

Review of the European Supervisory Authorities

AFEP Comments on the Commission's proposal for a regulation – January 2018

Procedure: 2017/0230 (COD)

Summary

The French Association of large companies (AFEP) is supportive of the Commission's objectives to achieve a Capital Markets Union and foster the integration of European markets. AFEP agrees, to a certain extent, that strengthening the supervision of European markets could help achieve these objectives. Harmonised rules are essential in achieving a single market and in ensuring a level playing field within the EU. Since their establishment, the three ESAs have significantly contributed to building a single rule book, although harmonisation of practices and consistent implementation of EU Legislation throughout the Union could still be improved. The key question in this regard, AFEP believes, is not whether the ESAs have sufficient powers but whether they make an efficient and relevant use of their powers. An extension of the powers or remit of the ESAs – in particular ESMA – would only be relevant in infrastructure and post-market activities, benchmark indices supervision and third country equivalence. AFEP does not support the proposals about direct supervision of regulated entities, such as listed companies.

Effective direct supervision requires proximity with the regulated entities, expertise in the applicable domestic legislations, not to mention knowledge of the language. Retail investor protection and supervision of advertisements also require proximity and familiarity with national rules, local practices and investment behaviour and patterns. AFEP considers that National Competent Authorities are better placed to carry out these tasks and that the subsidiary principle calls for maintaining direct supervision of the abovementioned entities at national level. Transferring the supervision to ESMA could result in a more complex and less flexible regime that will increase costs and administrative burden for the concerned regulated entities while major pieces of EU legislation are being implemented. With regards to the strengthening of the powers of the ESAs and the extension of their remit, AFEP also believes that there is, generally speaking, a lack of rationale and substance in the Commission's proposals. It is therefore difficult to assess whether these measures are relevant and proportionate.

As regards the changes in the governance of the ESAs, adequate checks and balances should be put in place to avoid any concentration of power in the hands of the Chairperson on the Executive Board – although companies would prefer a *status quo*. In order to reinforce the ESAs' accountability before the European Parliament and the Council, the work programmes of the Authorities as well as the strategic supervisory plans should be presented to the European Parliament and the Council for approval and not just for information. Transparency of the Executive Board should also be enhanced and agendas and minutes of the meetings should be made public. AFEP also believes that the role of stakeholders in the ESAs' governance should be reinforced, in particular through an improved review procedure of the ESA's guidelines and recommendations by Stakeholder Groups.

Finally, Afep is strongly opposed to a change of the current funding structure in order to move to an industry-funded model. The mission of the ESAs to develop regulatory and implementing technical standards should be funded by the European Union. The tasks carried out by the ESAs to foster a common supervisory culture and ensure supervisory convergence should be funded by the National Competent Authorities because they directly benefit from the convergence work. Companies consider that the current funding model is the best way of ensuring the ESAs' work programmes remain in line with their mandate. This model also ensures stable funding resources to the ESAs compared to a model that would be based on a direct, partial or full, industry funding.

Governance

As regards the changes in the governance of the ESAs the Commission is putting forward, the following issues should be highlighted:

- Granting a casting vote to the Chairperson of each ESA, while only few members make up the Executive Board (with a simple majority rule), might result in a concentration of the decision-making power in the hands of the Chairperson. Adequate checks and balances should avoid any concentration of power and favour a collegial approach. A better democratic control might be achieved by strengthening the general accountability of the Chairperson before the European Parliament and the Council.
- Supervisory functions of the ESAs: It is of high importance to clearly define in the level 1 legislation the purpose of supervision and the conditions under which supervision shall be exercised.
- In order to reinforce the ESAs' accountability before the European Parliament and the Council, the work programmes of the Authorities as well as the strategic supervisory plans should be presented to the European Parliament and the Council for approval and not just for information. As regards in particular ESMA, the strategic supervisory plan addressed to National Competent Authorities should not limit the powers of National Authorities to focus their attention and resources on risks most relevant to their local markets.
- The transparency of the Executive Board should also be enhanced: agendas and minutes should be made public.

Stakeholders group

Involvement of the industry and input from companies are essential in ESAs' work to ensure that the standards and non-legislative measures developed by the European authorities are fit for purpose and that supervisory convergence addresses the relevant issues and progresses in the right direction.

Regarding the role played by stakeholder groups, AFEP believes that:

- An overall assessment of the organisation, composition and functioning of the stakeholder groups and standing committees would be useful. This assessment could be the opportunity to reduce, for instance, the number of committees: as far as ESMA is concerned, beside the Securities and Markets Stakeholder Group (SMSG), there are 14 Committees covering various areas of financial markets and services including secondary markets, investment management, post-trading, credit rating agencies, corporate reporting, market integrity, market data, etc. The question whether this organisation is effective needs to be addressed and discussed with the industry.
- Appointment of members of the stakeholder groups should not be left to the ESAs' discretion, considering in particular the proposal to amend article 16 of the Founding Regulations¹ to allow stakeholder groups to send a reasoned opinion to the Commission. The Commission should have a say in the appointment process.
- A clarification of the role of the stakeholder groups would also be necessary. The documents sent to the members of these groups are confidential and cannot be shared; the members themselves

¹ Regulation (EU) N°1093/2010 establishing EBA, Regulation (EU) N°1094/2010 establishing EIOPA and Regulation (EU) N°1095/2010 establishing ESMA.

are not allowed to discuss the agendas with companies outside the groups. Companies understand the need for confidentiality but suggest that more flexible rules be established: some experts' applications are endorsed by business organisations and those experts should hence be accountable to the members of these organisations.

