Deutsches Aktieninstitut

European Supervisory Authorities Neither Need More Competences Nor a New Funding Structure

The ESA review should rather focus on making the ESAs mandate more concrete and on improving stakeholder participation

Deutsches Aktieninstitut's response to the public consultation of the European Commission on the operations of the European Supervisory Authorities, 16 May 2017

Introduction and Background

This position paper summarizes the response of Deutsches Aktieninstitut to the public consultation of the European Commission on the operations of the European Supervisory Authorities.[1]

Please note that comments made in this paper relate exclusively to ESMA s` work, if not indicated otherwise, since the members of Deutsches Aktieninstitut are primarily affected by ESMA`s activities.

1 Public consultation of the European Commission on the operations of the European Supervisory Authorities, https://ec.europa.eu/info/finance-consultations-2017-esas-operations_en.

Q1. In general, how do you assess the work carried out by the ESAs so far in promoting a common supervisory culture and fostering supervisory convergence, and how could any weaknesses be addressed? Please elaborate on your response and provide examples.

a) Supervisory convergence under the current European system of financial supervision

In a common market there is indeed a good argument for supervisory convergence so that the common rules are applied without significant differences regarding the scope and the economic impact. The ESAs rightly play a role in that process.

On the other hand, it has to be carefully evaluated if supervisory convergence is necessary for every detail of supervisory practices. There have been valid reasons for the current EU supervisory structure to be shaped in a way that respects national particularities by granting national competent authorities (NCAs) to be largely involved in the supervision of EU Financial Markets regulation: NCAs are closer to the national markets, they are better placed to know its specificities. It should also not be underestimated that language barriers can still play an important role when it comes to interactions between the supervisor and market participants. In addition, NCAs also do have sufficient powers to take action against individual entities in breach of Union law with widely harmonized supervisory measures and sanctions that can be applied. The current system lastly provides for checks and balances in the governance system of each ESA which ensures through the involvement of NCAs that the subsidiarity principle is incorporated into EU supervisory practices. In addition, it is much too early to come to a final assessment of the role ESMA played both for defining details of level 2 regulation and the application of common rules. Indeed, the experience we have made so far with ESMA is mixed: On the one hand, ESMA accomplished an enormous workload regarding level 2-measures in a relatively short period of time. On the other hand, there is no track record regarding the question whether the instruments of ESMA to coordinate NCAs supervisory practices are sufficient. In addition, there are examples where ESMA went beyond the level 1 mandate or has developed measures which in effect imposed significant bureaucratic burdens for listed companies. These examples rather show that re-allocating powers to ESMA at the expense of NCAs may have drawbacks.

As a consequence, it is at least much **too early to decide on major changes regarding the allocation of competences** between NCAs and the ESAs, in particular ESMA. We are rather of the opinion that the **existing instruments should be given time to work and to concentrate the work on ESA reform on other issues** where evidence about deficits is more obvious (see below).

b) Crucial issues to be addressed for improving the functioning of the ESAs

From Deutsches Aktieninstitut`s point of view, unfortunately the consultation questionnaire does not consider to a sufficient extent the crucial issues regarding the operations of the European Supervisory Authorities. In our opinion, the main issues to be addressed are firstly, to ensure an appropriate balance between level 1 and level 2 and secondly, to improve the governance and accountability of ESAs` activities.

Appropriate balance between level 1 and level 2

From our perspective, the major issue concerning the operations of the ESAs lays mainly in a **lack of appropriate balance between level 1 and level 2 legislation:**

It can be observed in a lot of financial services regulation that the amount of provisions in legislative proposals delegating issues on level 2 has been increased over the past years, thereby often also delegating crucial questions to be tackled on level 1 to level 2.

Legislative bodies of the EU, however, shall ensure that all crucial political issues of the respective issue at hand are being negotiated on level 1. The temptation of overcoming possible deadlocks in level 1 negotiations by deferring discussions on some key contentious matters to level 2 needs to be avoided. Otherwise, level 1 leaves too much room for interpretation thereby creating a situation where ESAs mandate to only supplement the level 1 text becomes blurred. There are cases, where this has resulted in an extremely wide interpretation of the unclear terms contained in the level 1 text by the ESAs – naturally taking the supervisor`s and not the legislator`s perspective.

We have observed this e.g. in the context of the wide interpretation of the term “transaction” by ESMA under the implementation process of the Market Abuse Regulation. We also currently observe it regarding the potential level-2-measures on a common Electronic Reporting Format for annual financial reports (ESEF) in the context of the Transparency Directive.

The examples show, that ESMA’s interpretations may lead to impracticable results for companies affected, which is possible because the level 1 text lacks precision. Therefore, Deutsches Aktieninstitut stresses the **importance that the delegation of power must be clear, precise and detailed and may only aim to supplement certain non-substantive elements of the legislative act**.

Governance and accountability aspects

Governance and accountability aspects should not be neglected in the upcoming ESA review. The past has shown that ESAs have on several occasions overstepped

the mandate conferred to them on level 1. An illustrative case in point is EBA's unsolicited, but continuous efforts to erode the exemption of own funds requirements of banks for so called CVA risks granted in the CRD IV/CRR for uncollateralized hedges of non-financial companies through a regulatory guideline.

Improvement in those cases is therefore needed.

