THE MANAGEMENT COMPANY PASSPORT: A NEW ERA OF CROSS BORDER UCITS

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A INTRODUCTION

The new provisions for a new management company passport (MCP) outlined in the UCITS IV Directive[1] (Directive) are the next chapter in the development of the UCITS story. The MCP will allow a management company[2] domiciled in a Member State to manage funds established in other Member States with or without the establishment of a branch. The European Union (EU) introduced the first UCITS (Undertakings for Collective Investment in Transferable Securities) framework Directive in 1985.[3] This Directive introduced a single format for the open-ended funds that invest in transferable debt or equity securities to be sold with a single authorisation throughout the EU.[4] Today, there are around 32,000 UCITS products,[5] representing over €6 trillion of assets under management. UCITS licensed products thereby represent about 79% of the total assets of European investment funds.[6] These figures may suggest that the UCITS story has been a successful one however, in recent years, issues such as industry consolidation and efficiency constraints have prevented the EU from fulfilling its main objective of the UCITS project, to foster the development of a European single market. It was hoped this objective would offer greater business and investment opportunities, for both industry and investors by removing Member States barriers for the provision of financial services throughout the European Community. [7]

This new Directive is at the core of the EU's Financial Services Action Plan (FSAP). This action plan follows on from the Communication of 28 October 1998 entitled *Financial services: building a framework for action*.[8] It was presented at the request of the European Council, meeting in Vienna in December 1998, which invited the Commission to draw up a programme of urgent work to achieve the objectives set out in the framework for action, on which a consensus had emerged. It is also based

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[1] European Parliament and Council Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities [2009] OJ L302/32 (UCITS Directive)(recast).

[2] A management company is a company whose regular business is the management of UCITS in the form of common funds or of investment companies.

[3] Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities [1985] OJ L375 (UCITS).

[4] K Lannoo 'EU Retail Financial Market Integration: Mirage or Reality?' in European Credit Research Institute (ECRI) Policy Brief No 3 (June 2008) [97].

[5] Some of the common types of UCITS products: UCITS bank deposits, UCITS Umbrella Funds, UCITS Index Funds and UCITS Guaranteed Funds.

[6] Council Directive 85/611/EEC (n 3).

[7] European Parliament and Council of the European Union Proposal for a Directive on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) COM (2008) 0458 final (Proposal).

[8] Commission Communication of 28 October 1998 'Financial services: building a framework for action' COM (98) 625
< http://ec.europa.eu/internal_market/finances/docs/actionplan/index/fs_en.pdf> (25 February 2011).

on the discussions held within the Financial Services Policy Group (FSPG), composed of personal representatives of the finance ministers and the European Central Bank (ECB). The action plan for a single financial market puts forward indicative priorities and a timetable for specific measures to achieve three strategic objectives, namely establishing a single market in wholesale financial services, making retail markets open and secure and strengthening the rules on prudential supervision. [9] The Directive participates in the FSAP's main objective: the improvement of the single market in financial services

In the first section of this paper we will examine the background of UCITS in order to understand the context of the latest proposals for a MCP after over two decades of development. This will help us understand the origins of the MCP and the reasons why the EU Commission were motivated to reform this legislation. In addition, a definition of the MCP will be outlined and the rationale behind the proposals shall be explained. In the second section we will briefly outline and discuss the new proposals for the MCP in the UCIT IV Directive. In the final section we shall consider the outcomes of the proposals in relation to whether they will have a positive impact on the European fund management industry. We will do so examining whether issues, such, as taxation and regulation will affect the ability of the MCP to function effectively. With this in mind, we can judge whether the MCP is a significant step towards a European single market.

B BACKGROUND

UCITS has been a story of constant evolution, a collaborative approach between regulators who have a clear vision of where they want to go and the industry that has contributed a lot to developing an adaptable framework.[10] Undertakings for Collective Investment in Transferable Securities (UCITS) are pan-European investment funds. The role of UCITS in the European financial services sector was to allow funds authorised in one EU country to be available to be sold to the public elsewhere in the EU, thus creating a European single market for investment funds. These funds aim to make stock market investments more accessible to the public and diversify the portfolios of private investors without the constraint of managing each fund individually. Currently, these funds can only be managed by financial institutions registered in the Member State, in which the fund's legal entity is situated. The public can buy either shares (OEIC)[11] or units (AUT)[12] of the UCITS.

