Date: 12 May 2015
ESMA/2015/SMSG/017

Detailed response to the Commission's Green Paper

Improving SME access to finance :

The Green Paper's analysis:

- for SMEs: diversity and scant credit information, preference to relationship based lending (hence banks);
- for start-ups: there is a lack of tangible assets to be used as collaterals for bank finance, leasing and factoring
- for mid-caps: access to public markets is costly
- Corporate bond markets lack transparency and standardisation
- Crowd funding remains focused on national markets

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

In the context of the publication of the SMSG own initiative report in 2012, the Group advised the following additional measures[1]:

- Improved EU coordination: When considering new policy initiatives, the European Commission should apply a cross-directorate approach and consider how policy as well as other initiatives impact SME's access to finance and investor's ability to invest.
- "Regulatory reconciliation": is key in the next years. Loose ends need to be reconciled with regard to finalisation, implementation and application of existing regulatory initiatives, making sure that these avoid any unintended consequences. Surplus or misdirected regulation raises costs for businesses, utilising valuable funds that could instead be turned towards innovation and growth creation. The previous European Commission launched important regulatory initiatives (e. g. CRD IV/CRR, MiFID II/MiFIR, EMIR, CSDR, AIFMD, UCITS V etc.) that should be integrated under the umbrella of the Capital Markets Union. Many important topics are addressed but need to be implemented and brought to life. In light of this, the Capital Markets Union should build on existing regulatory elements and ensure that these are fully implemented. Further, regulators and supervisors should see how existing and recently implemented regulation works in practice, understand the impacts and ensure any overlaps or misinterpretations are addressed, clearly defining the gaps and any market failures, before looking into creation of new regulation. Legal certainty is an important prerequisite for companies.
- Education of SMEs: There is a continuing need to increase awareness and education of entrepreneurs to ensure they understand the different sources of finance available to them. Initiatives to promote financial literacy, to develop a capital market culture and to revive investor trust are needed.
- Research and ratings on SMEs: EU legislation should include incentives to foster independent research and ratings of SMEs and avoid jeopardizing the present ecosystem of the financing of research.

[1] http://www.esma.europa.eu/system/files/2012-smsg-59.pdf

- Review of categorisation in the MiFID legislation of high net worth individuals/business angel type investors and other investors, e.g. such as local and regional associations or small pension plans that have the capacity (or within personal pension arrangements are required) to lock up some of their capital for a period and to diversify their portfolio beyond cash and high liquid securities -as 'retail': The criteria to assess retail clients that request to be treated as professionals are not entirely relevant to early stage/small cap investors. This assessment increases the cost of investment and disenfranchises an important set of investors from small caps. A review would also help to ensure that appropriate exemptions are made for venture capital and other early stage fund managers (and their end investors) in the AIFMD and the EuVECA, EuSEF and ELTIF pass-porting schemes.
- Creation of public support specific to these companies (for example, subsidised credit lines).
- Commissioning a comparative review of the EU and US high yield debt markets with a specific focus on providing investors access to smaller companies at mutually attractive terms.
- Developing a flexible EU "bankruptcy regime" (similar to the Chapter 11 provisions in the US).
- In addition, if start-ups were allowed to offset e.g. social charges against their tax-loss carry-forwards which they typically accumulate during their early years of existence rather than eventually selling them off to a more mature company (who will use them to off-set tax on corporate profits), this would help reduce their overall funding needs in the beginning while allowing them to employ staff during critical growth stages of their development.
- Regain the trust of individual investors and consumers in the intermediated ("packaged") investment products by standardising, simplifying, streamlining and reducing the cost of packaged investment products.

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

When SMEs decide to use rating agencies, incentives, also for corporate debt rating, could be considered as follows:

- Reducing information asymmetries between issuers and investors and, as such, the risk premium demanded on loans to SMEs.
- Protecting investors, through the provision of additional information about the additional risks they are incurring with these types of investments.
- Reducing costs by allowing reduced capital requirements of credit institutions if ratings are issued by recognized External Credit Assessment Institution (ECAI), and looking at ways in which the cost of the ratings assessment can be made cheaper, for example increased competition between agencies.
- Bearing in mind the low level of standardization in the SME market, it seems rather unlikely that such this could be done at an adequate price taking into account the transaction size.
- Reducing costs by making the assets accepted as collateral in liquidity-providing operations to banks by the ECB, if the ratings are issued by recognized ECAI.

3) What support can be given to ELTIFs to encourage their take up?

Retail investors' representatives in the SMSG argue that successful development of ELTIFs should consider the following:

    - Eliminating the plethora of already existing long term fund categories which are nationally incentivised (nine such categories existing in France alone, all with tax incentives).

- Granting the "most favoured nation" clause to ELTIFs for its tax treatment in Member States
- Selling the same ELTIFs to all investors – retail or not, and ban funds of funds which add a layer of fees
- Applying the product disclosure rules of UCITS funds;
- Making listed small cap equity an eligible asset class.
- Allowing as well closed-end listed ELTIFs to address the liquidity issue
- Setting a high threshold for minimum investments in ELTIFs: those should be "advised" only to qualified and very financially literate investors.

On the other hand, others are of the opinion that there should be two separate types of ELTIFS instead: i.e. those catering for the needs of institutional investors and those catering for the needs of retail investors. If all ELTIFs are modelled on the needs of retail investors (liquidity; investor protection etc.) it risks making them unnecessarily expensive for institutional investors, who after all are the ones channelling the majority of private savings into the private and public markets, and who are better equipped through their larger portfolios to handle liquidity and risk diversification.

