Deutsches Aktieninstitut

European Supervisory Authorities review– Comments on the EU Commission proposal and the draft report of the EU Parliament

Refrain to equip ESMA unnecessarily with extensive additional competences, such as the approval of wholesale prospectuses!

Deutsches Aktieninstitut's position on the proposal of the European Commission on the operations of the European Supervisory Authorities, COM(2017) 536 final, amended by the draft report of the EU Parliament, (COM(2017)0536 – C8 0319/2017 – 2017/0230(COD)), 17 October 2018.

Executive summary

Deutsches Aktieninstitut deems the review of the existing EU supervisory framework as important in order to ensure both that European Supervisory Authorities (ESAs) work efficiently and can be held accountable for their actions.

The EU Commission‘s proposal on the review of the EU supervisory framework however fails to improve the accountability of ESAs‘ activities. Instead, too much emphasis is put on enhancing regulatory and supervisory convergence in Europe by granting ESAs additional powers. More details can be found in our position paper on the EU Commission proposal from February 2018.[1]

The draft report of the European Parliament (EP) improves accountability and control of ESAs` work by the co-legislators. Nevertheless, it unfortunately follows the general line of the EU Commission to confer more powers to ESAs, in particular to ESMA.

Deutsches Aktieninstitut is of the opinion that:

1. Until now, no concrete evidence has been presented that the existing instruments of ensuring convergence have significant deficits. In cases where differences in national application of EU law occurred, this is either rooted in the fact that most of the regulation has been enacted rather recently so that the relevant instruments have not yet had enough time to work or it is rooted in a lack of clarity of the level 1 texts which forces national supervisors to take some kind of interpretation in order to form a supervisory practice and ensure some legal certainty in due time. However, both does not justify more centralization of supervisory competences in the EU.

2. There are valid reasons why the current EU supervisory regime respects national particularities by referring to National Competent Authorities (NCAs) which are largely involved in the supervision of EU Financial Markets regulation: NCAs are closer to the national markets, they are better placed to know their specificities. At the same time, the current regime ensures an adequate level of harmonization. Those established and efficient structures must not be destroyed (as it would be the case, e.g., if the competence for

[1] See Deutsches Aktieninstitut’s response to the proposal of the EU Commission on the operations of the European Supervisory Authorities, COM(2017) 536 final, 20 February 2018, https://www.dai.de/files/dai_usercontent/dokumente/positionspapiere/20180216%20ESA%20Response%20Deutsches%20Aktieninstitut%20FINAL.pdf .

the approval of wholesale prospectuses were transferred to ESMA. This would also have the consequence that issuers would face the problem that prospectuses would not be accepted in as many languages as it is currently possible with eg the Luxemburgish NCA. This might cause issues especially for multiuser prospectuses).

3. Therefore, Deutsches Aktieninstitut opposes the shifting of powers from NCAs to ESAs at least at this point in time-, especially with regard to ESMA. In particular, we are critical to transfer the competence for the approval of wholesale prospectuses to ESMA.

   Despite the fact that the EP draft report stresses the importance of the role of NCAs, it unfortunately doesn`t oppose the newly confered competences in the EU Commission proposal to a sufficient extent. This should be remedied in the course of the upcoming negotiations.

4. Much of the critique on the current supervisory system is instead rooted in overly complex and detailed level 2-regulations which itself is a consequence of a vague and too general wording on level 1. Rather than granting extensive new powers to ESAs, Deutsches Aktieninstitut believes that the ESA review should focus much more on ensuring an appropriate balance between level 1 and level 2: crucial political decisions should be taken by the legislator instead of being delegated to ESAs as it has occurred in the past.

   Unfortunately, this crucial topic is neither addressed by the EU Commission, nor by the EP draft report. It should urgently become part of the discussions. Otherwise we fear that the ESA review will miss its objective to improve the Europan Supervisory architecture.

5. Furthermore, improvements need to be made when it comes to holding ESAs accountable for their actions- as ESAs have repeatedly overstepped their powers in the past. Level 2 and 3 measures need to be better controlled if they are consistent with the political will of level 1.

   We appreciate that the EP draft report addresses accountability and control issues. In particular, we see improvement as regards to the procedure for adopting regulatory and implementing technical standards, allowing for better scrutiny by the co-legislators. It is also positive that mechanisms are being introduced for the co-legilsators as well as the ESMA Securities Markets Stakeholder Group to control ESMA guidelines. It is of utmost importance that those achievements are not jepoardized in the upcoming discussions.