After the first UCITS Directive was adopted in 1985, the text has been amended several times in order to adapt to developments in the financial markets and to expand its scope beyond pure transferable securities funds. An amended proposed revision of the Directive was tabled in 1994, however UCITS II was subsequently

[9] Commission Communication of 11 May 1999 'Implementing the framework for financial markets: action plan' COM(1999) 232.
<http://europa.eu/legislation_summaries/internal_market/single_market_services/financial_services_general_framework/l24210_en.htm> (25 February 2011).
[10]David Adams 'Ucits IV- the next stage' International Custody & Fund Administration Newsletter (24 September 2009), on the words of Jean-Michel Lower, Chief executive of industry and government relations at RBC Delia < http://www.icfamagazine.com/icfa/feature/1896809/ucits-iv-stage> (25 February 2011).
[11] Open Ended Investment Company (OEIC).
[12] Authorised unit trust (AUT).

abandoned as no common approach could be adopted. UCITS III[13] in 2001 enlarged the investment powers available to UCITS. However, UCITS III fell short in a number of areas and in particular the lack of a fully functioning MCP.

Following this, the European Commission engaged in preparatory work and a public debate to determine which areas needed improvement, the outcome of which was a *Green Paper on the Enhancement of the EU Framework for Investment Funds* was published on the 14 July 2005, followed by a White Paper announcing measures to amend the UCITS Directive in 2006 and an *Exposure Draft* in 2007 highlighting areas were addition legislation was needed to remedy inefficiencies in the financial markets. A draft UCITS IV Directive was published in 2008[14] without the MCP as this section had been submitted to the Committee of European Securities Regulators (CESR)[15] for advice conducive to providing high level investor protection and to deal with legal, regulatory and tax issues. The Commission issued a recast Directive with the MCP legislation, which was approved on 13 January 2009 by the European Parliament.

The rationale behind the MCP is to create economies of scale and reduce costs in the investment fund market. It will allow for the creation of centres of excellence while at the same time allowing companies the freedom to locate operations around Europe and through cross border business models in management and administration.[16] This is in contrast to the current situation in which a management company has to spend time and money establishing branches in a Member State if they want to manage a fund in that country. Critics argue that the controversy over whether to include the MCP in the proposals shows how the evolution from UCITS III to UCITS IV is far from being achieved and that inefficiencies will continue.[17] However, others believe that critics of the MCP are retrograde forces that would roll back the clock on the single market and prevent the development of a true European market for funds.[18] Also, in light of the economic crisis that engulfed Europe, supporters argue that the proposals help strengthen supervision. Therefore, this will safeguard funds from further collapse and the cost saving incentive will help revive the funds industry after the crash.

C PROVISIONS FOR A MANAGEMENT COMPANY PASSPORT

In this section we will explain the provisions in the UCITS IV Directive, relating to the MCP. The main principles of the MCP will be outlined, along with a breakdown

[13]Amending Council Directive 98/0242 [2001] 0J L41/20 and Council Directive 98/0243 [2001] OJ L41/35.

[14] Proposed Council Directive (n 7).

[15] The Committee of European Securities Regulators (CESR) was restructured into the European Securities and Markets Authority (ESMA). The changeover to ESMA took place in January 2011.

[16] KPMG ‘UCITS IV- Your new strategic options’ <http://www.kpmg.com/LU/en/IssuesAndInsights/Articlespublications/Documents/BrochureUcitsIV-version%202.pdf > (19 January 2011).

[17] O Sciales ‘Luxembourg - Investment Funds - From UCITS III to UCITS IV’ <http://investments.lawyers.com/blogs/archives/381-Luxembourg-Investment-Funds-From-UCITS-III-to-UCITS-IV.html> (19 January 2011).

[18] D Waters ‘Current regulatory challenges: an update from the FSA’ <http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2008/0124_dw.shtml> (19 January 2011).

of its various features including, who can authorise a UCITS with a foreign management company and the supervisory duties of the member states' regulators.

1 General Provisions

A management company authorised by its home Member State will be allowed to provide the full range of collective portfolio management services[19] to UCITS established either as investment companies or common funds in another Member State of the EU.[20] Therefore, a Management Company has a choice when deciding to carry out operations in another Member State: it can either do so by setting up a branch in another Member State or providing services under the freedom to provide services[21] without the establishment of a branch. The branch would not be subject to any authorisation requirement in the Member State or to any additional capital requirements.