However, at the same time there should be no single set of rules for all types of investors (retail, or professional; small- medium- or large) as this will fail to recognise the different needs of such a wide range of investors or and eligible assets ELTIFs seek to attract. Therefore, the possibility to adapt the structure on the different needs of the investors' base of each ELTIF is necessary to increase their market attractiveness and finally their success in financing the long-term needs of the EU economy.

The discretion of the asset manager to choose whether to open the ELTIF to retail investors or not, alongside discretion over portfolio composition and early redemption rights are welcome. Still, additional effort should be made to attract particular categories of investors such as:

- Small pension plans and local associations that have the capacity (or are sometimes even required) to lock up some of their capital for a period and to diversify their portfolio beyond cash and high liquid securities. As those investors are classified as retail investors they will be excluded from a number of ELTIFs open only to professional investors, whereas the request to be treated as professional investors based on the MiFID criteria is not relevant to them as it might generate too high a legal hurdle and important costs for them.
  Insurance companies' efforts to further diversify their portfolios through investment in long term illiquid assets such as infrastructure or non-listed SMEs are undermined, due to the additional capital requirements they bring.
- Considering accounting treatment at banks or insurance companies investing in ELTIF´s that does not impose mark to market, as long as they are held to maturity.
- Additional flexibility when it comes to the lifetime of the ELTIF in order to make it possible to adapt to the changes in the long-term landscape of its investment strategy, would make it feasible for ELTIFs to take advantage of market opportunities to the benefit of their investors.

Apart from the need to deliver a regulatory framework for ELTIFs able to meet their investors' needs, it should be stressed that their market potential will be linked to a great extent to the general regulatory environment. Ensuring that substantial incentives are in place includes also the provision of tax incentives and the removal of any fiscal or administrative barriers. Moreover, investors need and seek stable and predictable regulatory environments. This prerequisite becomes even more relevant in the case of illiquid investments, in which the link to a particular jurisdiction is of longer duration. Finally, education on financial principles and tools for retail investors will help them understand the risks associated with the financing of a long term project and the economic and social benefits.

Once the legislation is formally in place, ELTIFs have the potential to play an important role in capital market funding in the EU, if the right incentive are in place. Because ELTIFs are intended to invest in illiquid, often private assets, particular attention should be paid to national restrictions and barriers deriving from banking law, insolvency law and tax regimes.

Finally, to complement EU level action and in order to encourage the take-up of ELTIFs, the Commission needs to encourage Member States to remove the following restrictions at national level, among others:

- the inability of funds to originate loans;
- the need for a banking licence to originate loans;
- bank liabilities preferred on bankruptcy;
- the lack of standardised procedures for taking security, enforcement and for creating loans/bonds, like EU company registers for registering and enforcing pledges and similar charges;
- restrictions on the availability of credit data, which can be restricted to only actors with banking licences; and
- Different tax treatments on, for example, withholding tax on interest, depending on the type of investor.

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

The EU could undertake a review of the current obstacles to cross-border fundraising which have e.g. arisen through the implementation of the AIFMD. Investors who have indirectly invested in an SME from a different member state through a venture capital fund and whose development they have been able to closely follow, may be more inclined to invest directly into debt or equity issued by such SME at a later stage.

In addition to supporting market-led standards (such as the recent initiative from ICMA with the Pan-European Corporate Private Placement Market Guide published on 11 February 2015), we suggest that a revision of the final calibrations for insurers of the spread risk capital weightings in the Solvency II Delegated Act (Commission Delegated Regulation (EU) 2015/35) should be considered. Although the final calibrations in the Delegated Act (the "long term guarantees package") has helped remove obstacles to investing in certain long-term assets (infrastructure projects, SME loans or start-ups), the final calibrations are not optimal due to the focus on volatility risk as opposed to default risk, in addition they do not sufficiently address private placements. The European Commission should lead a consultation process to determine the appropriate adjustments to the calibration of the current long term guarantees package in order to incentivise investment in private placements, as well as more generally in long-term assets.

Taking into account that private placements can be documented in both bond and loan format, the Commission should encourage Member States to remove the restrictions at national level also identified in our response to question 3.

Finally, increase the number of investors to 500 as a maximum number for what constitutes a private placement.

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

Care needs to be taken to ensure that there are enough intermediaries, in the form of fund managers, providers of investment-ready programs etc., who can help bridge the gaps between institutional investors needing to deploy large amounts of capital and the relatively smaller amounts required by each SME as well as the relatively smaller amounts of capital to be invested by retail investors but still looking to spread their risks through diversification, e.g. rather investing through funds of funds or into portfolios of SME debt. Many SMEs and their management teams will need to better understand what investors are looking for as well as improve their corporate governance standards before they are ready to approach new categories of funders.

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

The 2008 crisis demonstrated that fixed income markets were much more illiquid than equity ones and virtually stopped in many instances. To redress that, access, transparency and liquidity (at least for the larger bond issues) should be improved and put on a par with those of equity markets.

It is questionable whether standardisation in corporate bond markets would promote liquidity, and regulatory action is therefore not necessarily advisable. Borrowers seek to choose maturities and coupon structures to match their cash-flows. They also require freedom to negotiate terms that suit their own business model, their other financing obligations and documentation and their particular funding needs. Standardisation would make it harder for borrowers to achieve consistent borrowing on the best terms by restricting these fundamental capabilities and inhibiting funding flexibility.