6. Changing the current ESAs funding regime would cause significant difficulties. Even more, a change of the current ESAs funding model to a system fully funded by the NCAs or by involving the private sector is to be rejected in any case.

We appreciate that the EP draft report makes it clear that at least 35 % of the ESAs budget needs to stem from the EU budget. This way,at least it is certain that budgetary control can be excerted. Nevertheless, also in the EP draft report private sector contributions are contemplated, which we do see critical. The current funding structure has worked well in the past. It should therefore be retained.

1 Comments on proposed conferral of additional powers to ESMA

As mentioned above, Deutsches Aktieninstitut deems the introduction of new competences for ESMA proposed by the EU Commission as excessive. In the following, concrete examples affecting members of Deutsches Aktieninstitut will be listed. It will be shown, why the conferral of those new competences is not appropriate and moreover in many cases not necessary.

1.1 Supervisory handbook[2]

According to the plans of the European Commission as well as the EP draft report, ESMA shall be authorized to draft a "Supervisory Handbook" with best practice proposals for the supervision of financial market participants within the EU.

Deutsches Aktieninstitut doesn't regard the introduction of a "Supervisory Handbook" necessary, since regular coordination between ESMA and the NCAs as well as the issuance of Q&As already today provide sufficient guidance for the supervision of financial market participants. Furthermore, a codified guideline leaves less flexibility for regulators to react to new or country-specific situations, as opposed to a coordination system. Hence, we deem the introduction as redundant to existing tools which are already at ESMA's disposal.

1.2 Consumer and investor protection[3]

According to the EU Commission's proposal, ESAs shall contribute "to foster consumer and investor protection". *The EP unfortunately appears to agree with the EU Commission's position, as it does not express any views on the newly introduced general competence.*

From Deutsches Aktieninstitut's point of view, the current powers of ESMA with respect to consumer and investor protection are already sufficient.

It is and should remain the task of National Competent Authorities to ensure that the EU legislation with respect to consumer and investor protection 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

2 Article 3 paragraph 5, page 108 of the EU Commission proposal.
3 Article 3 paragraph 5, page 108 of the EU Commission proposal.

measures and sanctions that can be imposed. We therefore recommend to delete the new competence in the forthcoming negotiations.

1.3 Accounting[4]

The EU Commission proposal as well as the EP draft report intend to strengthen the role of ESMA in the fields of accounting, auditing and enforcement of financial reports. The EU Commission proposal stipulates the Accounting Directive 2013/34 to be within the scope of ESMA activities (see Article 3 (1) (a) on changes of Article 1 (2) of Regulation (EU) No. 1095/2010 (ESMA Regulation)). The same applies to the reference made in Article 3 (1) (a) to Regulation (EC) No 1606/2002 on the application of international accounting standards.

The EP draft report adds that ESMA shall seek an observer status in the International Accounting Standards Board.[5] We struggle to understand the request that ESMA should "seek observer status on the International Accounting Standards Board." All meetings of the IASB are public and everyone is invited to attend as an observer, be it physically in London or via Internet. Thus, an observer status is nothing that needs to be specifically granted to ESMA. Should the idea be that ESMA obtains a status beyond the status of an observer (e.g. with a right to speak in the IASB board meetings) we do not agree with the request as it would be inappropriate for the IASB or the IFRS foundation, as a global standard setter, to grant special rights to authorities from individual jurisdictions. An approach under which authorities from all jurisdictions that apply IFRS have a right to speak in IASB meetings is not feasible considering that more than 150 jurisdictions apply IFRS. This is different, for example, in the US context where the U.S. SEC has a special observer status in meetings of the U.S. national standard setter FASB. As the SEC is the only enforcement authority in the U.S. this is feasible there while it would not be in the global setup of IFRS.

We reiterate that from our point of view, there is no need to equip ESMA with additional powers with respect to accounting, auditing and enforcement of financial reports beyond the status quo. This holds especially 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 ensuring that listed companies comply with the rules and auditors perform their tasks in a proper manner.

European companies already now take financial reporting very seriously. There is no evidence of major compliance deficits or significant potential misinformation of the public. Investors of European listed companies financials' can already be sure

4 Article 3 paragraph 1 (a), see page 107 of the EU Commission proposal.

5 Draft EP report, EU Regulation (1095/2010), Article 3 – paragraph 1 – point 18 – point b a (new), amendment 267.

that the companies are transparent as the reliability of accounts is ensured by various institutional settings. There is even less evidence that a potential deficit needs to be tackled at European level.

