BUSINESSEUROPE

POSITION PAPER

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EUROPEAN SUPERVISORY AUTHORITIES REVIEW
Commission Proposal (omnibus regulation)

Introduction

BusinessEurope supports the EU's broad economic aims of integrating financial markets while safeguarding financial stability. We previously supported the development of a Single Rule Book for financial regulation, the creation of the European Supervisory Authorities (ESAs) and the commitment to completing the Capital Markets Union (CMU). We favour the development of efficient capital markets in Europe, and the proposals to review the role of the ESAs are a step in the right direction. It is important that proposed reforms to the role of ESAs strike the right balance between achieving financial stability whilst enabling growth in the wider economy supporting the CMU agenda.

Supervisory convergence is an important aspect of the CMU and an important tool to remedy market fragmentation. The reinforcement of certain powers of the ESAs must be considered in tandem with the need to keep the day-to-day supervision at the local level. There should be a clear definition of the operational relationship between the areas of responsibility for oversight by the ESAs and day-to-day supervisory responsibilities by national supervisory authorities considering that the risk assessment flows directly from the hands-on experience in day-to-day supervision.

The added value of the ESAs lies in their sector expertise and the oversight of the national supervisors to improve co-ordination and ensure the convergence of supervisory opinions through peer group review and assistance with developing consistency to technical rule-making across Europe as well as to ensure harmonised application of those rules. The ESAs play an important role, not only in the protection of European consumers and investors, but also to enhance supervisory coordination and convergence and encourage the development of an efficient capital markets in Europe. It should be avoided that the existing ESAs framework is made more complex or burdensome for firms without clear benefits of integration or efficiency.

Efforts towards transparency and simplification remain unachieved

BusinessEurope welcomes proposals to improve the governance of the ESAs. It is key that the ESAs respect their mandate and better regulation principles. Improved governance structures will ensure that policy decisions can be made based on sound evidence and information, resulting in proportionate legislation. We welcome the strengthening of the stakeholder groups, but we strongly believe that further improvements are needed: they should be better balanced in order to make them more representative (including of the financial services industry and representatives of corporate end-users) and its members should be allowed to consult their constituencies and the organisations that nominated them. We also believe that the legislative proposal should go further and activate the possibility for the stakeholder groups to challenge ESA texts or decisions that arguably exceed their competence, following a single majority decision, and not a two-thirds majority. Moreover, the ability to challenge the legality of

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ESA texts or decisions should not be within the exclusive competence of the stakeholder groups. Hence the proposal should be clarified on that point.

It is important that the decisions made by ESAs are subject to independent oversight to ensure that technical decisions are made where there is strong evidence to make the case for change. We therefore welcome the establishment of the independent Executive Boards that are comprised of experienced and senior full-time members to support effective and impartial decision-making. However, the Board's decision-making process should favour a collegial approach through adequate checks and balances. In addition, the Board's mandate should include a specific mandate to ensure that regulations and technical guidance are formulated and applied in a fair and proportionate way, to avoid overly burdening financial and non-financial corporates which need to comply with these regulations.

The proposed set-up does not recognize the SSM reality for the Banking Union

Since the outbreak of the crisis, an extensive reform of financial services has made the financial system more resilient. Improved financial supervision through the ESAs, which has further been supported by the SSM in the Eurozone, has significantly improved cross-border independent oversight and contributed to greater financial stability.The Commission's proposal overlooks the substantial progress in harmonisation that has already been made. In this context, it is unnecessary to grant to the European Banking Authority (EBA) sanctioning powers and the power to override decisions taken by Competent Authorities (including the European Central Bank (ECB) for Significant Institutions) on outsourcing / delegation of material activities to third countries. It would also be misleading to grant the EBA the capacity to set EU-wide supervisory priorities against which Competent Authorities would be assessed. More broadly, no new institutional layer should overlap with the recent reforms establishing the Banking Union (the SSM and also the Single Resolution Mechanism (SRM)) or with forthcoming ones (e.g. the European Deposit Insurance System): the banking industry now needs a stable and clear institutional set-up.

