITS – would be deleted.
- A new article 32(a) would be inserted, dealing with the issue of the discontinuation of marketing of units or shares of EU AIFs in the Member States other than in the home Member State of the AIFM. Similarly to the aforementioned new article 93a in UCITS, an AIFM would be authorised to de-notify the marketing of an EU AIF it manages only if there would be a maximum of 10 investors holding up to 1 % of assets under management of this AIF in an identified Member State. The AIFM would notify the competent authorities of its home Member State of how it fulfilled the conditions for de-notification and for a public notice of the de-notification. The AIFM would also notify the authorities of the offers presented to the investors to repurchase units and shares of the AIF that was no longer going to be marketed in their Member State. All transparency requirements that investors must fulfil pursuant to Directive 2011/61/EU would continue to apply to investors who would retain their investment after de-notification of the marketing activities in the selected Member State.
- In Article 33, paragraphs 7 and 8, which empower ESMA to develop draft RTS, would be deleted.
- Article 43a would be inserted in Directive 2011/61/EU to ensure consistent treatment of retail investors, regardless of the type of fund in which they decided to invest. Where Member States allow AIFMs to market units or shares of AIFs in their territories to retail investors, these AIFMs would also make facilities available to retail investors to serve situations such as making subscriptions, making payments or repurchasing or redeeming units. For this purpose, AIFMs would be able to use electronic or other means of distance communication.

The changes the proposal would bring – the regulation

Article 1 of the [proposed regulation](#) would introduce the definitions and links to UCITS and AIFMD respectively.

Article 2 would set the requirements for marketing communications, namely (i) the communications would be identifiable as such; (ii) they would present the risks and rewards of purchasing units or shares of AIFs and UCITS in an equally prominent manner; and (iii) all information included in marketing communications would be fair, clear and not misleading.¹¹ UCITS management companies would make sure that no marketing communication that contained specific information about a UCITS contradicted – or diminished the significance of – the information contained in the prospectus (Article 68 of the UCITS Directive) and the key investor information (Article 78 of the UCITS Directive). Similarly, AIFMs would ensure that no marketing communication compromising an invitation to purchase units or shares of an AIF that contained specific information about an AIF made any statement that contradicted – or diminished the significance of – the information that needed to be disclosed to investors (Article 23 of AIFMD).

Articles 3 (publication of national provisions concerning marketing requirements) and 4 (ESMA central database on national provisions concerning marketing requirements) would introduce a transparency framework for national provisions on marketing requirements. According to these articles, NCAs would publish online – and notify ESMA about – all applicable national laws, regulations and administrative provisions governing marketing rules for AIFs and UCITS, and their summaries, in at least a language customary in the sphere of international finance. To streamline the information flows between the competent authorities and ESMA, article 3 would provide for the power to implement technical standards, and to determine standard forms, templates and procedures for the notifications. As for ESMA, withing one month after the entry into force of the regulation, it would have to publish and maintain on its website a central database containing the national laws, regulations and administrative provisions concerning marketing requirements, and the summaries thereof, and the hyperlinks to the websites of competent authorities.

Where NCAs require systematic notification of marketing communications that the UCITS management companies intend to use in their dealings with investors to verify compliance of such communications with relevant national provisions on marketing requirements, they would inform the UCITS management company within 10 working days of the need to amend its marketing communications. Furthermore, they would establish, apply and publish applicable procedures ensuring transparent and non-discriminatory treatment regardless of the origin of the verified investment fund. By 31 March of each year, the NCAs would inform ESMA of the decisions rejecting or requesting adaptations to marketing communications (the report to ESMA would be further detailed under article 5).

Article 6 would provide that, where the competent authority levied fees or charges, they would be proportionate to supervisory tasks carried out, and the relevant invoices – which would indicate the fees/charges, the means of the payment and the date when it was due – would be sent to the registered offices of the AIFMs or UCITS management companies.

Article 7 would require the competent authorities to publish and maintain on their websites in at least a language customary in the sphere of international finance, central databases on the fees or charges mentioned in the previous article, or – where applicable – relevant calculation methodologies. The NCAs would further notify ESMA of those levels and methodologies. The article would empower ESMA to develop implementing technical standards to determine standard forms, templates and procedures for the notifications, to streamline the information flows between ESMA and the NCAs.

Article 8 would entrust ESMA with the task of publishing and maintaining online an interactive database with the fees or charges charged by the competent authorities, or, where applicable, with the calculation methodologies used. Article 9 would provide further that, as part of this database,

ESMA would develop, make available and maintain on its website a publicly accessible interactive tool on fees and charges.

ESMA would also be required to publish and maintain on its website a central database on all AIFMs, UCITS management companies, AIFs and UCITS, as well as the Member States where those funds were marketed (article 10).

Article 11 would require NCAs to transmit the notifications and notification letters referred to in the previous article to ESMA. To standardise and streamline the information flows between investment funds/AIFMs or UCITS management companies and the NCAs, as well as between NCAs and ESMA, this article would empower ESMA to develop draft regulatory and implementing technical standards.

