



Vereniging VEB NCVB

Postbus 240, 2501 CE Den Haag  
Amaliastraat 7, 2514 JC Den Haag

T: +31 (0)70 313 00 00  
F: +31 (0)70 313 00 99

I: [www.veb.net](http://www.veb.net)  
E: [info@veb.net](mailto:info@veb.net)

IBAN: NL58 ABNA 0429 6550 02  
K.v.K.: 40408053

**EC Public consultation 'Building a Capital Markets Union'**  
*13 May 2015*

Consultation reply of:

**VERENIGING VEB NCVB (Dutch Investors' Association)**

Contact persons: mr. drs. N. (Niels) Lemmers  
drs. S. (Sibe) de Bok

Address: Amaliastraat 7  
2514 JC Den Haag

Phone : +31 (0)70 313 00 00  
Fax: +31 (0)70 313 00 99



## Introduction

The VEB is highly supportive of the European Commission's efforts to create a capital markets union. In particular, the VEB believes retail investment should be given a boost by (i) restoring trust in financial markets through increased investor protection, especially in relation to financial intermediation, (ii) increasing direct (cross-border) access of retail investors to capital markets (i.e. direct investments in shares and bonds) through pan-European trading platforms (iii) promoting the emergence of high-quality and cost-effective European (exchange traded) UCIT funds and (iv) eliminating barriers to individual shareholder engagement and enhancing minority shareholders' rights to investigation. Furthermore, the VEB believes that institutional investors should be incentivized to invest directly in public equity markets.

## 3. Priorities for early action

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

The VEB has taken note that none of the five priority areas is directly relevant to retail investors (with the exception of an improvement of the 'summary prospectus' for equity and debt securities).

The VEB believes that the Commission's priorities for early action must include measures to:

- Increase retail investors' confidence in financial intermediaries Their poor performance in delivering return as well as the costs of mediation should be addressed.
- Improve the direct (cross-border) access of retail investors to capital markets (i.e. direct investments in shares and bonds) through pan-European trading platforms (Graph below).
- Promote the emergence of high-quality and cost-effective European (exchange-traded) UCIT funds.
- Eliminate barriers to individual shareholder engagement and enhance minority shareholders' rights to investigation.



Source: Better Finance



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

The VEB supports further steps around the availability and standardisation of SME credit information. Interviews conducted by Better Finance show that there is a genuine interest among retail investors to invest in IPOs of SMEs. Improved accessibility of these investors to credit information is crucial. Information that is publicly available in the case of SMEs is often limited, while the risks associated with these investments are often higher than in the case of other listed enterprises. Improved credit information can help to close this gap. It is however important that SME credit information does not become a 'transferable product'.

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

The VEB is sceptical regarding the additional value of ELTIFs due to the fact that long-term investment funds are also run by UCITS. The VEB moreover believes that these ELTIFs are not suitable for retail investors due to their lack of liquidity. A higher threshold for minimum investments in ELTIFs would therefore be desirable. They should be 'advised' only to qualified or very financially literate individual investors.

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

The VEB is rather sceptical regarding private placement and its suitability for retail investors. Private placement markets differ substantially from the public markets, which have more disclosure and protections for investors. On private placement markets, investors cannot easily sell their securities (liquidity). The risks of business failure and the risk of fraud within is higher. It is of course true that some retail investors have done very well investing in start-up businesses. But this is usually because these investors have the necessary knowledge to assess whether the company has a good business plan, excellent management and leadership, and a product that produces profits in a timely way.

#### 4.1 Improving access to finance

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

Public equity financing is currently disincentivised when compared to debt financing. The VEB refers to the IPO task report The European IPO Taskforce Report *Rebuilding IPOs in Europe: Creating jobs and growth in European capital markets*<sup>1</sup> for measures that could be taken to create an equity culture in Europe. This is of great importance for SMEs seeking finance as well as for institutional and retail investors who wish to invest directly in public equity markets, incl. IPOs markets. In general, the direct access of retail investors to capital markets should be facilitated. Reliance on costly funds with a poor performance should be reduced.

<sup>1</sup> [http://www.europeanissuers.eu/mdb/position/292\\_Final\\_report\\_IPO\\_Task\\_Force\\_20150323.pdf](http://www.europeanissuers.eu/mdb/position/292_Final_report_IPO_Task_Force_20150323.pdf)



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

Standardization could contribute to more liquidity on corporate bond markets. Examples of measures that could be taken: larger bond issues, more use of fungibles, standard maturities, plain vanilla structures, standardised documentation, standard use of governing law and courts. The VEB is not convinced that this can be achieved by the market alone. Regulation action is thus needed. However, the VEB believes that promoting investment in public equity markets (see Q5) should gain priority.

