EMEA

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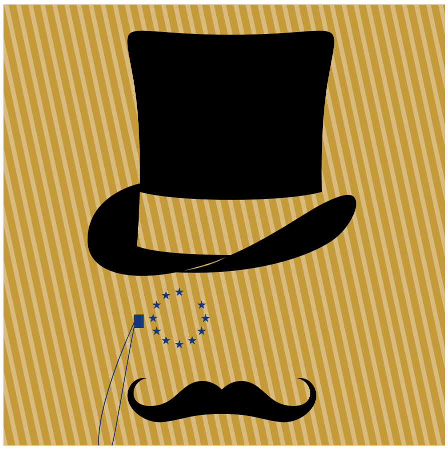

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Foreword

In the words of Charles Lamb "No one ever regarded the First of January with indifference. It is that from which all date their time, and count upon what is left."

January is the time for reflection and contemplation, for taking stock of the previous year and planning for the year ahead. Just like people, many companies make "New Year's resolutions" in terms of goals, strategies and aims. Perhaps this 25th milestone edition of Performance will provide you with the necessary food for thought.

For this first edition of 2018 we return from our globe trotting journey to Europe and more specifically France—considered by some as the gastronomical capital of the world. In terms of asset management however, did you know there are four French asset managers amongst the top 20 worldwide? To highlight the importance of the sector, the contributors for three out of the four articles featuring France come from you, our readers. Learn about their plans and hopes for the future.

From a regulatory perspective, 2017 was dominated by the challenges of implementing PRIIPS and MiFID II, the final impact of which is already being felt despite January only being a few days old. This year, the spotlight is firmly shining on the European insurance industry, which has literally weeks left until the deadline of 23 February 2018 for the implementation of the Insurance Distribution Directive. The priniciple of IDD is relatively simple i.e. that consumers should benefit from the same level of protection regardless of the distribution channel. However, as with any regulation, there are a number of nuances, approaches and interpretations across the European Union resulting in detailed analyses being required to ensure compliance across the region and potentially beyond.

The year of 2017 gave us buzzwords including Regchain, Blockchain, RPA, RegTech and FinTech, to name but a few. So what does 2018 hold for us? Consolidation? Distruption? Innovation? One word coined in 2016, that has generated a ton of press since, and which will continue to do so is of course Brexit. Even this issue of Performance is not immune with an update on tax restructuring measures.

Last but not least, another buzzword that transcends all sectors of the financial industry on a global scale is transparency. Just like PRIIPS, as of October 2017, the Australian Securities and Investment Commission required superannuation products to disclose fees and costs in periodic statements. Could this potentially lead to more global harmonization to the benefit of investors?

We would like to finish this short foreword by sending you and your families all our best wishes for 2018 and to making Performance the primary magazine to help shape your and your companies' futures.

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EMEA Investment
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Editorial

Dear Readers,

There are several paradoxes that spring to mind when we consider asset management in France:

- The French despise money because of a genetic predisposition to revolution. Yet they are also among the western hemisphere's greatest penny-pinchers, with one of the highest savings rates.
- They value their unusual pay-as-you-go pension system, but have known for some time that changing demographics will prove detrimental to intergenerational solidarity.
- The French see retirement as a savings priority (54 percent expressed this view, according to the Deloitte retirement survey). However, only 6 percent of their income goes to retirement savings (Deloitte retirement survey).
- Their tax system does not encourage risk taking, since short-term banking products are exempt, whereas interest income is taxed at over 60 percent, dividends at over 40 percent, and capital gains at 25 percent to 60 percent based on the holding period.
- Although there are 630 management companies in France, including 420 entrepreneurial companies (of which 200 are less than five years old), only 13 AM companies manage assets in excess of €50 billion, and only a single one is among the global top 10.

Why, then, is there a thematic focus on the "winds of change" in France?

- No longer in hiding, the asset management industry is looking to promote its economic role (€3.6 trillion in assets under management and 85,000 direct and indirect jobs) through the activity of its associations.
- In a country where public debt represents 99 percent of GDP (€2.2 trillion), the development of management activities is of vital importance to state authorities. The regulatory authority and the AM association have launched an industry-wide competitiveness program. The ministry of the economy is encouraging mutual fund trading via Blockchain, the tax on financial products has been revised (flat tax), and the balance is now shifting towards AM to the detriment of property holdings.
- Moreover, all signs are pointing to an industry refocus on retail and international expansion, which are well served by a wealth of talent and a revitalized technology scene.

In the words of the British writer Doug Larson, "Never doubt the courage of the French. They were the ones who discovered that snails are edible."

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The asset management industry

Pascal Koenig, Investment Management Leader in France, had an interesting conversation with Yves Perrier, Chief Executive Officer of Amundi on the asset management industry, its challenges and prognosis for the future.

Yves Perrier

Yves Perrier is Chief Executive Officer of Amundi since its creation in 2010 and a member of the Executive Committee of Crédit Agricole since 2003. He is also Head of the Insurance Asset Management and Real Estate activities for Crédit Agricole Group. As such, along with his position of CEO of Amundi he supervises the Insurance division (*Crédit Agricole Insurance)* and the Real Estate division (Crédit Agricole Real Estate). Yves Perrier is also Honorary Chairman of the AFG (*Association Française de Gestion Financière*).

Deloitte: Has asset management become a fully-fledged industry or is it still dependent on the banking or insurance industry?
Yves Perrier: The asset management business is a business in its own right with key links to distributors. Over the first four years following the creation of Amundi, the French asset management industry suffered redemptions, in particular from retail clients of banking networks. This was a direct consequence of new regulatory constraints: the banks favored deposits over investments in mutual funds. This environment pushed asset managers to find new drivers of growth. That was the case for Amundi, which had to grow outside of its partner networks and outside of France. Since 2010, Amundi's assets under management have increased by 50 percent from €670 million to €1.2 billion (excluding the integration of Pioneer), essentially from organic growth and international development. This development strategy has enabled Amundi to transform itself from being mostly captive in terms of its banking owners to a competitive open asset management platform that was approved by the market during its IPO in November 2015.

However, this development would not have been possible without the support of our majority shareholder. The Crédit Agricole group plays a key role in shaping our corporate culture and has also provided vital financial support on several occasions, as was the case when we decided to acquire Pioneer. Furthermore, being part of a group like Crédit Agricole offers a lot of potential for revenue synergies, in particular with regard to insurance

Further challenges to the asset management industry come from the development of passive management and competition from providers in the English-speaking world.

and real estate activities. The creation of the Savings business line (including insurance, real estate, and asset management) by Crédit Agricole has enabled us to develop and provide complete investment solutions that meet the client's needs according to their investment horizon, objectives, and risk/return profile.

D: In an industry with very little concentration, is big necessarily beautiful?

YP: The consolidation movement is part of a wider context: across the entire financial industry–asset management, banking, insurance– players are constantly seeking new ways to boost their competitiveness. The entire financial sector is facing a squeeze on profit margins due to very low interest rates. Nowhere is this trend more evident than in mortgage interest rates and returns on savings. And it will continue. Further challenges to the asset management industry come from the development of passive management and competition from providers in the English-speaking world. With their extensive domestic market (representing 50 percent of the global asset management market), US asset managers are well positioned to expand aggressively in Europe. In response to this context, asset managers have had to adapt by innovating and reducing their costs. Asset management is mainly a fixed-cost industry with substantial economies of scale. Achieving critical size is one way to address declining incomes. That is why we do therefore expect some consolidation in the industry. Mid-sized asset management companies are natural candidates for consolidation. However, consolidation is not the only solution. There is still room for boutique asset managers based on the talent and entrepreneurial spirit of their managers. So, in this case big is not necessarily the only form of beauty.
We believe the winners in this environment will be the companies that:

- Maintain consistency with their selected business model and strategic positioning, and avoid "stuck-in-the-middle" positioning.
- Improve agility, modularity, and time-to-market to be able to (I) expand into new products and investment approaches, (II) develop new activities and/or positions on new activities in the value chain, (III) adapt to new distribution and fee model scenarios, (IV) respond appropriately to clients' increasingly high expectations regarding services and reporting, and (V) react to external shocks.
- Achieve best-in-class efficiency and cost control.

For example, the acquisition of Pioneer Investments was not only motivated by issues of scale. Amundi and Pioneer have highly complementary investment capabilities. Pioneer will reinforce Amundi's expertise in various asset classes such as European, US, and Emerging Market equities, Multi-Asset, and US fixed income. Pioneer clients will benefit from the recognized and custom-designed services of Amundi, such as Smart Beta, ETF, real and alternative assets, structured and guaranteed solutions, as well as money market funds. Likewise, Amundi and Pioneer have complementary geographic coverage, generating strong cross-selling opportunities. In addition, a long-term partnership with the Unicredit networks allows Amundi to further strengthen its position as the preferred provider of savings solutions to retail clients in Europe. This integration will create a global player with a strong European identity, ranking among the top 10 worldwide in the asset management industry in terms of AUM (c. €1.4 trillion in AUM). This will position the company as the undisputed leader in Europe and strengthen its European leadership in four domestic markets (it is currently the market leader in France, holds top three positions in Italy and Austria, and has a strong position in Germany).

D: Do the major players in this industry carry a systemic risk?

YP: In the context of liquidity crises, bank and insurance companies are prudentially regulated entities. In terms of the asset management industry, where companies manage money on behalf of their clients, funds' liquidity risks are also monitored and minimized through comprehensive regulation (UCITS/AIFMD) and the multiple liquidity management tools available to managers. In addition, Amundi has established internal rules and risk management policies to protect clients' underlying assets. Daily liquidity stress tests and swing pricing are examples of the policies that Amundi employs to anticipate this risk and to assure redemptions. Nevertheless, we believe that, in addition to strict risk controls at the fund level, a strong financial structure is a supplementary protection in the event of major shocks.

There is still room for boutique asset managers based on the talent and entrepreneurial spirit of their managers.

On European financial management

D: The Brexit deadline is once again driving the debate on the management of the financial markets and dividing the community. Is there a risk that the landscape of players will be singularly altered?
YP: It is too soon to have a clear view on the consequences of Brexit because the real negotiations have not yet started. The critical points are whether or not UK-based players will be allowed to retain the European financial passport, and how this will affect investment management.

The portfolio manager's interpersonal skills and ability to summarize information will still be key parts of client relation management.

D: For the most part, asset managers are facing a deterioration in their margins. Can technology rise to the challenge and reverse this trend?
YP: It is important to neither underestimate nor overestimate the impact of new technologies on our industry. Like in the banking sector, we need to be both 100% digital and 100% human.

New technologies can help to identify the right saving solutions to meet the client's needs and may prove to be a real asset as we devise and structure an advice and investment process. Nevertheless, the portfolio manager's interpersonal skills and ability to summarize information will still be key parts of client relation management.

D. Will financial education solve our famous risk aversion?
YP: First of all, the French tax system has to be reviewed to favor long-term investments such as equities. These deliver higher yields to investors who are willing to accept more risk, while financing the real economy.
Up to now, the French tax system has been totally on the opposite side. But the flat tax proposed by the French government is a first positive step.

Our role is not only to offer mutual funds, but also to develop and provide our clients with investment and saving solutions based on their risk appetite, objectives, and investment horizon. Retail investors do not ask for complex products delivering high yields. Their first objective is to retain their capital. They also require advice and high-quality services. The success of Amundi's development is based on these four pillars: client-centric organization to offer solutions that meet clients' needs, performance, an ability to provide advice, and the quality of its infrastructure (IT, middle office, etc.). Finally, we need European regulators to adapt their rules to encourage equity investment. For example, the constraints of Solvency II are too restrictive for insurers to invest in equities in particular when we compare these to the US rules on pension funds.

D: What is holding Paris back from becoming the "European Boston"?
YP: Paris has dynamic asset managers, as evidenced by the number of companies created in recent years, offering various profiles in terms of shareholding, business, and client base. With more than €3 trillion in assets under management, it is an international investment hub.

France is ranked number two after the United Kingdom. It also benefits from a favorable ecosystem and a regulator that is finely attuned to the development of asset management. Finally, it is based on the recognized skills of professionals and a regulatory system that favors in patriates. France is a very strong market with many recognized players: four French asset managers are among the top 20 worldwide and 670 entrepreneurial asset management companies operate in France with high-quality managers and a wealth of talented individuals. France benefits from several recognized boutiques specializing in strategies such as active management, private wealth management, alternative management, multi-asset management and private equity.

D: Any new projects after the IPO and the ongoing integration?
YP: Our ambition as a company remains unchanged–to provide our clients with high-quality advice on the one hand, and savings or investment solutions in line with their objectives on the other.

The IPO in 2015 was made possible by the fact that Amundi reached its target in terms of AuM, revenue, and profitability, essentially through organic growth, and implemented its plan to operate as an open asset management platform. Our equity story sparked a great deal of interest from institutional investors, especially large international long-only firms. We had an extremely intense, open and valuable dialogue, and I think that investors were surprised to discover Amundi's strong and profitable growth, industrial model, and unique expertise, in particular in the retail segment. Crédit Agricole SA remains the majority shareholder of Amundi, with 70 percent of the capital.

By incorporating the strengths of Pioneer Investments in July 2017, Amundi has taken an important step forward in its development, building on the principles set forth at its creation in 2010.

This integration created a global player with a strong European base and a unique industrial model built around two client business lines: the Retail clients division and the Institutional & Corporate clients division, both offering a comprehensive and well-diversified set of investment solutions designed to address specific needs all over the world. The successful and complete integration of Pioneer Investments is our priority right now and we plan to achieve this by the end of 2019.

In the meantime, our expansion plan is primarily via organic development, but we can be opportunistic on smaller acquisitions to add to either our expertise, distribution channels, or local coverage outside of France.

What has become of French boutiques?

French third-party management: accompanying the "French boutiques" boom

Chairman of the Association Française de la Gestion financière, had an interesting conversation with David Benamou (Managing Partner and CIO of AXIOM AI), Eric Franc (CEO of DNCA Finance) and Laurent Deltour (Chairman of Sycomore Asset Management) on "French boutiques", its implications and reasons of its success.

Eric Pinon

Chairman of the Association Française de la Gestion financière (AFG) Chairman of the AFG since May 2017, he is also a Senior Advisor at La Financière de l'Echiquier and a Director at Acer Finance, where he had been a partner since 2006. He started his career at stockbroker Michel Puget in 1978, and was once its chief executives until the merger with the Barclays group at the end of 1989. That same year, he created Europe Egide Finance, which he headed until its sale in 2003 to Banque KBL France, where he served as CEO until 2006.

David Benamou

Managing Partner and Chief Investment Officer of AXIOM-AI, a management company created in 2009 that now manages €1.1 billion in assets for private and institutional clients. The company analyzes the financial institutions sector and has developed a unique expertise in subordinated bank debt. There are currently four managers for eight funds. The company is held by its natural person founders.

Laurent Deltour

Chairman of Sycomore Asset Management, an entity created in 2001. The company manages over €7 billion in assets for private and institutional clients, based on four areas of management expertise (European Equity, Absolute Return, Eurozone Corporate Bonds and Diversified). Some twenty managers apply a proprietary fundamental analysis model that covers four strategies: Sustainable Equities, Thematic Equities, Flexible Strategies and Credit Crossover SRI.

