European IMRE News

Informing on the changing face of Europe*

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MiFID's impacts on investment management

Several areas of ambiguity remain, especially over the treatment of outsourcing investment management and distribution of UCITS funds by UCITS management companies

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With the Markets in Financial Instruments Directive (2004/39/EC – 'MiFID') and its implementing measures, the European Union has created a comprehensive regulatory framework for financial services rendered by banks and investment firms. Due to its broad scope, the investment fund industry also has to deal with the MiFID regulation.

MiFID will have an impact on the investment management industry in the EU, as there remain several areas of legislation where overlaps between MiFID and the Undertakings for Collective Investments in Transferable Securities (UCITS) Directive (85/611/EEC as amended) have created uncertainty. This concerns in particular the outsourcing of investment management and the distribution of UCITS funds by UCITS management companies.

How UCITS management companies fall into the MiFID net

MiFID is a service-related piece of regulation that applies to investment firms and regulated markets, as well as to credit institutions providing investment services. Institutions that offer the services of investment advice or asset management have to comply with the MiFID provisions relating to areas such as organisational requirements, conduct of business rules and best execution standards. By contrast, the UCITS Directive is a product-related regulation, which exclusively regulates the management, administration and distribution of the UCITS product.

According to Article 2 (1) h) of MiFID, collective investment undertakings, their managers and depositaries are exempted from MiFID provisions. However, if fund management companies offer individual portfolio management on a discretionary basis, and/or investment advice, MiFID standards apply directly to these additional service lines, in particular the provisions regarding minimum capital, organisational requirements and conduct of business obligations. Furthermore, while MiFID applies clearly to UCITS distribution by MiFID investment firms, it does not apply where the UCITS funds are distributed by their collective scheme manager.

Areas of interaction

The areas where UCITS and MiFID legislation overlap raise several important questions which need to be clarified in order to prevent inconsistencies in the application of the two types of legislation on both European and national levels.

One area of overlap occurs where UCITS management companies delegate functions, particularly asset management and distribution, to MiFID investment firms or even other UCITS management companies. As yet it is unclear whether the outsourcing of asset management from one UCITS management company to another constitutes the insourcing of discretionary portfolio management for the insourcer and, consequently, means that the insourcer needs an extended scope license. The EU's 'Questions and Answers on MiFID', published in September 2007, seems to suggest that this is the case.

A second overlap occurs at the point of distribution. Currently, it is still under discussion whether distribution of third-party UCITS is a service which may be insourced by a UCITS management company or whether this is a service restricted to MiFID firms. If the latter were the case, the MiFID conduct of business rules, and in particular those on suitability or appropriateness and inducements, would be applicable. This would mean that clients and investors could be subject to different protection provisions depending on the point of sale approached. In any case, these points leave room for interpretation by the national regulators.

Clarification on these uncertainties is expected from the Vade mecum of the European Commission on UCITS/MiFID interactions, which should be released in early 2008. In the meantime, however, market participants should be aware of the ambiguities.

Member States had to transpose MiFID on 1 November 2007. While in most Member States implementation has been completed in time, others are taking their time.

Several countries have yet to transpose MiFID.

Transposition of Lamfalussy Directives – State of play as at 6/11/2007

Directive	AT	BE	BG	CY	CZ	DE	DK	EE	IE	EL	ES	FI	FR	HU	IT	LT	LU	LV	MT	NL	PL	PT	RO	SE	SI	SK	UK
Directive on Markets in Financial Instruments (2004/39/EC – MiFID)	OK	EX	OK	EX	NC	EX	EX	NC	EX	OK	NC	EX	EX	NC	EX	EX	OK	EX	EX	EX	NC	NC	OK	OK	NC	OK	OK
MiFID implementing Directive (2006/73/EC)	OK	EX	OK	EX	NC	EX	EX	NC	EX	NC	NC	EX	EX	NC	EX	CP	OK	EX	EX	EX	NC	NC	OK	OK	NC	OK	OK

CP: partially notified to the Commission
NC: no notification received by the Commission
EX: notification received and under examination by the Commission
OK: notification received and checked by the Commission

Source: http://ec.europa.eu/internal_market/securities/docs/transposition/table_en.pdf

Increasing real estate transparency and comparability: the way forward

A PricewaterhouseCoopers survey of European real estate entities' financial statements showed that IFRS enhances the level of comparability, but room for improvement remains

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The global shift to International Financial Reporting Standards (IFRS) is changing fundamentally the way real estate firms present their business and the way their financial statements are judged by analysts, investors and others. More information is finding its way into the opening sections of annual reports: for example, the wider inclusion there of industry ratios such as triple net asset value (NNNAV). But just how well is the industry absorbing these changes into its financial reporting and turning them to advantage?

PricewaterhouseCoopers[1] detailed analysis of the financial statements of 50 real estate firms reveals how they are applying these standards and what choices they are making within them.

The table opposite highlights the areas and the key findings of those areas.

Recognition, measurement and classification of real estate categories

Not all categories of real estate assets disclosed in the balance sheet are defined and described in the accounting policies. The accounting treatment upon initial and subsequent measurement for each category is, therefore, unclear, as is the treatment of recognition and derecognition. Real estate entities are diversifying their activities in order to achieve the performance levels their stakeholders expect: transparency in reporting new activities is key to the user of financial statements.

Income statement presentation

There is a variety of terms used in the definitions of revenue noted in the survey, and hence substantial divergence of practice. Comparability of the income statement is vital to the users' proper analysis of the results of real estate firms and individual real estate assets. Further, disclosure of whether the entity acted as a principal or as an agent is missing, information that may clarify the accounting treatments applied in the income statement.

Acquisitions – business combinations versus asset deals

It is clear that many investments are occurring each year and these activities are well described in the front sections of the annual report (that is, not in the financial statements). Differences in defining and describing the accounting treatment of an

[1] 'PricewaterhouseCoopers' refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

Topic	Key findings
Recognition, measurement and classification	Besides investment property which shows up in nearly all financial statements, the categories used in the balance sheets are PPE own use, PPE development, inventory, transaction property and assets held for sale. But not all these categories of real estate assets are defined and described properly in the accounting policies.
Income statement	Various components are presented as part of revenue. In some cases, not only various components of revenue but also costs are included as part of revenue, leading to a net presentation. Further, the notes and the accounting policies should clearly state what is included in revenue. Where service charges are included in revenue on a gross basis, it is unclear that the entity acts as principal rather than as an agent.
Acquisitions	The implications of the distinct accounting treatment of asset deals and of business combinations are missing, especially in relation to deferred taxes and to goodwill.
Development property	Where an entity has development property, this is presented separately in the balance sheet, or in the notes and, in rare circumstances, as construction contracts. Development property is measured at cost. The criteria of real estate transfer in and out of investment property are not disclosed in the accounting policies.
Deferred tax	Calculating the deferred tax balance is well understood in the RE industry, but it is not disclosed in all cases how this balance has been calculated and what the impact is of adjustments on this balance. The impact of different tax rates or of tax-efficient structures is not clear.
Lease incentives	Generally, the impact of lease incentives on the valuation of real estate assets is not disclosed.

asset deal compared with a business combination, and the implications on the recording of goodwill in the balance sheet, are disclosed in their accounting policies by only a few businesses. Further, the assessment of the goodwill (including deferred tax balances) and the use of the initial recognition exemption are not applied consistently.

Development property transfer into other categories

The criteria of real estate transfers in and out of development property are not disclosed in the accounting policies. It is difficult to assess valuation changes recorded upon transfers out of the development property category as these disclosures are limited.