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

The VEB thinks it is important that retail investors are equipped with the tools and resources needed to properly evaluate and compare sustainable investments across asset classes on the basis their financial characteristics as well as their ESG characteristics. There should moreover be one European label which reassures retail investors that they invest their household savings in funds which incorporate ESG consideration in their investment process. Currently, many private labels exist, such as LuxFlag, Novethic and Ethibel which cause confusion among retail investors.

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

Standardization with regard to financial reporting is necessary in order to promote (cross-border) investment in SMEs. The VEB believes that listed SMEs should follow the IFRS in order to make sure that their financial situation can be compared with other listed enterprises. There should not be a separate accounting standard for listed SMEs in general, or specifically for SMEs listed on Multilateral Trading Facilities (MTFs). MTFs are usually much less transparent and much less friendly and accessible to retail investors than the regular public equity markets. The VEB sees no reason for any discrimination against SME listings on regulated markets.

The VEB refers to the IPO task report The European IPO Taskforce Report *Rebuilding IPOs in Europe: Creating jobs and growth in European capital markets* for measures to facilitate IPOs for SMEs.

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

There should be a EU-level harmonized regulatory framework with regard to crowdfunding in order to enable a pan-European market to emerge and to develop EU-based platforms that could compete with the US ones. However, the VEB believes that is of great importance that investor protection is enhanced through increased disclosure (prospectus obligations) and better oversight by national competent authorities. The advertisement and sale to retail investors should be restricted by these NCAs if the protection of retail investors is not sufficiently safeguarded. This could be the case, for example, for subordinated loans and loans with profit participation. The VEB refers to the legislation



recently adopted in Germany regarding so-called 'grey markets' which introduces inter alia a prospectus requirement for companies raising more than 2,5 million through crowdfunding and an investment cap of 10,000 for retail investors. It also gives the BaFin the possibility to restrict or ban advertisement of crowdfunding projects.

## 4.2 Developing and diversifying the supply of funding

### *Boosting institutional investment*

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

Institutional investors have a fiduciary and commercial duty to generate sufficient return. There should therefore not be too much pressure on institutional investors to invest in a broader range of assets as this could result in allocation of funds to investments that are simply not attractive enough.

Furthermore, as stated as a response to Q5, the VEB believes that public equity investments by institutional investors should be facilitated. Institutional investors are currently incentivized by European as well as national restrictions on investments in IPO and public equity in general to invest in bonds which are not attractive to them (especially considering the current market conditions). The allocation of funds to equity in Europe is therefore rather limited in comparison with other markets. The VEB refers to The European IPO Taskforce Report *Rebuilding IPOs in Europe: Creating jobs and growth in European capital markets* for recommendations on how institutional investment in public equity markets can be promoted.

In general, prudential rules and supervision currently discourage institutional investors from investing in long-term projects that can contribute to the real economy (and which also generate a high return for these investors). If the European Commission would like to promote these kind of investments, it should adopt flexibility in its risk approach regarding these kind of illiquid assets. Increased direct access (or through intermediaries) to public equity markets, including IPO markets, on the other hand, would provide institutional investors with the possibility to invest in liquid assets with a relatively high return.

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

The VEB supports further harmonization with respect to the rules governing the setting up of funds. However, the Green Paper seems to suggest that the costs associated with the setting up of funds is too high and limits competition. The VEB would like to point out that there are currently more than 33,000 funds in the EU (versus 8,000 funds in the US, a market more than twice as big that the EU). The problem in the asset management is therefore not lack of choice *per se*. The VEB believes that the problem is a proliferation of socially useless products, poor value, embedded inefficiencies and lack of trust and confidence. Reducing barriers to entry to encourage even more choice will therefore



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not be effective. The focus should be on improving the quality of choices available. To do this the VEB calls for tough, targeted regulatory interventions on:

- increasing transparency on costs (TCO) as well as reducing the costs itself;
- streamlining the investment industry;
- encouraging economies of scale (see below);
- preventing misleading marketing and promotions
- product regulation to minimise the risk of toxic investment financial products being manufactured and distributed through the supply chain and promote the development of standardised, easily compared, good value products;
- promoting effective competition that works in the interests of financial users by tacking the conflicts of interest that exist in the supply chain between product manufacturers, intermediaries (advisers, salespeople and information providers) and financial users;
- ensuring that the various agents in the supply chain properly exercise fiduciary duties of care and take seriously their stewardship duties; and
- driving out short-termism and promoting long term patient investment.

