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Better Europe Public Affairs response to the European Commission's public consultation on the operations of the European Supervisory Authorities

5. To what extent are the ESAs tasks and powers in relation to guidelines and recommendations sufficiently well formulated to ensure their proper application? If there are weaknesses, how could those be addressed? Please elaborate and provide examples.

Guidelines and recommendations should help supervisors and industry apply legislation. However, guidelines and recommendations in terms of substance sometimes overstep the mandate given to the ESAs. In these cases, the guidelines are addressing interpretative or more political issues (e.g. the calculation of derivative positions under EMIR), which should be elevated to the Commission for consideration as a revision of Level 2 legislation.

Particular attention should also be given to the lack of legal value of Q&As. In some cases, not only the questions but also their answers are suggested by industry (see examples below) – and the ESAs are now even promoting this (see e.g. ESMA's Q&A suggestion form*).

It seems that some in the industry view the Q&As as the EU equivalent of the "no-action" staff interpretation letters common in the United States. However, in the EU these Q&As carry no legal value, and the interpretation of legislation could be challenged in national and EU courts. As such, suggesting manifestly biased Q&As will actually increase rather than reduce legal certainty.

Examples of industry suggesting Q&As to a supervisor (ESMA in these cases):
- AIMA-MFA, 2013: https://www.managedfunds.org/wp-content/uploads/2013/03/MFA-AIMA-Joint-Letter-Proposing-ESMA-EMIR-QAs-Final-Letter.pdf
- EDMA, 2016: http://www.edmae.org/wp-content/uploads/2017/01/EDMA-Position-Statement-Impact-of-Article-265-MiFIR-on-Trading-Venues-.docx

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*https://www.esma.europa.eu/sites/default/files/esma41-1104648009-877_qa.docx

6. What is your assessment of the current tasks and powers relating to consumer and investor protection provided for in the ESA Regulations and the role played by the ESAs and their Joint Committee in the area of consumer and investor protection? If you have identified shortcomings, please specify with concrete examples how they could be addressed.

The Joint Committee has improved its internal working over the past years, but the 22 December 2016 letter* to the Commission on PRIIPs clearly shows that divergences between the individual ESAs remain, and that part of the Board of Supervisors of one ESA can block adoption of a common JC advice.

This issue is closely related to the governance arrangements of the ESAs and should be addressed by revising decision-making structures in their individual Boards of Supervisors.

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*https://esas-joint-committee.europa.eu/publications/letters/esas-2016-81%20joint%20letter%20on%20rts%20on%20priips.pdf

7. What are the possible fields of activity, not yet dealt with by ESAs, in which the ESA's involvement could be beneficial for consumer protection? If you identify specific areas, please list them and provide examples.

The ESAs should be given more powers to remove authorization of products that are prone to consumer detriment or serve no meaningful societal purpose.

Even though some observers have made the case that the ESAs should ban certain morally or ethically "dangerous" products, the ESAs have always given this part of the ESA Regulations (Article 9) a rather strict interpretation, i.e. only considering intervention in the case of cross-border threats to financial stability (Article 18), and subject to non-intervention by the competent home NCA.

This limits what the ESAs can do to fulfil their mission to "enhance consumer protection" and therefore enhanced powers should be created in the ESA Regulations, before amending product-specific legislation. A first step would be to widen the definition of "dangerous" products beyond those with an impact on financial stability, to consider risks of consumer detriment (mis-selling) or even at societal utility of products.

Additionally, the ESAs could help setting minimum standards for NCA conduct of business supervision, including product checks and mystery shopping requirements, as well as a minimum organisational and legal framework to ensure member states have sufficient monitoring and enforcement capacity.

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*http://uk.reuters.com/article/uk-eu-financial-danger-idUKBRE90F17E20130116

9. Should the ESA's role in monitoring and implementation work following an equivalence decision by the Commission be strengthened and if so, how? For example, should the ESAs be empowered to monitor regulatory, supervisory and market developments in third countries and/or to monitor supervisory co-operation involving EU NCAs and third country counterparts? Please elaborate and provide examples.

Given Brexit and the UK equivalence decisions that will have to be taken by the EU, it will be even more important to strengthen the *monitoring* capacity of the ESAs related to equivalence decisions.

The European Court of Justice decision* on the Short Selling Regulation confirms that rather wide-ranging implementation powers can be delegated by the Commission to "agencies", and the Meroni doctrine should no longer be an argument to hold back delegation of equivalence decisions to the ESAs, or at least let the ESAs take the lead in equivalence decisions as arguably is already the case today.

Finally, note that the ESAs will also have to reconsider the role that observers play on their Board, as the UK in an observer status will significantly increase the economic weight of the observers on the Board as a whole.

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*https://curia.europa.eu/jcms/upload/docs/application/pdf/2014-01/cp140007en.pdf

11. Are there areas where the ESAs should be granted additional powers to require information from market participants? Please elaborate on what areas could usefully benefit from such new powers and explain what would be the advantages and disadvantages.