Importance should especially be given to enhance scrutiny of ESAs' activities by the European Commission, the European Parliament and the Council in order to better being able to **bringing the results of ESAs' work in line with the legislator`s will**. The European Institutions are directly involved in many acts and thus ultimately assume political responsibility, e.g. for ESMA`s activities. The European Institutions will however only be able to live up to their political responsibility if they are provided with adequate tools to thoroughly scrutinize ESMA`s activities.

Last, not least, **stronger** and more balanced **stakeholder engagement** is needed in the process in order to ensure that market participants' needs are better reflected in ESAs measures.

Accountability and governance aspects will be elaborated further in detail in responses to questions of the questionnaire, especially under question 32.

Q2. With respect to each of the following tools and powers at the disposal of the ESAs:

peer reviews (Article 30 of the ESA Regulations);
binding mediation and more broadly the settlement of disagreements between competent authorities in cross-border situations or cross-sectorial situations (Articles 19 and 20 of the ESA Regulations);
supervisory colleges (Article 21 of the ESA Regulations);

To what extent:
a) have these tools and powers been effective for the ESAs to foster supervisory convergence and supervisory cooperation across borders and achieve the objective of having a level playing field in the area of supervision;
b) to what extent has a potential lack of an EU interest orientation in the decision making process in the Boards of Supervisors impacted on the ESAs use of these tools and powers?

Please elaborate on questions (a) and (b) and, importantly, explain how

any weaknesses could be addressed.

Peer Review

We regard the "peer review" described in Art. 30 as a useful instrument to align supervisory practices and establish a supervisory "best practice" across the EU. The review process may help to form a common understanding on newly issued regulation, to avoid overshooting regulatory practice and – what also appears to be important – to uncover problems with the level 1-text itself as well as with its day-to-day application by NCAs and supervised entities. The latter could thus help to improve level 1-legislation by creating some kind of an informal feedback loop.

However, for the review process to work efficiently we would appreciate if ESAs were obliged to solicit comments of stakeholders when drafting EU peer reviews in order to have other case-specific comments than those coming from the reviewed authorities themselves. The ESMA Principles on stakeholder engagement in peer reviews point into the right direction, but need to be strengthened and improved.

We further would like to express our concerns regarding the peer review of guidelines and recommendations in accordance with Art. 30 no. 2(b). Guidelines and recommendations are not legally binding by definition and therefore they are not enforceable. However, it seems to be at least an intention of legally binding force deriving from guidelines and recommendations on the basis of its wording and terms. We believe it would be more appropriate to limit the scope of peer reviews to the breach of Union law, which include regulatory technical standards and implementing technical standards but not to guidelines and recommendations.

Q3. To what extent should other tools be available to the ESAs to assess independently supervisory practices with the aim to ensure consistent application of EU law as well as ensuring converging supervisory practices? Please elaborate on your response and provide examples.

No comment.

Q4. How do you assess the involvement of the ESAs in cross-border cases? To what extent are the current tools sufficient to deal with these cases? Please elaborate on your response and provide examples.

No comment.

Q5. 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.

a) ESA guidelines

Guidelines can be issued with a view to establishing consistent, efficient and effective supervisory practices within the ESFS, and to ensuring the common, uniform and consistent application of Union law. Although guidelines are legally not binding, they cannot and will not simply be ignored by national competent authorities nor by the supervised entities. As a consequence, they have de facto binding effects.

The case of ESMA guidelines may be illustrative in that respect: There are indeed very few instances in which national competent authorities have declared their non-compliance with the guidelines.

Against the background of the above mentioned far reaching effects, we feel the ESA regulation could be altered in some respects.

First, the competence to issue guidelines should be stated in a less general manner, so that ESAs make restraint use of guidelines and recommendations and, if they are issued, take a rather principle based approach. Otherwise there is the risk that guidelines are used for standard stetting "through the back door" and without a clear legal mandate on level 1. It should not be the role of the ESAs as supervisory authorities to act as the legislator. Also, Art. 16 of the ESA regulation does not only mention the purpose to establish *consistent*, but also *efficient and effective* supervisory practices. In this context, it should also be taken into account that national specifics still exist and therefore a certain flexibility is required in order to allow for an efficient and effective supervisory practice. Too many and too detailed guidelines and recommendations bear the risk that national authorities and market participants will face difficulties to comply with them in practice. We would therefore prefer that guidelines can only be issued on the basis of clear mandate within the level 1-regulation.

Second, a clearer distinction has to be drawn in the ESA-regulations under which circumstances guidelines on the one hand and RTS on the other hand can be issued. Regulatory Technical Standards are intended to ensure consistent harmonization and play the key role for supervisory practices. In order to avoid overlapping competences, it could e.g. be included in the ESA regulations that only in areas not covered by RTS, ESAs are granted the power to issue guidelines and recommendations, as currently only stated in Recital 26 of ESA regulations.

Third, against the background of the far reaching effects, greater stakeholder engagement needs to be guaranteed. We suggest that every guideline needs to be consulted among market participants in a transparent way. Currently there is some discretion left for the ESAs whether a consultation has to take place. In addition, there should be reflection on granting longer consultation periods (up to 12 weeks). Last, the process of the adoption of guidelines/recommendations has to form part of the Better Regulation Agenda of the EU Commission. They e.g. need to be published well ahead of the implementation of the legislation to avoid situations as experienced in the context of the Market Abuse Regulation where the guidelines were published only after the application date of the regulation.

b) Q&A

Besides guidelines and recommendations, we would like to address the issue of Q&As, which are largely used by ESAs to provide assistance in the interpretation of the level 1 and level 2 text. Under EMIR, market participants faced huge administrative burdens to implement the respective compliance processes due to frequent updates of the **ESMA Q&As**, exacerbated by their classification as binding part of the regulatory framework instead of an explanatory tool by some local regulators. The same problem arises recently under MiFID II/MiFIR, where the work on Q&A's has just started. A recent example for such controversial issues is the interpretation of DEA (direct electronic access to trading venues).