As a result, under this proposal a management company, once authorised in its home Member State,[22] defined in the Directive as where the management company has it registered office, can set up and manage funds set up in its home Member State. It can also manage funds set up and managed in other EU Member States. For instance, a management company set up and authorised in Ireland by the Irish regulator can create and manage common funds set up and authorised in Germany.

2 Authorisation Procedure by the UCITS Home Member State for the Foreign Management Company

The UCITS IV Directive defines a UCITS home Member State as the Member State in which the UCITS is authorised.[23] It is the regulator in this Member State who approves the choice of Management Company. In order to gain this approval the Management Company must submit to the regulator a number of documents outlined in the Directive[24] including, an attestation by the Management Company's regulator proving authorisation status, a description of the arrangements to deal with investor complaints and a written agreement with the depositary.[25] The UCITS home Member State regulator may request additional information from the Management Company regulator on the documentation submitted and on the authorisation to manage a specific type of UCITS. The regulator has two months from the date of receipt of

[19] The phrase 'collective portfolio management services' refers to activities that comprise of the distribution in all EU Member States of the units/shares of UCITS managed by a Management Company; including all associated functions and tasks and the provision of investment management, administration and/or other marketing services to other Management Companies.
[20] Directive 2009/65/EC (n 1) art 5(3).
[21] The freedom of establishment, set out in Article 43 of the EC Treaty and the freedom to provide cross border services, set out in Article 49, are two of the "fundamental freedoms" which are central to the effective functioning of the EU Internal Market.
[22] Directive 2009/65/EC (n 1) art 2(1)(c).
[23] ibid art 2(1)(e).
[24] ibid arts 17(3) – 18(2).
[25] ibid art 2(1)(a).

complete file to decide on the authorisation of the UCITS that will be managed by a foreign Management Company.

Subsequently, the UCITS home Member State may refuse to approve of application of the Management Company only in specific circumstances set forth in the Directive[26] and after requests for clarification and information from and consultation with the Management Company's home Member State. Before the Management Company tries to secure this authorisation it must first inform its regulator of its intensions to apply for UCITS authorisation and the program of activities it envisages it will undertake. The home Member Sate Authority will then forward this information to the UCITS home regulator.

3 Delegation of Activities by the Management Company

The home Member State of a management company may permit them to delegate to third parties one or more functions such as fund administration. Certain conditions as outlined in the 2009 Directive must be met and the management company regulator must inform the UCITS regulator of this permission in order for this to happen. It may be noted that there is no harmonised delegation arrangements imposed therefore, the UCITS home Member State rules do not apply in this regard, only the rules of the management company home Member State.[27]

4 Supervisory Competencies of the Management Company Home Member State[28]

The Management Company's home Member State regulator authorises and supervises the Management Company's compliance with the rules of it home Member State in relation to the organisation of a Management Company. This includes supervision of rules relating to delegation arrangements, risk management procedures, conflicts of interest and codes of conduct; and arrangements and organisation to comply with set-up and functioning of all UCITS and reporting requirements. The home Member State will duly inform the UCITS regulator of any change in the scope of the authorisation given to the Management Company.

5 Supervisory competencies of the UCITS Home Member State[29]

The Management Company will be subject to the UCITS home Member State rules and supervision, which relate to the constitution and functioning of the UCITS. In an effort to distinguish between the scope of the Management Company home Member

[26] ibid arts 5(4) and 20(3), for instance, may refuse to approve an application in the case where the Management Company is not authorised by its home Member State to manage a certain type of UCITS.
[27] ibid art 13.
[28] ibid arts 18 and 19.
[29] ibid arts 19(3) – 19(4).

State rules and those of the UCITS home Member State, the proposal specifically lists the rules which cover the constitution and functioning of the UCITS.[30] These rules relate to, inter alia, the set-up and authorisation of UCITS, issue and redemption of shares, restrictions on borrowing and lending; and the valuation of assets and accounting of the UCITS.

In order to monitor the compliance with these rules, the UCITS home Member States may require the Management Company to provide the necessary information. If a UCITS rule is broken the UCITS regulator will be permitted to take any preventative measure against the Management Company. The proposals allow for increased communication between regulators if authorisation of the Management Company is withdrawn.