Eric Franc

CEO of DNCA Finance, created in 2000 and serves private and institutional investors. The management company offers a range of 26 UCITS funds (French mutual funds and a Luxembourg-domiciled umbrella fund ("SICAV")) focusing on four major areas of management expertise (European Equity, Diversified, Convertible Bonds and Eurozone bonds). Over 30 managers oversee €25 billion in assets. In 2015, Natixis Global Asset Management acquired a 71% equity interest.

The creation of a portfolio management company status in 1989, followed by the Financial Activity Modernization Act in 1996 recognized third-party management as a distinct business line. Building on this legitimacy and the growing professionalization of the risk diversification and asset allocation processes underlying savings and investment solutions, French third-party management has become a flagship of the French financial industry, alongside banking and insurance. In fact, with €4.0 trillion in assets under management, the French AM segment holds the top spot in continental Europe, with an annualized growth rate exceeding 5 percent since the low point of 2008.

The French market has nearly 650 portfolio management companies encompassing all asset categories and management styles, including some of the leading AM providers on the international stage. However, the reason it stands out in the European landscape lies in the significance and vitality of its entrepreneurial network, which represents, in terms of both existing and newly created entities, two thirds of players and one third of management teams. Created by experienced and often widely recognized professionals, these companies represent a body of specialists whose success is derived from their capacity for innovation, organizational flexibility, familiarity with investor needs and, of course, a unique offering. Historically focused on private management, equity and company debt, particularly small-mid caps, and close client relations, these companies have gradually developed new expertise in unlisted, alternative, quantitative, structured, and absolute performance management, by communicating their knowledge via investment funds. In this context, the internationally recognized quality of French scientific training, particularly in mathematics, represents a substantial competitive edge for management teams in terms of financial innovation and technology.

One of the main challenges entrepreneurial companies currently face is achieving the necessary size to compete in international and/or institutional markets. This is all the more true in a context of intense competition and market tension that affect their margins with, on the one hand, downward pressure on prices and, on the other, higher costs relating to regulatory compliance (MIF2, PRIIPS, SOLVA2, GDPR, etc.), technological investment, and commercial development. While there is no one solution to meeting these challenges, business model adaptation and further reinforcement of ecosystem linkages are often required. This sharing of means and expertise is realized via company mergers, the pooling of resources (EIG), openness to institutional or distribution partner capital, the contribution of incubators, etc. Fintech offerings are also an asset in boosting the operational efficiency of management companies and client service quality. A number of "French boutiques" have already earned their stripes as pioneers in the field, with some 50 of them passing the €1 billion AM milestone, by opening foreign marketing offices or forging distribution partnerships, and by building strong brand images based on the impressive track records of emblematic funds. On average, over half the assets are managed for foreign investors who place their confidence in them, be they private or institutional, and this percentage is rising yearly.

Improving the competitiveness and appeal of the Paris financial center is the guiding mission of the Association Française de la Gestion financière (AFG). Working closely with the regulator (AMF) and the entire ecosystem, its goal is to roll out concrete measures aimed at broadening the visibility and distribution of French investment funds and management internationally. Supporting the "French boutiques" boom and focusing on savings markets will guarantee that our business continues to provide solutions that are tailored to our clients' needs and place third-party management at the forefront, based on the model in place in the English-speaking world.

Eric Pinon: Can you recap your entity's trajectory and the reasons for its success?

Damien Benamou: Axiom Alternative Investments was launched in 2009 by a team of investment professionals from both the investment bank sector and the asset management industry. At the time we had the strong view that the vast majority of investors had a very limited level of knowledge of the financial industry, its regulation frameworks, and its accounting principles, and that this had exacerbated the crisis. Having drawn the conclusion that investors would take time to come back to the sector, and in the meantime, would look for specialists, we decided to have a deliberate focus on financials, with a strong research component.

This has enabled Axiom to emerge and establish itself as a trusted expert with issuers, investors, the media, and regulatory bodies.

As timing often means (nearly) everything, 2009 was the perfect time to start out as the dislocation in financial instrument prices was unprecedented, with very few investors having the knowledge, the time or the risk appetite to invest in the space.

Starting in that context helped us to build a 12 percent annualized gross performance on our flagship fund since 2009, which is still one of the longest and best track records in the entire industry, year-to-date.

Laurent Deltour: There are several reasons for our success—and success in asset management is always a question of time and discipline.

We have been governed by a number of principles ever since the company was launched in 2001.

First and foremost, we have never chased assets. We believed—and maybe we were naïve in doing so—that if we delivered steady performances, clients would recognize the quality of our work and invest in our funds.

I said we were naïve, because even if a company offers great funds, in today's world, investors still need to be aware that this company exists somewhere in France.

Secondly, as stock pickers, we also believe that extra-financial criteria are as important as looking at balance sheets. Today, this is embodied in

Improving the competitiveness and appeal of the Paris financial center is the guiding mission of the Association Française de la Gestion financière (AFG).

our SPICE investment philosophy. SPICE is an acronym for Society & Suppliers, People, Investment, Clients, and Environment. Today, extra-financial analysis is embedded across our range of funds and we can say that we are, by far, the leading responsible investment independent asset management company in France.

Finally, as with any other company, it is vital to retain talented individuals. To achieve this, especially with millennials, you need to give your employees a vision. This vision has to be shared throughout the company and be applied in everyday work. Our vision is to "humanize investment".

Eric Franc: The company was launched in 2000 by Xavier Delaye, Joseph Chatel (both formerly at Richelieu), and Charles Nouailhetas. Jean Charles Meriaux (former CIO of Edmond de Rothschild) joined the company in 2002. One of the reason for our success has always been our ability to attract excellent senior portfolios managers (Isaac Chebar and Igor de Maack in 2007, Cyril Freu in 2009, Carl Auffret in 2011,etc.).

The second reason is our capacity to find shareholders able to bring industrial partnership. Banca Leonardo (2006-2015) gave us a strategy access to the Italian market, while since July 20015 Natixis has given distribution support in Spain, Switzerland, and the UK.

EP: What difficulties did you encounter in your development?

DB: The general context in 2009 was the other side of the coin: our flagship fund started with a small initial amount. Convincing investors was a true challenge as the entire community was either flying away from banks or trying to estimate potential losses they would suffer from their remaining exposure.

Most institutional investors could not invest with Axiom as the company, by virtue of being independent, was perceived as fragile and the track record of our only existing fund was only a few months old. Family offices, high net worth individuals, and generalist asset managers were our first investors in a context of very strong volatility in the industry and our home region, Europe.

This vision has to be shared throughout the company and be applied in everyday work. Our vision is to "humanize investment".

We were often perceived as the underdog or the riskier choice when competing with large, generalist asset managers. As Axiom has now grown and won the trust of institutional investors in Europe and the US with a much wider risk/reward investment solution range, this is no longer the case.

LD: In 2001, we had no assets under management and the tech bubble has just burst. At the time, no one knew how long the crisis would last and our failure to secure seed money with an institutional partner was a major mistake.

We therefore had to build up the essential three-year track record before seeing any growth in our assets under management. Another difficulty that we encountered was the launch of our retail distribution business via the French IFA market. The timing was disastrous (2007—just in time to catch the bear market) and at that point our range only included long-only equity products and our two long/short strategies.

During the crisis, we launched a flexible product (equity and cash) and a global asset allocation product. Today, these are our two best-selling funds among IFAs. But it took us eight years to be recognized by the IFA community as a genuine partner.

EF: The difficulties came mostly from the various financial crises, although it gave us the opportunity to deliver strong returns in difficult times. We have always been thankful to our first clients, the French IFAs who were the first ones to appreciate our performance and the quality of our portfolio management.

EP: Are international distribution and retail the primary focal points of your inflows?

DB: Although Paris-based, Axiom's investor base has for a very long time been predominantly international. We have invested time and energy in developing this international footprint, targeting four key countries outside France. We established an office in London, and listed a fund on the London Stock Exchange. This even prompted one journalist to call Axiom the "Franco-British boutique"! Our presence in the UK brought Axiom onto the radar of US investors.

Retail and high net worth individuals have indeed been our primary focus, as they have been the first movers in investing with us. Institutional investors who needed a minimal track record and who were at the same time suffering on their investments in bank subordinated debt took a much longer time to invest with us.

LD: Absolutely, like any other French asset management company, we have started to diversify outside of France.

There is no single recipe for success that can be applied to international development; furthermore, contrary to popular belief, Europe is not at all unified. There are many non-tariff barriers in different countries that make local presence costly and cumbersome.

To achieve any kind of success, it is important to be pragmatic and to adapt to the reality on the ground in each country. This is exactly what we have done, proceeding by trial and error. We made a failed attempt at running an office and local salesforce in London; we also had a third-party marketer for the Gulf region.

Luckily, we have been very successful in other countries such as Austria, Germany, Italy, Spain, and the usual French-speaking countries: Switzerland, Belgium, and Luxembourg. Our client bases are slightly different in each of these countries.

In 2017 our growth is evenly split between French IFAs, international clients, and our historical French institutional investors.

We are very satisfied with this set up, which allows us to walk on "three legs". However, we continue to favor long-term sales relationships, and tend to not chase growth for the sake of growth.

EF: We do focus both on local and international distribution. In France, historically we have had substantial market share with IFAs, but we have also developed strong relationships with private and retail banks, insurers and institutional clients. Internationally, we do a lot of business in Italy, Spain, Belgium, and Luxembourg. We are very careful not to go everywhere, we want to go step by step. Size alone is not the end goal for us. We just want to keep attracting new talent and providing good return on investment for our clients.

EP: Digital transformation—can it help you maintain your margins?
DB: Not for now. It is our research, our in-depth knowledge of the sector, and the access we provide to the more complex parts of the asset class that investors value. Robo-advisors, algorithm-driven strategies or risk premia strategies are, however, part of our business plan for certain area of our universe.

We have developed digital communication tools exclusively for social networks with a view to supporting our growth, we have also implemented new tools to facilitate the sharing of information and ad hoc documents.

LD: I cannot tell at this stage if digital transformation will help us maintain our margins over the mid-term. In our case, it is instead used to support our growth. Digital transformation is a major commitment and involves huge investment, both in terms of people and software. Our digital strategy is not limited to the field of marketing. We have developed digital communication tools exclusively for social networks with a view to supporting our growth, we have also implemented new tools to facilitate the sharing of information and ad hoc documents. Finally, digital developments have helped us to structure our recruitment process through the use of a unique platform, SmartRecruiters; we have also improved our staff assessment system thanks to BambooHR.

EF: We think digital transformation will greatly improve the quality of our reporting. Clients will therefore expect strong performances from their asset manager.

EP: What are the major strategic choices that enabled you to make a difference? Product, targeted clientele, marketing, customer service, aggressive pricing, etc.
DB: Being a specialist, being visible as experts to investors and the media in the European financial sector, and avoiding overcrowded investment areas have been key for us to emerge.

Building an entire product range on financials and offering investors a range of risk/reward investment vehicles helped us to grow and enlarge our investor base. Finally, our key edge has been our strong culture of focusing exclusively on financials. All functions, from sales, marketing, and middle office to risk management, understand our universe, instruments, and investment cases. This increases efficiency throughout the organization and maintains a very strong and cohesive company culture.

LD: The fact that Sycomore was not founded by one charismatic fund manager, but by four people with complementary backgrounds, is one of our main differentiating factors.

Secondly, as the investment industry is increasingly dominated by passive strategies, it is important to differentiate ourselves—not only in terms of alpha generation, but also by giving a sense of purpose to our clients. This is why our objective is to become one of the leading asset managers in Europe in the field of responsible investment.

In terms of customer service, we have always tried to be transparent and proactive. Ever since we began, we have been one of the few asset managers to send out the monthly reporting on the first day of the month. We have kept this commitment, despite the mounting complexity stemming from asset growth and the larger number of funds.

However, we have never practiced aggressive pricing. We believe that the work we do and the services we provide are worth a fair price; and we do not want to chase fast assets that can go out as quickly as they came in.

Furthermore, if we wish to continue delivering steady outperformance, we know that some strategies will have capacity constraints; entering a pricing war in these circumstances would make absolutely no sense.

EF: We are a conviction portfolio asset management firm. We differentiate ourselves through solid performance over the mid and long term. Our challenge is to keep hiring the best portfolio managers. We have to maintain the same culture, humility, entrepreneurial spirit, and client focus.

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A new world for real estate investors

As the world changes, progressive real estate asset managers are discovering new opportunities

Xavier Lépine
Chairman of the Board
of La Française Group

Marc Bertrand
Chief Executive Officer
of La Française
Real Estate Managers

Real estate rental market activity across Europe is flying high as business climate indicators hit their highest levels since the end of the recession in 2010-11. Investment has remained very strong, with €130 billion in investment[1], making H1 2017 one of the top two years since 2006 in terms of H1 performance. However, the headline figures mask some interesting geographical differences. The German investment market experienced a record-breaking start to the year with €26 billion in investment—up 44 percent on H1 2016. In the UK market, which is adjusting to the fallout from the EU referendum, investment nevertheless rose by 23 percent on H1 2016 to €44 billion.

1. Source: CBRE, LF GREIM Research

Meanwhile, in France, the rental market made a timid start to 2017. Real estate investment reached €9 billion over H1—stable compared with H1 2016. A broad desire for home ownership and historically low interest rates are expected to continue to underpin the French residential real estate market, leading to further price increases for both new and established homes. High demand from French home buyers is increasingly concentrated in cities. The most striking example of this is the greater Paris area, where despite a series of crises since 2008, prices have generally risen and are expected to hit new records in 2017. As a result, the share of expenditure on housing has soared, limiting household budgets allocated to other areas and acting as a drag on French economic growth. By contrast, analysts point to the strength of the German economy, where a better distribution of activity and residential areas across the country are increasing competitiveness and boosting household consumption by maintaining rents at reasonable levels.

Grand Paris

The Grand Paris project, an ambitious infrastructure project on a scale not seen in the French capital since the 19th century, has been developed to address some of the challenges facing the French rental market. It is also a good example of a new phase in the real estate development cycle, which is opening the door for real estate investment managers to broaden their activity from the acquisition, management, and sale of assets to the financing of development projects. The high-quality urban project has a budget of €25-35 billion to almost double the transport infrastructure around Paris, and this should generate investment in the construction of housing and offices totaling €75 billion.

This is partially financed by La Française Group, a French asset manager with €64 billion in assets under management that made €2 billion in investment in France and the euro zone in 2017—a substantial long-term commitment that means it is invited to tender for all major projects in the market. "Our group is not just active in asset management; with real estate assets of €15 billion in Europe and more than 500 assets in the Paris region (Île-de-France), we also possess a significant amount of land assets," says Chairman of the Board of La Française Group, Xavier Lépine. "It was, therefore, natural for us to participate in this monumental project, which has no equivalent in Europe."

Paris has not experienced changes on such a scale since 1860 when Napoleon III officially annexed the suburbs of Paris out to the ring of fortifications around the city, leading his prefect of the Seine, Georges-Eugène Haussmann, to enlarge his vast public works program and construct new boulevards to connect the new arrondissements with the center. As part of the Grand Paris strategy to better connect the French capital's banlieues with its center, and manage the city more inclusively, work is underway on the Grand Paris Express, which will expand the century-old metro system to include four new lines, 68 stations, and more than 120 miles of track. Some zones will do particularly well out of the massive investment. Saint-Denis Pleyel, for example, will get a giant rail station—a hub on the same scale as Paris St Lazare.