1.4 Environmental, social and governance factors[6]

According to Article 8 paragraph 1a (new) of the EU Commission`s proposal, ESAs shall "take account of technological innovation, innovative and sustainable business models, and the integration of environmental, social and governance related factors." The EP draft report doesn't express any views on the topic and hence follows the EU Commission proposal.

We oppose the introduction of such far-reaching competences. They are likely to be interpreted as a competence for ESAs to launch initiatives in the field of sustainable finance. This needs to be avoided as such a right exclusively lies with the legislator.

1.5 Collection of information[7]

The EU Commission`s proposal as well as the EP draft report grant ESMA the right to address a request for information directly to relevant financial market participants, whenever deemed necessary for the purpose of investigating an alleged breach or non-application of Union law, see Art 17 of the EU Commission proposal. [8] The same goes for the information request rights to market participants under Articles 35a to 35 h (new) (see Article 3 (21)), amended by the EP draft report.[9]

Deutsches Aktieninstitut considers it critical to grant ESMA such far-reaching powers, as they would not be proportionate: such a right is generally only granted to the competent authority having direct supervisory powers over the respective market participant. This even more as the proposals offer the possibility to fine market participants with up to 200,000 Euro for not following an ESAs' information request.

1.6 Market Abuse[10]

According to the EU Commission proposal, a coordinating role towards national supervisory authorities shall be assigned to ESMA in relation to orders, transactions

6 Article 3 paragraph 5, inserting Article 8 paragraph 1a (new), page 108 of the EU Commission proposal.
7 Article 3 paragraphs 8 and 21, pages 109 and 118 of the EU Commission proposal.
8SArticle 3 paragraph 8 of the EU Commission proposal.
9 EP draft report, EU Regulation (1093/2010), Art. 35 a-h new, amendment 102/103.
10 Article 3 paragraph 16, page 116 of the EU Commission proposal.

or activities with significant cross-border effect that have the potential to threaten the proper functioning of financial markets and the financial stability in the EU.

For this purpose, ESMA shall be allowed to set up a data collection point (see Article 3 (16) for the insertion of a new Article 31b in Regulation (EU) No. 1095/2010 (ESMA Regulation)). According to the explanation of the EU Commission proposal, this competence is of significant importance in the context of market abuse (see page 21 of the Commission proposal). The EP draft report doesn't express any views on this newly introduced competence

Whilst seeing the merit of a centralized data point to fight cross-border market manipulation, the necessity of such a competence is not clear to us.

Articles 24, 25 Regulation (EU) No 596/2014 on market abuse (Market Abuse Regulation) already provide far-reaching obligations for NCAs within the EU to cooperate with each other as well as with ESMA. In addition, the proposal contains a large number of vague legal terms without giving typical examples. Hence, it is unclear which competences shall ultimately be assigned to ESMA compared to the ones being granted to NCAs and compared to the status quo.

Clarification is therefore needed in the course of the upcoming negotiations.

1.7 Peer review[11]

For the peer 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 input than those coming from the reviewed authorities themselves. *Unfortunately, neither the EU Commission, nor the EP draft report have addressed the issue. The topic thus deserves closer attention in the forthcoming negotiations.*

1.8 Prospectus[12]

The EU Commission proposes to transfer the approval and the advertisement powers of certain prospectuses under the Prospectus Regulation from NCAs to ESMA. This, inter alia, relates to prospectuses for wholesale non-equity securities (wholesale prospectus). *We have significant concerns regarding this transfer of competences, which has not been remedied by the EP draft report.*

The plan to focus on wholesale prospectuses feels unsuitable. By definition wholesale prospectuses target qualified professional investors only. If the European

11 Article 3 paragraph 13, page 113 of the EU Commission proposal.
12 Article 9 EU Commission proposal, amending Regulation (EU) 2017/1129, page 235 of the proposal.

Commission would indeed be of the opinion that a transfer of wholesale oversight would enhance consumer and investor protection than it is unreasonable that the much weaker group of retail investors is carved out and left with less comfort relative to market professionals.