6 The Depositary's Obligations Regarding UCITS that are Managed by a Foreign Management Company[31]

In the case of cross border management services, the depositary must put in place mechanisms to provide, on request of the UCITS regulator, all the information that it has obtained while discharging its duties as a depositary. This information is necessary in order for the UCITS home Member State to supervise the UCITS. In addition, the depositary of the UCITS must sign a written agreement with the Management Company regulating the flow of information required for the depositary to carry out its supervisory duties.

7 Implementation Measures Necessary for the Adoption of the Directive by the Commission

In a number of areas, the Proposal provides that the Commission may adopt implementing measure to amend non-essential elements of the Directive. These measures include structuring and organisational requirements to minimise conflicts of interest[32], code of conduct criteria,[33] particulars to be included in the standard agreements used by the Management Company[34] and measures regarding the risk management process. The Commission has started preparing these implementation measures with the assistance of CSER and intends for the full body of implementation measures to be ready for adoption by Member States before the 1 July 2011. This is the final date in which the Directive will need to be transposed into the national law of each of the Member States.

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[30] Luxembourg Fund Review 'Update on UCITS – The Management Company Passport' <http://www.ehp.lu/uploads/media/LFR_3_Update_on_the_UCITS_-_The_management_company_passport.pdf> (20 January 2011).
[31] Directive 2009/65/EC (n 1) arts 23(4) – 23(5).
[32] ibid arts 12(3) - 14(2).
[33] ibid arts 14(2).
[34] ibid arts 33(6).

D THE IMPACT OF THE MANAGEMENT COMPANY PASSPORT

In this section we will discuss the prospects of the MCP provisions in the UCITS IV Directive. We will examine whether it will lead to increased competition and efficiency in the investment funds market. Finally, we will consider whether the MCP will bring a single pan-European market for investment funds a step closer.

1 Increase in Competition

The positive elements of the MCP have been clearly acknowledged by a number of industry players and experts. They agree that without the implementation of a well functioning MCP in this Directive, competition on a pan-European basis would be clearly restrained and efficiency and flexibility gains to be expected by the industry would be limited.[35] Industry support was highlighted by the findings of a recent survey[36] showing how some of Europe's largest asset managers plan to capitalise on UCITS IV and identifies how these reforms will contribute to wider changes across the European Investment fund landscape. The main findings were that *a)* the vast majority of UCITS managers are taking a proactive approach to UCITS IV, *b)* the number of Management Companies will increase; *c)* a new wave of fund mergers lies ahead and *d)* immediate cost savings are expected. This final point is seen as especially pertinent in a time when the funds industry is in turmoil as it is now grappling with the effects of the economic crisis. Experts believe the MCP will help fund managers to rationalise fund arrangements which should lead to cost savings, and the passport should reduce the need for mind and body in each domicile.[37]

2 Strengthened Supervision

Strengthened asset management supervision is a key concept in the Directive's provisions and has increased significance at a time when the economy has suffered due to poor regulation. The importance of tightened supervision was emphasised by Commissioner Charlie McCreevy in speech at an industry forum:

> [W]ith upwards of $60 trillion in assets under management in conventional and alternative funds world-wide and around £4 trillion in the UK alone, the importance of this sector to investors, the financial markets and the economy as a whole cannot be under-estimated. G20 leaders have all agreed that regulation must be comprehensive: No

[35] M Lamandini 'The Commission's UCITS IV Proposal: Is It Sufficient to Create a True Single Market Platform?' <http://works.bepress.com/marco_lamandini/14> (19 January 2011).
[36]RBC Dexia and KPMG 'UCITS IV: Which business model for tomorrow?' <http://www.rbcdexia.com/MarketInsights/p_UCITS_IV.aspx> (19 January 2011).
[37] Proposed Council Directive (n 7).