Vector of wealth

The city's reinvention, however, entails much more than enlarged rail infrastructure. During September and October 2017, more than 50 roundtable meetings were held as part of the call for projects to "Invent the Metropolis of Greater Paris". These meetings, chaired by Patrick Ollier, president of Métropole Grand Paris, saw 153 finalist groups present their proposals for the development of 56 sites.

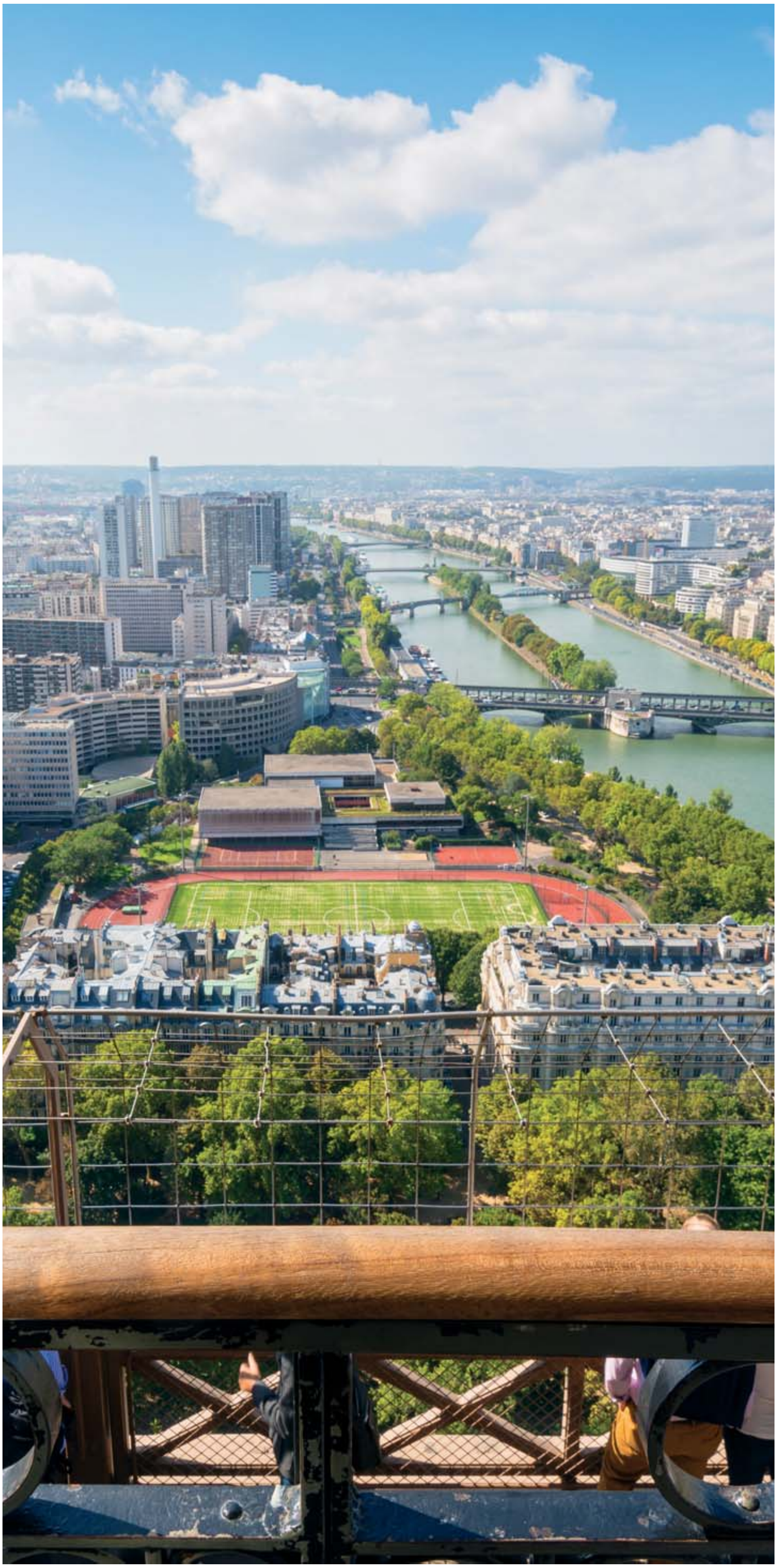
The competition generated a total investment of an estimated €6.4 billion, or one point of GDP for the metropolis, to build 2.6 million square meters of offices, housing, leisure, and public amenities. Following the consultation, La Française won three of the five largest sites: the Pleyel crossing in Saint-Denis, the Ardoines in Vitry-sur-Seine and the Rungis Bridge in Thiais and Orly.

Alongside its cultural and architectural significance, Grand Paris has huge importance from an economic perspective. It aims to streamline and facilitate the daily movements of two million people by creating hubs of activity at the regional level—innovation and research in Saclay, healthcare in Villejuif, aeronautics in Bourget, and TV and cinema in Saint-Denis Pleyel, for example. "These developments will clearly be a vector of wealth when we consider that the GDP per capita is 15 percent higher in the major developed cities," says Xavier. "With Brexit and the Paris 2024 Olympic Games, the project benefits from a buoyant context that could allow Paris to become the European capital."

Ownership for life

In addition to its three key projects, La Française Group wants to help develop the eco-districts that will be created to support the major infrastructure developments. "To do this, we will create an unlisted real estate company in which we will make a €50 million commitment with the objective of generating €1.5 billion in inflows within two years," says Xavier. However, for the Grand Paris project to achieve its full potential, La Française Group believes innovative thinking around the evolving needs of tenants is essential.

Marc Bertrand, CEO of La Française Real Estate Managers (REM), the group's real estate investment arm that is managed by a 140-strong team, of whom 120 are based in France, 15 in Germany and five in the UK, says: "We reckon that the Grand Paris project currently has a glut of office development, particularly around second-string stations. In these zones, we would rather invest in housing developments where demand



remains strong. This rebalancing is necessary, but still tricky for the municipalities for whom house building inevitably entails major investment in public infrastructure with little in the way of additional resources to fund it."

In order to better meet the needs of tenants, La Française suggests proposing the concept of propriété à vie or "ownership for life" whereby residents can become "owners for life" instead of "owners in perpetuity." Inspired by a model in place in the UK, it is an alternative to "ownership in perpetuity" or simple rentals. "The idea is to acquire a property from an institutional investor for use during a very long predefined period," says Xavier.

"Everyone wants to live in the same place, but scarcity of land means that the prices of real estate for residential properties are not within financial reach for the next generation."

Akin to a long-term lease, the property would be held in a real estate investment trust (REIT) and could be returned to the investor at a price that is protected against inflation. For example, say you bought a 50-year lease and had used 10 of those years, the REIT would buy it back at 80 percent plus inflation. The investment vehicle, in return, would typically receive an annual return of 4 percent, akin to returns from offices and higher than the 2.5 percent average on residential property investments. A second proposal is the "partially perpetual loan", which echoes existing systems in Switzerland, Sweden and the Netherlands, whereby the borrower repays the capital over a period of time in line with his or her expected lifespan. "Everyone wants to live in the same place, but scarcity of land means that the prices of real estate for residential properties are not within financial reach for the next generation," says Xavier. "These proposals could really help."

Space optimization

In the office sector, the investment manager has proposed injecting greater flexibility into rental leases so that premises can be converted and transformed to better suit a tenant’s needs for a fixed period of time. The asset manager is witnessing rapid changes in the use of spaces and services within office buildings and is investing in high-tech buildings, green buildings, and new concepts, such as co-working and incubation platforms.

"The panel of the calls for projects were particularly sensitive to our innovative proposals for offices and housing," says Xavier. Connectivity is one big issue. "It is obvious that these days any building that is non-connected—in other words, a building where wi-fi and mobiles do not work—is not going to be let," says Marc. This, he says, is only the tip of the iceberg, with recent buildings featuring highly sophisticated building management systems. He points to a mismatch, however, between the way buildings are constructed and how they are used. "For instance, a consultant might rate the energy consumption of an office building at a very different level from what it actually consumes when occupied. You have to make sure the technology in place remains within the reach of users. If they do not understand the technology, people try to improvise, which generally proves pretty costly in energy terms."

Optimizing space usage is an even greater issue. "Company restaurants are no longer canteens but have become living spaces, used all day long, with creative decor and a convivial atmosphere that better suit the way companies are organizing themselves and working now," continues Marc. "A single space can, therefore, serve multiple uses. This is the biggest change we have seen."

Going beyond this approach of optimizing space usage, La Française is seeing new living spaces appear: a vegetable garden in the courtyard, a music room or a gym on the ground floor. "These new services come with an operating cost and we have found that only significant-sized buildings can absorb these new expenses," says Marc. "Streamlining and developing these services in a way that makes them accessible to smaller buildings is a key issue for managers like us."

Investment diversity

As opportunities abound and inflows rise, today's real investment market is going through an intense process of diversification. Investing across the euro zone does not bring any great change in returns as yields in Europe's major cities are broadly comparable, ranging from around 3.7 percent to 4.5 percent. However, it allows investment managers to take positions in markets at different stages of the economic and rent cycle, which vary considerably from country to country. "The UK, for instance, has entered a declining cycle, Germany is still in a growth phase and in France rents remain low, but growth prospects are clearly improving," says Marc. La Française has around 80 percent of its investments in France with the remaining 20 percent mostly in Germany and the Benelux countries, and to a lesser extent the UK and Ireland.

"Over the last three years, we have used our presence in the German market to diversify the real estate portfolios of several French collective real estate investment vehicles, which have been enthusiastically received by French retail investors," adds Marc. Investors should consider both geographic and sector diversity. An analysis of "metropolization" shows that Lille, Bordeaux, and Nantes are among the French cities outside Paris that have undergone urban renewal and are successfully expanding their economic activities. Conversely, Rouen and Orleans, although only an hour from Paris, have seen some of their economic activity sucked out by the Paris region.

An analysis of towns' development policies, meanwhile, points to Lyon as the model to follow, according to Marc. "Its urban community policy sets it apart in the market, notably as regards business real estate. In terms of dynamism, it is easily the equal of European cities like Milan or Dusseldorf."

In terms of sector diversity, investors have numerous options. "They should keep in mind that it is social and demographic trends that drive demand for buildings," explains Marc. La Française is finding interesting opportunities in student and young worker residences, tourist accommodation, non-medical senior homes for people who are still independent looking for leisure services, and nursing homes for dependent elderly people. "Cash flow is highly visible and very long-term," he says.

Investors from further afield—Asia being a notable example—are becoming increasingly alert to the opportunities in Europe. In 2016, China became the largest cross-border real estate investor, overtaking the United States. In the decade to 2017, its commercial property outflow soared from less than US $1 billion to more than US$20 billion annually.

Sustainability

Just as Grand Paris has at its heart the desire to create a sustainable and innovative metropolis, new sustainability criteria are also priorities for modern-day real estate investors. Demand for reporting on socially responsible investment (SRI) criteria is on the rise, driven by new regulations. Generally, the bigger the investor, the likelier they are to take a mature approach to SRI. "Today, for a northern European investor, it is unthinkable to invest in a non-SRI asset or fund," concludes Marc. "Small investors take a different approach. Not that they are in any way opposed to SRI, but they are waiting for clear proof of the economic case. It is our job to explain the virtuous circle created by renovating buildings to the new standards. Such renovation means they can be let faster and sometimes for higher rents. Tenant demand for buildings that are compliant with the new standards is also pushing the market forward much faster than legislation alone could have done."

New business model

Against the backdrop of an ever-evolving real estate landscape, traditional real estate asset managers are modifying their business models in order to meet new challenges and take advantage of new opportunities in financing. To remain competitive, they are getting involved in the earlier stages of the value chain by financing development projects, as well as in the latter stages by thinking innovatively about the needs of tenants.

In addition to adapting its business model, La Française Group is modifying its distribution chain to better suit new consumer behavior. In October 2016, it launched Moniwan, the first 100 percent digital real estate investment platform for private individuals. A year later, it has recorded net inflows of more than €15 million for its collective real estate investment vehicle product range.

To the point:

- Against the backdrop of an ever evolving real estate landscape, traditional real estate asset managers are modifying their business models in order to meet new challenges and take advantage of new opportunities in financing.
- La Française is getting involved in the earlier stages of the value chain by financing development projects, as well as in the latter stages by thinking innovatively about the needs of tenants.

BREATHING A NEW LIFE INTO INVESTMENT TAXATION

The French Finance Bill 2018

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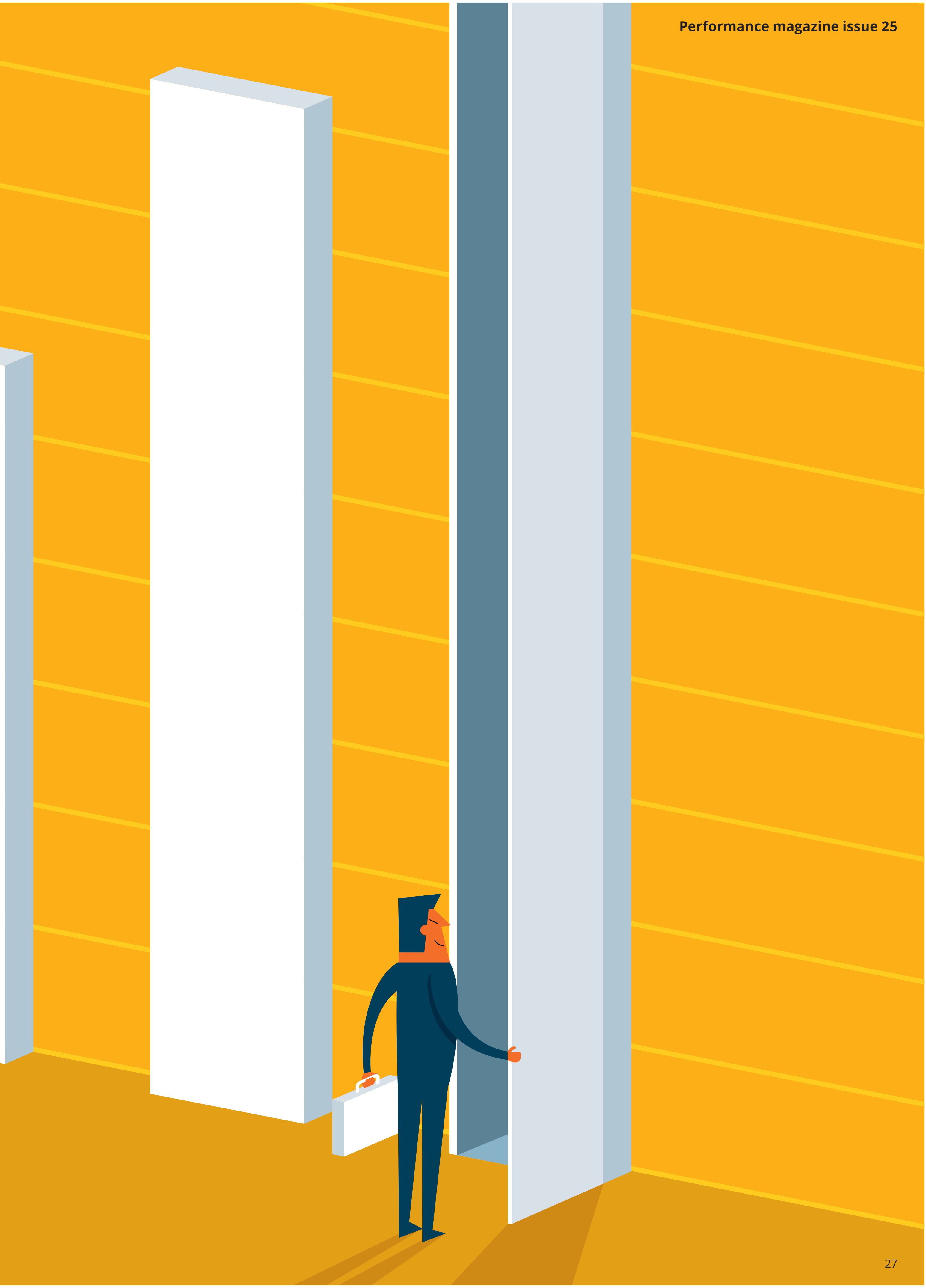
On 21 November 2017, the lower house of the French parliament (*Assemblée Nationale*) adopted the draft finance bill for 2018 (*Projet de Loi de Finances pour 2018 or "PLF 2018"*) at the first reading.