Disclosures on deferred tax

Potentially significant considerations to deferred tax in the real estate industry, using the applicable tax rates for settlement (use of corporate tax, capital gains tax and other applicable tax rates, on an asset by asset basis, to assess the applicable effective tax rate) are well understood within the industry but not well disclosed. The disclosure of tax-efficient structures, such as the wrapper or the REIT, or reinvestment, is made only by a few entities.

Lease incentive disclosures

The potential impact of lease incentives on the valuation of real estate assets is generally not mentioned. The correct treatment of lease incentives is well known in the real estate industry. The survey results provide no evidence of double counting of lease incentives, but the lack of disclosure in this area may lead to some doubt (in the eyes of the uninformed user) about whether or not real estate asset valuations are in fact adjusted to take into account the impact of lease incentives.

Conclusion

It is clear from this survey that real estate firms have some way to go to increase the transparency and comparability of their financial statements. The choices available in IFRS can lead to the adoption of different options, making comparisons difficult. Nevertheless, this has been an important year for financial reporting in the real estate industry. Continued co-operation and communication within the industry should lead to the greater transparency that will in turn produce increased comparability – to the benefit of all stakeholders in the business.

Focusing on outsourcing controls

Growing derivatives use and the call for greater transparency in alternatives are making the control of outsourcing partners an urgent topic

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New trends in both mainstream and alternative investment are driving increased derivatives use, as providers seek to increase absolute returns and develop ever more complex product structures. Yet the non-uniform nature of derivatives contracts, especially OTC contracts, means that existing middle and back office systems cannot automatically process many derivatives trades/margin calls or settlements.

Derivatives processing is a non-standard task that requires advanced IT systems that fund administrators are even now racing to build. As a result, investment managers are increasingly relying on the fund administrators to invest in new systems and provide solutions to the technical issues faced. Clearly, as complexity increases, the control and oversight of outsourced administration becomes far more difficult.

For investment managers, tackling this issue is critical to achieving business plan objectives. Failure to have adequate administration, backed by robust controls, can prevent them from moving into new product areas.

As a starting point, investment managers need to remember that they are ‘delegating not abdicating’ administrative or regulatory responsibilities. They then have to assess the most effective way to outsource administration, which may not always be the most straightforward. Finally, they need to consider how they can communicate the robust nature of their outsourcing model to both investors and regulators.

Mainstream managers are following hard on the heels of hedge fund and other alternative managers, where the model typically outsources pretty much everything apart from the front office investment decision-making.

Both institutional investors and regulators are becoming aware of the operational risks surrounding derivatives use and outsourcing. For this reason, institutional investors are increasingly keen to understand the operating models used by their investment managers, while the UK’s Financial Services Authority continues to focus on core operations and outsourcing arrangements.

Calling on specialist administrators

But the greatest difficulty for investment managers is that even the large fund administrators do not yet have systems able to cope with all areas of derivatives processing. In spite of considerable investment, most still have ‘silos’ of derivatives expertise rather than integrated application infrastructures.

Consequently, it may make most sense for investment managers to work with several niche administrators, selecting the best specialist firm in each area. In order to do this, an investment manager may need infrastructure internally that allows it to ‘plug and play’, or move from one administrator to another as it makes sense to do so.

What is more, this increased level of outsourcing may need to be reflected in the investment manager’s operations department. New skills may be required, for example to manage and provide oversight over the relationships with administrators.

The role of assurance reports

In an environment where institutional investors are generally demanding more transparency, there is an awareness of the hazards of derivatives processing. This is leading to more control reports being conducted, such as the AAF 01/06 assurance report that the Institute of Chartered Accountants in England and Wales (ICAEW) published guidelines for in June 2006. (SAS 70 reports, issued by the American Institute of Certified Public Accountants, are the US equivalent.)

Certainly, several of London’s larger hedge fund managers have either commissioned, or are considering commissioning, controls reports such as this. Additionally, the majority of Dublin-based administrators have done so for their businesses.

Given the expectation that derivatives use will continue to grow across all sectors, and that institutions will continue to seek more transparency from alternative investment managers, we anticipate that such independently conducted control reports will become far more common.

Widening the scope of VAT exemption for asset management

As the full implications of the June European Court of Justice (ECJ) decision in the JP Morgan Fleming Claverhouse case become clearer, asset managers need to tackle the issue of falling VAT recovery rates, as well as reclaims and reimbursements

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The recent judgment of the European Court of Justice in JP Morgan Claverhouse[1] threatens to significantly extend the scope of VAT exemption for asset management, potentially enabling investment funds to achieve ongoing VAT savings as well as retrospective windfall claims. Whilst this is potentially an opportunity for funds, greater VAT exemption would have more serious financial consequences for asset managers, who would have to deal with falling VAT recovery rates on overheads and the thorny issue of agreeing reclaim and reimbursement positions with their clients.

In essence, the ECJ held that the UK's implementation of the VAT exemption for 'the management of special investment funds as defined by Member States'[2] is unfairly discriminatory and supported JP Morgan's contention that, rather than the exemption being limited to Authorised Unit Trusts (AUTs) and Open-Ended Investment Companies (OEICs), it should also extend to the management of Investment Trust Companies (ITCs). Although the ECJ recognised that ultimately this is a question for the referring court to decide, its expectation is clear from the judgment: it considers the management of ITCs to be exempt.

Latest reports suggest that HMRC is now prepared to concede the case but is eager to limit the application of exemption to other funds.

Extension to other funds

HMRC has issued a Business Brief making clear that it considers that the case only applies to ITCs and will not recognise claims by other funds. Furthermore, it will not recognise claims on a protective basis and will force other funds to litigate one by one. While the case itself only concerned ITCs, the same principles would be applied to claims for VAT exemption brought by other fund types.

The ECJ held that Member States do have an element of discretion to pick which funds get VAT exemption, but that this discretion is fettered by both the purpose of the exemption and the principle of fiscal neutrality. The ECJ considered that the purpose of the exemption was to create a level playing field between investments in securities directly and investment via pooled funds. The principle of fiscal neutrality is effectively a competition principle that competing suppliers of similar goods and services should not be treated differently for VAT purposes.

[1] JP Morgan Fleming Claverhouse Investment Trust plc and The Association of Investment Trust Companies v Commissioners of HM Revenue and Customs (Case C-363/05) (unreported).

[2] Article 135(1)(g) of Directive 2006/112/EC, formerly Article 13B(d)(6) of the EC Sixth VAT Directive.

[3] Decision, paragraph 50.

[4] TAXUD/2139/07 – EN.

[5] In respect of which the investor has the right for his investment to be redeemed at any time.

[6] Case C-169/04.

The ECJ asked whether the funds were competing products from the perspective of investors and found that ITCs were in competition with AUTs and OEICs because all three types of fund are 'forms of special investment which spread risk' and involve 'investment in securities through the intermediary of a collective investment undertaking which allows private investors to invest in wide-ranging investment portfolios and thus reduce the stock market risk'.[3] Clearly these features are present in all collective investment funds.

HMRC and the asset management sector now face the prospect and uncertainty of legal claims for VAT exemption by a range of funds. Whilst obvious claims would seem to exist for venture capital trusts (VCTs), unauthorised unit trusts and unitised and unit-linked life products, it is undoubtedly claims in respect of personal and occupational pension schemes that will be the main event.

Pension funds

Pension fund management is VAT exempt in a number of other member states and the management of pension funds is included within the draft revised exemptions recently issued by the European Commission for consultation.[4] It is understood that this proposal has the overwhelming support of the Commission and the other member states.