> significant financial market actor can be allowed to slip through the regulatory net.[38]

In light of this, proponents of the MCP have suggested the solutions provided by CESR,[39] incorporated into the 2009 Directive will provide pragmatic solutions to the supervisory arrangements that will enable the passport to work well in practice. It enables European supervisors to co-operate on cross border activities in the true nature of the single market.[40] At the same time proponents argue the proposals for an MCP will provide a high level of investor protection, which has always been the cornerstone of the UCITS regime. The MCP strengthens investor protection by improving transparency of the management structure and enabling more effective management by the centralisation of functions in the core of the asset management business. That is, instead of having a number of offices across Europe, a Management Company can centralise its functions in one office, while being able to manage funds in a number of Member States on a pan-European basis.

3 Economies of Scale

Furthermore, advocates of the MCP believe it will deliver real economies of scale, of which a moderate estimate is in the range of €500-800 each year.[41] The Commission estimate that the new management opportunities provided by the MCP will allow UCITS to make up to €6 billion in savings. It creates economies of scale as the number of cross border funds a Management Company manages increases, the greater the savings it will receive. These savings could in turn be shared with investors in the form of lower investment costs.[42] In addition, they argue that the MCP will improve competition by lowering the barriers of entry for small and medium sized firms to operate across Europe, as they do not need capital to establish offices and employ staff across Europe. In turn, improved competition will help to ensure that consumers benefit from the economies of scale. Moreover, it is expected that the MCP will fulfil the objectives of the EU Treaty, by bringing freedom to provide cross-border services, at last for the asset management industry. This principle of the passport was included in the UCITS III Directive but the wording did not in practice allow the passport to work effectively.

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[38] Charlie McCreevy ‘Charlie McCreevy, European Commissioner for Internal Market and Services, Speaking at the PriceWaterhauseCoopers' European Asset Management Senior Executive Forum London (17 November 2009) <http://www.eulib.com/charlie-mccreevy%20internal-market-7853> (19 January 2011).

[39] The Committee of European Securities Regulation ‘CESR’s Advice to the European Commission on the UCITS Management Company Passport’ <http://www.esma.europa.eu/popup2.php?id=5367> (20 January 2011).

[40] < http://www.cesr-eu.org/data/document/081014_MCP_CESR_BVI_com_fin.pdf> (20 January 2011).

[41] The Investment Management Association ‘CESR Draft advice on Management Company passport’ <http://www.cesr-eu.org/data/document/CESR_draft_advice_ManCo_passport_IMA_Response.pdf> (24 February 2011).

[42] European Commission *UCITS, Improved EU framework Proposed for Investment Funds (*No 51, 2008) <http://ec.europa.eu/internal_market/smn/smn51/docs/ucits_en.pdf> (20 January 2011) (Commission Paper).

Despite the positive reception the MCP has received as shown above, a number of dissenting views have been expressed. We will now outline the reasons why certain experts and organisations feel that the MCP is problematic and why it is not a step in the direction of a pan-European single market. Primarily, we can gain an understanding of the negative aspects of the proposals by examining CESR's letter in response to Commissioner Charlie McCreevy on the UCITS MCP.[43] This letter outlines that the large majority of CESR members support the plan for a MCP however, a number of members (Ireland, Luxembourg, Poland, Slovakia and Slovenia) dissented and it is from these dissenting opinions we can glean the negative aspects of the proposals.

4 Ineffective Supervisory Framework

The main issue that the dissenting members expressed most concern about was the issue of the supervision of UCITS. They felt the proposals would not put in place a sound supervisory framework that would allow the UCITS regulator to perform its duties effectively and as a result of this investor protection may suffer.[44] Moreover, they believe that the split in supervisory duties and responsibilities between the Management Company Home Member State and the UCITS home Member State, does not provide realistic measures to ensure that the UCITS regulator will be able to effectively supervise the foreign Management Company with respect to the matters which fall within its remit. They fear that this may affect the principle that the rules governing the constitution and functioning of UCITS should be the same irrespective of whether it is managed from the home Member State or by a foreign Management Company.

A further concern expressed by some of the members of CESR was that the MCP might result in the creation of 'letter box entities', where a Management Company has no physical presence in another country other than a mailing address. Letterbox related concerns are important among regulators as effective supervision could be jeopardized if the fund is just a virtual/legal construction emptied of any substance and devoid of any activity. This would leave supervisors in a situation where they have difficulty in discharging their responsibilities. This situation could reduce effective oversight of part of the fund value chain.[45] In order to combat this problem the dissenting members feel more substance is necessary to ensure the legal existence of UCITS.