Articles 12 and 13 would amend Regulation (EU) No 345/2013 (Venture Capital Funds) and Regulation (EU) No 346/2013 (Social Entrepreneurship Funds), to add the concept of pre-marketing in those regulations and allow managers of qualifying EuVECA or EUSEF funds to engage in pre-marketing in the EU.

Finally, article 14 would provide that at most five years after the date of entry into force of the regulation, the Commission would conduct an evaluation of its application, on the basis of a public consultation and of discussions with ESMA and the NCAs.

Advisory committees

The European Economic and Social Committee (EESC), which is consulted on both proposals, is expected to adopt its [opinion](#) on the proposals during its July plenary session.

National parliaments

None of the 18 parliamentary chambers from 16 Member States that scrutinised the proposals raised subsidiarity concerns by the deadline of 11 May 2018, on either the proposed [directive](#) or [regulation](#).

Stakeholders' views¹²

No major views have been expressed on the subject since the publication of the proposals.

Legislative process

Both proposals are still at an early stage. In Parliament, they have been assigned to the Economic and Monetary Affairs Committee (ECON). The Budgets (BUDG) and Legal Affairs (JURI) Committees decided not to give an opinion on the proposal for a regulation. The Legal Affairs (JURI) Committee decided not to give an opinion on the proposal for a directive. The ECON committee has appointed Wolf Klinz (ALDE, Germany) as rapporteur for both proposals.

EP SUPPORTING ANALYSIS

Werner H., [Cross-border distribution of investment funds](#), Implementation Appraisal, EPRS, European Parliament.

OTHER SOURCES

Cross-border distribution of collective investment funds: [pre-marketing and de-notification](#), Legislative Observatory (OEIL), European Parliament.

Cross-border distribution of collective investment funds: [marketing and regulatory fees](#), Legislative Observatory (OEIL), European Parliament.

ENDNOTES

- ¹ For more information, see G. Malmersjo, [European venture capital and social enterprise funds](#), EPRS Implementation Appraisal, European Parliament, October 2016, and A. Delivorias, [Reviving risk capital: The proposal to amend EuVECA and EuSEF](#), EU Legislation in progress Briefing, EPRS, European Parliament, September 2017.
- ² For a short overview, see A. Delivorias, [European long-term investment funds](#), EPRS, European Parliament, March 2015.
- ³ For more information, see M. Szczepanski [Money Market Funds: Measures to improve stability and liquidity](#), EU Legislation in progress Briefing, EPRS, European Parliament, July 2017.
- ⁴ For an overview of passporting, see M. Szczepanski, [Understanding equivalence and the single passport in financial services](#), EPRS, European Parliament, February 2017, and British Bankers Association, [What is 'passporting' and why does it matter?](#), Brexit Quick Brief No. 3, December 2016.
- ⁵ EU funds marketed to investors are usually required to comply with national requirements set by host Member States. These marketing requirements, especially those relating to the content of marketing communications (invitations to purchase those funds), differ across the EU. The European Commission notes, as an example, that some Member States require ex-ante approval of the marketing communications while other Member States monitor the communications ex-post. For more, see the European Commission consultation document [CMU action on cross-border distribution of funds \(UCITS, AIF, ELTIF, EUVECA AND EUSEF\) across the EU](#).
- ⁶ The European Commission notes that to obtain the 'passport', EU investment funds must follow a formal notification process. Regulatory fees are referred to as the fees applied by national competent authorities (NCAs) to process such notifications. The Commission notes that the level of fees levied by host Member State on asset managers varies considerably, both in absolute amounts and in how they are calculated.
- ⁷ The European Commission notes, in this respect, that contrary to *initial notification* for such funds, which takes place between NCAs (i.e. without asset managers being involved), a *change in the information* provided to the home Member State NCA obliges asset managers to provide written notice to the host Member State NCA.
- ⁸ The European Commission, in its proposal, notes that 'the enhanced requirements for the marketing communication are laid down in the proposal for a regulation on facilitation of cross-border distribution of funds. These principles established for marketing communications will apply to all asset managers who market their funds, irrespective of their type. This change will ensure a level playing field and the same level of investor protection across Member States'.
- ⁹ The Commission, in its proposal, notes that 'a parallel proposal for a regulation on the facilitation of cross-border distribution of funds provides for specific rules on the transparency of national laws and requirements applicable to marketing communications with respect to all collective investment funds. These new rules will ensure that comprehensive, clear and up-to-date information is collected and published by ESMA'.
- ¹⁰ These tasks include processing orders relating to the units of the UCITS, the provision of information on how orders can be made and how repurchase and redemption proceeds are paid, or the provision to investors for inspecting, and obtaining, copies of the fund rules or the latest annual report of the UCITS.
- ¹¹ The Commission notes that it is broadly based on Article 77 of Directive 2009/65/EC and extends the scope of application to Directive 2011/61/EU.
- ¹² This section aims to provide a flavour of the debate and is not intended to be an exhaustive account of all different views on the proposal. Additional information can be found in related publications listed under 'EP supporting analysis'.

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