When drawing up a base prospectus it is a normal procedure to incorporate certain documents like financial statements, articles, certificate of incorporation by reference. Depending on the country of origin the language of these documents might because of local laws and regulations differ from that of the prospectus. This fact proofs to be an issue since different NCA would each accept a different set of languages. At present issuers are free to choose where to seek approval for a wholesale prospectus. Since it is most efficient this choice will be strongly influenced by the question to what degree languages of need are accepted by the NCA in a particular place. Such problem is most pronounced for multi issuer programs. Still more general we see the risk that an additional burden of translation works like a non-tariff-barrier and could hold potential issuers from using the capital market as source of funding.

The variety of language regimes which exists among NCA is a very good example how efficient the current system of multiple NCA is for the market development in Europa. Specialization, excellence in a particular filed and burden sharing in oversight is a strength of the European capital market which should be persevered. We mustn't forget, that the competition to attract capital is global. The ability to respond timely and flexible to market participant needs is in the end a decisive factor when it comes to fund investments and to create jobs in Europe.

Not least because of better fitting language regimes a few Member States have emerged as centers for the approval of wholesale prospectuses, where national regulators are highly experienced in this. Important structures, know-how and efficiency have been formed at these locations. The existing certainty and predictability of the approval process, speed of procedures and cost efficiency is very important for the professional market. Even with great effort, it seems very doubtful that ESMA can fulfill these requirements even in the medium term. In light of the upcoming challenges, such as United Kingdom's exit from the Union (Brexit), it is important to build on established structures instead of creating additional disruptions and risks.

In addition, the approval competence of ESMA in this context would trigger inefficiencies in supervision and unnecessary burdens for issuers and the respective NCA: for example, under current practice, a prospectus is often used for both retail and wholesale. In such cases, a subsequently used prospectus for retail investors would result in a new approval procedure at NCA level. This means unnecessary burdens on both sides and inefficient supervision. More problems with double supervision arise when supplements have to be made.

Effective supervision is ensured if it is conducted closely in the respective markets and takes into account the specific national market conditions. It should be noted that the vast majority of new issuances are only available in one or a few Member States. Here, a prospectus check by the NCAs is more appropriate as they know the specifics of their national market and the market participants. This also allows the NCAs to react quickly and appropriately to changes. Therefore, it does not make sense to create completely new structures and additional resources at ESMA in these areas, as supervisory convergence is already ensured with the existing instruments (such as the implementation of peer reviews and the adoption of guidelines). As a result, potential regulatory arbitrage is already effectively countered. In addition, the harmonization of new regulations also takes time, so that market-specific features can be taken into account sufficiently.

Therefore, we do not see any necessity nor added value to grant ESMA the competencies mentioned above. Rather, we do fear negative consequences, if those competences were conferred to ESMA. We therefore urge the co-legislators in the upcoming negotiations to remove the respective competencies.

1.9 Stress test[13]

According to the EP draft report, ESMA shall consider at least once per year "whether it is appropriate to carry out Union-wide assessments referred to in paragraph 2 with regard to significant financial market participants….." The EP draft report extends the competence for conducting a stress test to significant market participants whilst the EU Commission proposal only referred to financial institutions.

We oppose the far-reaching new competence, as we do not see the necessity for ESMA to conduct stress tests or assessments for stress tests as regards to market participants that are not under the direct control of ESMA. Respective stress tests on financial stability are already regulated in EU supervisory, capital markets and banking regulation, referring to market stability risks eg in case financial institutions face bankruptcy or illiquidity. Those situations can barely be compared with regular capital markets participants. As we have expressed several times in the past, we do not believe those participants do pose any kind of significant risk for the stability of financial markets. This perception for example correctly resulted in reliefs and exemptions for non-financial companies in major regulations like EMIR and MiFID/MiFIR.

13EP draft report, ESMA Regulation (1095/2010), Article 32 – Paragraph 2a (new), amendment 266.

1.10 Prohibition of Financial instruments[14]

The EP draft report appears to enlarge the scope of the ESMA's competence to temporarily prohibit or restrict certain financial activities that threaten the orderly functioning and integrity of financial markets or the stability of the whole or part of the financial system in the Union: the draft report adds the cases „…marketing, distribution or sale of certain financial instruments or financial instruments with certain specified features or a type of financial activity or practice…"[15] to the scope of activities/instruments that can be restricted or prohibited temporarily.

Again, we don't see evidence being put forward which suggests that present powers under Art. 9 ESMA Regulation aren`t sufficient to react on threats to market stability. Powers exerted under Art 9 ESMA Regulation can have serious damaging impact on businesses and have hence to be proportionate and be used only as a matter of last resort. Enlarging the scope of application does not respect those principles.