Along with the concern expressed by dissenting members, the letter addressed some of the members in support who raised concern about a number of issues. Belgium echoed the concern in the paragraph above, stating that the complexity of the new framework, inherent in cross-border activities provides various regulators with different responsibilities. The risk of this is to hamper prompt and effective supervision in the circumstances of a crisis. In addition, the Czech Republic expressed

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[43] The Committee of European Securities Regulators 'Re: CESR's advice on the UCITS Management Company Passport'<http://www.esma.europa.eu/popup2.php?id=5368> (20 January 2011).
[44] Commission Paper (n 42) 1, 1.
[45] European Commission 'Initial orientations for discussion on possible adjustments to the UCITS Directive' < http://ec.europa.eu/internal_market/investment/docs/legal_texts/orientations/mcpexposure_en.pdf> (20 January 2011) (Exposure Draft).

a specific reservation in relation to the general functioning of the passport framework, arguing it would be too complicated to operate in practice and that it would raise costs.

5 Policy Obstacles

Furthermore, industry experts warn that the growth of the EU fund industry should not obscure that fact that the market is far from being a single market. In order for the successful marketing of funds using the MCP, two kinds of obstacles have to be overcome.[46] These obstacles are 'policy induced' and 'natural' obstacles. Policy induced hurdles to cross border sales of funds include, for instance tax discrimination of foreign funds, and can be directly dismantled by appropriate adjustments of EU and national legislation. Natural obstacles resulting from consumer preferences or the inherent characteristics of the market are not under the control of policy makers. However, this does not mean that 'natural' means they are unalterable but instead it may be the case that market trends or changes in consumer behaviour tend to overcome existing 'natural' obstacles.[47] We will now discuss which policy induced and natural obstacles the MCP faces, which may prevent it from creating a unified market for investment funds.

6 Natural Obstacles

Natural obstacles to cross border sale of funds in Europe envisaged under the MCP could result from first *a)* consumer preferences and *b)* existing distribution channels. Consumer preferences may inhibit investors embracing the MCP in two ways. Firstly consumers have a preference for investment funds from domestic companies usually in well-established centres of excellence, the two main centres in excellence being Dublin and Luxembourg. In the same way, due to the existence of these consumer preferences, management companies are encouraged to set up in these places to attract consumers. Therefore, if those trends continue management companies will not embrace the MCP and instead revert back to the status quo. Experts argue that the scalability from the marketplace and technical infrastructure found in centres such as Dublin and Luxembourg are hard to replicate.[48] These centres cannot be packed up and passported away as the whole infrastructure takes years to build up thus a change in the status quo may not happen quickly. An additional attraction of these centres for consumers is that this expertise base brings with it greater consumer confidence and in turn attracts consumers, as their investment may be exposed to less risk in the hands of experienced management companies.

A major obstacle to the establishment of a truly pan-European competitive market for UCITS funds through the MCP remains outside the scope of the Directive

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[46] F Heinemann 'The Benefits of Creating an Integrated EU Market for Investment Funds' < http://en.scientificcommons.org/34267883> (20 January 2011).
[47] Exposure Draft (n 45) 10-11.
[48] Proposal (n 7).

and is represented by existing distribution channels.[49] The distribution obstacle is 'natural' in the sense that legislators do not have direct instruments to overcome it. Based on market forces alone, an open architecture for their distribution is still lagging behind. A major part of funds are sold over the bank counter. Banks often advise their customers with a bias towards fund products in their own group rather than towards the best performing funds. Thus, experts believe community action is needed to push investment firms and banks towards an open architecture for UCITS distribution. This could be achieved through the creation of rules to correct such market failure and restore a truly competitive European market where product selection is based merely on the criterion of fund performance in the best interest of retail investors.[50]

7 Taxation Issues

The new Directive extensively discusses the regulatory issues, investment products and the legal aspects involved in UCITS, however due to taxation aspects not being included within the scope of the Directive, it can be anticipated that taxation issues could create obstacles to the effectiveness for the MCP. It is anticipated the MCP will be hindered by *a)* discrimination caused by Members States treating non-resident UCITS differently from resident UCITS and *b)* the diversity in Member States' national tax legislation.[51]