We understand that requests for clarification of certain rules coming from market participants were a key reason for the permanent updates of the Q&A:

- However, the legal character of the Q&A is ambiguous. While many market participants (and also regulators) regard the Q&As – correctly, in our opinion – as not legally binding explanations providing guidance for the coherent compliance, others see them as integral part of the regulation. Due to these diverging perceptions the Q&As are applied differently within the EU, which forestalls a level-playing-field.

- In addition, market participants have no possibility to comment on the ESMA Q&As with regard to their practical feasibility. Improvements regarding market consultation should thus be made having in mind that the Q&A – though non-binding – will have an impact on the behavior of market participants.

- In the same vain, it is problematic that the implementation periods for the Q&As changes are not clearly defined. It is very challenging for market participants to apply the updates immediately, lacking other timing information.

As a complementary step, the legislator should clarify that the instrument Q&A is not a legally binding instrument but guidance, and in addition always provide

companies with enough time to implement the respective adjustments following the updates (e.g. 6 months after the publication of the update). Nevertheless**, Q&As should be issued reluctantly and on a principle based approach for the same reasons as for guidelines and recommendations (see above).**

Q6. 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.

Before starting a discussion on a potential extension of ESAs' powers as regards to consumer and investor protection, it has to be borne in mind that first and foremost, this consultation and the review should focus on potential improvements of the current system in terms of accountability, governance and appropriate balance between level 1 and 2. Further explanations can be found under Q1 and Q32. Only after having remedied the current shortcomings it should be reflected on possible extensions of ESAs' powers.

From Deutsches Aktieninstitut's point of view the current rights of ESAs with respect to consumer and investor protection are already sufficient. The role of the ESAs is and should remain to encompass regulatory convergence, in particular where a lack of convergence would be a real threat to financial stability or the functioning of the capital markets.

Nevertheless, we urge the legislator as well as the ESAs to implement a consumer and investor protection which is more evidence based. E.g. detailed transparency requirements which are laid down for instance in the PRIIPs-Regulation or the investor protection rules under MiFID-II should better reflect economic research on what information consumers and investors really need for their investment decision. Otherwise, we see the danger that too much information is required which could not be used by consumers or investors adequately and which leads to a huge bureaucracy on the side of the product supplier.

It has also to be noted that most of the more recent financial regulation has been justified (at least also) with the argument of investor or consumer protection. It could therefore even be argued that the Art. 9 of the ESAs regulations is redundant to some extent as the mandate of consumer/investor protection is already incorporated in Union law.

It is and should however stay the task of national competent authorities to ensure that the EU legislation is properly applied bearing in mind the national specifics of financial markets and market participants. In addition, NCAs also have sufficient powers to take action against individual entities in breach of Union law with widely harmonized supervisory measures and sanctions that can be imposed.

Overall, the division of labor between the ESAs and the NCAs has proven to be adequate. ESAs mandate should stay to encompass supervisory convergence (with the existing tools), the mandate of NCAs should be the enforcement of Union law vis-a-vis market participants.

We therefore neither miss a field of activity for the ESAs (rather the contrary, Q6), nor is there an objective reason to change the ESAs mandate or widen its direct supervisory powers (Q7). In our view, additional ESA powers could result in unclear competences as well as double supervision and, thus, bear the risk of additional bureaucracy being created. This would not fit to the critique regarding overstretching mandates by ESAs and provide too detailed level 2- and level 3-measures.

Q7. 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.

Please refer to Q6.

Q8. Is there a need to adjust the tasks and powers of the ESAs in order to facilitate their actions as regards breach of Union law by individual entities? For example, changes to the governance structure? Please elaborate and provide specific examples.

No comment.

Q9. 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.

For the industry it is crucial that processes and responsibilities are explicit, practical and effective.

As the equivalence decision is originally taken by the EU Commission, the subsequent decision-making power should stay with the EU Commission. However, as equivalence includes close cooperation between supervisory authorities in the third country and the EU, the ESAs should support the EU Commission in constantly monitoring and supervising third country regulation and supervision. That way resources could be used more efficiently and synergies would be created. Yet, this should stay an advisory position and not become a decisive role.

Moreover, irrespectively of the responsibilities of the different EU institutions involved, the procedure needs to become more transparent, quicker and more streamlined. Although equivalence decisions take into account many details/rules and thus have to be conducted thoroughly, unnecessary longitude and complexity should not deter third countries from applying.

In addition, no improvements can be achieved, if the EU Commission does not take into account the recommendations of the ESAs. One example is the equivalence under AIFMD. In this regard, the EU Commission's equivalence decision is built on a recommendation from ESMA which evaluates the regulatory regime of the third country in question. A number of countries have already gone through this process, and ESMA has given the EU Commission a positive recommendation, e.g. for Canada, Guernsey, Japan, Jersey and Switzerland. However, the EU Commission has not yet granted the third-country passport under AIFMD.