Subject to amendments, noteworthy provisions of the finance bill 2018 will include:

- The introduction of a 30 percent flat tax on investment income.
- A new real estate wealth tax.

Although the level of taxation would remain relatively substantial, asset managers and investors have high expectations for this proposed regime.

The new 30 percent flat tax on investment income

Under the proposed tax legislation, a 30 percent flat tax would replace most current tax regimes for investment income and capital gains on securities.

The 30 percent flat tax would apply, provided that there are no stipulations to the contrary, where the operative event ("*fait générateur*") occurs on or after 1 January 2018. The rate would be composite, including a 12.8 percent flat income tax and a 17.2 percent flat social income surtax.

The flat tax would most notably apply to the following:

- **Dividends** (qualified and non-qualified)
- **Interest**
- **Capital gains**
- **Gains on life insurance policies** (under certain conditions)

The flat tax would also apply to capital gains and distributions of funds. There should be no distinction between retail and closed funds, or European (UCITS/AIF) and non-European funds.

However, it is still beneficial to use a PEA ("*Plan d'épargne en Actions*"—investment savings account in shares) to invest in shares because, after a five-year holding period, there should still be an income tax exemption. This means that only the social security taxes would be due, i.e., taxation would be limited to 17.2 percent instead of 30 percent.

The reporting, withholding, and remittance of the flat tax on the 15th day of the month following the payment of the investment income would be the responsibility of the "paying agent" ("*établissement payeur*").

The paying agent is the entity paying the income to the beneficiary (e.g. company, bank, insurer, etc.). The paying agent is either:

- An entity located in France, to which French tax law is applicable and mandatory.
- An entity located in the European Economic Area (EEA), were:
  - The entity has voluntarily entered into an agreement with the French tax authorities for the purpose of withholding tax on its behalf.
  - The beneficiary has voluntarily mandated the entity to withhold tax and remit it to the French tax authorities.

This represents a significant improvement compared to current tax legislation in which, unless there are stipulations to the contrary, investment income is subject to[1]:

- Social income surtax[2] of 15.5 percent.
- Income tax of up to 45 percent.

1. Excluding the 3 percent or 4 percent tax on high income (Contribution sur les hauts revenus or CHR).
2. The current rate is 15.5 percent. Under the latest draft of the social security finance bill 2018, the 1.7-point increase in social income surtax would be applicable to some investment income arising in 2017.

However, in-depth analysis shows that a series of different rates and regimes apply:

- **Qualifying dividends**[3] are taxed at 42.5 percent, after deduction of a 40 percent[4] allowance on the sole income tax base for "qualified dividends".
- **Non-qualifying interest**[5] is taxed at up to 60.5 percent.
- **Qualifying capital gains**, after tapered relief of 50 percent, 65 percent (after eight years), or 85 percent is applied, depending on the holding period, are taxed at either 60.5 percent, 31.25 percent or 22.25 percent (additional fixed-sum allowances may apply).
- **Non-qualifying capital gains** are taxed at up to 60.5 percent.
- **Gains on life insurance policies** are taxed at the point of partial or full surrender, depending on the length of time that has elapsed since the life insurance policy was taken out, at 60.5 percent, 50.5 percent, 30.5 percent[6], or 23 percent after eight years.

The taxation of capital gains and distributions from funds depends on whether or not they fall under a specific regime. Where this is not the case, funds are subject to a tax rate of up to 60.5 percent.

The specific case of gains on life insurance policies

The application of the new flat tax to life insurance products is one of the more controversial elements of the tax reform. Under the provisions of the draft finance bill 2018, the following would apply:

- A decrease in the taxation of gains on life insurance policies taken out less than eight years before surrender.
- An increase in the taxation of the fraction in excess of €150,000 of the gains on life insurance policies taken out more than eight years before surrender (30 percent vs. 24.7 percent).

The taxation of capital gains and distributions from funds depends on whether or not they fall under a specific regime.

3. Dividends are also currently subject to a non-final 21 percent withholding tax, which can then be offset against income tax.
4. The 40 percent allowance on "qualified dividends" is subject to the following conditions: (1) the company paying dividends is established in the European Union or in a state which has entered into a tax treaty with France; (2) the company is liable to pay corporate tax in France, or if incorporated in a state with which France has a double tax treaty with a clause on administrative assistance, a tax equivalent to corporate tax; (3) the distributed income must be eligible (dividends and similar); (4) the distribution has been decided in accordance with applicable laws (e.g., shareholders meeting resolution).
5. Interest is also currently subject to a non-final 24 percent withholding tax, which can then be offset against income tax.
6. Including a 15.5 percent social income surtax, in addition to the 45 percent, 35 percent, 15 percent and 7.5 percent income tax.

Transitional provisions have been issued regarding gains on life insurance policies in order to maintain the tax rates that were applicable at the time the policyholder paid the premiums (i.e., gains on premiums paid before 27 September 2017).

It should be noted that the implementation of the aforementioned changes to the taxation of gains on life insurance policies is likely to prove challenging for insurers. Indeed, their IT systems will have to be able to determine the applicable tax regime for each fraction of the gain depending on: the date on which the life insurance policy was taken out, the date on which the premiums were paid, whether additional, even older, tax regimes apply, etc.

Finally, the inheritance tax advantages of life insurance would continue to apply, including tax allowances of between €30,500 and €152,000.

The safeguard clause mechanism
As the introduction of the flat tax is also intended to simplify the existing structure, none of the current proportional allowances would apply.

However, the taxpayer may opt to retain the current tax regime through a "safeguard clause" mechanism ("clause de sauvegarde") (e.g., if the taxpayer's effective tax rate is below 30 percent). In that case, the 40 percent dividend allowance would apply; and, for shares acquired before 1 January 2018, the proportional allowances on capital gains (up to 65 percent only) would also apply.

It should be noted that this option is global for the taxpayer, meaning that the option would apply to all types of income otherwise subject to the 30 percent flat tax, rather than just one particular income stream or type of income.

The paying agent is responsible for correct withholding and could incur heavy penalties when paying investment income if the withholding is not correctly applied.

The new real estate wealth tax

In an effort to incentivize investment, the French government has decided to exempt non-real estate assets (such as equities, securities, bonds, life insurance, etc.) from wealth tax.

Under the proposed tax legislation, the wealth tax would be repealed and replaced with a real estate wealth tax ("*Impôt sur la Fortune Immobilière*" or IFI), meaning that tax households would then

As the introduction of the flat tax is also intended to simplify the existing structure, none of the current proportional allowances would apply.

only be subject to tax on the net value of their sole private real estate wealth.

Real estate wealth tax would need to be paid on the following assets:

- For individuals who have been tax residents of France for five years or more: real estate located in France or outside of France.
- For non-tax residents of France, and for individuals who have been tax residents of France for under five years: real estate located in France only.

Real estate assets should be reported at fair market value (FMV) on 1 January of the year in question.

Under current tax legislation, tax households (individual, spouse, minor children and other dependents) are taxed on the overall net value of all their private assets, including the value of their life insurance policies, but excluding business assets. Tax households are only taxable if the overall net value of their private assets exceeds €1.3 million on 1 January of the year in question.

The inclusion of real estate assets held through entities

Real estate held indirectly through one or more legal entities (partnerships, companies, trusts, etc.) is included in the real estate wealth tax base[7], except:

- Rights in UCITS, investment funds, securitization funds (subject to conditions), (OPCI—real estate collective investment schemes would be included in the tax base).
- Shares, rights or similar in operational entities (subject to conditions).
- Real estate assets held by an operational entity and used in the course of its business activities (e.g., a factory held by a manufacturing company).

The cap on deductible debt

The real estate wealth tax base is the net overall value of the private real estate assets of the tax household, which means that debts relating to chargeable real estate assets, such as mortgages, may be offset against the gross value of chargeable real estate assets.

However, as an anti-abuse measure, subject to conditions, the ratio of deductible to chargeable assets would be capped.

Rates would remain unchanged.

The deductions for donations and investment in SMEs

Additionally, 75 percent of amounts donated to eligible entities (charities, research foundations, etc.) would continue to be deductible from the amount of real estate wealth tax, up to €50,000.

However, direct investments in SMEs, which are currently eligible for a 50 percent deduction under the wealth tax, would no longer be deductible under the real estate wealth tax.

To the point:

- The new investment income tax regime, along with the introduction of a flat tax and wealth tax reforms are a welcome change and a step in the right direction for most financial industry players and investors.
- Asset managers and insurers for all financial intermediaries will now have to adapt in order to offer tax attractive products and ensure beneficial treatment for their investors, particularly as regards life insurance products.

[7]Technically, the taxpayer's shares, rights or similar, in the legal entity would be included in the real estate wealth tax base, in proportion to the value of real estate held by the legal entity relative to all of its assets.

Insurance Distribution Directive

2018: a challenging year for the European insurance sector

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After months of rumors of a possible delay of the IDD, the European Commission has finally, just before the Christmas break on December 20, 2017, adopted a proposal[1] to delay the application date of the Insurance Distribution Directive (IDD) until 1 October 2018. The transposition date for Member States remains 23 February 2018. The proposal will need to be discussed in the Council of the European Union and the European Parliament before it can be finalised. The Commission states in its legislative proposal that, given the short timeframe, the proposal should enter into force without delay. The European Parliament invited the Commission to adopt a legislative proposal setting 1 October 2018 as the application date of the IDD. It substantiated the request by the need to give insurance undertakings and insurance distributors more time to prepare for the implementation of the IDD and the necessary technical and organisational changes to comply with the Delegated Regulations.

In the pages that follow, we provide the results of an EMEA IDD analysis performed just before the summer of 2017 and updated in December 2017. We collected information on the IDD transposition and expected challenges and impacts from a number of EU countries, as well as information on similar legislation in a selection of third-party countries. The information was collected informally through our Deloitte network based on local market experience and expertise. Our main conclusion is that the IDD is expected to have a significant impact on the business strategy, and the (operational) organization of insurance companies and intermediaries. Firms that have just started will need a structured implementation approach in order to reach the deadline.

What is the Insurance Distribution Directive (IDD)?

The Insurance Distribution Directive (IDD)[2] is a full recast of the existing Insurance Mediation Directive (IMD)[3]. Member States have until 23 February 2018 to transpose it into national law, at which time the existing IMD will be repealed. Insurance distributors will be required to comply with the new rules by October 1, 2018. In line with one of the main objectives of MiFID II[4] and PRIIPs[5], the IDD is designed to increase consumer protection. One of the main goals is that consumers should benefit from the same level of protection regardless of the differences between distribution channels.

The scope of the IDD is broader than the IMD and covers the entire distribution chain, including direct sales by (re)insurers and certain activities of aggregators and price comparison websites where the client can directly buy a product. Distributors for whom insurance is only an ancillary service such as car rental/leasing firms and airlines are also in scope (with certain limited exemptions). It is important to note that this Directive is aimed at minimum harmonization and therefore does not preclude Member States from maintaining or introducing more stringent provisions provided that these are consistent with the Directive.

1. Proposal for a directive of the European Parliament and of the council amending Directive (EU) 2016/97 as regards the date of application of Member States' transposition measures.
2. Directive (EU) 2016/97 of the European Parliament and of the Council of the 20 January 2016 on insurance distribution.
3. Directive 2002/92/EC of the European Parliament and of the Council of 9 December 2002 on insurance mediation.
4. Directive 2014/65/EU of the European Parliament and of the Council of the 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.
5. Regulation (EU) No 1286/2014 of the European Parliament and of the council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs).

Key provisions included in the IDD

In order to enhance consumer protection and to ensure a level playing field, the IDD introduces (or reinforces) a number of the conduct of business rules that already apply to the banking, investment, and insurance sector. The main provisions include:

Needs analysis
Data collection to allow specification of client's demands & needs where providing advice, a personalized recommendation is to be provided explaining the link between the product and the client's demands and needs

Product Oversight & Governance
Extensive product oversight and governance requirements, that have an impact on the end-to-end product value chain, including the distribution channel

Suitability and appropriateness assessment
In-depth know your customer (KYC) process to be put in place - obtain information on the knowledge & experience, financial situation and investment objectives of the client - in case of advice, a suitability statement is to be provided explaining the link between the product and the client's preferences, objectives etc.