In order to promote economies of scale, the VEB supports a full harmonisation of marketing rules for UCITS funds in order to promote the emergence of truly European UCITS funds. Asset managers spend significant amounts of money on tweaking their marketing material to meet diverging national marketing requirements. Most of those diverging marketing requirements are not justified by the different characteristics of the markets or consumers, but rather are caused by the fact that each Member State retains discretion over marketing rules. The Commission should look at national best practices in preventing misleading marketing.

The VEB furthermore believes that, in order to promote economies of scale, preference should be given to exchange traded funds which can be categorized as UCITS, not to AIFs. AIFs are more numerous, smaller and often purely sold on a national basis. It is much more common for UCITS to be sold cross-border. Moreover, the

VEB believes UCITS are better suited for retail investors as they are more transparent. Important to note in this regard is that various Member States have preferential tax treatment for non-UCIT funds.

With regard to taxation, it is furthermore important to mention that local funds sometimes get preferential tax treatment and that some fund domiciles have a better tax treaty network. Tax laws should not discriminate between different fund domiciles and the EU should develop a harmonised tax treaty network for funds. In particular, the VEB would like to urge the European Commission to take all necessary actions to tackle the so-called dividend tax leakage which retail investors experience when investing in index and exchange traded funds that are domiciled in another Member State.

Finally the VEB would like to note that fund mergers can cause capital gains tax. Therefore mergers can be detrimental from the tax perspective for clients even though leading to economies of scale.



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

Don't know/no opinion

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

Don't know/no opinion

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

Don't know/no opinion

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

The VEB is rather sceptical regarding private equity and venture capital and its suitability for retail investors. Private equity markets differ substantially from public markets, which have more disclosure and protections for investors. On private equity markets, investors cannot easily sell their securities (liquidity). The risks of business failure and the risk of fraud within is higher. It is of course true that some retail investors have done very well investing in start-up businesses. But this is usually because these investors have the necessary knowledge to assess whether the company has a good business plan, excellent management and leadership, and a product that produces profits in a timely way or not.

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

Don't know/no opinion

### *Boosting retail investment*

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

As already mentioned in the answer to Q11, there should be a truly European fund market with genuine Europe-wide funds. Participation in funds should not be restricted to residents of the Member State in which the fund is registered. Access to non-residents should be provided, if necessary with lesser levels of investor protection than the retail investor would enjoy if investing in his home Member States.

The VEB would like to note that while UCIT funds are, relatively speaking, widely distributed most of the distribution channels that offer retail investors direct access to funds and shares are restricted to





those residents in the same Member State, restricting the free movement of capital. For example, an online platform such as Fidelity Funds Supermarket only offers access to UK residents. There do not appear to be truly pan European web platforms in this area. The VEB believes that direct access should be promoted due to the poor performance of UCIT and non-UCIT funds in delivering return and the high costs of intermediation.

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

ESAs should first make full use of their legal duties and powers in terms of data collection, analysis, and publication, in particular in the areas of returns and prices (fees) (article 9.1 of the ESAs Regulations) and of product intervention (article 9.5) to ban toxic products that bring negative value to investors.

They should also better enforce existing investor protection rules.

- a. Product intervention: The ESAs and the National Competent Authorities should also make use of their product intervention powers to ban any toxic retail investment product, including those for which the probability to meet their stated investment objective is non-existent or very low. For example, this would be the case of «closet index funds» (falsely active funds) and of retail «index» funds (i.e. with a promise to closely track the index) which charge 1 to 2% annually (making it de facto impossible to closely track the index), when the same index funds but in an ETF version charge 5 to 10 times less per annum.
- b. ESAs must better comply with their legal duty to analyse and report on long term and pension investor trends, including actual net performance and fees of all retail long term and pension products (article 9.1 of the ESAS Regulations).
- c. Single rulebook, supervisory convergence and governance of the ESAs should be improved
- d. Similarly, the EU should entrust ESMA with full competency and powers on all savers and investors' protection issues, and stop fragmenting investor protection between three different ESAs.
- e. Next to its involvement in the operation of the proxy advisory industry, ESMA should be entrusted with improving the proxy voting process for shareholders e.g. by ensuring for standardized workflows within the intermediaries chain and by developing harmonized EU-wide accepted proxy forms.