Q10. To what extent do you think the ESAs powers to access information have enabled them to effectively and efficiently deliver on their mandates? Please elaborate and provide examples.

From the perspective of a supervised entity it is not that important who collects data provided the data to be collected is not too voluminous, does not create red tape and provided that it is clearly regulated which data will be asked for (see below for an example of overly burdensome data collection requirements).

It has definitely to be avoided that data has to be submitted twice, i.e. to a NCA and ESMA. Also, it has to be avoided that ESMA and/or NCAs have too much discretion as to which kind of data can be collected. However, we see no severe problems with the current regime from an organizational perspective. It is rather preferable that national competent authorities play the key role in data collection, because they know better the particular situation of the supervised entities and – what should not be neglected – speak the same language as the supervised entities.

Besides the question on who collects the data it is also important to address the question on the volume/scope of data to be collected. Data collection is only justified where there is an objective need of increased market transparency in order to allow for proper supervisory processes. Recently, in many areas, e.g. EMIR trade repository reporting, data collection exercises are highly bureaucratic and resulted in a huge additional burden for market participants requested to deliver the data. Furthermore, the EMIR reporting regime clearly shows that a too broad and detailed approach reduces the data quality and creates massive application problems for both NCAs and market participants. The rationale for many reporting fields, e.g. the time stamp which is not possible to determine in OTC trading, are difficult to comprehend. Some of the current data problems, however, result from the opposite: ESMA in the beginning of the process should have consulted all trade repository providers and come up with a common set of field definitions which would have made matching across repositories more efficient. That problem was

not due to a lack of powers, but of coordination with market participants. We would in general request to apply more of the latter in future. Therefore, we request ESAs to justify the data requirements with regard to supervisory purposes and to communicate these reasons to market participants. Information requirements, which do not fit these requirements, should be abandoned.

Q11. 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.

No. As laid in our response to Q10 above, the data collection process currently suffers rather from too detailed and bureaucratic requirements, and a lack of coordination than from an inefficient allocation of competences among the ESAs and the NCAs.

Before starting a discussion on a potential extension of ESAs' powers as regards to access to information, the current system regarding accountability, governance and appropriate balance between level 1 and 2 should be evaluated. For further explanations, please see our answers to Q1 and Q32.

We suggest ESAs should concentrate on unfinished tasks instead, like the provision of data about overall market trading activity per derivative asset class, which is required to allow firms to calculate relevant threshold tests for MiFID compliance or the above-mentioned (Q10) deficiencies in matching rates between trade repositories. In addition, we are still waiting for a consistent overview of market activities out of trade repository data for the wider public, which we understood was one of the goals of the EMIR reporting obligation.

Q12. To what extent would entrusting the ESAs with a coordination role on reporting, including periodic reviews of reporting requirements, lead to reducing and streamlining of reporting requirements? Please elaborate your response and provide examples.

Deutsches Aktieninstitut appreciates that the EU Commission raises the issue of undue, overlapping or voluminous reporting requirements for market participants. Speaking for listed companies, it is really an important issue to reduce compliance costs and make the use of capital markets more attractive from a legal as well as a practical perspective.

However, the issue of overlapping and voluminous reporting requirements is to a significant extent an issue of level 1-legislation, which ultimately defines the requirements or at least the scope for level 2 measures prepared by the ESAs.

In implementing the political will of level 1 the ESAs have two different sorts of tasks. On the one hand, there are examples where they went too much into details and/or in effect overstretched the level 1-mandate. On the other hand, non-binding clarifications to (unclear) level 1-textes can be helpful to clarify compliance duties.

Our request would therefore be twofold. First, more details should be decided on level 1 even if this might lead to the fact that negotiations will take more time. Second, for level 2 measures the ESAs should avoid additional bureaucracy as far as it is possible and they should not go beyond the mandate of level 1.

Q13. 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.

Please refer to Q14 and Q15.

Q14. What improvements to the current organisation and operation of the various bodies do you see would contribute to enhance enforcement and supervisory convergence in the financial reporting area? How can synergies between the enforcement of accounting and audit standards be strengthened? Please elaborate.

From our perspective there is no need to equip ESMA with additional powers with respect to accounting, auditing and enforcement of financial reports beyond the status quo – rather the opposite is the case. This holds true for both the endorsement of the IFRS and the enforcement of financial reporting. Regarding the latter Member States have – based on their legal traditions and their market specifics – developed different models that ensure that listed companies comply with the rules and that auditors perform their tasks in a proper manner.

As a consequence, the legislators/regulators should accept the fact that European companies already now take financial reporting very seriously. Thus, there is no evidence for significant compliance deficits and a significant potential misinformation of investors. Investors of European listed companies can already be sure that the companies are transparent and that the reliability of accounts is ensured by various (overlapping) institutional settings. Even less there is evidence that a potential deficit needs to be tackled at European level.

Against this background, we don't see any additional need for further action and in particular for any additional ESMA involvement in auditing, accounting or enforcement issues. Rather the opposite is true.

Q15. How can the current endorsement process be made more effective and efficient? To what extent should ESMA's role be strengthened? Please elaborate.

What holds true for the enforcement (see Q. 14) is also true for the endorsement of International Accounting Standards. The endorsement of newly issued or amended standards is a task that has to be done very thoroughly. In our opinion, EFRAG fulfills this task in a very efficient and effective way and, thus, we don't see any necessity to change the endorsement with regard to EFRAG's work.