Granting direct and indirect supervisory competences to the EBA will also blur the lines between the supervisory function and the role of regulation setter, which should be kept distinct to ensure the coherence and the clarity of the European institutional framework. At present these roles are clearly defined within the EU banking regulatory governance. On the one hand the EBA, a standard setter, looks after the consistency and the substance of the EU's Single Rulebook. On the other hand, the ECB, a supervisor, ensures the adequate and timely application of the technical standards and best practices developed by the standard setter.

Changes to the funding model unjustified and harmful to companies

In the absence of direct supervision from ESAs, we see no reason to change the funding arrangement to a direct contribution from the industry. Indeed, the legal basis for direct contributions paid by market participants to an authority which has only indirect supervision powers on them is questionable. Furthermore, any proposed change to the funding model of the ESAs should not lead to an overall increase of companies' contribution to the financing of EU and national supervisory authorities, also in view of the fact that, contrary to what is stated in the proposal, there are already some (partial) industry-paid models in some Member States. Direct contributions from the industry

would see companies charge those additional costs to end-customers which affects access to finance.

Additionally, it is vital that the European Commission, the Council and the European Parliament continue to bear the ultimate responsibility over the establishment and approval of the ESAs' budget, in order to ensure budget discipline and protect companies from double financing burdens arising from their continuing contributions to the funding of national supervisors.

New fund delegation arrangements with third countries should ensure a real level playing field while not placing undue restrictions on the ability of funds to delegate management activities to third countries

In the asset management sector, delegation of material activities is regulated at levels one, two and three. At level one the UCITS and AIFM directives require that the delegation of portfolio management is subject to principles of on-going due diligence towards delegates, approval by the national competent authority (NCA) of the delegates, equivalent supervision and business standards and cooperation between the supervisory authorities concerned in the case of delegation to third countries. The NCA approving the delegation remains responsible that a management company does not delegate the totality of its functions so as to become a letter-box entity. At level two the AIFM regulation further specifies requirements regarding the delegation of AIFM functions and in particular article 82 provides further details as to when a management company would become a letter-box entity. Further substance requirements in the member state of the management company is given at level three via the ESMA opinion on investment management dated 17 July 2017.

The new powers of EBA and ESMA on outsourcing / delegation of material activities to third countries entities must not create uncertainty and undue additional costs for EU and non-EU financial cross-border groups.

It is important that the European investor community and corporates continue to benefit from the large reserves of asset management expertise available in financial centres across the globe. New fund delegation arrangements should not place undue restrictions on the ability of funds to delegate management activities to third countries while ensuring a real level playing field with third countries with common rules effectively applied in a harmonised way across the EU.

More powers to supervise investment funds and approve internal models for solvency capital are unjustified and not evidence based

We do not support the Commission proposal to grant ESMA direct supervision of some very specific niche products (EuVECAs, EuSEFs and ELTIFs). An obvious development of this would be to extend these supervisory powers to include UCITS and AIFs. This would, in our view, hamper the development of these products which runs contrary to the aims of the Capital Markets Union. The responses to the ESMA consultation on the ESA review in spring 2017 have shown that a majority of stakeholders reject this vision. Furthermore, the Commission's own impact assessment does not convincingly make the case for such a change. The proposal also goes against the principle of subsidiarity. Indeed, in order to authorize and supervise these products, ESMA would need to confront the challenge posed by the wide variety of legal forms and legal regimes enshrined in the law of the various EU Member States as well as a wealth of national

case law. National supervisors are already familiar with the legal framework. They are more suitable and better equipped to continue this task.

BusinessEurope is also concerned about the introduction of additional powers proposed for EIOPA on the authorisation of internal models used to calculate requirements on solvency capital. This introduces an additional layer of authorisation within EIOPA that is over and above national level decision-making by national competent authorities. We are concerned that this introduces uncertainty to insurers, institutions for occupational retirement provision (IORP) as well as companies with occupational pension schemes, since this raises the risk of EIOPA vetting or revising national decisions. This adds significant business complexity, as this could mean having to involve multiple stakeholders in the internal model process and lengthened timescales for gaining the necessary authorisations that will have significant operational impacts for businesses.