The ESAs are too reliant on NCAs to collect information from individual supervised entities that might be relevant for macro-level supervision, e.g. in the field of bank stability or technical stability of trading platforms. This information should be collected directly from market participants where relevant. To allow the collecting of data where required when reviewing sector-specific regulation, a process and legal basis should be foreseen in the ESA Regulations now.

Market information data should also be available for the general public, so that academics and others can scrutinize the ESA's work and decisions, and inform future policy-making. Examples where better data could have improved decision making are the Consolidated Tape and the calibration of the Position Limits regimes in MiFID.

13. In which particular areas of reporting, benchmarking and disclosure, would there be useful scope for limiting implementing acts to main lines and to cover smaller details by guidelines and recommendations? Please elaborate and provide concrete examples.

This is not a desirable development. Many smaller details in implementing acts remain of political nature and should be subject to scrutiny by the European Commission and/or the co-legislators. Examples include the treatment of netting of derivatives and the way that position reports under MiFID are established (e.g. the grouping of participants, or the thresholds for disclosure). It would also further exacerbate the problems of Level 3 legal certainty as detailed in the response to question 5.

19. In what areas of financial services should an extension of ESMA's direct supervisory powers be considered in order to reap the full benefits of a CMU?

The reality of the post-MiFID 1 internal market in investment services is that retail investment products are increasingly distributed on a cross-border basis, and that distributors are commonly selling products authorized in another member state. Consumers are encouraged to buy products that are not authorized by their national NCA and/or sold by intermediaries from another member state.

Several NCAs (FSMA, AFM and AMF, recently joined by BaFin) are pushing ahead with a ban on the distribution of products that provide no “investment” opportunity and are prone to mis-selling, such as leveraged Contracts for Difference and betting products constructed as forex transactions and binary options.

The fact that a selected group of NCAs move ahead of ESMA is an indication that there is demand for expanding ESMA’s powers to direct supervision over (retail) investment products.

Such powers should go far beyond the current (MiFID) provisions which only allow banning of products that create an immediate cross-border systemic threat to financial stability, as argued in the answer to question 7.

22. To what extent do you consider that the current governance set-up in terms of composition of the Board of Supervisors and the Management Board, and the role of the Chairperson have allowed the ESAs to effectively fulfil their mandates? If you have identified shortcomings in specific areas please elaborate and specify how these could be mitigated.

The decision-making process inside the ESAs should be reformed to remove incentives to defend narrow national interests, provided a strict separation of political and technical issues is applied.

The governance problems within the Boards of Supervisors, in particular when Member States defend national interests rather than a European perspective, seem to be concentrated in decisions related to competences that are new in the post-Lisbon ESA setup, such as the drafting of Technical Standards (Level 2) and sanctions and measures aimed at individual Member States. To deal with this matter, the governance of the ESAs should evolve to allow for European interest-based decision-making, by introducing softer majority requirements or indeed setting up an Executive Board partly or fully consisting of “denationalized” individuals such as ESA staff and independent members.

However, this setup does require a more rigorous approach to the separation of political and technical decisions. From a purely democratic perspective, it is unacceptable that political or interpretative decisions within the Level 2 framework are taken by executive staff of the financial supervisors (whether NCA or ESA). These decisions should be taken in the appropriate political process (Level 1) or at the very least by the European Commission under delegated powers. Even though formally the Commission retains the delegated law-making powers in Level 2, in reality the margin for manoeuvre is very limited for the Commission, once the technical ESA advice has been delivered.

Member States in general have a stronger impact on Level 2 decisions than the European Parliament. This is because in addition to the formal rejection powers (which the EP also has), the Member States 1) sit on the expert groups (e.g. EGESC) that advise the Commission during the drafting stage of delegated legislation and 2) those standards are based on ESA Technical Advice endorsed by the NCA-controlled Boards of Supervisors.

As an example, in the case of MiFID, some standards (related to inducements and position limits) were modified during ESMA’s internal drafting process to avoid the risk of Board of Supervisors rejection, whereas Parliament could only exert its influence through (threatening) a formal rejection of the Level 2 standard (a right that the Member States also have). While the Parliament did have regular written exchanges and personal meetings with the Commission and ESMA before adoption of the Delegated Acts by the Board of Supervisors, its influence was much more limited,.

Finally, some stakeholders advocate for greater transparency of Boards of Supervisors meetings as a way to improve Board governance. I believe this is a mistake. Increased transparency of the Board of Supervisors process, most importantly publishing draft documents ahead of the Board’s approval, is NOT a solution to improve Board governance. Just like the four-week stakeholder consultation introduced as part of the Better Regulation strategy, these mechanisms will only worsen the equilibrium between industry and other stakeholders, as only industry participants are able to benefit from additional consultations (even if they are extremely short), and the industry input will put pressure on member states to stronger defend their national interests when acting as members of the Board of Supervisors.