Information to clients
PID (Insurance Product Information Document), a standardized document summarizing the main features of a non-life insurance contract. Alongside PRIIPs, the IDD imposes increased disclosure of costs and charges for insurance-based investment products

Conflicts of interest
Insurance distributors shall act honestly, fairly, and professionally in accordance with the best interests of their customers, with internal arrangements to be put in place, including disclosure if necessary

Professional requirements
Fit & proper & training requirements (15h per year) for relevant persons within the management structure and any staff directly involved in insurance distribution

Inducements
Insurance distributors should not be remunerated in a way that has a detrimental impact on the quality of the relevant service to the customer. Customers are to be provided information on the nature of the remuneration received by intermediaries or employees of insurance companies in relation to the insurance contract

The IDD Regulatory framework

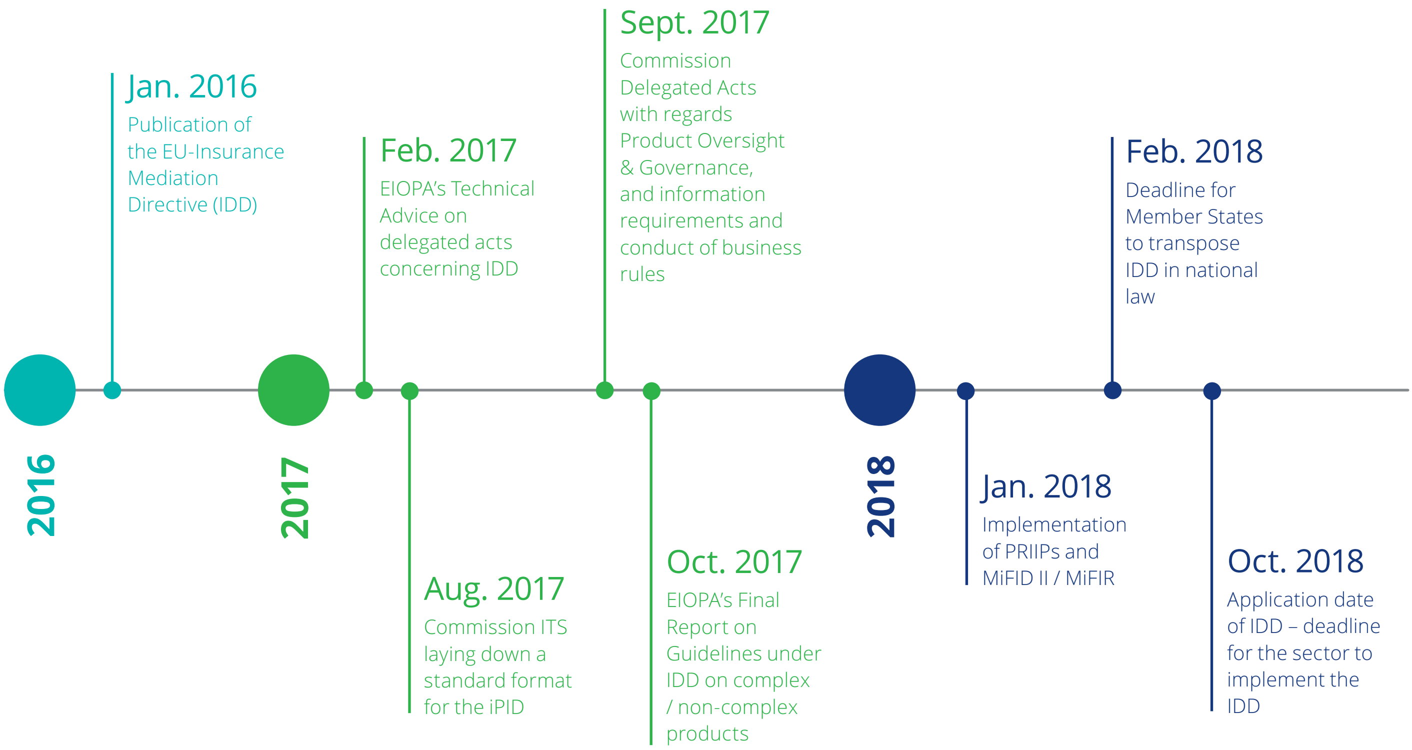
The Insurance Distribution Directive was published in January 2016. In February 2017, the European Insurance and Occupational Pensions Authority (EIOPA) submitted its Final Technical Advice to the European Commission on possible delegated acts to further specify certain provisions related to product governance and oversight, conflicts of interest and inducements, and the suitability and appropriateness assessment. After consulting the sector at the end of July 2017, the European Commission published 2 final delegated regulations on 21 September 2017, one on product oversight and governance, and the other one on information requirements and conduct of business rules for IBIPs. The current proposal of the Commission is now also to change the application date of these Delegated Acts to 1 October 2018[6]. In August 2017, the Commission published an implementing regulation regarding the Insurance Product Information Document (PID), and in October 2017 EIOPA published its Final Report on Guidelines on IBIPs that incorporate a structure which makes it difficult for the customer to understand the risks involved.

Consumer interests at the heart of the business

As EIOPA states in its 2016 Annual Report, the IDD is a significant milestone in strengthening consumer protection in Europe. EIOPA considers it of utmost importance that the interests of consumers are taken into account throughout the end-to-end insurance life cycle. Nevertheless, EIOPA recognizes that in order to realize this objective, a cultural change will be required from the industry to place consumer interests at the heart of their businesses. However, firms that succeed in realizing this cultural shift stand to benefit, as they will be able to leverage their strengthened risk and conduct culture to achieve better client outcomes and, subsequently, a competitive advantage.

To strengthen the weight of consumer interests, the IDD includes a strong set of sanctions and other measures in its Chapter VII. These go far beyond the existing rules included in the IMD and could have severe consequences, such as a temporary ban on exercising management functions within insurance undertakings, fines, public statements, and lawsuits, not to mention the negative impacts on reputation, etc.

The European regulatory landscape



6. Commission delegated regulation (EU) amending Delegated Regulation (EU) 2017/2358 and Delegated Regulation (EU) 2017/2359 as regards their dates of application.

Transposition of the IDD into national law

Comparative view of the transposition in a selection of Member States

The information currently available to us seems to demonstrate that competent authorities are not taking the same approach in transposing the IDD. Preparatory work is ongoing in all countries with draft texts and consultation papers being circulated to the sector. However, we see that the expected transposition date varies considerably among countries. Germany and Italy are clearly the frontrunners, whereas in the Czech Republic, for instance, the upcoming elections are expected to have an impact on the IDD transposition process. The country may, therefore, face a delay in meeting the deadline of February 2018. Most other countries expect to be ready slightly before or just around the deadline.

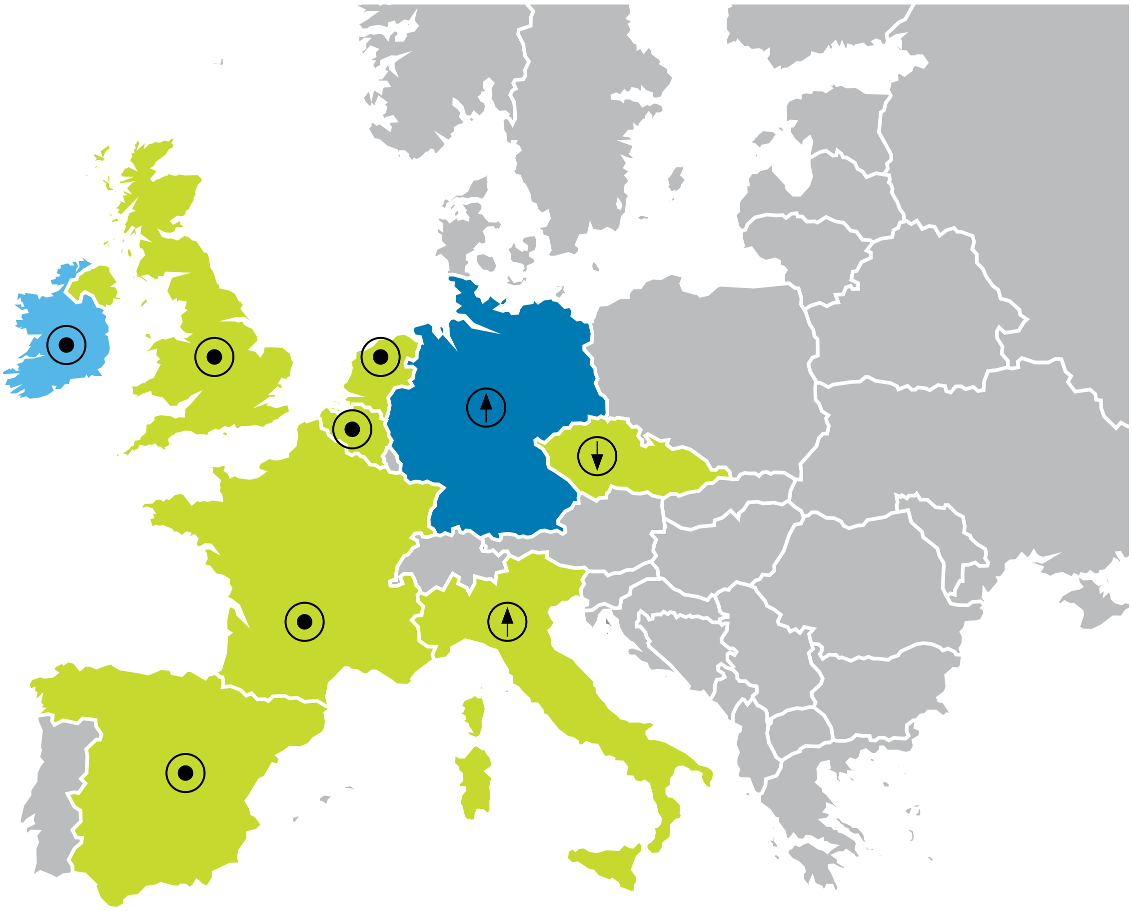
In the UK, the regulator made it clear that despite the recent referendum on exiting the European Union, firms must continue to abide by their obligations, including those derived from EU law, and continue with implementation plans for legislation that is still to come into effect.

These differences in the transposition approach by national authorities will also be driven by the existing regulatory regime in each of the jurisdictions. Table A demonstrates the substantial differences in existing insurance mediation and conduct rules among the different European countries and beyond. The diverse set of rules within the EU is the result of the first generation of EU insurance mediation rules (IMD) introduced in 2002. Although the objective of the (minimum harmonization) IMD was to introduce a similar set of consumer protection rules across Europe, the result was a patchwork of national insurance mediation regulations. Some countries such as Belgium, Italy, and the UK also have domestic consumer protection regulation, further fragmenting the regulatory landscape.

With the IDD, the European Commission aims to strengthen the internal European insurance market, ensuring professionalism of insurance intermediaries and increased consumer protection. The IDD still leaves a lot of flexibility and permits national Member States to impose stricter rules and requirements ("gold plating") in certain areas. As table B demonstrates, national regulators are taking different positions in a number of areas, including the provision of an execution-only sales regime, whether to limit or prohibit inducements in general or in relation to advice, and whether to make the provision of advice mandatory (formally or informally).

We have collected information on the IDD transposition and expected challenges and impacts from a number of EU countries, as well as information on similar legislation in a selection of third-party countries. The information was collected informally through our Deloitte network based on our local market experience and expertise. Most positions are not yet official or based on consultation papers, and hence, are or may still be subject to further refinement or change. The following countries have been consulted: Belgium, the Netherlands, France, Germany, Ireland, Italy, Spain, the Czech Republic, and the United Kingdom. To have a view outside the EU, we also consulted Switzerland and South Africa.

With the IDD, the European Commission aims to strengthen the internal European insurance market, ensuring professionalism of insurance intermediaries and increased consumer protection.



What is the status of the national IDD transposition in your country?

Consultation Paper | Draft text available | Final | NA

At what date do you expect the IDD transposition to be finalised?

On time | Ahead | Delayed

By what date do you expect the IDD transposition to be finalized?
The information available to us leads us to conclude that the regulatory regimes in Belgium, the Netherlands, Ireland, and the UK are probably most aligned with the IDD requirements (albeit that there may be differences in the detailed requirements), whereas the regimes in France and Spain seem to require the most adjustments to be brought into compliance. Nevertheless, overall, it appears that the provisions in the area of product governance and comparison websites—and to a lesser extent inducements—require the most updating vis-à-vis existing rules and regulations.

Table B includes the areas where national regulators are permitted to impose stricter rules. The overall conclusion is that in many areas, national regulators have not yet taken a position, or the position taken varies throughout the different jurisdictions; this again demonstrates the divergence in the European regulatory insurance landscape (cf. IMD). We have added a view of the regulatory insurance framework in Switzerland and South Africa for comparison purposes.

Facts & figures

Table A - Existing regulations

Do similar requirements exist in your jurisdiction/country for the topics listed?

	UK	BE	FR	SP	NL	IRL	IT	D	CZ
Needs analysis	Less strict	More strict	Similar	Less strict	Similar	Similar	Less strict	Similar	Less strict
Suitability and appropriateness regime (IBIPs)	Less strict	Similar	More strict	None	None	Similar	Less strict	Less strict	Less strict
Inducements	More strict	More strict	None	Less strict	More strict	Similar	None	Less strict	Less strict
Conflicts of interest	Less strict	More strict	None	Less strict	Similar	Similar	Similar	Similar	Similar
Professionalism requirements	Less strict	Less strict	Less strict	More strict	Similar	Similar	Similar	Less strict	Less strict
Information to clients	Less strict	More strict	Less strict	Less strict	Similar	Similar	Similar	Similar	Similar
Product governance	Similar	Less strict	None	None	Less strict	Less strict	None	Similar	None
Comparison websites	Similar	None	Less strict	None	Less strict	Similar	None	Less strict	None

Table B

Gold plating intentions (where known) of national legislators and comparison with current framework in Switzerland and South Africa

Table B covers the areas where the IDD explicitly states that national regulators may impose stricter rules. However, it should be noted that the regulation may be gold plated in other ways, for example, through the extension of the requirements to a wider range of entities or sectors than those stated in the regulation.

Expected intentions of the national regulators (gold plating)	United Kingdom	Belgium*	Netherlands	France	Spain	Ireland	Italy	Germany	Czech Republic	Switzerland	South Africa
Intermediary registration	-	-	Y	-	Y	-	Y	Y	Y	-	Y
Professional requirements	Y	N	N	-	Y	-	Y	-	Y	Y	Y
Information to clients	Y	N	N	N	N	-	N	Y	Y	Y	Y
Provision of advice	N	N	Y	Y	N	-	-	Y	Y	Y	Y
Inducements	Y	N	Y	-	N	-	-	Y	Y	-	Y
Execution only	Y	N	N	N	N	-	-	N	N	-	Y

* Gold plating intentions have been interpreted taking into account the existing regulatory regime in Belgium (which is already stricter than those stated in the IDD in many areas). The Belgian regulator has announced its intention to not gold plate the IDD requirements beyond what already exists.

"Our research has demonstrated that competent authorities are not taking the same approach in transposing the IDD"

Diverse positions	Diverse positions
Inducements	**Intermediary registration**
Member States may limit or prohibit the acceptance of inducements in relation to distribution or the provision of advice: Spain and Belgium are not in favor, whereas Germany, the UK, the Netherlands and the Czech Republic are in favor.	Most countries tend to agree with a broader registration mechanism under the supervision of the competent authority as well as the principle that where an intermediary acts under the responsibility of an insurance company/other intermediary, the latter shall be responsible for ensuring that the intermediary meets the conditions for registration.
Execution only	**Professional requirements**
Member States may permit firms to carry out insurance distribution activities without performing the appropriateness test (known as the execution-only regime) under certain conditions: the UK and Spain seem to be in favour, versus Belgium, The Netherlands, France, Germany and the Czech Republic which are not.	A number of countries intend to make it a requirement that a certificate must be obtained to prove the successful completion of training.

In Switzerland and South Africa, most of the IDD requirements are, to a certain extent, provided for in the current regimes, with the exception of product governance, comparison websites and the inducement regime (only applicable for Switzerland). In Switzerland, there is a distinct overlap between the European Commission's intentions with the IDD and the intended focus of FINMA (the Swiss Financial Market Supervisory Authority) on increased client protection, clearer cross-border procedures for insurance markets, and stringent product oversight and governance rules for product manufacturers and distributors.

With the IDD, the European Commission aims to strengthen the internal European insurance market, ensuring professionalism of insurance intermediaries and increased consumer protection.

Impacts and challenges of the IDD

From the information that we collected through the Deloitte network, we anticipate that the IDD will have an impact on a wide range of areas within firms across Europe. These areas include Business Strategy, Processes & IT Systems, and Organization & People.

Business Strategy: the IDD reinforces a more client-centric approach by requiring that firms have clear charging structures that consider the best interests of their clients. This will lead firms in certain jurisdictions to rethink their charging and distribution strategies and increase market competition, resulting in pricing and margin pressures. New product governance requirements will mean firms must align their strategy with their target market through an ongoing product development and review process that centers on clients' demands and needs and proactively manages client risks and conflicts of interest.