Furthermore, standardisation may actually work against smaller issuers in corporate bond markets. Owing to their funding profiles, very frequent, large borrowers may in principle be qualified to issue on a standard schedule. However, to apply a broad-brush approach to all borrowers would be to disadvantage those smaller borrowers with their own particular funding habits. This would not only be inconsistent with the Capital Markets Union objective of expanding bond market access for smaller, mid-cap borrowers, but a push towards standardisation for very frequent, large borrowers could also lead to greater market segmentation, resulting in issuance of standardised bonds, on the one hand, while issues from the rest of the sector could come to resemble the more bespoke private placement market, on the other hand.

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

As a preliminary comment, it is important to note that green bonds like any other listed bond come under the scope of existing financial regulation both at the EU and national levels. Green bonds are therefore not being issued in any form of regulatory void. They also benefit from a successful selfregulatory industry initiative known as the Green Bond Principles (GBP). The GBP provide voluntary process guidelines that recommend transparency and disclosure and promote integrity in the development of the green bond market by clarifying the approach for issuance. The GBP document is regularly updated, most recently in March 2015 based on a broad consensus of market participants.

Also as a generic reference for other ESG bonds, the flexible and reactive market-driven process represented by the GBP is preferable to a top-down normative approach leading for example to a green bond "label" formally recognised at a regulatory level. This would risk creating unnecessary market segmentation, as well as the perception of potential liabilities for issuers that could dissuade them from entering the market.

There are reasons to consider creating future incentives for investors and issuers in the green bond market as they both experience additional costs compared to mainstream alternatives, and/or in order to maintain or accelerate the development of the market in support of wider public policy objectives related especially to the fight against climate change. The GBP require additional work from green bond issuers both during (e.g. process for project evaluation and selection) and after the transaction (e.g. dedicated reporting). Similarly, investors require additional resources to evaluate and monitor green bonds and the underlying environmental projects. These costs are not reflected in the economics of green bonds that are priced in line with the credit profile and mainstream bonds of the issuer.

The difficulty, however, in designing and implementing such incentives would most likely be the need to agree on some form of regulatory and/or legal definition of green bonds which may defeat the goal identified above of avoiding a top down normative approach to these securities.

At this stage, therefore it is not necessary for the EU to take any legislative action for the development of Environment, Social and Governance 'ESG' investment. Numerous recent pieces of legislation introduce ESG disclosure requirements, such as country-by-country reporting, Revision of the Shareholders' Rights Directive, efforts on conflict minerals, transparency requirements in the UCITS KIID and PRIIPs KID. The impact of these pieces of legislation now needs to be reviewed. However, the European Commission could play a non-legislative role in the promotion of ESG. Finally, given the evolving nature of the industry, standardisation of processes should not be discussed at this point of time as market driven initiatives need to be given the space to grow.

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

There are arguments both in favour and against the introduction of a common accounting standard for SMEs listed on MTFs. Arguments in favour include the benefits for any SME that has users located in different countries or that wishes to be comparable with other SMEs from other countries; and because accounting is about reporting economic events and when events the same across countries then the reporting should be the same around countries. However, there are drawbacks, too, such as the issue that culture and socio-economic systems do differ around countries and imply different rules in different countries, not to mention the additional costs involved.

In the context of facilitating the growth of SMEs, the benefits of facilitating financial market access through common EU level accounting standards needs to be balanced against the regulatory burdens imposed. As such, the SMSG suggests the Commission reviews the subject further before deciding to develop a common EU level accounting standard for SMEs listed on MTF.

Once properly assessed, if the EU were to move in this direction we think that the IFRS for SMEs published by IASB in 2009, originally tailored for the unlisted small companies, should be expanded to the SMEs listed on MTF. This IFRS for SMEs would be a direct (and "ready to apply") means to help the listed SMEs by simplifying the preparation of the notes to financial statements and making them less costly to produce and easier to read, while remaining comparable with listed firms applying full IFRS and compliant with EU regulations. Moreover, the chosen regime should be 'scalable' i.e. it should easily be scaled up to meet the additional accounting standard requirements in force in the standard regulated market. IFRS for SMEs are already devised in this way.

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

Crowd funding is one of the emerging financing models that contribute to helping start-ups move up the "funding escalator", as it can be followed by other forms of financing, such as venture capital or an Initial Public Offering (IPO).

The expression "crowd funding" does not apply to a specific financial vehicle but rather to a channel of financing, which can be used in many different ways. The terms refer to open calls to the wider public to raise funds for a specific project. These calls are often published and promoted through the internet, by means of specialised platforms, and try to attract a large number of contributors in the form of relatively small contributions.

Under those common elements, there are many different types of crowd funding depending on the purpose of the fund raising as well as the instrument used to contribute the funds. The most widely used taxonomy distinguishes between non-financial and financial crowd funding, the difference being what the providers of money get in return for providing funds:

- Non-financial crowd funding, includes all forms of money contributions where the provider of money is not expecting any financial return. Donations, sponsoring, or reward seeking (in the form of a product or service of lower value than the contribution) are among the most cited categories of non-financial crowd funding.

- Financial crowd funding, includes all those contributions where the provider of money expects some financial return. Among these are included loan-based (also known as peer-to-peer lending), and securities-based, also named investment crowd funding. Securities issued may be shares or bonds. It is this category of crowd funding the one that should be of concern to ESMA.