However, once a final Endorsement Advice has been issued by EFRAG, it takes the EU Commission quite long to finally endorse new and amended Standards and Interpretations. We therefore see the need to speed up the endorsement process. In our view, this can be achieved – for example – by simultaneously starting discussions and translation instead having a purely sequential process. By making the endorsement process shorter, certainty about future changes among prepares would also be enhanced.

ESMA's perspective as a regulator should – in our view – not to be involved in standard setting, since there might be a conflict of interests. This conflict of interests results from ESMA's role as a supervisor and could indicate a preference towards enforceable standards rather than standards that provide useful information to investors. One possible outcome may be that the endorsement process would prefer comparability over relevant information. In the sense of "Checks and Balances", we think that ESMA should be involved only in the enforcement of existing standards (within the EU) but not in the transformation of standards issued by the IASB into European law.

Against this background, we are concerned that ESMA has already used the existing competences to become more and more a de facto standard setter in the field of reporting and accounting. Examples are the issuance of opinions on IFRS standards that have not yet come into force (e.g. ESMA's statement on the implementation of IFRS 15), the issuance of the Guideline on Alternative Performance Measures (APMs), and to a smaller extent the database of enforcement decisions (which are taken by national enforcement authorities).

Even if ESMA's action in this field is non-binding, ESMA's publications might in fact have a binding effect on preparers. One might therefore say that ESMA's action – effectively – endorses a certain accounting treatment without passing the endorsement process. In essence, this means that legislative competences are partly taken over by the supervisor.

In addition, we are of the opinion that ESMA's statement/interpretations on the application of accounting issues de facto undermine principles based standard setting. ESMA should therefore refrain from issuing more interpretations on issues regarding IFRS accounting. In our view, the interpretation of and clarification on the application of IFRS accounting standards should be the sole responsibility of the IASB and IFRS IC, respectively.

Overall, ESMA's role in accounting, auditing and enforcement should rather be reduced than enhanced.

Q16. What would be the advantages and disadvantages of granting EIOPA powers to approve and monitor internal models of cross-border groups? Please elaborate on your views, with evidence if possible.

No comment.

Q17. To what extent could the EBA's powers be extended to address problems that come up in cases of disagreement? Should prior consultation of the EBA be mandatory for all new types of capital instruments? Should competent authorities be required to take the EBA's concerns into account? What would be the advantages and disadvantages? Please elaborate and provide examples.

No comment.

Q18. Are there any further areas were you would see merits in complementing the current tasks and powers of the ESAs in the areas of banking or insurance? Please elaborate and provide examples.

No comment.

Q19. 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?

Again it has to be noted that before talking about conferral of additional powers to ESMA, deficiencies of the current system need to be remedied. Concrete suggestions are being provided under Q32, but also e.g. under Q26.

We do not see why the perspective of the UK leaving the common market should change the rationale for the allocation of direct supervisory powers. Basically the European system of financial system currently rests on three pillars:

1) Harmonized legal standards for European regulated entities ensure that users of financial services and the general public can trust in the integrity of capital markets and in that misbehavior will be sanctioned.
2) This makes it possible to rely on the principle of reciprocity which mainly takes the form of the EU passporting. I.e., if a certain activity is supervised

by one NCA, the activity can be performed EU wide. Only for very particular circumstances, there is already now the possibility to bring together the NCAs of more than one country in colleges of supervisors.

3) For third country market participants there are additional third country regimes that also incorporate the principle of reciprocity.

From our perspective the system has worked well so far. At least, it is too early to review it given relatively little experience.

Q20. For each of the areas referred to in response to the previous question, what are the possible advantages and disadvantages?

No comment.

Q21. For each of the areas referred to in response to question 19, to what extent would you suggest an extension to all entities or instruments in a sector or only to certain types or categories?

No comment.

Q22. 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.

No comment.

Q23. 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.

No comment.

Q24. To what extent would the introduction of permanent members to the ESAs' Boards further improve the work of the Boards? What would be the advantages or disadvantages of introducing such a change to the current governance set-up? Please elaborate.

No comment.

Q25. 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.

No comment.

Q26. 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.

Decisions should be based on the broadest possible input. In this context, we appreciate that expert and stakeholder groups (SG) have been established in each ESA. Nevertheless, we still see room for improvement regarding greater industry involvement and adequate opportunity to comment on level 2/level 3.

Recommendations

1. Better engagement of ESAs with stakeholders, especially in the framework of the Consultative Working Groups to the Standing Committee as regards to ESMA:

    a) There is not sufficient transparency regarding the group meetings: no information is being published about the meetings (even no dates of meetings), no documentation is being disclosed (even no agendas), no outcomes or next steps are being announced (e.g. Consultative Working Group to ESMA's Corporate Finance Standing Committee). It is emphasised that documentation is strictly confidential, meaning it cannot be shared with anyone outside the CWG, and that the CWG

members have been appointed in their personal capacity and therefore should not discuss with outsiders or within the trade associations the proposals. Those deficiencies should be remedied.

b) There is also no sufficient degree of transparency on how members of the Consultative Working Groups are being selected. There is no explanation on what categories of experts / stakeholders are being sought and in what proportions. While on the webpages of ESMA Secondary Markets Stakeholder Group there is a list of members with the CVs and information in which category they have been selected, on the website of CWG there is only a list of names and what company / institution they work for but no other details. We would like to see more transparency in that respect.