Processes & IT systems: in line with MiFID II, the IDD introduces a number of changes to the sales process, for example, assessing appropriateness and suitability, enhanced client information and disclosure, and more complex record-keeping requirements. Firms offering automated digital sales and advice and aggregators/price comparison websites will need to ensure that client journeys, including underlying algorithms, adhere to these requirements.

Organization & People: new professionalism requirements will mean firms must review their training, development, and performance management processes. The aim will be to increase the ongoing knowledge and capability of staff, in particular of those who are client-facing. Any subsequent changes to a firm's products and processes will need to be incorporated into this training.

Table C below illustrates the breadth of changes facing firms. As summarized above, changes to charging structures and inducement frameworks will have a fundamental impact on the European insurance and distribution landscape, while the requirements of the needs analysis, the suitability and appropriateness regime, and client information are expected to have the greatest impact on firms' target operating models.

Table C

	Value Chain Impacts		
	Business strategy	Processes & IT	Organisation & people
Needs analysis	L	H	M
Suitability and appropriateness	M	M	M
Inducements	VH	L	L
Conflicts of interest	M	M	M
Professionalism requirements	L	L	H
Information to clients	M	H	L
Product governance	M	M	M
Comparaison websites	M	M	L

VH= Very high **H**= High **M**= Medium **L**= Low

Impacts in a selection of European countries

Impacts in Belgium

The Belgian insurance sector has been subject to conduct of business rules similar to MiFID since 1 May 2015 (commonly known as AssurMiFID[7]). The conflicts of interest and inducement requirements that are stricter than those under the IDD have had a considerable impact on the remuneration flows and, hence, the business model of insurance companies and (non-tied) intermediaries. Other key challenges have been the implementation of the suitability and appropriateness process, as well as the record-keeping requirements. Both have mostly had a significant operational impact (depending on the existing operating model). Together with other drivers like margin pressure, digitalization, and other challenges, insurance companies have been and still are fundamentally rethinking their way of doing business. The Belgian insurance distribution landscape has also changed as a consequence of AssurMiFID.
For instance, the number of intermediaries has substantially decreased in the Belgian market.

Given the existing AssurMiFID regulatory framework5, the impact of the IDD on the Belgian market will most likely be somewhat limited; nevertheless, the IDD introduces additional requirements like the enhanced product oversight and governance requirements, the "Product Information Document" for non-life insurance contracts, the suitability statement for insurance-based investment products, and additional professional requirements, etc. Hence, Belgian firms will need to undertake a gap analysis to identify the required changes to their internal processes and procedures.

7. The AssurMiFID regulatory framework:
- The Twin Peaks II law (TP II), dated 30 July 2013
- Part IV of the Insurance Law of 2014
- The three implementing Royal Decrees, dated 21 February 2014
- The Circular Letter of the Financial Services and Markets Authority (FSMA), dated 16 April 2014, and revised in September 2015, to include additional guidelines with regard to record-keeping requirements

Impacts in the UK
The Financial Conduct Authority (FCA) has traditionally been quite proactive in adopting conduct regulation and, consequently, the IDD is not expected to have as great an impact in the UK as in some other EU jurisdictions. Nevertheless, the IDD introduces developments in a number of areas and UK firms will need to undertake a potentially extensive gap analysis (depending on the complexity of their business models) to identify necessary changes to their governance, systems and controls, sales practices, client disclosures, and distribution arrangements. In particular, the implementation of the IDD will affect distribution channels by introducing stricter conduct of business requirements for insurance distribution, imposing new requirements on authorized firms distributing through firms that are outside the UK's regulatory perimeter, e.g., out-of-scope ancillary insurance intermediaries, and introducing new principles (for example, the "client's best interest" rule) that apply to all intermediaries in the distribution chain—even where they do not have direct contact with the end-client.

Impacts in Germany
As the national IDD law was passed through parliament and Bundesrat in July 2017, German insurers have stepped up their efforts to become IDD-compliant. As the consumer protection focus of EIOPA is similar to a code of conduct for primary insurers (GDV-Kodex), most insurers are familiar with the IDD requirements and will close identified gaps with legal requirements applying insights from previous years. Nevertheless, we clearly see differences concerning IDD readiness, i.e. large insurers started their IDD projects in the fall of 2016, whereas mid-size/small insurers only started in the first quarter of 2017 for the most part. Demand for IDD support ranges from legal interpretation and content reviews of existing IDD concepts up to considerable deployment support. The key issue is the interdependency with MiFID II and PRIIPS that requires organizational alignment with regard to Insurance-Based Investment Products (IBIPs); this entails a longer-than-expected IT implementation lead-time, and increases the regulatory uncertainty for multinational insurers in countries where an IDD transposition draft is not yet available. In summary, German insurers may well be the IDD frontrunners within the EU, but all market segments still have a significant number of measures to complete by the end of February 2018.

Impacts in Spain
In the Spanish market, one of the main impacts of the IDD transposition is related to the scope of policies to which the new law will be applicable, specifically with regard to conduct rules. Based on the latest draft available, the Spanish regulator has decided to extend the scope of the law to include not just new insurance policies (i.e., those written after the new law comes into force), but also existing policies if they are amended in certain ways. Consequently, several conduct of business requirements (such as post-contractual information and product oversight and governance) will not only impact new business, but also the millions of existing policies that are amended each year. If this extension of scope is considered alongside requirements that all client information should be readily recoverable for the Supervisor, the impacts will be significant. Another very important impact of the future regulation are the Product Oversight and Governance (POG) requirements, as the Spanish market is not used to this type of conduct of business regulation in the insurance sector. Manufacturers and distributors will have to put in place governance arrangements that comply with their new duties and responsibilities. This will require new information, processes, and activity that will impact firms' IT systems, processes, operational efficiency, renewals, and future business.

> "The greatest impact of the IDD will be on the process and IT side of insurance distributors, as well as on their business strategy."

Impacts in France

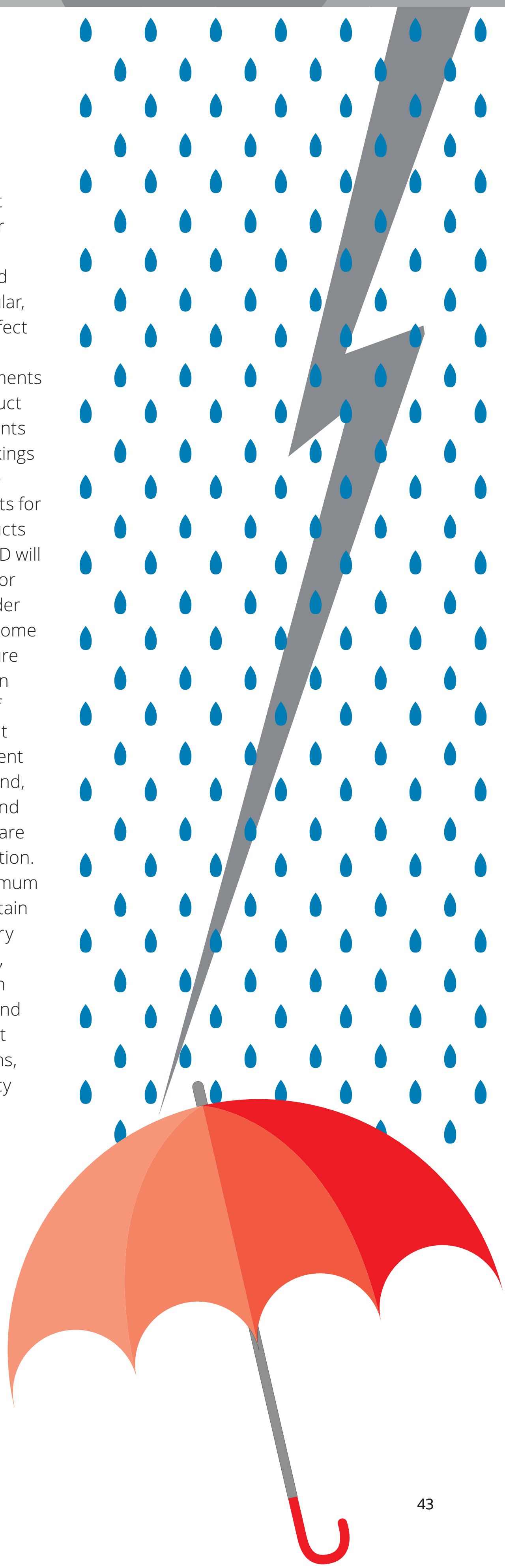
In the French market, the IDD is a major shift for insurance companies and intermediaries. Some of the provisions already exist in French law (similar suitability and appropriateness requirements for IBIPs have applied since 2009). However, several conduct rules are completely new in the insurance sector and are expected to have a major impact on insurance undertakings' strategy, sales processes, and ultimately on their business models. The rules on inducements and conflicts of interest will require that insurers map and undertake an in-depth diagnosis of the commissions paid to their distributors. If deemed necessary, they will have to adapt their inducement schemes (boosters, sales target), for example by including qualitative criteria and taking better account of clients' interests.

It is also important to note that changes in remuneration are a long-term issue, including potentially difficult negotiations with distributors' representatives.

Complying with Product Oversight and Governance requirements will be another challenge for the French insurance market, especially regarding the oversight process. In order to ensure that the products they manufacture are distributed to the defined target market on a regular basis, insurers will have to strengthen controls over their distribution channels—including independent brokers—and develop management information. Finally, some difficulties regarding the articulations of the IDD provisions with existing French law still remain, given that they will be implemented by means of a regulation directly applicable in local law (e.g., with regards to suitability and appropriateness). This should be clarified by the final version of the transposition texts and the positions of the ACPR (French banking and insurance supervision authority).

Impacts in Ireland

There are a number of provisions of the IDD that will require Irish firms to assess their current business models and compliance environment to identify necessary changes to their governance, systems and controls, sales practices, client disclosures, and distribution arrangements. In particular, the implementation of the IDD will affect distribution channels by introducing stricter conduct of business requirements for insurance distribution. New product oversight and governance requirements will apply to both insurance undertakings and intermediaries that manufacture insurance products, and requirements for insurance distributors offering products that they do not manufacture. The PID will be a mandatory pre-sale document for any insurance product not falling under the PRIIPs regulation. While there is some overlap with the information disclosure requirements in Consumer Protection Code 2012, the prescriptive nature of the PID in terms of content and layout makes it a very challenging requirement for non-life insurers. On the other hand, many of the training, development, and probity requirements under the IDD are already catered for in national regulation. For example, the Central Bank's Minimum Competency Code 2011 imposes certain requirements on individuals who carry out functions on a professional basis, such as the provision of advice, etc. In addition, the Central Bank's Fitness and Probity Regime already requires most senior managers to have qualifications, experience, competence, and capacity to perform their roles.



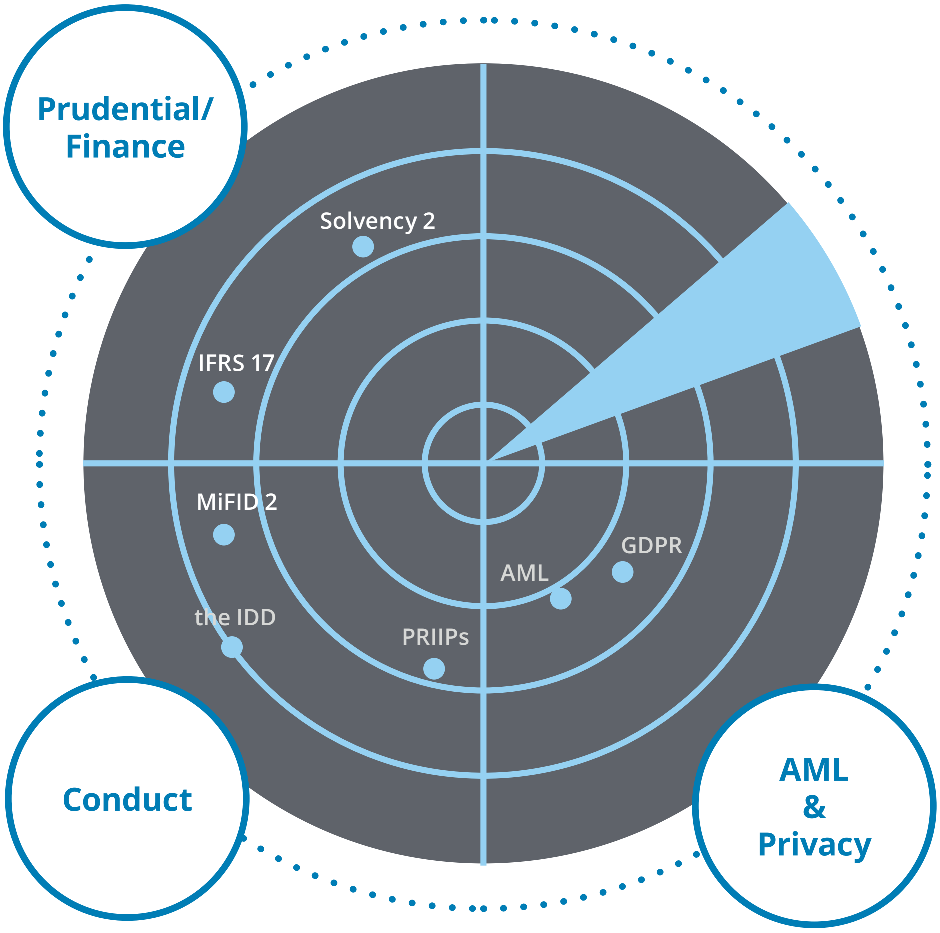
What firms should be doing

We understand that the IDD has prompted an intense sector debate where sector associations of both insurers and independent intermediaries have been preparing position papers and providing lengthy feedback statements to EIOPA's consultation papers.

The IDD will have an impact on the entire value and distribution chain, including (re) insurers, tied and untied intermediaries, aggregators, and price comparison websites, but also ancillary distributors such as car rental/leasing firms and airlines (with certain limited exemptions). Nevertheless, we understand that firms are in different increasingly undertaking analysis to identify gaps against the incoming regulations and determine the impact on their businesses. At this stage, firms need sufficient insight into the EU and country-specific regulatory framework to be able to implement the IDD and mitigate the impacts so as to avoid, as much as possible, any detriment to their business models, profit and loss, etc. stages of putting in place implementation projects. In France, Spain, and particularly Germany, implementation activities are clearly underway, driven by either the major impact of the IDD (as in France), or the fact that their local regulators are clearly in pole position (Spain and Germany). Firms in these countries are increasingly undertaking analysis to identify gaps against the incoming regulations and determine the impact on their businesses. At this stage, firms need sufficient insight into the EU and country-specific regulatory framework to be able to implement the IDD and mitigate the impacts so as to avoid, as much as possible, any detriment to their business models, profit and loss, etc.

The insurance sector
What is on Firms' regulatory agenda?