Investment-based crowd funding amounts to very small figures, when compared to non-financial one (around 5% to 10% of total crowd funding is investment-based), but is showing important growth rates. Overall investment crowd funding in Europe was estimated at less than 100 million euros in 2013, a figure representing less than 1% of total IPO market. More recent estimates of equity crowd funding in the UK (Nesta, *Understanding Alternative Finance*, Peter Baeck, Liam Collins, Bryan Zhang, November 2014) point to a doubling up of activity in 2014, though still reaching extremely small amounts (some 80 to 90 million pounds) when compared to IPO market, or venture capital.

Project owners raising finance through crowd funding are usually very small firms, innovative or otherwise, and project sizes are also extremely small. In fact, most platforms through which these projects raise funds are themselves also relatively small businesses. According to the same report previously quoted, average deal size of an equity-based crowd funding campaign in the UK has been around £200,000, with an average of 125 investors participating as contributors. The same UK data source shows that 60% of investors in equity crowd funding described themselves as retail investors with no previous investment experience. Estimation of activity for the European Union is not easy, and overall figures are probably much smaller than a pure extrapolation from UK figures. In fact, a large proportion of UK equity-based crowd funding deals in 2014 were eligible for some of the existing schemes (EIS or SEIS) offering tax reliefs to investors in smaller higher risk companies. This illustrates the need to complement crowd funding regulation with other measures (tax, rising awareness, etc.) addressed at promoting its usage as a financing vehicle. ESMA recently published advice on Crowd funding to European Parliament, Council, and Commission taking into account the need of promotion and clarification, while at the same time preserving investor protection at its highest

The main objective of the report is to assist NCA´s and market participants, and to promote regulatory and supervisory convergence around an activity which is relatively young, and business models are evolving. The report also identifies issues for consideration by policymakers in relation to the regulatory framework for crowd funding at EU level.

Given the key role platforms perform in crowd funding, the report is especially dedicated to the analysis of their activities, as they will determine the applicable legislation. The most likely activity identified is pure reception and transmission of orders, in which case a 50,000 euros capital requirement would be applicable. The report shows concerns about some platforms structuring business in such a way to avoid MiFID requirements, which could incorporate risks for investors not addressed at EU level. Additionally, the lack of a passport could also make it harder for platforms to achieve the scalability they need. In this sense, ESMA considers that an EU level regime should be desirable for platforms operating outside the scope of MiFID. Additionally, the report considers that the use of collective investment schemes in crowd funding could become more widespread and so the relevance of AIFMD, EuVECA and EuSEF legislation could increase. Development of more detailed proposals would need to fit within the context of the Commission´s programme of work on the Capital market Union.

It would be advisable to keep the situation under review, and to consider legislation to harmonise consumer protection measures should a divergence of approaches emerge.

Supply side: institutional investors

The Green Paper’s analysis of current regulation and tools
UCITS V and AIFMD
- The directives are still insufficient to reduce cost and diversify managed funds investment.

On pensions and insurance:
- There could be a review of Solvency II (and CRR) delegated acts, to adapt prudential rules for identified sub-classed of lower-risk infrastructure investment.
- The Commission asks which sub-classes should be prioritised for.

On professional pensions:
- Commission suggests introduction of a standardised product, via a 29th regime to remove barriers to cross-border access.

Private equity and venture capital:

- EuVECA and EuSEF Regulations - the clause impeding managers with portfolio above €500 million to apply to set up and operate such funds or use these designations to market the funds in the EU is harmful.
- Commission asks which measures could be proposed to: increase scale of venture capital funds (both via public and private contributions, improve exit strategies and supply for investors and boost supply of venture capital to start ups.

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

The AIFMD does not apply to private equity and venture capital funds under €500m (as these funds are typically closed-ended and unleveraged; if not - the € 100 m threshold would apply) and is therefore not likely to impact the majority of European VC funds unless they need to opt-in in order to get access to the EU-wide marketing passport. Hence the importance of assuring that the national private placement regimes do not work against one another in ensuring cross-border marketing access for such funds wanting to target investors in only one or a handful of Member States.

However, some believe that funds fear being caught by AIFMD and this could deter funds from gaining scale. As the European VC sector grows, develops and matures the likelihood of venture capital funds also becoming larger increases. Today, growth and expansion of capital funds, which are in many cases the natural next taker of an early stage company not yet ready to go public, are in many cases unable to benefit from the EuVECA label but too small to carry the full cost and administrative burden of full AIFMD authorization and its ultimate impact on investor returns. US VC funds tend to be larger and therefore are able to back more enterprises and generate good returns. For example, Germany has only four independent VC funds >€100m compared to 227 in the US[2]. The SMSG is aware that the AIFM Directive was controversial and would like to stress that although this report points out several negative consequences of the Directive, the intention is not to challenge what is already valid EU law, but to highlight what we see as unintended consequences in respect of SME's that should and can be addressed by special measures directed as SME's while respecting the intended scope and purpose of the Directive.'

There needs to be better differentiation between the real risks profiles of different sets of assets/funds and thus also an ensuing differentiation in the capital requirement ratios for each asset class. In many EU countries there are still institutional barriers to larger investments by e.g. pension funds, insurance funds etc. into alternative assets where limits are set as % of overall portfolio rather than e.g. following the so called prudent person rules.