It may be suggested that the particular features and long-term nature of pension funds mean they should be distinguished from UCITS funds and ITCs; one would have sympathy with the argument that the statutory controls on redemption of interests in a pension fund mean they do not occupy the same market space as retail fund products. However, it is notable that the ECJ did not consider the differences in liquidity between redemption of investments in open-ended funds (such as AUTs and OEICs)[5] and closed-ended funds (such as ITCs) to be a relevant consideration and made clear that differences of national law are not relevant criteria on which to deny exemption.

Furthermore, the common features of AUTs, OEICs and ITCs as discussed by the ECJ seem equally applicable to pension funds. The ECJ took a fairly broad-brush approach to the question of whether ITCs are in competition with UCTIS funds, but how would it approach a more difficult case such as pension funds?

Exposure of asset managers

The big question for asset managers is how to balance the demands of customers to file protective claims while protecting their own legal and financial position. There is a clear tension between managing the all-important customer relationships and managers' own interests. At the heart of the issue is that if it is proved that services should be VAT exempt, the manager will be able to reclaim VAT overpaid from HMRC, but will suffer a disallowance of VAT previously recovered on costs. This means that VAT reclaims from HMRC will be less than the VAT originally charged to customers. Agreeing how much will then be reimbursed to customers raises a number of complex legal and commercial issues.

Furthermore, fund customers will have recovered some of the VAT originally charged, which in principle is repayable to HMRC if VAT exemption is claimed. This means that funds with high VAT recoveries (such as those investing in non-EU markets or local authority pension schemes) may not financially benefit from VAT exemption if they are only reimbursed whatever partial VAT reclaim is received from HMRC. This can put the manager of a range of funds with differing recoveries in a very difficult position when determining whether to claim for exemption.

The industry has now dealt with many of these issues following the ECJ decision in Abbey National[6] and is now dealing with them in respect of ITCs. It is imperative that asset managers learn the lessons from those experiences and understand the risks they face. Whilst the effort involved in addressing the issue and dealing with claims is a burden, there is an opportunity for managers to take the right steps now to manage their risk and exposure effectively. Hopefully lessons have been learned and that opportunity is not missed.

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New VAT exemptions on the horizon

The European Commission's review of the application of VAT to the financial services sector continues to progress. Draft proposals for a new Directive and Regulation redefining the VAT exemptions were published in July and the final versions were received in November. The planned implementation date for the reforms is 31 December 2009.

There remains some uncertainty over the future scope of the investment management exemption under the proposals. The drafts published in July specifically refer to the management of both pension funds and hedge funds as being exempt, however recent drafts appear to have dropped the reference to pension funds. The Commission may have changed its approach in favour of a more general definition referring to undertakings for collective investment in exempt securities (and, importantly, real estate). The current scope of the exemption is the subject of much uncertainty following the European Court's decision in the JP Morgan case.

The draft Regulation lists a large number of activities that are included within the concept of 'management' (notably including safe custody and market analysis) as well as some that are excluded (such as regulatory compliance and systems development). However, this does not necessarily mean that the included services will be exempt if supplied in isolation.

Investment funds and their suppliers should continue to monitor these developments carefully.

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Watch the wealth management gap

Further analysis of our 2007 global survey shows that while this is a time of rapid growth in wealth management, those that will be tomorrow's leaders are beginning to pull ahead of the rest

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Within wealth management, all is booming. Growing individual wealth is fuelling fast expansion in assets under management, feeding through to real expansions in profit.

Yet these new clients are different from their predecessors. Having made their fortunes themselves, they are often more demanding. And they are more diverse – both by race and by age.

Our further analysis makes it clear that wealth management is evolving. Tomorrow's leading wealth managers will be those that focus on delivering excellent client service. Doing this requires major strategic shifts and investment, as well as operational and cultural changes. It will not be easy, but those that succeed will reap the rewards offered by market growth.

The recent 2007 Global Private Banking/Wealth Management Survey, published in June, revealed a contrasting picture of growth and challenges. CEOs were predicting the highest annual growth in assets seen in the survey's 14-year history – a staggering 30%. At the same time, the challenges of serving the new wealthy surfaced again and again.

The foresighted few prepare for the future

Most significantly, a gap appeared to be emerging between those wealth managers taking actions to prepare for a new world, and those not doing so. Such is the magnitude of change required that implementing it is a long-term business. The danger is that by failing to change, some wealth managers fall behind, becoming firmly consigned to the sector's second division.

The very shape of the survey bore witness to the new type of client. We questioned 265 organisations in 43 countries. Participants came not only from the established markets of the Americas and Western Europe, but also in large numbers from Eastern Europe and countries such as India and Singapore. Russia, for example, has a fledgling wealth management sector that is getting bigger by the day.

Excellence is key

Delivering excellence is obviously the key to the new client. While all of our participants appeared to agree with this, there was less understanding as to what it really meant. For example, more than 80% of client relationship managers (CRMs) believed they had achieved 'trusted adviser' status – yet nearly 50% admitted their knowledge of extended family issues was at best moderate.

And with people issues the wealth manager's greatest challenge, few showed signs of properly addressing this. The sector's growth will demand more and different types of CRMs. But only a few firms are tackling this through more innovative recruitment, better talent management, leadership development and training.

There is also a gap emerging in systems. In the past few years almost 60% of wealth managers have executed major upgrades of their core systems. Even so, nearly a third of COOs regard systems as not fit for purpose. With business volumes expected to significantly outstrip current capacity, clearly this could lead to poor client service.

These are not the only areas in which our further analysis illustrates an emerging gap between the foresighted and the short-sighted. It is easy at a time of rapid growth to be lulled into a false sense of security, but actions taken today are already determining the leaders of tomorrow.

ICVCs make their way to Switzerland

Following their introduction at the beginning of 2007, ICVCs offer considerable potential for private labelling

In September 2007, Switzerland's first Investment Company with Variable Capital (ICVC) was authorised by the Swiss Federal Banking Commission (SFBC) – some eight months after the investment vehicle was introduced in the country.

The Collective Investment Scheme Act (CISA) and its implementing ordinance, the Collective Investment Scheme Ordinance (CISO) have been effective since 1 January 2007. One of the most innovative creations of this new law is the ICVC, an investment company with variable capital (also known as SICAV: Société d'investissement à capital variable). The ICVC's introduction extends the spectrum of investment vehicles available to investors and, in particular, appeals to small independent asset managers looking for pooled structures to manage their clients' assets.

Product and institution rolled in one

The basic structure of the ICVC is similar to the Luxembourg legislation on ICVCs, and complies with the Swiss Code of Obligations (CO) for public limited companies. The ICVC is legally organised as a company with its own governing bodies (Board of Directors, general assembly, audit firm). Its exclusive purpose is the collective investment of assets. Unlike fund management companies, it cannot offer any other services to third parties, such as investment advisory or asset management services.

As its name implies, the capital of an ICVC is not predefined but varies. As an open-ended collective investment scheme, its shareholders can redeem their shares at any given time. Additionally, an ICVC may also issue new shares at any time. Neither case requires an amendment to statutes or a new entry in the commercial register.

A characteristic of the ICVC is the separation of its equity into 'investor' and 'entrepreneur' shares. The 'investor' share capital is raised from individual investors, and then invested according to the rules of the investment policy. The investment policy is regulated by the same rules as those applicable to contractual investment funds. Therefore, ICVCs can be set up as securities funds, real estate funds or other funds for traditional and alternative investments. They can also be designed as umbrella funds, with different categories of shares specified in the statutes.