For all these key tasks to be effectively performed, the resources of the ESAs created in 2010 should be reinforced, not reduced as decided by the ESAs

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

*Restoring trust in financial markets* is essential for increasing retail investment. Investor protection should remain a key driver of EU financial legislation in order to revive confidence in financial markets. Only when investors feel adequately protected they will be willing to channel their savings into capital markets.





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ESAs should focus more on the returns and prices (overall fees) of “retail” investment products (total costs of ownership), which are neither clearly disclosed or decent overall. Also, ESAs should have more powers to ban “retail” distribution of toxic packaged investment products.

It is also necessary to *strengthen the ability of (especially) individual investors to engage with the companies they are invested in*. An important means, especially for individual investors in that respect is the exercise of their voting rights stemming from their shares. While voting within one Member State today seems to work without inadequate burdens or costs for shareholders, the voting process across borders still remains difficult

and is very often too costly. Although these issues have been tackled by the SRD, the provisions will not suffice to solve all problems described. This is mainly due to an inefficient custody chain complemented by a lack of knowledge at the deposit banks’ “point of sale”. First steps could be the introduction of a common EU voting form and the introduction of a uniform record date for the entitlement to attend/vote at a general meeting. Repealing barriers to cross-border shareholder engagement as well as introducing common minimum corporate governance standards across Member States is therefore urgently needed.

*Adequate collective redress mechanisms* should be developed, modelled on best practices in Member States, e.g. the Dutch collective settlement procedure/collective action.

Finally, improvements in the quality and quantity of *financial education* by advocating/fostering respective initiatives is needed.

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

The VEB wants to see more effective cross border competition with higher levels of transparency and investor protection. A race to the bottom should be avoided. We have observed too many examples of risky practices and poor value products and services transferred cross-border within the EU, rather than good practices which should be expected if the market was working for financial users. Far too many EU citizens are being denied the best the market can offer due to the barriers which prevent them from buying financial services in countries in which they are not resident.

With regards to retail financial services, there is still much to be done to create a well-functioning single market for financial consumers. But it is important to distinguish between the illusion of competitive activity and competition that works in the interests of financial users.

This effective single market will not be delivered by liberalising the market or removing perceived barriers to entry. This risks promoting regulatory arbitrage and a move to lowest common denominator consumer protection. This will undermine consumer confidence and severely curtail the development of a real single market that works for financial users.



## *International investment*

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

Further integration European capital markets should ensure the necessary scaling that benefits markets like China and the US. The VEB furthermore supports a more active EU international investment policy focusing on investment liberalisation and investment protection. Reliance on BIT's should be reduced. European markets can furthermore become more attractive by increasing investor protection levels across Europe.

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

The VEB furthermore supports a more active EU international investment policy focusing on investment liberalisation and investment protection, thereby opening up markets for all European retail and institutional investors, not only those from a specific Member State. It is important that investment liberalisation does not go at the expense of investor protection.

## **4.3 Improving market effectiveness – intermediaries, infrastructures and the broader legal framework**

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

- Restore investor confidence and trust in capital markets: much stronger emphasis on EU market abuse and MiFID (best execution, conduct of business rules, misleading information, etc.) rules enforcement.
- This means improving further supervisory effectiveness and convergence, setting up collective redress mechanisms for all EU savers and private investors (private enforcement), improving tracking and sanctioning of market abuses.
- Rehabilitate equity investing (in particular for SMEs) and individual share ownership, by ensuring a level-playing field for simple securities at the retail point of sale.
- For politicians, policy makers, industry and media to refer to “all-tradable” indices instead of blue chip ones when they communicate on “equity markets”.
- Eliminate barriers to individual shareholder engagement; in particular ensure free cross-border voting for individual investors, actual voting rights for shareholders in nominee/omnibus accounts, full rights of association for individual shareholders of any EU domiciled listed company.
- Improve the summary prospectus for shares and bonds by making it as user-friendly, formatted, standardized, short and comparable as the KID for funds and the future KID for PRIIPs and possible “PBS” for pension fund participants (IORP review proposal from the EC) and KID for personal pension products (current EIOPA work for the EC).
- Reduce market fragmentation, “dark” and OTC trading; impose same transparency requirements to the new market venues (example: SIs – typically big banks - selling equity



- warrants without the best execution rules applying to RMs to unaware individual investors), or ban any promotion to individuals for those venues.
- Easily accessible and free “consolidated tape” (consolidated pre – and post- trade data) for individual (non-professional) equity investors within a reasonable time lag (3 minutes max), like they had before the MiFID I induced market fragmentation.
- Ensure easy and free access of retail investors to all major capital markets: market transparency is correlated to retail access (see 2007/2008 fixed income markets crisis): improve fixed income markets transparency and retail access; much improved retail access to bond trade data.
- Any resumption of securitization must be highly standardized and kept as simple as possible; banks should keep significant “skin in the game”.
- Align securities lending disclosure and profit sharing rules for share ownership to those applicable to UCITS funds ownership. Re-lending of lent securities should be banned, as well as the re-pledging of securities as collateral, following the Canadian example.