2. More balanced representation of interests is needed

   We would like to see a **balanced representation** of stakeholders: while in recent years' investors and financial services consumers have become overrepresented on ESMA stakeholder and consultative WGs, there is often a lack of representation of non-financial companies.

3. Improvement of the timeline

   To further improve stakeholder consultation and engagement, it would be useful to ensure longer consultation times, e.g. 12 weeks.

Q27. 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.

No comment.

Q28. 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?

No comment.

Q29. The current ESAs funding arrangement is based on public contributions:
a) should they be changed to a system fully funded by the industry;
b) should they be changed to a system partly funded by industry?
Please elaborate on each of (a) and (b) and indicate the advantages and disadvantages of each option.

Ad a)

Deutsches Aktieninstitut strongly opposes to change the current ESAs funding model to a system fully funded by the industry.

The current model most importantly empowers the Budgetary Authority (European Parliament and Council) to exert budgetary control over the ESAs and thereby ensures that ESAs can be held accountable. It guarantees democratic control which would otherwise be missing. At present, better control and accountability of the ESAs would be needed (see above). The current funding model is a tool to control the ESAs. Should this possibility be reduced or even eliminated, it would be necessary that the EU-Institutions are compensated by at least being enabled to take the political responsibility for the acts of ESAs as it is eg the case of the German NCA (BaFin).

Even though being independent, BaFin nevertheless is also part of the Federal administration. It is hence subject to the legal and technical oversight of the Federal Ministry of Finance, within the framework of which the legality and fitness for purpose of BaFin's administrative actions are being monitored.

Furthermore, it would be necessary that the “industry” is part of a representative body. Each ESA should have a body which represents in equal terms the supervised companies and the officials which are politically responsible for the ESAs. These bodies could monitor the management of the ESAs and support the ESAs in the performance of its supervisory functions. Furthermore, these bodies should be responsible for decisions over the budget of the respective ESA like the Administrative Council in Germany.

Another point that must be considered is that national constitutions place high demands on the legitimacy of such special levy on private companies. For example, according to the German Constitutional Law, these contributions must be justified both by legal reason and by amount of the contribution.[2] According to the jurisdiction of the German Federal Constitutional Court (BVerfG), only companies may be charged which are the cause of supervisory acts or are at least the main beneficiaries of the financed activity.[3] The levy must also be documented in budgetary terms und regularly be reviewed by the legislator.[4] In Germany, the

[2] Cf. BVerfG v. 03.02.2009 – 2 BvL 54/06, Rn. 104; BVerfG v. 28.01.2014 – 2 BvR 1561/12, Rn. 121; BVerwG v. 23.11.2011 – 8 C 20.10, Rn. 31 und 32 ff.
[3] Cf. BVerfG v. 28.01.2014 – 2 BvR 1561/12, Rn. 121.
[4] Cf. BVerfG v. 17.07.2003 – 2 BvL 1/99 u.a., Rn. 120 and at last for the BaFin-Levy BVerwG v. 23.11.2011 – 8 C 20.10, Rn. 27.

contributions will basically then be allocated according to the principle of causation and in an activity-based costing structure in order to achieve legitimacy of the model (§§ 16 ff. FinDAG).[5] In practice, there are always difficulties being encountered, which is why it is necessary to constantly improve. The required transparency and the activity-based costing structure which takes into account the causation principle creates huge administrative expenses and other costs because every single act of an employee has to be allocated in the activity-based costing structure. For the ESAs, therefore, a legitimate change would entail a lot of time, very high introductory costs and increased administrative burdens and costs.

Regarding the principle of causation we are strongly of the opinion that this principle cannot be applied to the tasks ESMA has vis-à-vis listed companies and the non-financial sector. Listed companies are primarily affected by ESAs` activities when it comes to regulatory measures on purely issuers` related matters. Those measures only form a minor part of the ESAs` activities and expenditure and clearly have the character of a public good which cannot be financed according to the causation principle (see also Q 30). **The difference between non-financial and financial companies leads to the consequence that it doesn't seem to be proportionate to burden the funding obligation on listed companies we represent, see also under b) below.**

The role of ESMA is to coordinate supervisory activity and – to a significant extent – to develop supervisory standards such as RTS. The activities of ESMA thus have the character of a public good which cannot be financed according to the causation principle.

For all these reasons Deutsches Aktieninstitut strongly opposes to change the current ESAs funding model to a system fully funded by the industry.

Ad b)

Deutsches Aktieninstitut has serious misgivings about changing the current ESAs funding model to a system partly funded by industry.

First of all, we strongly reject any change regarding the contribution of the general EU Budget (40%) for the reasons stated above.

Moreover, requiring non-financial companies to contribute to the ESA budget would create an additional burden for non-financial companies, who are already exposed to a significant amount of obligations under capital markets regulation. This contradicts with the European EU Commission`s agenda on the establishment of a Capital Markets Union, which is supposed to make capital markets more attractive for companies throughout Europe in order to foster investment and growth.

Furthermore, it would be necessary that the "industry" is part of a representative body of each ESAs. The more the funding is shifted to the "industry" the more the

[5] Compare also the official justification of the FinDAG - BT-Drs. 17/11119, S. 30.

involvement and competences of the NCAs have to be shifted to the “industry” too. See, for example, the Administrative Council of the German NCA explained above.