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The entrepreneurial shares are created by the fund's promoters, serving to hedge operational risks and to finance the operating assets (real estate, movable property, IT, etc.). Apart from the assets necessary for operations, the entrepreneurial capital may be invested analogously to the investors' shares, or used to acquire units in the sub-funds.

Self-managed ICVCs versus ICVCs managed by a third party

An ICVC may either be a self-managed institution or be managed by a third party. A self-managed ICVC performs its own administrative tasks as if it were a mini fund management company. ICVCs managed by third parties outsource such tasks to a regulated fund management company.

Incorporating an ICVC

As regulated entities, ICVCs require a licence from the SFBC. They must, therefore, take into account not only CO requirements but also the regulatory licensing requirements. These are described in a generic manner in article 14 CISA and specifically stipulate that:

- the persons responsible for the administration and the management of the company must be able to provide guarantee of proper business conduct;
- those holding qualified participations have good reputations;
- there are sufficient financial resources;
- the operation is adequately organised.

Capital requirements differ significantly. At incorporation, the entrepreneurial shareholders of self-managed ICVCs must contribute a minimum of CHF 500,000, whereas the capital requirements for an ICVC managed by a third party is only CHF 250,000. Furthermore, a self-managed ICVC must cover its fund assets with its own capital resources for the duration of its existence, just like a fund management company. An ICVC managed by a third party does not need to fulfil capital adequacy regulations as the fund management company in charge of managing it is already subject to minimum capital requirements.

Shareholders' position

Shareholders of a traditional investment fund are only entitled to a contractual claim towards the fund management company to a part of the fund assets; shareholders of an ICVC, on the other hand, are considered partners. This entails certain membership rights which can generally be separated into rights to assets, control and participation.

While the rights to assets and control of an ICVC shareholder are generally equal to those of an investor in a traditional investment fund, these two types of open-ended collective investment schemes actually offer different participation rights. In a traditional investment fund, such rights are limited to the investor's right to object to proposed amendments to the fund regulations (as per article 27 paragraph 3 CISA). On the contrary, shareholders of an ICVC, in their status as a partner, have the right to participate and to pass resolutions at the annual meeting. Such a meeting must take place annually within four months of the business year-end, and shareholders must be invited at least 20 days in advance. If an ICVC is split into several sub-funds, there may be additional separate general meetings, at which only resolutions concerning particular aspects of a sub-fund are voted. Voting rights reflect the stipulation of article 47 CISA, which proclaims that each share is entitled to one vote.

The role of the Board of Directors

The Board of Directors must consist of at least three members and acts as the executive body of the ICVC. CISA has introduced a new requirement (article 51 paragraph 1 CISA) limiting the size of the Board to seven members. According to the regulators, this should lead to an improvement of corporate governance; however, it could also lead to the situation where not everyone willing to participate is represented at the Board. What was not taken into consideration at the time is that individual fund promoters were attracted to this new investment vehicle precisely because of the opportunity to directly influence the business activities.

The tasks and duties of the Board of Directors are described in article 64 CISO. They not only include a list of

non-transferable tasks as per article 716a CO but also the duties to determine an investment policy and assign a custodian bank. Furthermore, they are responsible for the creation of new sub-funds, and for coordinating the preparation of the prospectus and the simplified prospectus, as well as for administrative tasks.

ICVCs managed by a third party: potential for private labelling

Private labelling – also called white labelling – is especially popular among independent asset managers. Instead of creating their own structures – generally a cost-intensive endeavour – an external fund management company is assigned to create a tailor-made fund. The investment policy of this private-label fund is tailored to the requirements and wishes of the client asset manager, to whom the investment advisory services, the asset management and the distribution of the fund are delegated. In order for the investors to appreciate that the fund is a proprietary product of the client, a private-label fund generally carries the client's name rather than the name of the actual fund management company.

For private labelling, the ICVC managed by a third party is an attractive alternative to the contractual investment fund. The ICVC delegates the entire administration to an authorised fund management company but its investment policy to the promoter. In comparison to the contractual investment fund, this set-up specifically has two advantages: on one hand, the promoter can be part of the ICVC's Board of Directors, and can thereby directly influence its activities; on the other hand, the investment management company reduces its liabilities because it is only liable for the tasks it has been delegated.

Securitisation in the UK – The new permanent regime

Establishment of a UK permanent tax regime for securitisation provides a model for competing with securitisation platforms elsewhere in Europe

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Securitisation began in the UK in the 1980s and has since been mostly used by banks as part of managing risk in their balance sheets and to help meet regulatory capital requirements.

However, in recent times it has become a key structuring tool for many within the alternatives market, particularly within the hedge fund space. The process enables funds to securitise or package debts of differing credit ratings, and to tailor the end risk/reward product to different clients.

The EU introduction of the requirement for listed companies to use International Financial Reporting Standards (IFRS) created a difference of treatment between IFRS and UK GAAP, resulting in difficult tax positions for UK securitisation vehicles. Representations were made by the industry and it was announced by the UK government that a permanent tax regime for securitisation companies would be created.

Details of the new regime

In the UK, for periods beginning on or after 1 January 2007, where an entity meets the definition of a 'securitisation company' it will be taxed under the new regime whereby only retained profit, which can be nil if so decided by the directors of the entity, is taxed. There are various conditions to be met for the regime to apply. Also where certain of these are breached the favourable tax treatment will be lost and cannot be reinstated.

The favourable regime has taken a global approach and covers not only UK-resident entities but also non-resident entities with a UK permanent establishment. The regime also includes extended definitions to incorporate Shari'a-compliant bonds, otherwise referred to as 'sukuk' issuing companies, into the securitisation regulations such that they may also obtain any favourable tax treatment.

The UK securitisation regime is a rapidly changing sector, and the tax rules are new and may face further legislative change as we move forward. However, the UK now has a model to compete with the securitisation platforms found in continental Europe.

Germany catches up

Following 2007's amendments to the Investment Law, Germany's investment managers are catching up with their peers elsewhere in Europe in being able to offer their clients far more complex products

Hardly any limits remain to what German investment funds can do. Amendments to the Investment Law, which are likely to be introduced in December 2007, together with the Commission Directive, the Committee of European Securities Regulators' guidelines for eligible assets and the newly aligned administrative practice of the Federal Financial Supervisory Authority (BaFin), have created far more possibilities.

They have extended the range of instruments permitted within the scope of portfolio management, created new types of funds and, consequently, provided investment companies – particularly institutional investors – with the possibility of offering tailor-made investment products.

At the same time, however, the demands made on risk management rise in line with the level of complexity of the instruments being used.

Wider range of underlyings

The purchase of closed-ended funds and the no-longer-required 'look-through' when using certificates that track the performance of underlying instruments, represent fundamental innovations in security-based asset management. This follows a widening in the range of possible underlying instruments earlier in the year. Derivatives on real estate and, in some cases, on hedge fund indices are now allowed, as well as derivatives on commodity indices. With this wide range of instruments, it is now possible to offer interesting new return/risk profiles for investors, which also include underlying instruments previously not permitted.

A new type of fund has been created with the 'Sonstigen Sondervermögen' which is positioned between 'Gemischten Sondervermögen' and 'Hedge Fonds'. This is characterised by the considerably wider range of permitted derivatives, which include instruments on individual commodities and precious metals. In addition, it is possible to effectively invest in precious metals, non-listed companies and non-securitised loan receivables. This is combined with reduced investment restrictions, such as no requirements governing the minimum number of issuers necessary to make up an investment fund. And the borrowing limit has been doubled to 20%.