The Directive proposes to regard the home Member State of the UCITS as the Member State in which its Management Company has applied for authorisation and in which the depositary is established. The concept of residency could be easily challenged by tax authorities across the Member States who generally consider the place of effective management and the place of the registered office of the entity as critical in determining its tax residency. The taxation of dividends, interest capital gains and other portfolio income derived from UCITS in EU Member States differs substantially for resident and non-resident UCITS. In many cases income derived by way of a non-resident UCITS are in many cases subject to more taxation. For example in Luxembourg, a fund is recognised as a Luxembourg fund if the registered office of its Management Company is located in Luxembourg. This means that currently, if a fund in Luxembourg is managed by a foreign Management Company, it automatically loses its status as a Luxembourg domiciled fund. In absence of a branch of the Management Company being in Luxembourg, the fund will lose its tax exemption from income tax.[52] In the absence of the Directive requiring the various tax authorities to adopt the definition of the UCITS home Member State as proposed, Management Companies will not be encouraged to embrace the MCP if the monetary gains they make by not opening a branch in another Member State are nullified by the taxation imposed on these funds.

[49] M Lamandini 'The Commission's UCITS IV Proposal: Is It Sufficient to Create a True Single Market Platform?' <http://works.bepress.com/marco_lamandini/14> (19 January 2011).
[50] Proposal (n 7) 16.
[51] R Adema 'Towards Harmonisation of the Taxation of UCITS in the EU' <https://www.deloitte.com/assets/Dcom-Netherlands/Local%20Assets/Documents/NL/Branches/FSI/nl_nl_fsi_magazine_no3_mei2008.pdf> (20 January 2011) [34].
[52] P Noel 'UCITS IV Management Companies: The Dark Side of the EU Passport' [2009] Luxembourg Fund Review 18.

The success of the MCP may be hindered by disparities between the Member States' national tax legislation. The taxation of dividends, interest, capital gains and other portfolio income derived by ways of UCITS differs substantially between the Member States. Take for instance Italy, whose domestic funds are required to pay taxes on behalf of their investors, based on capital gains accrued over the year, regardless of whether they are realised or not. Elsewhere in Europe, taxes are paid on capital gains only when funds are sold. As a result of this anomaly, Italian mutual funds look less competitive and less flexible than foreign funds from other Member States that are not subject to the same treatment. Fabio Galli, director general of Italian fund association Assogestioni, believes a revision of the tax regime for domestic funds in Italy is 'urgently' needed if the UCITS Directive is to be a success: 'So long as taxation rules remain different to those of Luxembourg-based funds, UCITS IV will be a dead Directive for the Italian industry.'[53] As a result the competition playing field for UCITS funds is not the same. As a result a Management Companies will not be encouraged use the MCP to passport services and establish new funds to other Member States. Instead, status quo remains that the Management Company will chose the Member States whose taxation system is more attractive.

E CONCLUSION

In conclusion, the positive outcomes of the MCP are apparent, in the form of financial savings, increased investor protection and the creation of real economies of scale as a Management Company can now centralise its functions in one Member State. As a result of this the barriers to cross border trade will be lowered allowing small to medium sized companies to enter the market and improve competition. With the barriers lowered to cross border trade and the existence of incentives such as monetary savings, it may be argued that the MCP helps foster a single European Market for investment funds.

However, it may be more justified to conclude that the disadvantages outlined in the article outweigh these advantages. Instead of increasing competition and delivering real economies of scale, the MCP may not be able to overcome the market status quo and therefore, will not overcome obstacles such as consumer preferences and existing distribution channels. These obstacles cannot be conquered overnight by a piece of legislation and the pattern of the market can only be changed by the market alone.

Probably the largest hurdle the MCP will face is the taxation regime across the Member States, as the financial savings envisaged by the MCP can be easily outweighed by Member States' taxes on the profits of foreign UCITS. It has been suggested that for the MCP to function effectively a new UCITS Directive or a Directive on the taxation of UCITS will need to be drawn up.[54] At the end of the day, the objective of the asset management industry is to make the highest profit margins for investors, if the MCP cannot provide this due to taxation problems, the consequence is the industry will not embrace it and the much desired single European market for investment funds will not be achieved.

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[53] D Ricketts 'A Dead Directive: UCITS IV in Italy' <http://www.assogestioni.it/index.cfm/3,144,4837/ignites_europe_ucitsiv.pdf> (20 January 2011).

[54] Noel (n 52) 34.