- Review of the ESAs' guidelines and recommendations by Stakeholder Groups: AFEP welcomes the Commission proposal that when members of the relevant Stakeholder Groups consider that the ESAs have exceeded their competences when issuing guidelines or recommendations, they can issue an opinion to the Commission and that the Commission can then withdraw the guidelines/recommendations concerned. However, the current proposal should be amended to be made truly effective:
 - The relevant Stakeholder Groups should decide on this matter by absolute majority of their members instead of two-third majority (keeping the current majority makes the provision inapplicable);
 - The Commission should follow the opinion of the relevant Stakeholder Group and withdraw the guideline/recommendation when it requires it;
 - Relevant Stakeholder Groups should be able to issue an opinion also on Regulatory Technical Standards (RTS).
- The composition of the stakeholder groups should guarantee a balanced representation of the parties concerned. For instance, in the ESMA's SMSG, experts from companies are underrepresented: out of 30 members, only 2 members represent listed companies.
- Transparency of the stakeholder groups and committees should also be enhanced. For the time being, there is little information made public on the meetings, their agendas or on the conclusions and/or output of these discussions.

Funding

Afep strongly opposes a change of the current funding structure in order to move to an industry funded model. The funding model is directly linked to the architecture of European supervision and the tasks and powers of the ESAs; and Afep does not support the extension and strengthening of the ESAs' direct supervision powers. National Competent Authorities still have a key role to play and there is hence no rationale for moving from the current funding arrangements to a new regime that will increase the overall costs of supervision for regulated entities without clear added value as it is unlikely that the fees paid to National Competent Authorities will decrease.

Furthermore, the current ESAs funding arrangements should not be changed to a system funded by the industry for the following reasons:

- The mission of the ESAs to develop regulatory and implementing technical standards should be funded by the European Union since this responsibility stems from a delegation of powers from the Parliament and the Council to the Commission to adopt technical standards.
- The tasks carried out by the ESAs to foster a common supervisory culture and ensure supervisory convergence should be funded by the National Competent Authorities because they directly benefit from the convergence work. The building of a European System of Financial Supervision was specifically aimed at upgrading the quality and consistency of national supervision. One could argue that, in the end, the industry benefits from an enhanced quality of supervision and, as a

matter of fact, the industry already contributes indirectly to the funding of ESMA in some Member States.

- Where an ESA has specific direct supervisory powers, additional fees could be levied from the regulated entities as is the case for the supervision of credit rating agencies by ESMA.
- The current funding model is the best means of ensuring the ESAs' work programme remains in line with the mandate given to them. This model also ensures stable funding resources to the ESAs compared to a model that would be based on a direct, partial or full, industry funding.
- Finally, the current funding model empowers the European budgetary authority (European Parliament and Council) to exert budgetary control over the ESAs for the part of their budget financed from the general EU budget and thereby ensures that ESAs can be held accountable.

If the proposed changes are adopted, AFEP insists on the following points that will have to be addressed:

- The financial institutions and the criteria to determine the annual contributions should be clearly and precisely defined in Level 1 legislation. Whilst contributions should be proportionate, there should be no size criterion to determine whether a financial institution should pay, as the measures adopted by the ESAs must equally apply to all financial institutions.
- As a result of a direct financing from the industry, financial institutions should have their say and a seat in the governance bodies of the ESAs.
- The ESAs budget should be capped.
- There is clearly a lack of clarity regarding the scope of voluntary contributions from Member States or observers and the 'services' that can be charged. AFEP is concerned that these expenditures are at risk of being billed to individual financial institutions.

Remit and powers

As regards the strengthening of the powers of the ESAs and the extension of their remit, Afep considers that there is, generally speaking, a lack of rationale and substance in the Commission's proposals. The lack of explanations regarding the purpose of some of the proposed measures makes it difficult to assess whether these measures are relevant and proportionate. The conditions under which some would-be powers could be implemented need to be clarified (e.g. powers granted to ESMA when there is *"reasonable grounds to suspect that orders, transactions or any other activity with significant cross-border effects threaten the orderly functioning and integrity of financial markets or the financial stability in the Union"*, to recommend to a National Competent Authority to initiate an investigation).

Increasing direct supervisory powers of ESMA over certain entities will also make supervision more complex as some regulated entities will eventually be monitored by different authorities.