Greatest opportunities in institutional business

Investment companies have the greatest opportunity for creativity in institutional business. With the exception of the hedge fund, which still exists as a separate type of fund, all other permitted fund components – whether in the form of a cash instrument or derivative – can be combined into a special fund. In the future, there is only a limit to the market risk (200%) and borrowing (30%), on condition that the investor has agreed to these considerably relaxed requirements.

The possibility of a considerable rise in the degree of complexity of the products used, however, places high demands on risk management. Investment companies must be in a position to be able to recognise, measure and control in a due and proper manner the risks – such as commodity or real estate risks – involved with individual instruments.

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130/30 funds on a growth curve

Hybrid 130/30 funds are growing assets under management. In spite of criticism, expansion appears set to continue, with even European UCITS III funds being launched

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There is a new and increasingly popular fund in town called the 130/30. Many traditional long-only investment firms offer, or are developing, these new alternative products. Significantly, they show the narrowing gap between traditional managers and hedge funds, as the former bow to demand, adopting tools such as short selling to deliver more flexible strategies.

As with all long-short funds, 130/30 funds carry the advantage of effectively leveraging the fund manager's skills. Of course, this can also highlight a manager's stock-picking prowess (or the lack of it) – especially for those inexperienced in the fine art of shorting.

Within Europe, it is likely that these funds will be more than just an institutional product. UCITS III rules give managers sufficient flexibility to market them to retail investors. For example, State Street Global Advisors is managing a £165m UCITS-compliant 130/30 product.

All the signs are that 130/30 is more than just a fad. Merrill Lynch estimates that around US$50bn has been placed in the strategy 130/30 managers in the last two years. While this is paltry compared with US$9trn in US mutual funds and US$1.5trn in hedge funds globally, it is a number that is expanding rapidly.

Europe has seen a lesser US$5bn raised, with the forecast for 2007 in the US$30-40bn range. Asia is further behind but probably on a growth trend.

The advantages of 130/30

130/30 funds can be seen as an attempt to take the best from both traditional and alternative worlds. Broadly speaking, these hybrid investment strategies achieve 100% net long exposure by being 130% long and 30% short. The 130/30 product has full market exposure or 'beta' – but also creates the opportunity for skilled managers to generate additional 'alpha'. This relaxation of the long-only constraint can improve performance with limited impact on expected risk.

From a marketing perspective, the potential for delivering these funds within a UCITS offers a distinct opportunity to devise more innovative retail funds. With the exception of Ireland, EU jurisdictions prevent UCITS III managers from selling short in a physical manner, but they are permitted to do so using synthetic instruments. State Street's product is an example of this.

Disadvantages

The first thing to remember is that 130/30 is a structure, not a strategy. It is still up to the fund manager to pick the right stocks. The manager has more flexibility, but also comes under more pressure to select the right stocks. Shorting is a difficult game that requires an experienced manager with access to high quality market intelligence.

A disadvantage for investors, although not for managers, is higher fees. According to the recent Merrill Lynch report, US long-only managers typically charge 30-50 basis points management fees while a 130/30 fund may charge 60-100 basis points.

Are 130/30 funds here to stay?

There are many who have doubts about these new products. The danger is that managers with little or no experience in shorting will launch products that perform poorly. They may not deliver the promised alpha and fail to match market beta.

But, overall, 130/30 funds are a natural evolution in the blending of traditional long-only and hedge fund capabilities.

A recent worldwide survey examined the investment attitudes of asset managers, consultants, institutional investors and service providers. Its key findings were:

- 16% of investors polled have already implemented 130/30 strategies;
- 26% are planning to use a 130/30 approach in the next 12 months;
- 25% of consultants polled are actively researching and advising on 130/30;
- 16% of asset managers polled offer 130/30 strategies;
- 31% of asset managers polled are planning to develop 130/30 in the next 12 months.

This shows 130/30 is no passing fad. And, in Europe, it may be about to bring greater choice not only to institutional investors but also the retail market.

Preparing for real estate IPOs in Central and Eastern Europe

With a number of Central and Eastern European real estate IPOs planned, managements need to prepare their companies thoroughly

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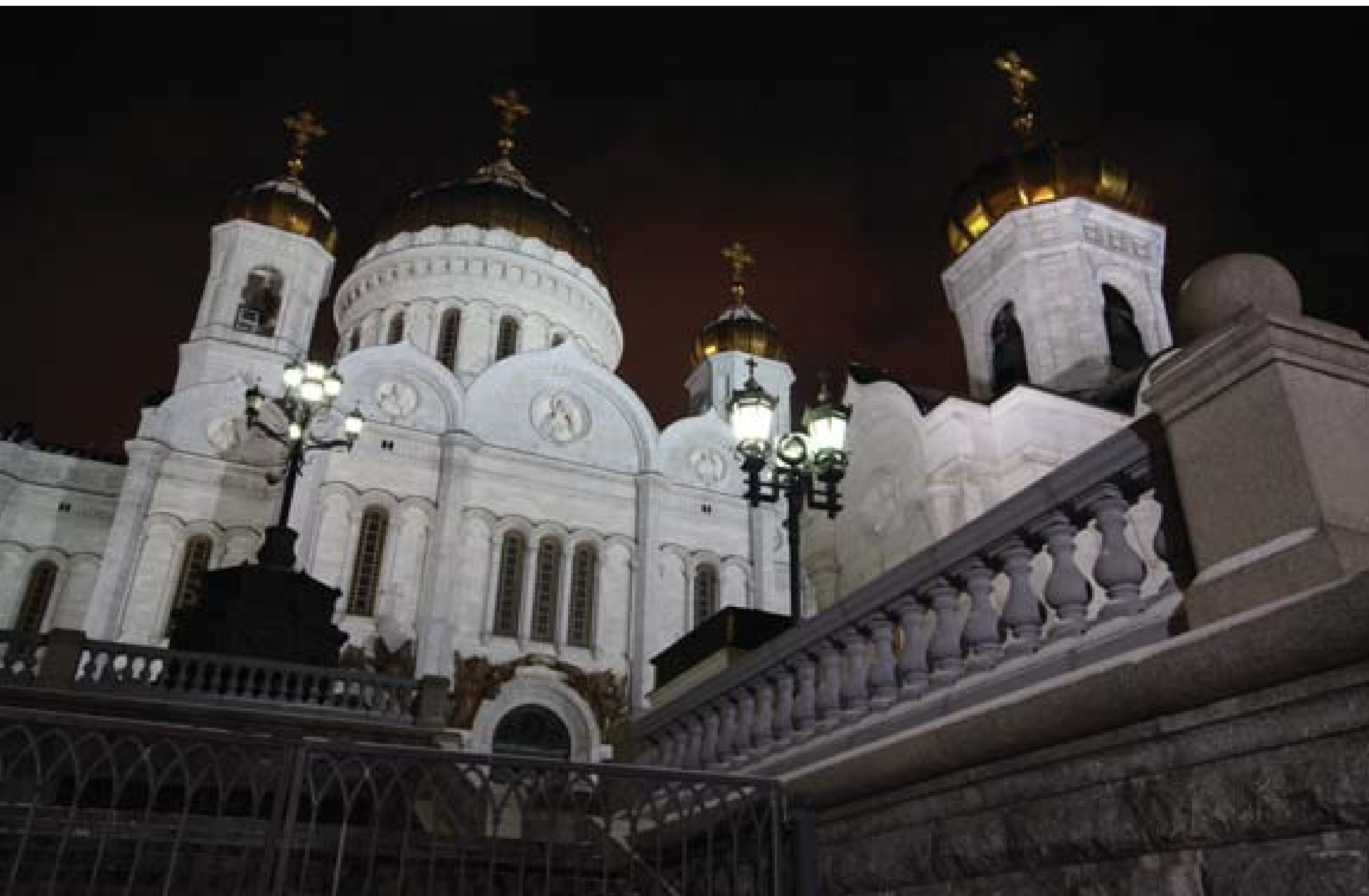
There has been a significant uptake in the number of real estate Initial Public Offerings (IPOs) in Central and Eastern Europe over the last 18 months, with a number of prominent IPOs having already taken place already and a number being slated to come on line over the next 18 months. These transactions are typically being structured as GDR listings on main exchanges, primary listings on domestic exchanges, or as listings on markets such as the London Alternative Investment Market (AIM).