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

- Incentives to create investment funds specialised in shares and/or debt of SMEs, for example through a more favourable tax regime and more flexible investment rules, possibly through closed-end funds, given the lower liquidity of the underlying assets.

[2] Earlybird Europe Venture Capital Report – July 2011

- Review of the tightening of the national private placement regimes for cross-border marketing of especially below threshold funds that followed as a result of the implementation of the AIFMD.
- Review of the practice of many national CAs to impose additional charges and/or additional conditions (like a French paying agent) for managers who have already been granted the EU-passport in their home jurisdiction.

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

EU Regulation applicable to institutional investors (such as Solvency II for insurance funds) and any future proposals to introduce similar regulation for pension funds must not place conditions that adversely impact the ability to directly or indirectly invest in small caps. The capital and liquidity requirements under Solvency II are likely to exacerbate the tendency of institutions to only hold the largest and most liquid blue-chip equities or even only interest bearing instruments like government bonds due to the lower risk weightings for these than equities in general and deter any existing appetite for smaller companies. An appropriate exemption for direct or indirect investment in small cap securities should be implemented.

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

Yes, the creation of a European standardised personal pension product would facilitate cross-border activity since it would allow providers to offer the same product in different member states. Currently, pension providers have to offer country-specific products in line with national legislation, which increases the costs of engaging in cross-border activity. This market fragmentation limits competition between providers, and cost-effective products available to EU citizens.

Importantly, the EU legislative framework for a European personal pension should not aim at harmonising all types of existing personal pensions. Instead, the aim should be to create an EU-wide personal pension product that could be offered to EU citizens, in addition to the products that are currently available at national level.

The creation of an EU legislative framework for a European personal pension would open domestic markets to all EU regulated financial institutions, and facilitate cross-border activity thanks to the granting of an EU passport that would allow providers to sell the same European personal pension across the EU. This would allow providers to centralise some functions, particularly in the areas of investment management and administration, thereby achieving economies of scale and lower operational costs.

It is also important to mention the benefits to EU consumers with the introduction of a standardised European personal pension. Cross-border selling of such product would increase competition between providers, by diversifying the range of products offered and reducing their cost. The increased cross-border activity of providers should also convince leading providers to ensure the cross-border portability of their European personal pension products, thus facilitating the mobility of EU citizens.

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

The European Venture Capital Funds Regulation (EVCFR) and Social Entrepreneurship Funds (EuSEF) Regime aim to provide an EU-wide marketing passport to qualifying funds thereby enabling institutional investors across the EU to indirectly invest into SMEs. We support the current proposals to include holdings in SME markets as 'qualifying portfolio companies'. This will allow VC funds to appropriately consider their exit options (including via IPO) and provide them with the flexibility to follow portfolio companies even after IPO, as appropriate. Also the criteria of the MiFID definition of Professional Investor needs to be adapted so as not to exclude traditional investors into VC funds like entrepreneurs and business angels who bring both funds and relevant experience.

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

Some suggestions:

- As mentioned above overly restrictive capital requirements which do not reflect actual risks, imposed on different types of institutional asset classes, can deter such investment and should be reviewed.

- Adapting the MIFID definition of professional investor to better suit traditional investors into VC funds (business angels, entrepreneurs, family offices, HNIs etc) or introduce a harmonized definition of semi-professional investor.

- Using public capital to leverage private capital through allocating investment funds to such fund managers with a proven track record of raising private funding and successfully investing it in SMEs. This is especially important in the earlier and more risky stages of SME funding to ensure there are funds catering for the different stages of a company's development before it is mature enough to list/do an IPO. While many start-ups manage to find funding for the seed and incubator stage they too often run into difficulties doing so at later stages of development.

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

No response given.

Supply side – retail investors

- Commission asks how to increase participation in UCITS by cross-border retail;
- Share best national best practices in the development of simple and transparent investment products for consumers;
- The Commission suggests that in the review of the ESAs their mandate in consumer/investor protection could be enhanced. Commission announces vaguely it will begin preparatory work on the single market for retail financial services.

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

Given what UCITS represents especially in the eyes of Asian regulators and investors and their sensitivities - as we've recently learnt – against continuous and further changes to the UCITS framework, we should not attempt to the unity of the brand suggesting further revisions. Moreover, the claim that a sub-type of UCITS be allowed to invest in SMEs is in stark contrast with the renowned liquidity features of UCITS. For investments in SMEs, the ELTIF is certainly the most appropriate vehicle.

Due to the differences in the national transposition of AIFMD and further Member States' specificities, the amount of AIFs is higher than the US. The reduction of AIFs should be the result of the creation of a true single European market and not top-down capping of AIFs.

Individual investor representatives are highlighting that UCITs are much more cross-border than AIFs already because the two major domiciles for UCITs are largely "off-shore": Luxembourg and Ireland (i.e. most of Luxembourg- and Irish-domiciled funds are distributed in other EU countries) whereas the vast majority of AIFs are purely sold on a national basis. One way to increase cross-border distribution of funds in the EU is therefore to drastically reduce the number of retail AIFs .

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

The ESAs should first make full use of their existing powers in terms of data collection, analysis, and publication, in particular in the areas of returns and prices (fees, article 9.1 of the ESAs Regulations) and of product intervention (article 9.5) to ban toxic products that bring negative value to investors. They should also better enforce existing investor protection rules. For all this they need their resources to grow, not to be cut.