Collection of data

Afep considers that National Competent Authorities should remain the main source of information for the ESAs and the main contact point with market participants and issuers.² Any replications or inconsistencies of reporting requirements between the ESAs and the National Competent Authorities that would result in imposing additional burden by introducing additional data collection exercises and reporting channels should be avoided. Multiple data requests are operationally burdensome to manage with no business value for companies and financial institutions, and no obvious value for market stability.

AFEP is concerned by the risks of fines related to the potential misunderstandings of what an “incorrect or misleading” information may constitute. A clear definition of what constitutes such an information should be provided in the level 1 text.

The Commission should take into account the specific context due to the implementation of new requirements introduced by MIFID 2. Afep considers furthermore that any step forward in this area should also take into account the future results of the Fitness Check exercise launched by the Commission to assess the costs and efficiency (relevance, effectiveness, EU added value) of the reporting requirements in the Financial sector as well as the results of the FDS Project. In this regard, Afep is concerned that the Fitness Check, similarly to the EU cumulative impact assessment on financial services legislation performed in 2015, is focused solely on the financial sector (i.e. intermediaries and investment companies). Meanwhile, there is a strong need for a fitness check and / or to measure the cumulative impact of financial legislation and other regulation on non-financial companies as users of financial markets. There is indeed a need to ensure that the reporting requirements EU listed companies face are efficient (EMIR, MAR, Transparency Directive, Accounting Directive, REMIT, Non-Financial Information Directive, CBCR etc.).

As regards in particular ESMA, the new provision that would be introduced in article 8 of the Regulation establishing the Authority lacks a clear rationale for granting new powers to collect data: purpose and objectives of these new powers should be more clearly stated.

Approval of certain prospectuses

Afep does not support the proposal to transfer to ESMA the approval of prospectuses established by EU registered companies falling under the definition of property, mineral, scientific research based or shipping companies. In the same way, Afep would not support the transfer to ESMA of the approval of wholesale debt prospectuses with a denomination per unit of at least EUR 100,000, although not foreseen in the Commission proposal. Companies consider that there is no rationale for transferring the approval of prospectuses established by these companies:

- They do not raise any specific pan-European issues in terms of supervision that cannot be handled by National Competent Authorities;
- The passporting regime works fine considering the significant amounts of passports “in” and “out” notified every year according to the data published by ESMA.

² In the case of EBA, banks that are member of AFEP believe that the ECB should be the single contact point for information requests, as banking institutions already report extensively to the ECB.

Generally speaking, effective direct supervision requires proximity with the regulated issuers, expertise in the applicable domestic legislations and knowledge of the officially accepted language(s). Transferring the supervision to ESMA could thus result in a more complex and less flexible regime that would increase costs (e.g. legal costs for issuers which will rely on lawyers to handle relations with ESMA) and administrative burden for issuers and would not make access to capital markets easier, particularly when issuance windows are narrow and deadlines to complete a financial transaction are tight. Retail investor protection and supervision of advertisements also require proximity and familiarity with national rules, local practices and investment behaviours.

As regards the proposed amendments to the Prospectus Regulation to grant ESMA powers to conduct investigations and on-site inspections, the new provisions put forward by the Commission require more detailed explanations regarding their objectives and purpose.

Sanctions

Regarding the proposed amendments to the Prospectus Regulation, the sanction powers that ESMA would be granted – including the power to impose fines when an entity fails to provide information requested by ESMA – seem disproportionate considering the potential breaches and the fact that the most severe sanction for an issuer filing a prospectus for approval would be a refusal to approve the prospectus: the Commission proposal amending the Prospectus Regulation stipulates that the maximum amount for a fine can be of 6% of the annual turnover for a legal person.

The same comments apply to the sanction powers the Commission would grant to the other ESAs, which seem disproportionate and raise concerns since the ESAs will simultaneously exercise the powers of regulation, prosecution and sanction. There is an obvious lack of separation between these powers within the ESAs (as the final decision to impose fines rests with the ESA's Board of supervisors). AFEP believes that such a proposal constitutes a setback for the evolution of the NCAs' own procedures: the French Prudential Authority (ACPR) and Financial Markets Authority (AMF), for instance, have a Sanctions/Enforcement Committee, which is distinct from their Board (College) and is composed of independent members.

About AFEP

Since 1982, Afep is the association which brings together large companies operating in France. The Association is based in Paris and Brussels. Afep aims to foster a business-friendly environment and to present the company members' vision to French public authorities, European institutions and international organisations. Restoring business competitiveness to achieve growth and sustainable employment in Europe and tackle the challenges of globalisation is Afep's core priority. Afep has around 115 members. Afep is involved in drafting cross-sectoral legislation, at French and European level, in the following areas: economy, taxation, company law and corporate governance, corporate finance and financial markets, competition, intellectual property and consumer affairs, labour law and social protection, environment and energy, corporate social responsibility.

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Transparency Register identification number: 953933297-85