It is not uncommon for real estate structures, especially development companies, to list at significant premiums to the net asset values of the underlying assets. Notwithstanding this, there is significant evidence to suggest that a well-prepared company with appropriate corporate governance, financial reporting procedures and internal control structures will command an improved valuation premium – this is common sense. In the process of an IPO, management can optimise the valuation of their business and ensure that the IPO process itself runs relative smoothly.

Articulating the investment story

A well-rationalised and presented investment story is essential in order to be able to communicate effectively with investors, intermediaries and regulators. Most importantly, it should clearly identify the unique features of your company which sets it apart from its peer group and clearly articulates the objective of the offer and the rationale underlying them. Management focused on creating and enhancing shareholder value will be better able to present their investment story to investors. You should explain your company's market position, its strategy, how it is being managed to deliver shareholder value and the nature of activities that drive value creation. This is becoming increasingly critical as entities seek to differentiate themselves from other similar structures seeking to list around the same time.

Experience demonstrates that some of the most successful company IPOs are those where quality management have been in place for some time and have been able to prepare the business for an IPO. Quality of management is one of the most important criteria by which fund managers assess investment opportunities. Investors expect the board of directors and management team to have the



appropriate collective experience and expertise to run all areas of the business. Be prepared to justify your current board's experience and structure.

Prior to IPO your company may need to reconsider its capital and organisational structure. Such structural changes may include the sale of non-core assets and/or businesses, the simplification of legal and/or general corporate tax planning measures. The resulting corporate structure can create issues about how best to present the financial information to investors', while at the same time complying with regulatory requirements. Early advice should be sought for issues arising in this area.

Ensuring effective corporate governance

Effective corporate governance is the core of an efficient market economy. This requires shareholders to have the information, rights and practical ability to influence management through the governance process, in order to ensure that the company's assets are being used fairly in the interests of all financial stakeholders. This involves both efficient internal financial reporting systems and controls, and external legal and regulatory mechanisms. If investors are unable to evaluate governance risk, they are likely to be reluctant to invest or they will require a significant price adjustment to mitigate uncertainty. In many cases where the investor is unable to evaluate the risks associated with governance practices, equities may be inaccurately assessed. This disadvantages the company and raises the cost of capital. Market participants have numerous and vivid examples that show how poor corporate governance can destroy value.

The quality and standard of reporting demanded by the investment community and regulatory authorities is high. Institutional investors, both during and after the IPO, will require accurate financial and non-financial information to be produced efficiently and on a timely basis. The benchmark is extremely high. The investment community expect, and the regulatory authorities require, a company to publish periodic financial and other information within tight timescales, as well as publishing all price-sensitive information immediately.

Lithuanian real estate market bubble: more illusion than reality

Current indications are that steady rental growth will underpin asset prices. This provides a positive backdrop for the introduction of local real estate funds

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There is currently a debate about how overheating in the US and closer European real estate markets will affect Lithuania's rapidly growing real estate market.

Over several years, the ratio between Lithuanian real estate asset prices and rents has doubled, which means that renting has become more and more attractive as compared to acquiring real estate. This has been cited as evidence of a bubble forming.

However, rental fees have recently started to grow. Considering the slowly growing supply, this can be viewed as a sign of a healthy market.

To summarise, demand for real estate continues to grow while supply lags somewhat behind, and real estate asset prices are on an upward curve. However, forecasts of real estate price trends should be made very carefully, as real estate supply in Lithuania is arguably too low and structural changes such as liberalisation of zone planning, and other legislation regulating the construction industry, may have a significant impact.

The first steps have already been made in this direction, and Lithuanian business is looking forward to positive changes and notably increased supply. On the other hand, rising interest rates tend to slow demand growth. Therefore, depending on how supply reacts to the growing needs of Lithuanian business, two possible scenarios for rental price trends would be as follows: firstly, stabilisation if supply more closely satisfies demand; or, secondly, further moderate increases if demand grows more quickly than supply. Currently, the latter scenario is thought more likely than the former. Moderate growth in rental prices should reduce the probability of a local bubble bursting and, therefore, any negative impact on the stability of the mortgage banking system or development of the wider economy.

Introducing real estate funds

As of 1 January 2008, amendments to the Law on Collective Investments come into force. These amendments provide a legal basis for the establishment of Real Estate Investment Funds in Lithuania. There has been no legal basis for establishment of such funds in Lithuania until now.

Under these amendments, real estate funds have two main investment options. They can either invest directly in real estate or indirectly through securities (shares, derivatives etc.) collateralised by real estate.

When investing directly, they cannot invest more than 30% of net assets in one property or real estate company, and the total investment in construction in progress may not exceed 20% of net assets.

When investing indirectly through securities, the total investment in the securities of a single real estate holding company, its money market instruments or liabilities arising from derivative instruments, may not exceed 30% of the net assets of the real estate fund.

Jersey launches Unregulated Funds Regime

Following a review of what investment managers want from offshore jurisdictions, Jersey is taking the innovative step of allowing certain types of fund to launch without regulatory approval

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Just a year after canvassing some of the leading investment managers and their advisers about what they wanted from an offshore jurisdiction, Jersey is responding by launching its new Unregulated Funds Regime. As the name suggests, promoters of these funds will not need to have them approved or authorised by the island's regulator.

When Jersey Finance, the local finance industry's promotional body, carried out the review in late 2006, its clear conclusion was that promoters wanted 'simplicity, certainty and speed' when setting up certain types of specialist fund.

In all respects, Jersey is taking a step forward in offering these characteristics to investment managers. While carrying a risk warning making clear that they are only suitable for professional and expert investors, and with some carrying a high minimum investment, there are no restrictions on who can invest. And there is no requirement for a local audit sign-off.

Increasing simplicity

Set for introduction in early 2008, the new Unregulated Funds Regime includes an Unregulated Eligible Investor Category and an Unregulated Exchange Traded Category.

Consultations continue with the Jersey Financial Services Commission (JFSC), the island's regulator, to fine tune the proposals ready for the launch. Some of the key features of the Unregulated Eligible Investor Fund are:

- A minimum investment criterion of $US 1 million or a need to be a sophisticated investor;
- Applies to both open- and closed-ended funds, and can be structured using companies, unit trusts or limited partnerships;
- No requirement for Jersey-domiciled administrator, directors or custodian;
- Open-ended vehicles are permitted to list but only on exchanges that allow transfer restrictions.

Key features of the Unregulated Exchange Traded Fund Category include:

- Choice of structures using companies, unit trusts or limited partnerships;
- No requirement for Jersey-domiciled administrator, directors or custodian;
- Applies to closed funds only;
- Choice of exchanges on which a listing may be made.