In addition, more transparency about the cost structure and cost allocation of the ESAs is needed. The higher the burden for the “industry”, the higher need to be the requirements regarding transparency, cost structure and cost allocation of the funding model (see more above).

Q30. In your view, in case the funding would be at least partly shifted to industry contributions, what would be the most efficient system for allocating the costs of the ESA's activities:

a) a contribution which reflects the size of each Member State's financial industry (i.e., a "Member State key"); or

b) a contribution that is based on the size/importance of each sector and of the entities operating within each sector (i.e., an "entity-based key")?

Please elaborate on (a) and (b) and specify the advantages and disadvantages involved with each option, indicating also what would be the relevant parameters under each option (e.g., total market capitalisation, market share in a given sector, total assets, gross income from transactions etc.) to establish the importance/size of the contribution.

Deutsches Aktieninstitut recommends not to change the distribution of the ESAs’ funding model. There are no valid reasons for changing the current system.

First of all, the question of shifting funding obligations to the “industry” entails also to distinguish between financial and non-financial companies. There are no valid grounds to oblige non-financial companies to contribute to the funding of the ESAs: In general, markets are financed by those trading and not by those, whose goods are being traded on the respective markets. The mere circumstance that securities of non-financial companies are traded on capital markets doesn’t make non-financial companies to active market participants.[6] They should thus not be required to contribute to the financing of the ESAs, whose task is first and foremost to regulate and supervise capital markets and those being considered as active market participants.

Non-financial companies are primarily affected by ESAs` activities when it comes to regulatory measures on purely issuers` related matters. Those measures only form a minor part of the ESAs` activities and expenditure and therefore can`t be

[6] See also reasoning of the U.S. Securities and Exchange Commission in the Securities Exchange Act, Section 31, https://www.sec.gov/divisions/marketreg/sec31feesbasicinfo.htm.

compared with those for really active market participants. Furthermore, the ESAs activities regarding listed companies clearly have the character of a public good which cannot be financed according to the causation principle Consequently, it doesn't seem to be proportionate to burden the funding obligation on listed companies.

A few criteria are not capable of making funding more just. There is not only the size of a Member State's financial industry or the size/importance of sectors/entities to be taken into consideration. A small financial industry may require much more supervisory activities than a proven big one. Furthermore, the beneficiaries of a financial market are also investors of other countries. There are so many criteria and all of them must be valued and put into relation.

A more proportionate division than the current distribution (qualified majority voting rule of the Council) would be possible at most by a large number of various criteria and key figures which are very difficult to calculate. This would lead to considerable additional expenses and costs. A simpler solution would only give the impression of a fairer financing, but in reality would not be better. A fairer distribution would only be possible by taking into account the principle of causation. An example of this would be the financing of the German NCA (BaFin). But such a financing has the disadvantage that is causes a lot of time, very high introductory costs and increased administrative burdens and costs (compare under question 29.

Moreover, in the event of any changes in the cost relationship between the NCAs (respectively their supervised companies), the voting rights of the NCAs in the ESAs must also be changed equivalently. Otherwise it would not be comprehensible, if those who are not or only slightly affected can just as well determine as those most affected. Furthermore, the most affected NCAs have also more experience, resources and responsibility towards a single European financial market.

In any case, non-financial companies should not be unfairly burdened (compare under question 29).

Q31. Currently, many NCAs already collect fees from financial institutions and market participants; to what extent could a European system lever on that structure? What would be the advantages and disadvantages of doing so? Please elaborate.

In principle, fees are to be welcomed because the causers of the costs themselves need to pay for their costs. In addition, market participants may also be obliged who are normally not accessible (e.g. foreign investors).

Q32. You are invited to make additional comments on the ESAs Regulation if you consider that some areas have not been covered above. Please include examples and evidence where possible.

As mentioned above, within the ESA review special attention needs to be drawn to accountability and governance aspects.

1. Accountability aspects

Importance should especially be given to enhance scrutiny of ESAs` activities by the European Commission, the European Parliament and the Council in order to better being able to hold ESAs accountable for their work.

The options that need to be considered are:

a) Extend deadline for the EU Parliament and the Council to object Regulatory Technical Standards (RTS)

According to Art. 13 ESA regulation, the European Parliament or the Council may object to a RTS within a period of 3 months from the date of notification of the RTS adopted by the EU Commission. At the initiative of the European Parliament or the Council this period shall be extended by 3 months. This set up basically creates the right balance between the necessity of delivering legal certainty in due time and the possibility to employ political control and should not be changed.

However, whenever the EU Commission adopts a RTS without changes to the one submitted by the Authority, the period during which the European Parliament and the Council may object is only 1 month from the date of notification by the EU Commission. At the initiative of the European Parliament or the Council that period shall be extended by 1 month. Having in mind the limited resources available to MEPs and smaller member states as well as the complexity of most of the drafts the standard endorsement period of one month for the co-legislators appears to be too short. The Parliament and the Council should be given more time to consider the draft RTS, even if the EU Commission sees no need to change the draft RTS. This would ensure that the political will can be incorporated in the delegated measures, in particular where the level 1 texts leave room for interpretation.

b) Clarify criteria determining deadlines for objection to RTS:

In addition, there is the threat that the Commission considers the RTS as being "the same" as in the draft RTS submitted by the ESA, even though they had been changed in a way that goes beyond pure linguistic corrections and amounts instead to a substantial change.