The implementation of the ESAs guidelines through peer reviews and their consistent application across the 28 Member States is the most crucial element in ensuring consistent supervision as well as their contribution to consumer and investor protection.

The importance of a level playing field for financial product services regulated by the three ESAs would require better coordination between all three agencies.

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

As mentioned in our introductory statement, an effective capital markets union will only function if EU citizens as individual investors are also attracted to invest in capital markets. Personal pension savings have an important role to play, by channelling EU citizens' savings into capital markets. Since Europe needs to foster a greater retirement savings culture to ensure pension adequacy, and given the market fragmentation in product design, investments, marketing and distribution rules, a new cost-effective and simple European Personal Pension product with high consumer protection standards could capture the much needed consumer trust. Given the long-term nature of retirement savings, such product could channel savings into long-term and less liquid assets. The creation of a single market for personal pensions - on which EIOPA is currently working - should therefore be seen as a building block of a Capital Markets Union that puts individual investors at its core. We therefore encourage the Commission to take action on the build-up of a single market for personal pensions once it receives EIOPA's final advice.

Review of categorisation of high net worth individuals/business angel type investors as 'retail': The criteria to assess retail clients that request to be treated as professionals are not entirely relevant to early stage/small cap investors. This assessment increases the cost of investment and disenfranchises an important set of investors from small caps. A review would also help to ensure that appropriate exemptions are made for venture capital fund managers (and their end investors) in the AIFMD and the EuVECA and EuSEF passporting schemes.

Tax reforms should be considered in order to encourage more long-term holdings (i.e. better pre-tax offsetting of gains and losses, and tax push forward if realisation proceeds are re-invested). Creation of specific benefits to certain (especially individual) investors who can directly invest in finacila instruments available in capital market, tax relief or personal internal revenue taxes lower on capital gains on securities of these companies, under conditions of maintenance of such securities over a minimum period of time and a maximum concentration by company (in value and in percentage of capital of each company). Further investigations of ways to remove factual double taxation of dividends and interest in case of cross-border investments by reviewing cross-border refund/exemption procedures for withholding taxes on dividends and interest would be a further step to encourage cross-border investments.

Recreate trust in capital markets. Investor protection is a key driver of EU financial legislation and will serve to revive confidence in financial markets. Only when investors feel adequately protected will they be willing to channel their money into capital markets. To that end it is necessary to repeal barriers to cross-border shareholder engagement, e.g. by facilitating the exercise of shareholders' voting rights cross-border which is still cumbersome and costly, by introducing common minimum corporate governance standards, and by encouraging Member States to, at the least, introduce minimum standards, e.g. in relation to insolvency law.

The quality of the distribution channel is crucial. Therefore all relevant competent authorities should monitor the practice of distribution and should bear in mind that there will always be an asymmetric information level between retail/individual investors/consumers and the suppliers which cannot be compensated by more financial education.

Clear and prominently placed risk warnings are essential as investing in a single SME is usually a high risk investment.

Retail/individual investors are not a homogeneous group. Therefore it is necessary to define which kind of investment should be allowed for consumers and define different groups of retail investors e.g. establish a threshold for minimum investments e.g. EUR 100.000 or maximum investments (e.g. EUR 5.000 in case of crowd funding) for certain investments.

Development of a collective redress mechanism, similar to the Dutch collective settlement procedure/collective action. The commission has already published (non-binding) recommendations regarding collective redress (http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013H0396&from=EN). The commission should proactively publish a proposal for a directive.

Improvements in the quality and quantity of financial education by advocating/fostering respective initiatives.

One should look at differentiating the capital gains tax regimes so that lower capital gains taxes are e.g. incurred when holding a share for 3 years or longer. While interest payments are typically (wholly or partially) tax deductible expenses for a company and then taxed in the hands of the recipient, dividends are subject to double taxation (made out of taxed corporate profits and then taxed again in the hands of investors).

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

A simple, standardized Pan-European personal pension plan is needed to increase consumer confidence, thanks to standardised product rules and robust consumer protection rules (please check Q13).

The Commission might want to examine the UKs Simple Financial Products Initiative.

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

Yes:

- The PRIIPs Regulation should include shares, bonds and pension funds in its scope to further standardise and simplify pre-contractual investor information, or, at least, the Prospectus, Insurance Mediation and IORP Directives should be amended in order to make their summary documents more standardised, simpler, shorter, in Plain English and more comparable between each other and with other investment products.
- IMD 2 and IORP 2 conduct of business rules should be fully aligned to those of MiFID 2.
- The Shareholders Rights Directive should be amended to facilitate the exercise of voting rights cross-border, and in nominee/omnibus accounts, and free-up the right of small shareholders to freely associate and for these shareholder association to easily collect proxies from their members. Next to its involvement in the operation of the proxy advisory industry, ESMA should additionally get involved in improving the proxy voting process e.g. by ensuring for standardized workflows within the intermediaries chain or by developing harmonized EU-wide accepted proxy forms.

Supply side – non-EU investment

Attracting non-EU investment:
- The Commission notes that EU markets must be open and globally competitive to attract foreign investments.
- The EU has undergone a sizeable decline in the amount of gross capital inflows as a % of GDP, the gross capital inflows were lower in 2013 than in 2007.

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

The EU should not to discriminate against non-EU based managers as doing so will make it less attractive for them to market their funds to EU-based investors. Such discrimination could also result in it becoming more difficult for EU-based managers to market internationally, should third-countries reciprocate with their own discriminatory actions.