Few restrictions

Jersey's existing regulated fund regimes, including the Expert Fund Regime introduced by the JFSC in 2004, and the Listed Fund Guide launched this year, successfully streamlined the authorisation process for regulated alternative investment funds. They led to a surge of new business in the alternative funds sector.

Unregulated funds take the island a step further forward in meeting investment managers' needs – and particularly those of alternative investments – for a swift and straightforward fund launch process.

Incoming Belgian changes to tax on savings income

From the beginning of 2008, changes to the Belgian tax regime will have particularly burdensome implications for foreign SICAVs

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Since 1 January 2006, Belgian private individuals have suffered a withholding tax of 15% on certain capital gains derived from investments in bond funds and funds investing more than 40% of assets in fixed interest-bearing securities. This new withholding tax only affects the Belgian retail market for bond funds and balanced funds.

Until 31 December 2007, the tax base of this new tax corresponded to interest income received by UCITS, regardless of the financial result realised by the investor upon redemption of its UCITS shares or the UCITS's liquidation.

An administrative decision confirmed that during this first period, the tax base could be calculated by relying on the so-called 'home-country rule', i.e. on the 'taxable income per share' (TIS) used for the purposes of the European Savings Directive (EUSD).

Capital gains to become taxable

As from 1 January 2008, however, the tax base will be extended to capital gains (reduced by capital losses, if any) realised by the UCITS on its debt investments. The tax charge will be limited to the effective capital gain realised by the investor when exiting its investment.

Comparing the TIS assessed based on the home-country rule will thus no longer be satisfactory for calculating the tax base of the new tax. Account will also need to be taken, firstly, of the capital gains and losses realised by the UCITS on the debt instruments held in its portfolio (an element not included in the TIS used for EUSD purposes) and, secondly, of the gains actually realised by the investor when exiting its investment (this assumes that the paying agent knows the acquisition value of the shares by the investor and its holding period).

Implications for foreign SICAVs

The new tax regime introducing this 15% withholding tax on 'bond SICAVs' is complex and imposes quite burdensome reporting for some foreign SICAVs marketed in Belgium. Indeed, the tax base for this withholding tax being 'specific' (no longer comparable with the to the Savings Directive tax base), it compels (foreign) fund managers to compute a TIS specifically for Belgian tax purposes. Moreover, there are many uncertainties on several issues (such as in determining whether a fund is in or out of scope of this new Belgian tax, in determining the tax base on which the 15% applies), rendering the task of the (foreign) fund managers even more difficult.

But the good news is that 'case-by-case' rulings can be obtained to clarify some of these issues. Meanwhile, we are waiting for further practical guidance from the Belgian tax authorities.

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OECD Consultative Group on Treaty Access for Funds makes progress

The latest meeting of this group took place in Kyoto in October (2007). The group consists of government and industry representatives and has been mandated to examine how international treaty relief procedures for funds and other investment intermediaries can be improved.

Substantial progress was made. There seems to be a genuine desire on the part of governments to tackle the particular problems faced by funds and to improve the treaty relief procedures generally. While it is too early to say what will emerge from the discussions there are reasons to be optimistic that substantial progress can be made.

The EU Commission's Fiscal Compliance expert group ('FISCO') published a report on 23 October and proposed the introduction of an EU Tax Relief Procedure based on passing pooled withholding tax rate information to upstream intermediaries. While the mandates of the two groups are different, there is a strong overlap and the FISCO report underlines the importance of reforming the current system for the benefit of all stakeholders – investors, intermediaries and governments.

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Belgium improves private equity tax and regulatory regime

Regulations governing the Belgian collective investment vehicle for private equity investments (the 'Private Pricaf') have recently been amended, introducing increased prudential flexibility as well as a novel withholding tax exemption, specifically aimed at non-Belgian corporate investors

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In mid-2007, the legislation regarding the 'Private Pricaf', a corporate investment vehicle for collectively investing in the equity of SMEs and unquoted (growth) companies was modified. The legislation not only increased flexibility for creating and operating such a 'Private Pricaf' but also introduced a new withholding tax (WHT) exemption applicable to foreign corporate shareholders. The WHT exemption comes in addition to the already existing tax advantages.

Regulatory flexibility

When introduced in 2003, the Belgian 'Private Pricaf' carried a significant regulatory burden. As a result, national and international investments via Belgian 'Private Pricafs' never really took off. But from 22 June 2007, new legislative measures entered into force simplifying the statutory requirements. The following text outlines a few of these.

The threshold for the initial investment has been lowered substantially and can now take place in kind. Furthermore, the 'Private Pricaf' is now able to invest in ordinary and hybrid loans (not necessarily represented by bearer debt securities), allowing certain mezzanine financing techniques to be used that are well-established in the private equity sector.

Shareholding requirements also changed, replacing the complex shareholding thresholds under the former rules. Shareholdings in a 'Private Pricaf' can now be held by associated companies or by individual shareholders linked by a family bond. In principle, a 'Private Pricaf' requires a minimum of six distinct shareholders, and demands decisions to be taken by a majority of a minimum of four shareholders possessing more that 50% of the voting rights. However, the given shareholding and majority requirements are not applicable in cases where one or more shareholders of the 'Private Pricaf' have a special status specifically mentioned in the law (a.o. collective investment vehicles, pension funds, etc.), and where the special status shareholder(s) has more than 30% of all voting rights.

The 'Private Pricaf' has now also been granted the right to conclude shareholder agreements.

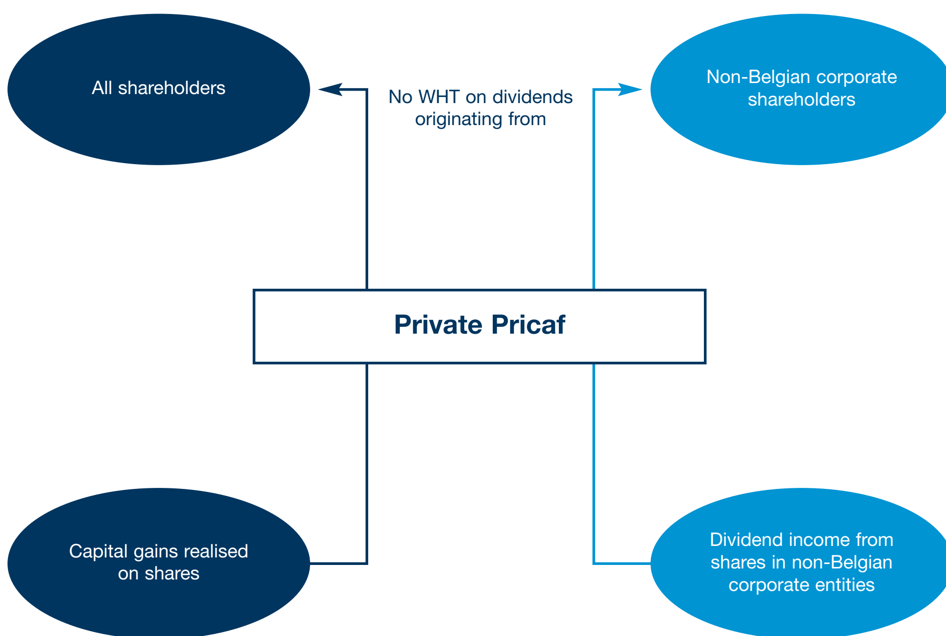
New WHT tax exemption

Even under the previous legislation, the Belgian ‘Private Pricaf’ was surrounded by some specific tax advantages. For example, the ‘Private Pricaf’ had a minimum taxable basis leading to almost zero corporate tax. And dividends distributed by a ‘Private Pricaf’ were already exempt from withholding tax to the extent that they originate from capital gains on shares realised by the ‘Private Pricaf’.