In our view, criteria according to which deadlines for objection to RTS are set out and/or extended need to be clarified, i.e. in which cases can it be considered that draft and final RTS are not "the same" and the 3-month deadline for objection applies. Furthermore, any amendment of the EU Commission beyond a correction of an obvious mistake of the ESAs' initial draft should be reported to the co-legislators as soon as possible and at the latest at the time of the adoption of the

act. Lastly, the EU Commission should be required to provide, on request, clarifications about changes made to the draft RTS in case there are doubts about their non-substantial nature.

c) Concerns regarding the so called "bundling"

"Bundling" is called the process when the EU Commission regroups several empowerments for draft RTS into one single act. For doing so, the EU Commission uses two main criteria: possible interlinks in the subject matter of the empowerments and the common deadline for the adoption of the measures.

However, there are downsides of this procedure: Firstly, the relative reduction of time for the Parliament as well as for the Council to scrutinize the proposal during the objection period, since there is only one deadline for several acts running at the same time.

Secondly, according to the EU Commission`s view, in the case of "bundling", no right to oppose only part of the bundled delegated act is granted to the Parliament and the Council. The institutions can only approve or object the whole "package". In our view, it should however be possible for the Parliament and Council to object to each of the delegated acts separately. Otherwise, democratic control would be impeded. For each of the bundled delegated act an individual empowerment by the legislator had been granted beforehand. Thus, respective control of each Delegated Act by the legislative bodies must be ensured.

d) Participation of the institutions already in the drafting phase

Regular informal exchange between the EU Institutions and the ESAs – e.g. as established between ESMA and the ECON-committee of the European Parliament since 2012 – is deemed as being useful. The consultation might probe the idea of ESAs forwarding preliminary versions of draft regulatory technical standards, working documents or non-papers to at least the rapporteur on the file in the Parliament and the chair of the working group of the respective Council Presidency before they are approved by the Board of Supervisors (BoS). Such an approach would help the EU institutions to better follow the discussions and would speed up the process in case of sensitive issues.

e) Improvement of hearings of the chairs of the supervisory authorities

In our opinion there is room for improvement of how hearings of the chairs of the supervisory authorities before the European Parliament are conducted. The current procedures regarding such hearings do not allow for a proper debate - MEPs cannot ask questions related to the responses provided by the chairs to the previous questions. We believe the procedure could be improved in that respect.

2. Transparency and determination of tasks, priorities and competences of ESAs

The review could be an opportunity to assess ESA`s tasks, priorities and competences. We believe that the work programmes of the ESAs should be

focused on ensuring resource efficiency as well as effectiveness. Redundancies or overlapping competences on European and national level between ESAs and NCAs should be avoided.

3. Better regulation agenda

The European Better Regulation Agenda aims at ensuring that European law-making procedures remain at the highest standard in terms of impact assessment, transparency, public consultation, and implementation. Laws should be finalized well before their application and stakeholders should have the time to prepare for the new rules. Improvement is specifically needed regarding the timeline for the adoption of level 2 measures.

A perfect example in that respect it the entry of force of the Market Abuse Regulation. Here, the level 2 measures applied from 3 July 2016, as the main Regulation (MAR). However, out of 16 level 2 measures, 7 have been published only in June (2 of them on 30th and 29th June); 6 in April; 2 in March; 1 in December. Guidelines were published on 13 July. Therefore, companies did not have enough time to look at those measures and to put in place the appropriate arrangements.

In addition, as MAR extends some disclosure requirements also to companies on MTFs. Those companies did not have any experience nor structure in place to cope with those requirements. Moreover, the lighter regime foreseen for companies on the "SME Growth Market" is not yet applicable because of the postponement of MIFID II application.

Given heavy obligations and serious consequences in case of non-compliance (including criminal sanctions) stemming from MAR provisions, the situation is particularly difficult. Thus, we think that the consultation should consider this kind of situations and possible solutions. Our recommendations for improvements are:

- when level I foresees many level II measures, the legislator should allow a longer transition period.
- a general provision in the ESMA regulation (or a specific provision at level I) should state that level II measures must be published at least 6 months before the date of application of level 1.
- a general provision in the ESMA regulation obliging ESMA to notify the EU Commission in case ESMA is not able to deliver certain measures on time. Subsequently, the EU Commission should take an appropriate action (for e.g. postponement of the date of application of level 1).

Contact

Maximilian Lück, LL.M.
Head of EU Regulatory Affairs
Deutsches Aktieninstitut e.V.
EU Liaison Office 58, Rue Marie de Bourgogne
B-1000 Bruxelles
Phone +32 2 7894102
lueck@dai.de

Dr. Gerrit Fey
Head of Capital Market Affairs
Deutsches Aktieninstitut e.V.
Senckenberganlage 28
60325 Frankfurt am Main
Phone + 49 69 92915 - 41
Fax + 49 69 92915 - 12
fey@dai.de

Sven Erwin Hemeling
Rechtsanwalt (Syndikusrechtsanwalt)
Policy Advisor Capital Markets Law
Deutsches Aktieninstitut e.V.
Senckenberganlage 28
60325 Frankfurt am Main
Phone + 49 69 92915 - 27
Fax + 49 69 92915 - 12
hemeling@dai.de
www.dai.de