23. To what extent do you think the current tasks and powers of the Management Board are appropriate and sufficient? What improvements could be made to ensure that the ESAs operate more effectively? Please elaborate.

As argued above, in a way the governance problems in the ESAs came to be after the expansion beyond 3L3 work. If the ESAs still had been the 3L3, the governance issues would have not been as pressing as they are today. Arguably, for a strict separation of powers, the ESAs could have been created *in addition* to the 3L3, with the 3L3 Boards consisting of NCA representatives, and the ESAs as autonomous EU agencies.

As there is no way back, giving the Management Board more powers is the most sensible way of correcting this, provided that the Management Board (or Executive Board) is empowered to take decisions on matters that otherwise would lead to NCAs defending positions of national interest.

25. To what extent do you think would there be merit in strengthening the role and mandate of the Chairperson? Please explain in what areas and how the role of the Chairperson would have to evolve to enable them to work more effectively? For example, should the Chairperson be delegated powers to make certain decisions without having them subsequently approved by the Board of Supervisors in the context of work carried out in the ESAs Joint Committee? Or should the nomination procedure change? What would be the advantages or disadvantages? Please elaborate.

In line with the above, the Chair of an ESA and the independent members should have a strong influence on all decisions that do not require specific NCA expertise, to guarantee the defence of pan-European interests. On such interpretative matters, e.g. related to the implementation of legislation, Member States should use the formal Level 2 scrutiny process as the main channel to exert their influence on the outcome.

26. To what extent are the provisions in the ESA Regulations appropriate for stakeholder groups to be effective? How could the current practices and provisions be improved to address any weaknesses? Please elaborate and provide concrete examples.

In the stakeholder groups as well as the standing committees, industry representatives continue to be better prepared in terms of data, presentations, and studies than non-industry and academic representatives. This is because non-industry stakeholders do not have the resources that industry representatives put into preparing their participation in the stakeholder groups, despite the appointment formally being on an individual basis. In addition, non-industry stakeholders will be reluctant to apply if they are not adequately compensated for research expenses that allow them to work on an equal footing with much better resourced industry members. An alternative to direct funding of non-industry stakeholders could be additional in-kind assistance from the relevant ESA secretariat.

27. To what extent has the current model of sector supervision and separate seats for each of the ESAs been efficient and effective? Please elaborate and provide examples.

The three ESAs having different seats and legal structures is an immediate consequence of their set-up as successors of the 3L3. This consultation focuses on the question of whether the current sectoral separation should be replaced by a functional (prudential/conduct) separation, and whether EBA-EIOPA cooperation would be an intermediate step towards a twin peak approach.

However, a more interesting question is whether the EBA-ECB-SSM setup should be replicated in the two other sectors. As micro-prudential supervision has been moved from national central banks to the SSM framework, the scope of EBA's role is very clear. In securities, the lines are more blurred, with ESMA directly supervising certain financial entities such as CRAs and hedge funds. And in insurance and pensions, there seems to be little political appetite for integration of supervision.

The issue is therefore not to discuss whether to merge EBA with EIOPA, but ensure that any steps towards single/twin peaks do not make it impossible to revisit the split of supervisory competences between member states and the European level, including over time by moving towards a pan-European single supervisor in markets, insurance and pensions, once there is political support for such a move.

28. Would there be merit in maximising synergies (both from an efficiency and effectiveness perspective) between the EBA and EIOPA while possibly consolidating certain consumer protection powers within ESMA in addition to the ESMA's current responsibilities? Or should EBA and EIOPA remain as standalone authorities?

Yes. Due to the nature of the issues discussed, ESMA is in practise already taking a leading role in the Joint Committee. The lack of a strong legal basis for decisions inside the Joint Committee, as evidenced by the inability to publish an advice to the Commission on PRIIPs (see reference in the answer to question 6), should be addressed.

However, the Commission should ensure that ESMA's increased powers are matched with appropriate resources. Both the SEC and the CFPB employ hundreds of staff for market surveillance tasks. Creating a European Financial Consumer Protection "Authority" within ESMA without sufficient resources will be a political Trojan Horse. It would create the illusion that consumers are protected whereas there is not sufficient firepower to follow-up on anything beyond responding to scandals.

Especially given the increased role of retail investments as part of the Capital Markets Unit strategy, it is important to show consumers of financial services that the EU is committed to making the internal market work for consumers by strengthening ESMA's powers and capacities.

For consumers, (economically) equivalent products should be regulated and supervised in a similar way. The is not the case today – there are significant differences between product distribution under IDD and MiFID, between UCITS and PRIIPs KI(I)Ds, and between private pensions and life insurance products. The current review of the ESMA Regulation should be used to create a legal basis framework allowing for the introduction of new intervention powers when these vertical Regulations (MiFID, IDD, PRIIPs) are reviewed, e.g. to ensure intervention on financial products that carry non-systemic risks (see question 7 and 19).

Citizens acting as consumers would also benefit from a strengthened role of non-industry stakeholders on expert groups and Stakeholder Groups (see question 26).