The recent legislative changes have now also introduced a new withholding tax exemption for dividends distributed to a corporate non-Belgian shareholder, providing they represent income originating from foreign (non-Belgian) dividend income.

This makes the ‘Private Pricaf’ more appealing as a collective investment vehicle for non-Belgian private equity funds investing in non-Belgian unquoted companies.

Private Pricaf – Withholding tax exemptions on dividends



■ = WHT exemption already existing ■ = new WHT exemption as of 22 June 2007

France opens to EU competition

Introduction of the ‘foreign withholding tax collector’ has truly opened the French market in capitalisation products to EU competitors

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In March 2004, the European Court of Justice made a famous judgment against the French state, which was convicted of breaching the general principle of ‘free’ establishment and ‘free’ movement of capital set under articles 49 and 56 of the European Treaty. The decision stated that by maintaining distinct tax regimes for similar financial products depending on the residence of the debtor, the French tax system breached the above rules. As a result, the French government embarked on a period of becoming compliant with EU legislation regarding financial markets.

Three years later, the situation has evolved and foreign financial institutions are now able to compete with French market players with the chief form of tax discrimination removed. From a practical standpoint, however, it is not certain that the new regime is the success initially intended.

Withholding tax regime of fixed income and capitalisation products

For a long time, the French legislator has favoured the tax treatment of fixed income products held by French individual investors. In particular, this benefits capitalisation instruments used in the insurance business. A French investor receiving interest and income of similar nature, or cashing capital gains from such instruments, can exclude them from its annual taxable income taxed at progressive income tax rate (up to 40% + 11%), and instead elect for taxation at a reduced fixed rate. For life insurance and capitalisation products, the rate depends on the duration of the contracts (35%, 15% or 7.5% increased by 11%) .

Although this results in an anticipated payment of the tax, immediately on payment, the withholding tax regime is obviously more favourable for most individual French taxpayers. (Tax is paid when the investor cashes the income rather than in the following year.)

New opportunity for foreign institutions

The withholding tax regime was only extended to capitalisation instruments whose debtor is a non-French institution from 1 January 2005. Up to this date, foreign source incomes on the above instruments were taxable at a progressive income tax rate. French financial institutions benefited, therefore, from a real competitive advantage and, as a result, from a ‘de facto’ monopoly in the distribution of these instruments.

Since 2005, foreign institutions have been able to envisage introducing new offers to the French market and distributing capitalisation products competing with those of local institutions. But they have yet to do so extensively. Besides cultural aspects – capitalisation instruments for insurance purposes are a specific characteristic of the French market – the reasons probably also lie within the level of awareness regarding the scope of the new regime and formalities imposed on foreign institutions.

(i) The withholding regime applies on fixed income securities derived from bonds, negotiable debts and receivables. Most importantly, it includes capitalisation instruments such as insurance life products. These are defined as contracts 'whose effects depend on the duration of the human life'.

(ii) It concerns any foreign debtor on capitalisation notes and contracts who is established in the European Union, Norway or Iceland. Life insurance contracts can be placed under the withholding tax regime, provided they are subscribed with an insurance company established in one of these jurisdictions.

(iii) The withholding applies upon specific election by the investor. As a principle, the investor makes the decision to elect on his own by filing a specific withholding tax return with the tax authorities and making the relevant payment within the first fortnight of the month following the income payment date.

However, the French legislator acknowledges that putting such a liability on the investor still discriminates between French and foreign institutions, which could impede effective competition.

Therefore, and in addition to extending the scope of the withholding tax regime to foreign contracts, the law has also set the new concept of 'foreign withholding tax collector' vis-à-vis the French tax authorities.

The concept of 'foreign withholding tax collector'

As an assumption, a foreign institution or insurance company shall be able to offer to its French clients the same services as a French company. It shall be allowed to levy the withholding tax on payment and to remit the corresponding amount to the French

In addition to the IT systems upgrade which might be required, there are some concerns that this may be another Qualified Intermediary regime with further audits to be made upon instructions from the French tax authorities.

Treasury, as a French institution does when its client elects for the withholding tax regime on similar products.

Depending on the number of its French clients, a foreign company will use one of the following alternatives:

(i) It may require a mandate from its client and make the appropriate individual filing and payment pursuant to this mandate in the name of, and on behalf of, this specific client. This mechanism is not substantial and meets the needs of most foreign institutions engaged with French clients on a punctual basis. While not yet widespread, it is effectively applied by some market participants.

(ii) An alternative solution consists of signing a general agreement with the tax authorities in order to collect, report and pay the withholding tax globally.
In this case, filing and payment are made for all the French clients of the institution who choose this regime and grant a mandate for these purposes.

This regime is not yet commonly used by foreign institutions and insurance companies. In addition to the IT systems upgrade which might be required, there are some concerns that this may be another Qualified Intermediary regime with further audits to be made upon instructions from the French tax authorities.

While this concern made some sense when the law was passed, it can be said now that this is not the route which has been chosen by the French administration. In this respect, it is also worth noting the 2007 bill which provides for a similar regime on securities incomes – including stock dividends – paid through foreign banks. There is little doubt that, as a consequence of this legal environment, foreign participants interested in distributing their products or services in France should be sufficiently comfortable with the French approach and will quickly decide whether to enter the market.

The Holland Financial Centre aims to boost competitiveness

Following its foundation in July 2007, the Holland Financial Centre is taking steps to boost the Netherlands' standing as a European financial centre

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The Dutch government and market are working together towards positioning the Netherlands as an important European financial centre, and improving the financial services and investment climate in the Netherlands. As one of the first steps, the Holland Financial Centre was founded in July 2007.

Globalisation and developments at financial institutions have led to a period of exciting and dramatic change in the financial sector, as financial centres around the globe attempt to gain an increased share of the world's economy. Although the Netherlands has traditionally enjoyed success in this field, there is a growing awareness that maintaining a high quality, competitive financial sector requires new tools, methods and solutions.

A joint initiative

The Holland Financial Centre is a joint initiative set up by organisations from throughout the financial sector. They include the Dutch Central Bank, the Ministry of Finance, the Ministry of Economic Affairs, the Ministry of Social Affairs, the NYSE Euronext, banks, insurers, trading firms, pension funds, asset managers, audit firms and law firms. The Dutch PricewaterhouseCoopers firm is among the founders.

The main purpose of the Holland Financial Centre is to develop a strong, open and internationally competitive financial centre in the Netherlands. In order to achieve this, the Holland Financial Centre holds consultations with key organisations that play a leading role in the sector's development, collects and processes data and performs any other activity which may be relevant in this area.

Setting targets

Over the next few months, the Holland Financial Centre will formulate a number of key targets in consultation with the market, so that it can achieve its medium and long-term goals. In the short term, the Centre has the following targets:

a) Establishment of a top academic centre for outstanding research and education in the field of financial markets (the so-called 'Duisenberg School of Finance');

b) Facilitation of the further development of the Dutch pension sector;

c) Establishment of a single entry point towards regulators and supervisors for market participants (the so-called 'Innovation Room');

d) Implementation of '10 Quick Wins', a series of easily achievable improvements to boost the financial industry.

Investment Management and Real Estate contacts

European IMRE News is produced by experts in their particular field at PricewaterhouseCoopers, to address important issues affecting the investment management industry. If you would like to discuss any aspect of this document, please speak to your usual contact within the network of member firms of PricewaterhouseCoopers International Limited or one of those listed below:

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