Given that many regulatory initiatives are newly implemented in Europe, and taking into account that markets have become global, the topic of third-country recognition is important. In general, the same level of requirements for third-country enterprises providing their services in a European Member State should be maintained in order to preserve the desired standards of services in the EU. The potentially lower standards from third countries for the same services should not be introduced via recognition procedures. This is particularly sensitive with regard to foreign competition, affecting the growth potential for EU companies.

Therefore, a fair balance needs to be found to allow non-EU companies to provide their services in Europe.

It is important to ensure that global standards and rules put in place by institutions such as the International Organization of Securities Commissions, the Bank for International Settlements and the Financial Stability Board are carefully considered when drafting regulation in order to avoid regulatory arbitrage that could have negative consequences for growth. Safety standards, risk mitigation measures and data protection rules, for example, should be put in place at the highest level possible. A "race to the bottom" should be avoided, so that individual players cannot exploit weak regulatory regimes. Isolated national regulation should be avoided as well.

On the other hand, it is important that European companies are allowed to enter third country markets to provide services abroad. It should be noted that other countries may have high barriers of access to their markets, which is another reason to consider initiatives to ensure that EU market participants are able to offer their services outside the EU on a level playing field with non-EU providers.

In this regard, reciprocity should be requested and maintained with regard to third-country regimes.

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

An attraction of large numbers of individual investors to directly invest for a long term across borders in equity and bond market would make the market more liquid and efficient.

The Commission should also give serious consideration to the recommendations in the IPO Task Force report.

Improving the investment chain

Commission's analysis regarding the single rule book, enforcement and competition includes:

- The single rulebook is a major step forward to enforce EU regulation consistently but the single rule book's success depends on consistent implementation and enforcement.
- Supervisory convergence: the ESAs play an important role to ensure a level playing field. Active use of dispute settlement is needed – but more may be needed in a more integrated CMU.
- Common Data and reporting across the EU will help the CMU – common IT approaches for reporting requirements would help the CMU.
- Market infrastructures are regulated by CSDR, EMIR and T2S. The Commission is working on CCP recovery and resolution. The fluidity of collateral across the EU is currently restricted. Where there may be potential to make further improvements.

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

Regulatory reconciliation is key in the next years. The Capital Markets Union should ensure that the long-term goal is to reduce the regulatory burden to what is essential to attain the public policy objective said regulation is intended to deliver. Unintended consequences should be eliminated. Additionally, loose ends need to be reconciled with regard to finalisation, implementation and application of existing regulatory initiatives, making sure that these avoid any unintended consequences.

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

Is the current governance structure the optimal to ensure that e.g. ESMA has the necessary powers to drive regulatory convergence allowing it also to "crack-down" on national CAs who go further than what has been envisaged under certain Directives?

Clearly there is a limit on the extent to which supervisory powers can be centralised further without a change in the EU Treaty. Even if proposals passed the subsidiarity test, a Treaty change does not appear to be politically practicable, at least for the time being. In any case, it is unclear why more centralised supervisory powers would help maximise the benefits of capital markets for the real economy.
So we should consider how more can be done, and indeed is being done, to ensure consistent supervision within the existing framework, and recognise that there are constraints on how further developments can pragmatically be achieved.

One evident factor is going to have to be a resolution to the debate regarding the ESAs funding, as they are evidently stretched at the moment. This should involve resolution of the debate about how the ESAs are funded.

Indeed, there are some respects in which the ESMA and other ESAs could, given the budget, go even further than they have thus far planned. In particular it makes sense that they should be able to play a fuller role in contributing their views to inform the formulation of new Level 1 EU legislation. This would help to ensure that requirements which then come to be handed to them for subsequent Level 2 work are fully understood, have an adequate amount of time for their orderly adoption, and are more likely to be framed in a way which leads to effective regulation,. Where new regulations are brought into force and problems then become evident, consideration should also be given to allowing the ESMA to promptly propose No-action Letter type of reliefs, subject to approval from the Commission and a process for reporting and oversight designed to properly respect the authority of the co-legislators.

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

The overall legal framework for securities varies widely by country. For example, legal barriers make it much more complex to hold securities cross-border, and lead to higher costs for transactions. In addition, they cause difficulties and uncertainty among investors when they exercise their rights abroad and should therefore be targeted, e.g. by ensuring that end-investors holding their shares in nominee/omnibus are able to make full use of their voting rights.

Given that legal uncertainty of this nature acts as a barrier to financial stability and growth, the European Commission has been examining barriers within securities markets for several years, with the aim of creating a stable and efficiently functioning single market.

Continued harmonisation of rules and standards is essential to eliminate costly barriers and reduce complexity for investors and companies. Initiatives in this area, building on the Single Rulebook as a harmonised regulatory framework, should increase the attractiveness and returns on investment, thereby stimulating economic growth.

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

Collateral fluidity is important. Indeed if it is inhibited, this poses a risk to the overall functioning of capital markets, with serious repercussions throughout the whole economy. As an important building block on which to base Capital Markets Union, some work is needed to identify and address problems, taking particular account of the cumulative effect of EU regulations.

First the Triparty Settlement Interoperability (TSI) project remains important and needs to be concluded, along with essential related work necessary to upgrade the settlement bridge between pan-European clearing and settlement operators.

Second the tracking of collateral in securities financing transactions is not feasible. It is unclear why attempting to track reuse is really necessary and what benefits this would bring.