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

See Q18 and FSUG reply to consultation on EFSF<sup>2</sup>

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

See Q18 and FSUG reply to consultation on EFSF

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

Yes. In particular, omnibus and «nominee» accounts should be strictly regulated to ensure that:

- no shareholder or bondholder has its securities lodged in such omnibus accounts without its prior and explicit consent,
- any use (collateral, lending) of his securities also requires his prior consent and clear information about who will benefit and how much from the transactions’ profits
- The intermediary responsible for the omnibus account must provide timely voting material to ensure that shareholders holding their shares in nominee accounts can truly exercise their voting rights, as they are the economic owners, not the intermediary.

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

Don’t know/no opinion

<sup>2</sup> [http://ec.europa.eu/internal\\_market/consultations/2013/esfs/contributions\\_en.htm](http://ec.europa.eu/internal_market/consultations/2013/esfs/contributions_en.htm)



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

One of the main obstacles to a real integrated European Capital Markets Union is the absence of an effective set of EU rules for minority shareholder protection. A minimum, pan-European set of rights for shareholders to hold boards of companies accountable to shareholders is required. This minimum set of rights should comprise at least – in addition to the current set of rights encompassed by the Shareholder Rights Directive:

1. The right for shareholders to appoint, nominate and remove company directors.
2. The right for shareholders to approve fundamental corporate changes, initiated by the board, e.g. large acquisitions. Numerous studies show that many acquisitions destroy value for acquirer shareholders and that the losses from the worst performing deals are very large, also to society at large. Shareholder approval can block undesirable acquisitions, deter executives from initiating them, and give executives leverage to negotiate better acquisitions.
3. Shareholder approval of the use of anti-takeover devices that can be used by the company to frustrate or to block a hostile takeover attempt.

Moreover, shareholders who decided not to tender their shares in a public bid situation should be offered a higher level of protection in post offering restructurings – e.g. a delisting, a legal merger, a triangular merger, an asset sale, etc.

And last but not least we recommend – as the High Level Group of Company Law Experts already did in 2002 – the introduction of an EU framework rule on special investigation rights for minority shareholders. A shareholder or a group of shareholders, representing a specific amount of the company's share capital, should be given the right to apply to a court or appropriate administrative body to order a special investigation when there is a serious suspicion of improper behaviour by the company's board. This could be an effective instrument for minority shareholders for holding board members to account for possible mismanagement, especially in the circumstance that a company is controlled by a controlling shareholder who is also a company's related party. Moreover, we would also be in favour of a European mechanism for collective redress by shareholders as a concluding piece of engaged share-ownership.

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

So far concrete actions towards harmonising substantive insolvency legislation have been slow despite some progress in the area of conflict-of-laws rules for cross-border insolvency proceedings. Council Regulation (EC) 1346/2000 and its proposed reform do not attempt to impose a common system at EU level, but instead to ensure that insolvency proceedings opened in one Member State are recognized in all other Member States. A common system at EU level would however be desirable.

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



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- Double taxation of cross-border dividends and administrative nightmare to recover the originating country's withholding tax.
- Tax discriminations against EU investors not residing in the issuer's or provider's country.

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

Don't know/no opinion

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

The VEB is highly supportive of the European Commission's efforts to create a capital markets union. In particular, the VEB believes retail investment should be given a boost by (i) restoring trust in financial markets through increased investor protection, especially in relation to financial intermediation, (ii) increasing direct (cross-border) access of retail investors to capital markets (i.e. direct investments in shares and bonds) through pan-European trading platforms (iii) promoting the emergence of high-quality and cost-effective European (exchange traded) UCIT funds and (iv) eliminating barriers to individual shareholder engagement and enhancing minority shareholders' rights to investigation. Furthermore, the VEB believes that institutional investors should be incentivized to invest directly in public equity markets or through intermediaries who provide simple, effective and liquid long term direct investment products.

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