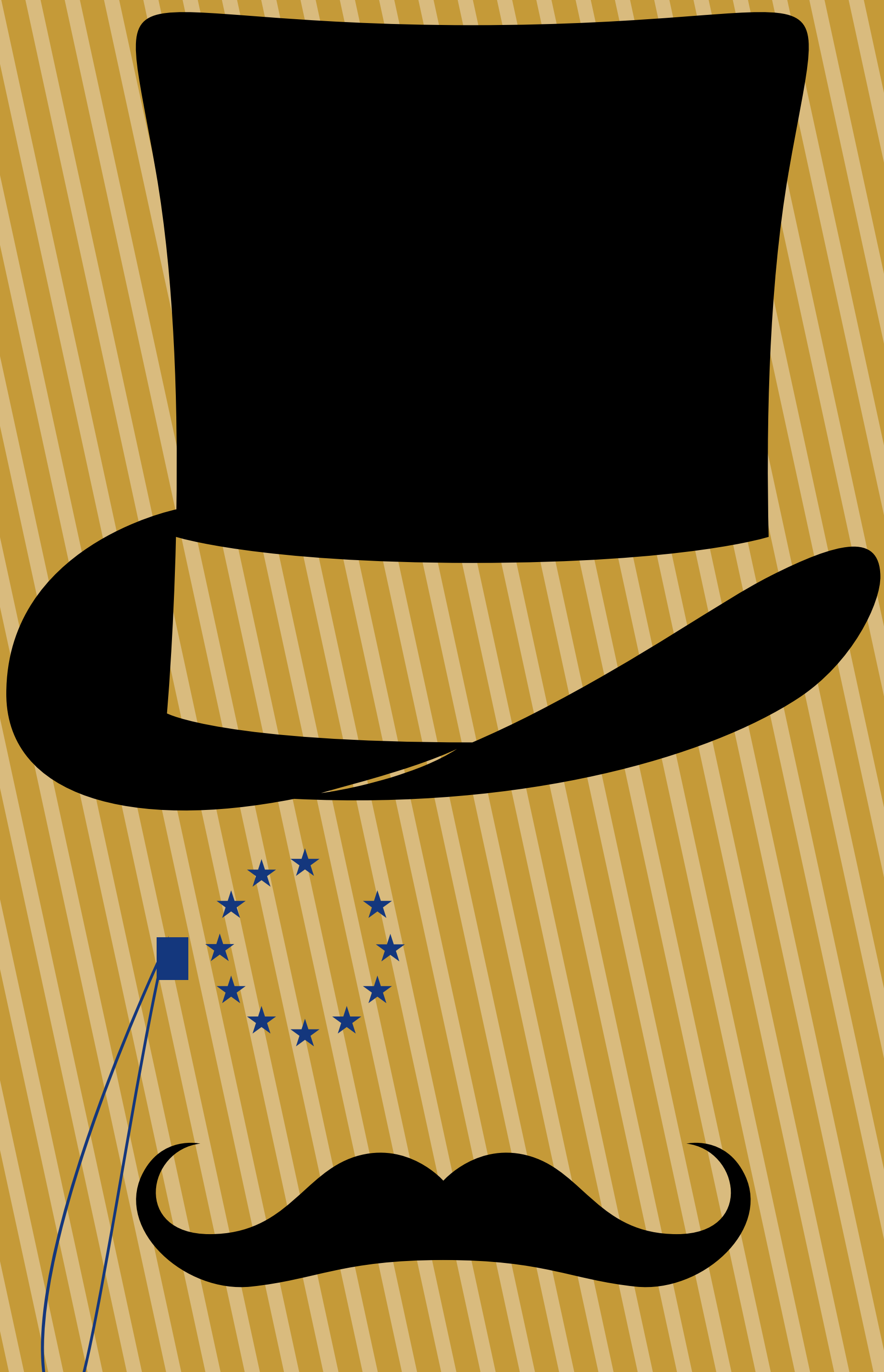
The closer a dot is to the center of the radar, the higher the topic is on the regulatory agenda (based on our understanding).



Action plans

In October 2018, , firms will need to be IDD-compliant. Therefore, they will need to be able to demonstrate the measures they have taken and the actions they will put in place to implement the IDD requirements and to prevent threats arising from non-compliance. Below, we have provided a typical implementation approach firms apply when analyzing and preparing their organization for such large-scale change. Against the background of the defined phase objectives, an effective implementation approach addresses a set of key questions in order to design proposals for implementation. Where are you in this phased approach?

Steps	Mobilization	Gap analysis	Options identification	Impact assessment	Implementation planning
Objectives	Engage stakeholders, confirm project objectives, scope and detailed project plan, and tools.	Identify the current regulatory implementation status and derive the business requirements tailored to the institution.	Identify and define business design options.		Prepare planning decisions to be taken and schedule their implementation.
Key activities	• Project objectives. • Scope and timeline. • Most effective project governance structure. • Interaction with all stakeholders and other jurisdictions. • Methods and tools used.	• Main differences from current regulatory framework (per jurisdiction/gold plating). • What is/are competition/market players doing. • Business change areas. • Culture change/change management.	• Design options per business activity. • Interlinkage between options. • "Net" options from an aggregated and end-to-end perspective.	• Business impacts (Strategy/process & IT/Organization). • Financial impact of implementation areas. • Risks and rewards. • Impact on customers.	• Key decision proposals. • Proposal options. • Quick wins. • Decision work streams. • Level of readiness.
Key outputs	Up and running core project team.	Repository of high level business requirements.	Option portfolio.	Business impact against risk/reward.	Way forward.



BREXIT BILL

Could transitioning to a new structure create tax costs?

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With a little over a year to go until the UK's departure from the EU, many UK-based asset managers are moving forward with Brexit restructuring plans. Significant business change always has tax consequences, and this is particularly so here. In this article we explore some of the emerging tax issues which businesses planning for Brexit need to consider.

How does Brexit affect UK asset managers?
EU directives currently allow UK regulated companies to "passport" across the EU. UK-based asset managers ("UKcos") may currently rely on these passporting rights to manage assets for EU clients, and distribute their products in the EU.

The impact of Brexit and any transitional period on these arrangements is not completely clear. However, many UK asset managers are making structural changes to ensure they can continue to operate in the EU post-Brexit. In most cases, these changes include conducting more activity through companies established and regulated in the EU, which we refer to here as "EUco".

Substance
For many managers planning for Brexit, the biggest issue relates to substance. What activity will need to be undertaken by EUco, how much can be undertaken in the UK, for example under delegation arrangements? Will some activities need to be undertaken in both the UK and the EU-27?

The need for local substance has important practical implications for the business. More substance in EUco implies more local roles and infrastructure. In many cases this will in turn mean greater disruption to existing business structures and processes.

Substance is also important for tax. The greater the substance in EUco, the more profit it would be expected to earn and pay tax on in its local jurisdiction. If meeting substance requirements involves the relocation of staff, this will have tax implications for the individuals involved as well as their employers.

Substance requirements may also have an impact on the quantum of any "exit" charges (more on this later) and intra-group payments. Intra-group payments are significant because, depending on what they are, they could attract VAT charges.

A lot has been said about delegation over the past year. ESMA, the EU financial regulatory institution, published two opinions in 2017 which set out its views on what local supervisors should require. In addition, the European Commission intends to grant supervisors new powers to monitor delegation and outsourcing outside the EU. However, the position is still not completely clear. Tax teams need to stay close to the debate, because where it ends up will have a direct impact on Brexit's tax impact.

Where Brexit planning involves the transfer of an asset (or a business) to a related party overseas, UK tax rules can deem the transfer to take place at market value.

"Exit" charges

A key tax issue which many managers have been focussing on is whether an "exit" charge could arise on the transfer of activity from the UK to EUco.

Where Brexit planning involves the transfer of an asset (or a business) to a related party overseas, UK tax rules can deem the transfer to take place at market value. UK tax on a market value disposal is a potential cost of moving activity out of the UK: an exit charge.

Management agreements with EU clients are examples of assets which may need to be transferred out of the UK. Other examples could include assets used in EU distribution activity, for example customer relationships currently managed in the UK. There could also be a transfer of goodwill.

Determining the market value of the transferring assets is not necessarily straight forward. Take management agreements, for example. In the absence of an active market for management agreements, what would a willing buyer be prepared to pay for one, in the open market? How do the unique circumstances surrounding Brexit impact value? And is value impacted by the transfer mechanism itself?

A feature of many asset managers' Brexit planning involves delegation back to the UK. Whilst management agreements with EU clients will be transferred to EUco, many managers intend to continue performing portfolio management in the UK, under delegation arrangements.

From a tax perspective, this is significant because it should reduce the net fee income stream, and therefore any economic value, which leaves the UK. EUco will receive the gross income which arises on a transferring management agreement, but will pay a proportion of this back to the UK for the portfolio management services which it receives.

Transferring distribution activity can also give rise to interesting considerations. One key question is: where does the value of EU distribution activity reside? Is it in the UK, or in EU branches where customer relationships may be owned?

Where value is in the branches, it may be possible to transfer it to EUco tax neutrally (more on this in the next section).

However, to the extent that value moves from the UK head office to EUco, this could create an exit charge in much the same way as transferring management agreements. Understanding the functions which contribute to value, and determining which ones will move to EUco, is likely to be key here.

EUco's position

For transferring assets, much of the focus has understandably been on the potential for UK exit charges. However, there are likely to be tax implications for EUco too.

From a corporate income tax perspective, an important question is whether EUco will obtain tax relief for the market value of the assets it receives. In other words, will any taxable gain in the UK be matched by a deductible expense in EUco's jurisdiction? If so, then the overall group impact might be considered neutral. If EUco is in a higher tax jurisdiction, or if there are unvalued tax losses in the UK which can cover an exit charge, then the transfer could in fact create a corporate income tax benefit at a group level.

The treatment of the transfer for VAT purposes is also important. EUco's tax authority may regard the transfer as a supply which is subject to local VAT under reverse charge rules.

Some tax authorities might regard the transfer as a VAT-free "transfer of going concern". Whether this relief will apply is fact-specific, and different jurisdictions can take different views on what does and doesn't qualify.

If the transfer isn't VAT-free, the cost to EUco will depend upon how much VAT can be recovered. EUco's VAT recovery position will be determined by the nature of its activities for local VAT purposes. Significantly, activities which were regarded as taxable or exempt for UK VAT purposes, may not have the same VAT treatment in EUco's territory. There are variations in how each Member State has interpreted EU law, particularly in the investment management sector.

EU branches

Many UK managers currently conduct EU distribution activity through branches. Brexit planning may involve transferring those branches to EUco.

In principle, the transfer of branches from the UK manager to EUco should be relatively straight-forward. The EU territory should have rules which allow the branch assets to move tax neutrally, and an election can be made to exempt overseas branch profits, thus mitigating any UK corporate tax charges which might otherwise arise on the transfer of branch assets to EUco.

Complications can arise though.

In some overseas territories, the branch transfer relief might be clawed-back on Brexit. This is because the rules require the transferor (i.e. UKco) to be an EU company for a specified period after the date of transfer. When the UK leaves the EU, this condition will no longer be met.

The tax authorities in Ireland, one of the affected jurisdictions, have addressed this issue by removing the claw-back rule for the transfer of Irish branches. But the tax neutral transfer of branches in other jurisdictions, like Germany, can still be problematic.

Even if a tax-neutral transfer is possible, the conditions which must be met to access the relief can cause complications. Depending on the mechanism being used, the transfer may need to be for the issue of shares by EUco to the transferor, UKco. This can create split share ownership structures where EUco is not already a subsidiary of UKco. In some cases, the structure could be tidied up by transferring the shares intra-group, but this is not always possible.

There are things to consider from a UK tax perspective too.

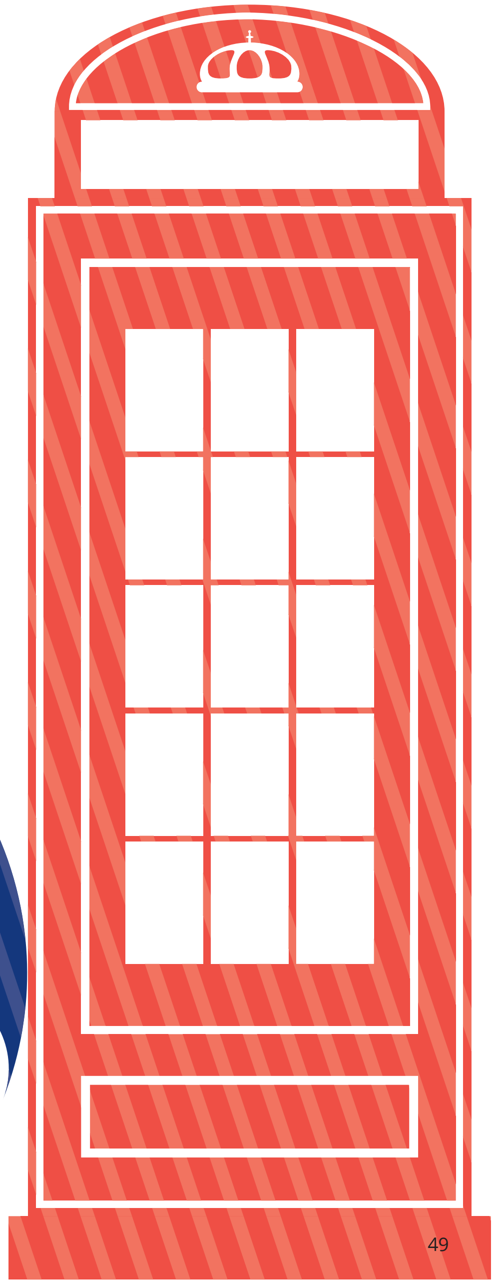
Without a branch exemption election, the transfer of branch assets from UKco to EUco will be a market value disposal for UK tax purposes, which could trigger a taxable gain. The branch exemption election can in many circumstances exempt that gain, but it won't always work.

One thing to bear in mind is timing. The election needs to be made before the start of the accounting period in which the transfer takes place. So if UKco has a calendar year end and intends to transfer its branches in 2019, the election needs to have been made before the end of 2018. A "loss recapture" rule means that the election may not be effective for branches which have been loss-making in the years prior to the transfer, and the election may not exempt branch assets which have previously been owned by head office in the UK. These could include customer relationships or other intangibles which were managed in the UK prior to the branch being set up.

Helpfully, if the branch election isn't effective, there are other reliefs which can defer or eliminate the UK tax which would otherwise arise on the transfer of branches. These reliefs are subject to a number of detailed conditions, which need to be worked through carefully. One of the reliefs is also subject to a clearance procedure, which needs to be built into project plans.

To the point:

- Many UK-based asset managers are transferring EU business to companies in the EU, ahead of Brexit
- These transfers could create taxable disposals and VATable supplies
- To mitigate costs and avoid pitfalls, tax needs to be thought about at an early stage



International Investment Disclosure Trends

The dawn of the fully transparent era

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In 2018, regulatory change and competition for investors will support a global trend towards further transparency. As a result, international capital markets will require transaction costs to be included in investment products' disclosures. This requirement is generating significant challenges for market participants.

In Europe, fund managers have to produce new information documents for their products by January 2018 owing to implementation of the Packaged Retail and Insurance-based Investment Products (PRIIPs) Regulation. In addition, anyone supplying investment products alongside financial advice to European retail investors must ensure they provide information that complies with the Market in Financial Instruments Directive II (MiFID II), which will also be effective as of January 2018.

Similarly, in Australia, as of 1 October 2017, most super funds had to comply with the Australian Securities and Investments Commission's (ASIC) new Regulatory Guide 97 (RG97)—Disclosing fees and costs in PDSs and periodic statements. The intention of RG97 is to enhance comparability among superannuation products. Consequently, many financial services providers have joined forces to form the RG97 industry working group in order to determine consistent fees and costs disclosure across the industry.