Finally mandatory buy-ins, as required by CSDR, are a particular concern, as they will have the effect of significantly reducing liquidity across secondary European bond and securities financing markets, while bid-offer spreads will widen dramatically. They should be deferred at least until after T2S is fully implemented, and their application should be recalibrated.

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

Despite significant progress towards the European single market, capital markets are still fragmented with regard to company law and corporate governance rules, creating barriers that hamper the free flow of capital. Those barriers across regions make cross-border investments complex and expensive, and therefore less attractive. The Single Rulebook has not yet been fully achieved.

Continued harmonisation of national rules and standards on transparency and shareholder engagement in order to eliminate costly barriers and reduce complexity for investors is essential and can be achieved while respecting national corporate governance structures and local traditions.

Without common applied **corporate governance** principles/control that guarantee sufficient transparency and shareholder engagement the Capital Market Union cannot be done successfully. Thus further harmonisation of national rules and standards in these areas are needed in order to eliminate costly barriers and reduce complexity for investors who do not act within national boundaries.

The varying degree of transparency on company reporting for example. Whereas in some countries like Sweden any and all (irrespective of whether public or listed and size) company statutory reporting info for the last 12 years is available (for purchase) via the web-site www.allabolag.se as is info on Directors, credit ratings etc this is not the case throughout the EU.

Language is another impediment.

The exercise of cross-border voting rights and the operational complexity of the voting chain is an obstacle to integrated capital markets arising from company law and corporate governance.

A consistent legal framework for creditor protection and insolvency across the EU would also facilitate cross-border investment.

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

Different national insolvency laws make cross-border services expensive. Reducing the existing inefficiencies will play an important role in unleashing the wider macroeconomic benefits from integrating European securities markets.

Harmonisation proposals should look into the nature of the insolvency proceedings (administrative vs. judicial procedure). In any case, measures should include among others the opening or the management of an insolvency proceeding as well as the scope of liability of involved parties. Further harmonization could include initiatives to overcome the current restricted local effect of insolvencies in case of group companies.

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

Address the distortions created by the current system of taxing cross-border dividends[3] and eliminate the double taxation of cross-border dividends and interests at investor level within the EU and end tax discriminations against EU investors domiciled in another Member state than the investment provider.

Review of EU State Aid risk capital guidelines to allow for effective incentive schemes to be adopted by Member States. The guidelines should recognise the role of expansion capital as genuine risk capital. Tax reforms may be considered in order to encourage more long-term holdings (i.e. better pre-tax off-setting of gains and losses, and tax push forward if realisation proceeds are re-invested). Creation of specific benefits to certain investors who can invest in SMEs, tax relief or personal internal revenue taxes lower on capital gains on securities of these companies, under conditions of maintenance of such securities over a minimum period of time and a maximum concentration by company (in value and in percentage of capital of each company). Exemption of certain investment rules imposed on certain investors in the case of investments in SMEs (e.g., minimum ratings, liquidity of securities, etc.). This would need to be balanced with any risk of misallocation of capital.

The **Financial Transaction Tax**, would increase transaction costs in European financial centres and could therefore impede the goals of the Capital Markets Union. SMEs in particular would face higher capital raising costs as a result of rising transaction costs. Retail investors would also suffer greater financial losses as the tax directly hits retirement provision products.

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

No response given.

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

MiFID has posed serious challenges to the bank and broker intermediation chain potentially harming local funding ecosystem. With regard to Regulated Markets and MTFs, and the increased transparency requirements can represent a challenge for market venues and SMEs, resulting in a suboptimal time allocation for SMEs' board and management and ensuing increased costs of accessing public markets. In addition, MiFID has also heightened the pressures faced by small and medium sized intermediaries in respect to their cost base, the very ones that were traditionally the ones most involved in SME research activities.

[3] With regard to identified distortions we refer to a respective study carried out by Copenhagen Economics already in 2012 on behalf of the EU Commission:
http://ec.europa.eu/taxation_customs/resources/documents/common/consultations/tax/venture_capital/tax_crossborder-dividend-paym.pdf

SME Market Segments such as Deutsche Börse's Entry Standard (http://www.boerse-frankfurt.de/en/basics+overview/market+segments/entry+standard) and the Elite programme, which was started in 2012 by Borsa Italiana, part of the London Stock Exchange Group, could be a partial solution to the lack of support from the local intermediation chain. At the end of last year, 176 businesses had joined the program in Italy; it is supported by a network of 70 advisors and 120 investors. The average yearly turnover of Italian Elite companies is 124 mn €, ranging from the smallest (6 mn €) to the largest (1,2 bn €); their average Ebitda amounts to 15% and exports total 45%. Elite Companies have been involved in one Aim listing, 13 private equity investments and 10 small corporate

The Shareholders Rights Directive should be amended to facilitate the exercise of voting rights cross-border, and in nominee/omnibus accounts, and free-up the right of small shareholders to freely associate and for these shareholder association to easily collect proxies from their members.

Actual retail data provided by investment firms – free for individual investors after a few minutes – should be made more readily available in Europe. A debate on the consolidated tape, as included in the data and reporting section, should be addressed within MiFID II. Article 90.2. MiFID II even includes a review clause for the CTP regime. To avoid double regulation, its strongly recommended to delete the part on consolidated tape.

The TA proposed by ESMA to the Commission regarding the financing of research may destroy its present ecosystem at the expense of research on SMEs since research is not a profit center but a cost center.