Additionally, BusinessEurope questions the need for publication of stress tests' results by individual entity for insurers. These should only be made public at an aggregate level in view of the fact that Solvency II is already based on stress tests; individual company information is already available as part of the regular Solvency II reporting.

Concerns about integrating sustainable finance considerations into financial supervision

Sustainable developments are discussed in the Communication that accompanied the legislative proposals. Reference is made to the goals set by the United Nations 2030 Agenda for Sustainable Development, the Paris Agreement and the Sendai Framework for Disaster Risk Reduction. The Commission will present in early 2018 an Action Plan on sustainable finance with regulatory measures. It is also mentioned that the High Level Expert Group on sustainable finance established by the Commission pointed out in its interim report that environmental, social and governance (ESG) risks – for example, unprecedented and growing climate-related risks – are not yet properly integrated into financial risk assessment processes, and that the present review of the ESAs provides an excellent opportunity to clarify and enhance their role in assessing these risks in order to secure the long-term stability of Europe's financial sector and benefits for a sustainable economy at large.

As a first step towards a more comprehensive strategy, the proposals accompanying the Communication specifically require the ESAs to take account of environmental, social and governance factors arising within the framework of their mandate. For example, this will enable the Authorities to monitor how financial institutions identify, report, and address environmental, social and governance risks, thereby enhancing financial viability and stability. The ESAs can also provide guidance on how sustainability considerations can be effectively embodied in relevant EU financial legislation, and promote coherent implementation of such rules upon adoption.

In our view, the very idea that more regulation and supervision regarding ESG factors related to financial institutions and financial markets can enhance financial viability and stability can be challenged. Further, the ESAs are not experts in this field. The amendment of the Accounting Directive regarding non-financial information for some companies already obliges companies in the scope to report on non-financial information. BusinessEurope believes that the best way to improve ESG reporting is to enhance the dialogue between stakeholders and entities (for example on the purposes and scope of reporting) not further regulatory interference.

Data collection should not duplicate reporting requirements

Lastly, whilst we recognise the need for ESMA to collect data on transactions in financial instruments, it is important that this requirement does not result in duplicative reporting requirements for market participants, who in many cases are also required to supply similar data to national competent authorities. We suggest that one way to streamline the data collection process is to collect this data from national competent authorities to avoid duplication.

More powers to approve prospectuses would increase burdens

We do not support the proposal to give ESMA new powers to approve certain prospectuses, such as those issued by specialist issuers. Whilst it might be useful for certain cross-border operations, we strongly believe that the NCAs should remain the competent authority for the selected sectors. ESMA lacks competence on this matter, and any transfer of competences to ESMA would increase existing problems and further complicated an already complex process.

Need for clarification of the legal status of the Q&As

We very much welcome the proposal for systematic ex ante consultation (save exceptional circumstances) on Guidelines and recommendations. However, we regret that the proposal does not clarify the legal status of the Questions and Answers (Q&As) since they are being used extensively by the ESAs.

Indeed, the Q&As are not mentioned in article 8(2) of the founding Regulations as a regulatory power given to ESAs. There is a possibility open under article 29 (2) to "develop new practical instruments and convergence tools to promote common supervisory approaches and practices" but Q&As are not specifically defined or even mentioned in the ESAs Regulations. As a consequence, legally speaking, Q&As are not legal instruments and as such cannot be considered as binding measures. However, some regulators systemically apply Q&As, hence making them de facto binding without possibility of introducing any flexibility, even where justified, while other regulators consider them (rightly) as non-binding instruments. This is detrimental to Member States whose national regulator has a very prescriptive approach compared to others and lead to distortion of competition in the single market.

Consequently, we urge for a clarification of the legal status of the Q&As. Indeed, the non-binding nature of the Q&As should be officially recognized (based on the article 29 of the founding regulations) and imposed to NCAs in the view of having a harmonized approach at the European level.

We also suggest that ESAs (or at least NCAs) could consult before and after the Q&As. The strict minimum would be for ESAs (or NCAs) to communicate in advance on the questions they intend to address at the European level as currently the process how answers to questions are given is not transparent.

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