International comparability of fees and costs

Comparability and alignment between countries and markets is another challenge owing to the complexity of market structures, legal frameworks, and historical business practices. The recent changes around disclosure have been predominantly driven by regulators wanting global alignment as financial services markets become increasingly interconnected. Regulators in Europe and Australia want the common disclosure objectives for consumers to be comparability, transparency, and ease of understanding. These are enshrined in ASIC's RG97 objectives of:

- Consumer protection.
- Enabling analysis of the superannuation and managed fund industries, including benchmarking of fees and costs.
- Enhancing a consumer's ability to compare fees and costs of products effectively.

PRINCIPLE
01

Improved transparency reflects good culture and governance

- Transparent disclosure of all fees, underlying costs, and conflicts of interest reflect a good governance culture and conduct within a fund.

PRINCIPLE
02

Consistency

- Disclosure requirements should apply consistently to all funds, regardless of the fund's structure, investment approach or asset allocation.
- Consistency across asset classes is needed, e.g. infrastructure investments should be treated in the same way as property investments.
- A level playing field across all disclosure and reporting requirements is a key goal for consistency.

PRINCIPLE
03

Comparability

- Information on fees and costs should enable members to compare the costs of different funds.

PRINCIPLE
04

Transparency should be provided

- Funds should disclose all fees and costs that impact an investor's net returns, including the costs borne directly by the fund, and costs that are indirectly charged and which reduce investment returns.

PRINCIPLE
05

Disclosure that is informative and understandable for investors

- Fees and costs should be disclosed in a clear and comparable format that is informative and useful to both prospective and current investors.
- Disclosure should help investors distinguish what is essential.

Individual country regulatory authorities are trending towards alignment when considering their own comparability with other relevant markets. However, despite the ongoing alignment between European fund disclosures and those of their US peers, there is plenty of room for improvement for Australian funds, especially in performance and risk reporting.

- In August 2016, the International Organization of Securities Commissions (IOSCO) published its final report on "Good Practice for Fees and Expenses of Collective Investment Schemes." In the report, the IOSCO identified 23 "Good Practice Principles" and provided a detailed explanation of its methodology and observations. The two best practice examples given as evidence were:
  - The Key Information Document (KID) fee table for Undertakings for Collective Investments in Transferable Securities (UCITS) in the EU.
  - The fee table for Securities and Exchange Commission (SEC) Registered Mutual Funds in the US.
- The US, UK and EU regulators and leading investment management associations consistently refer to trends in their respective counterparty markets in commentaries, publications, and submissions to regulatory forums. This is also evident in the international development of "investment product passports," e.g., UCITS from the EU, ETFs from the US, and the ASEAN and Asian Passports.

IOSCO suggests fees and costs should be classified into the following broad categories:

- Fees paid directly to the fund or its operator or related party
- Fees and expenses borne by the fund:
  - Investment management fees.
  - Distribution costs.
  - Other fund operating costs.
  - Transaction costs related to the purchase and sale of assets.

There is a global trend towards the "all-in fee" concept. The all-in fee concept aims to disclose all fees and costs incurred by investors. This concept can be used to explain the total fees and interest included in a financial transaction. However, IOSCO has not recommended including transaction costs in the all-in fee. Rather, it stresses the need to balance this argument with the practicalities of measurement and the relationship to net return if the fund is remunerated on a net performance basis.

Lessons learned from the ongoing implementation of Australia’s RG97

- Although ASIC encouraged market participants to create an industry working group to think of the best way to implement RG97, many aspects are still open to interpretation. This means that meeting the deadline will be challenging, and it is questionable whether the new requirements will be able to be applied consistently.
- The impact of RG97 on headline costs varies enormously between funds. ASIC indicated that additions to disclosed fees and indirect costs range from a few basis points for some funds to nearly 1% p.a. for others.
- Ultimately, the underlying costs and net returns to members have not changed; however, the appearance of a large increase in fees presents major communication challenges.

High-level RG97 impact on business processes

System	Process	Teams
Statement changes—changes to statement disclosures and layouts have occurred and need to be explained to members.	**Data collection supply**—processes for the collection, supply, and estimation of fees and costs are required.	**PDS team volume increase**—it is likely that PDSs will now need to be rolled out annually as the actual fee and cost information for the previous financial year becomes available.
Indirect costs changes—there will be an increased emphasis on disclosing indirect costs to encompass all relevant fees and costs that are directly and indirectly incurred by investing through external fund managers.	**Data collection**—processes need to be developed to collect and provide fee and cost dates for Product Disclosure Statements (PDSs).	**Complaints team volume increase**—increases are likely due to the changes in statements not being understood, or perceived price increases.

RG97 also creates several interpretative and operational challenges such as:

- Definition of fees, costs, and indirect costs.
- Definition of "Interposed vehicles".
- Collecting data from underlying fund managers.

In response to these challenges, ASIC announced in early November 2017, that it will conduct an external review on the effects of the RG97 fee disclosure reforms, and will again extend its previous 30 September 2017 compliance deadline. ASIC said the move was in response to the industry's difficulty in implementing the changes. ASIC was pleased that funds have been investing in improving fee disclosure thus far, but recognized that "accurate fee and cost disclosure is complex to implement and that this implementation takes time."

Market challenges—common pressure points across Europe and Australia

Technical content challenges have emerged around the lack of consensus with regard to:

- Including transaction costs and performance fees.
- Using estimates for certain disclosure elements.
- Responsibility for revision of Product Disclosure Statements when circumstances change.
- Fiduciary Duty: Best Execution, Value for Money, Responsible Manager, Best Interest of the Investor.

There are also practical institutional challenges in the EU, which are relevant for other markets:

- Pension and/or investment products that are wrapped inside a life insurance fund will be designated as a PRIIP and therefore included in transition requirements.
- Separation of research into a separate fee for service rather than included in commission or distribution charges.
- Financial Institutions not wanting to subsidize their asset management arms for the additional IT and restructuring compliance costs, despite being "vertically integrated" within the institution.

Another key effect of RG97 is that it will force the superannuation sector to further examine the costs of a manager, especially considering the after-fee performance.

Focus on transaction costs disclosure

There is no generally accepted definition of transaction costs. However, International Financial Reporting Standard 9: Financial

Another key effect of RG97 is that it will force the superannuation sector to further examine the costs of a manager, especially considering the after-fee performance.

Instruments defines transaction costs as: "incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability. An incremental cost is one that would not have occurred if the entity had not acquired, issued or disposed of the financial instrument."

A granular understanding of the several types of costs and charges is important for all market participants. These can have a substantial effect on investors' returns and, if disclosed effectively, should facilitate market efficiency. With this in mind, regulators have gone to considerable lengths to implement all the necessary requirements related to the disclosure of all costs and charges associated with providing investment services, thereby increasing transparency in the market.

Areas of immediate concern tend to look towards the methods required to estimate transaction costs and more specifically implicit costs.

Implicit costs

One of the most controversial areas that remain unresolved is the common approach to the definition of "implicit costs. "Implicit transaction costs are difficult to compute. They are described by the European Securities and Market Authority (ESMA) in Europe and ASIC in Australia as all costs incurred in order to acquire and dispose of investments.

In most cases, the professional associations' guidance is that implicit costs will equate to the bid-ask spread for the asset. However, in markets such as fixed income, foreign exchange, and derivatives markets, transaction costs are embedded in the bid-ask spread of the financial instrument, so it makes them hard to quantify. The issue deepens when other categories of implicit costs considered by the practitioners of Transaction Cost Analysis (TCA) are added into the equation. Typically, these variables arise in response to the market for a trade or its timing. Specifically they consider:

Market impact—executing a large order in one go can move the market and obtain a different price from that expected.

Delay—is the price differential from initiating the order to placing it on the market. Fund performance can be affected if the market moves and elicits a cost.

Opportunity cost—if a trade is partially executed, it may run the risk of missing out on the opportunity to participate in favorable movements in the market. This risk is typically considered to be a loss in value and, consequently, a potential cost.

Typically, these transaction costs are estimated by fund managers using proprietary models. However, there is a lack of common harmonized models to calculate these costs across firms.

RG97 vs. MiFID II: the growing focus on reducing implicit costs and improving best execution

ASIC's RG97 can be considered a mini MiFID II. It increases focus on the implicit costs that can be minimized with best execution. MiFID II's best execution regulation primarily focuses on indirect transactional costs. When executing orders, it seeks to compel the industry to take sufficient steps to obtain the best result possible for their clients.

In 2014, the British Financial Conduct Authority (FCA) investigated the asset management industry and calculated that around £4.2 billion in implicit transaction costs could have been avoided.

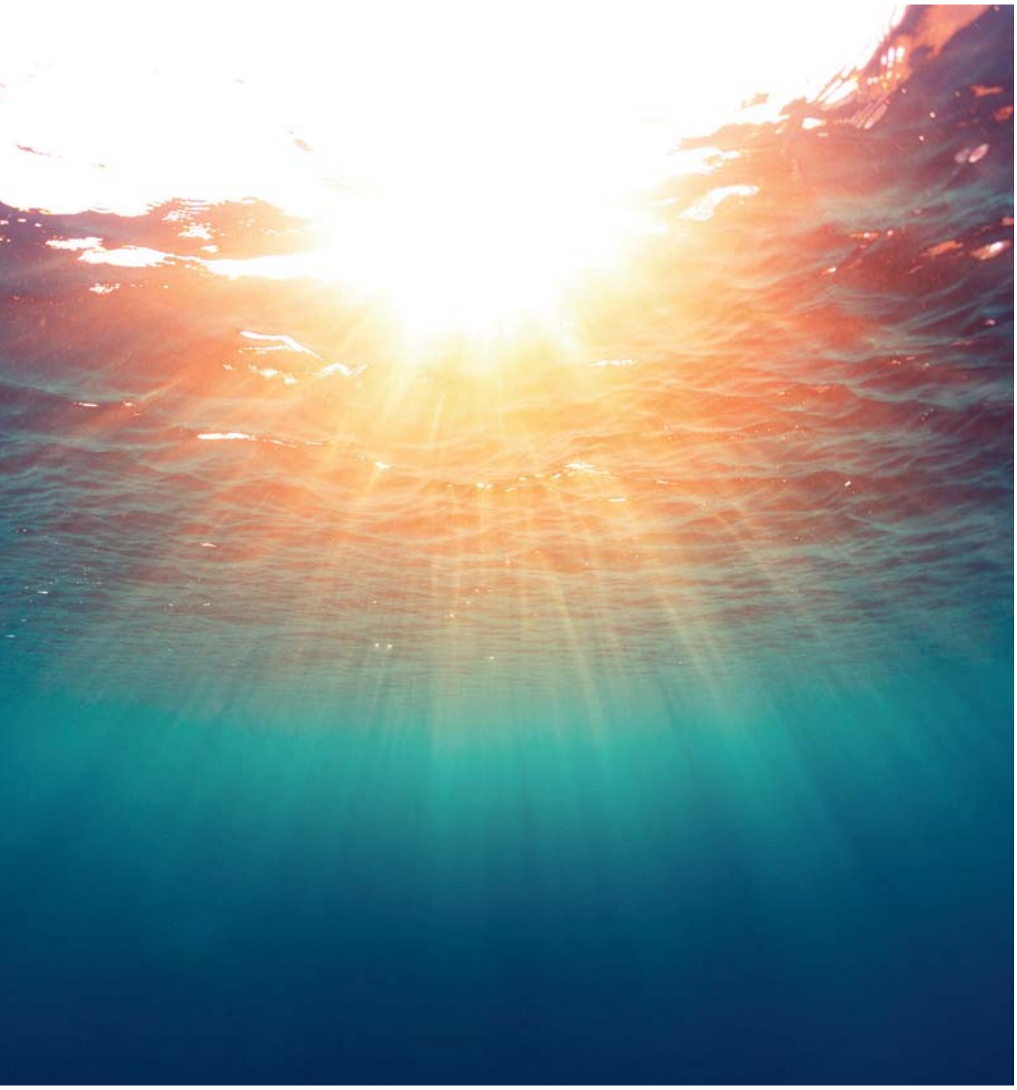
Both regulations strive for "client's best interest" and "transparency". Where costs are made transparent, all sufficient steps need to be taken to minimize these costs as much as possible.

As a result, Multi-Asset Transaction Cost Analysis (TCA) is expected to gain traction in the Australian market. TCA improves execution quality and fund performance, and should ultimately help attract more business, or increase assets under management. Many asset managers in Australia are already conducting sophisticated TCA, which is often essential to winning institutional mandates.

RG97 requires trade data, market data, and transparent implicit cost calculations.

- Obtaining trade data can still be a major hurdle. Under MiFID II, time-stamping trades to the millisecond is now required. This will ultimately benefit buy-side clients. However, it is essential for buy-side firms to evaluate their execution management systems and improve the capture of their trade data. Date-stamped custodian data will take this challenge to the next level. TCA is only as good as the quality of trade data.

Both regulations strive for "client's best interest" and "transparency". Where costs are made transparent, all sufficient steps need to be taken to minimize these costs as much as possible.



- Market data is the second challenge, especially for OTC instruments. Reference points other than bid-ask prices for both bonds and FX are needed for in-depth TCA. Relying on bid-ask prices from competing quotes as reference points in order to calculate the true implicit costs is irrelevant when selecting the five worst dealers during the RFQ process. Analysis should account for quotes from as many dealers outside the RFQ process as possible when analyzing execution quality. Data providers will be essential to administering this level of data. Again TCA is only as good as the quality of market and pricing data.

The compliance challenges of RG97 are not vastly different from the best execution requirements under MiFID II. Although it has a direct impact on asset managers and superfunds, it will also affect banks and broker dealers when their client bases become more sophisticated.

Like MiFID's best execution requirements, we expect RG97 to cut down implicit transaction costs and improve overall fund performances in the long term.

Analysis should account for quotes from as many dealers outside the RFQ process as possible when analyzing execution quality.

To the point:

- The key international best practice trends are:
  - **Disclosure:** regulators and market participants continue to align market practices with regard to the disclosure of investment fees and costs.
  - Interconnectedness: trends are driven by the need to promote trust as markets increasingly interconnect.
  - **Technology:** the use of technology enables data to be collated across the investment execution value chain, to improve transparency for consumers.
  - **Transparency:** the level of transparency prescribed by market regulators is generating significant cost and technical challenges.
  - **Integration:** the complexity of markets requires the alignment of disclosure practices to be integrated.
- The EU frameworks recognize that the investment decisions are complex and not solely driven by cost. Consequently, the disclosure framework includes risk, return, and remuneration. However, in Australia, the regulator has focused on remuneration reporting and is yet to focus on risk and return reporting.
- ASIC stated that "Asset allocation, investment risk and strategy are clearly also very important, as are elements of services. One area we are very interested in is that the focus should move to looking at net returns, and that if you have consistency and accuracy in terms of fee disclosure, then the focus can shift to net returns." ASIC is eventually expected to turn its attention to how reporting investment performance can be improved.
- The industry recognizes the need to provide consumers with both the understanding and the power to make better decisions when choosing superannuation products. While both the EU and Australia are moving towards those frameworks through various legislations, there is still a long way to go. Various functions within the industry, ranging from fund managers, product developers, regulatory bodies, and superannuation providers need to come together to achieve comparability, transparency, and ease of understanding.

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  31 May
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