14EP draft report, Regulation (EU) No 1095/2010, Article 9 – Paragraph 5 – Subpara 1, amendment 258.

[15] See above..

2 Accountability and governance

In the past few years, members of Deutsches Aktieninstitut have made the experience that on several occasions acts stemming from ESMA have gone beyond the text adopted on level 1 or contained extremely wide interpretations. This either led to over-detailed rules or even counteracted he legislator's will set out on level 1. [16]

We therefore deem improvements of accountability and governance aspects necessary in order to better control the outcome of ESMA's work. *Unfortunately, the EU Commission proposal has not given accountability and governance aspects the attention needed whilst the EP draft report is ambiguous in that respect. On the hand we see some improvements (in particular regarding better scrutiny of draft regulatory standards), on the other hand the draft report may too strongly interfere with ESMA's day-to-day operations as well as with processes that have proven reliability.*

2.1 Accountability aspects: improvements in the EP draft report

The EP draft report puts forward a series of changes as regards to the adoption of draft regulatory and implementing standards that increase accountability and control via the co-legislators. Deutsches Aktieninstitut supports the following changes proposed:

We appreciate the deletion of the 1 month scrutiny period for the EP and the Council of draft regulatory technical standards, introduced by the EP draft report.[17] Bearing in mind the limited resources available to Members of the European Parliament 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 appeared to be too short. The regular three months period is more appropriate or scrutiny by the co-legislators. Also, the obligation for ESMA to submit its draft regulatory standards to the EP and the Council for information at the same time as to the EU Commission for endorsement enhances the role of the co-legislators in the process and is hence to be supported.[18]

Furthermore, we welcome the obligation for ESMA to publish on its website, and to update regularly, all regulatory technical standards, implementing technical

16 Examples can be identified following measures by ESMA on the Market Abuse Regulation (e.g the extremely wide interpretation of managers' transactions), the Transparency Directive (e.g. the latest proposal on the ESEF) or within EMIR (e.g. the very detailed data fields).

17 EP draft report, Regulation (EU) No 1093/2010, Article 10 – Paragraph 1, amendment 21.

18 EP draft report, Regulation (EU) No 1093/2010, Article 10 – Paragraph 1, amendment 21.

standards, guidelines, including over-views which contain the state of play of the ongoing work and planned timing of the adoption of the draft regulatory technical standards, draft implementing technical standards, guidelines and recommendations.[19] *It fosters the transparency of the regulatory process and also serves market participants as indication for their internal planning.*

Last, we support the notification procedure proposed by the EP draft report in case of a delay of transmission/endorsement of draft regulatory technical standards by ESMA or the EU Commission: it allows the co-legislators, but also companies, to plan accordingly.[20]

2.2 Stakeholder engagement

Regulatory decisions should be based on the broadest possible input. It is of utmost importance that especially issuers having to deal with day-to-day compliance of capital markets regulation are given the opportunity to provide ESMA with feedback.

Deutsches Aktieninstitut has the following remarks/recommendations:

2.2.1 Consultations:

We think that it would make sense to launch consultations on draft regulatory technical standards after they have been submitted to the EU Commission on the initiative of one of the co-legislators: as the co-legislators have the right to scrutinize the standards it might be deemed important to receive feedback from stakeholders. Like this, the co-legislators would be better prepared to assess the impact the standards will have on the market.

Unfortunately, our proposal has not been picked up by the EP report. This needs to be changed in the forthcoming discussions.

2.2.2 Competences of ESMA Securities Markets Stakeholder Group (SMSG):

The EP draft report substantially extends competences for the Securities Markets Stakeholder Group (SMSG), the central forum within ESMA representing stakeholders `interests. We generally support greater involvement of the group in ESMA activities, especially the right to submit an opinion to one of the EU Institutions in case a majority of the SMSG deems a guideline issued by ESMA as

[19] EP draft report, Regulation (EU) No 1093/2010 Article 8 – Paragraph 1 – Point ka (new), amendment 15.

[20] EP draft report, Regulation (EU) No 1093/2010, Article 10 – Paragraph 1 and 2, amendments 21/22.

being unlawful.[21] *Nevertheless, we are critical that a two-thirds majority of the members of the Securities and Markets Stakeholder Group is required according to the EU Commission proposal to do so. We believe the majority requirement is too high, given the quite diverse backgrounds of its members. A simple majority would therefore be preferable, especially when competences are to be enlarged. The EP draft report does only partly remedy this drawback: It requires a simple majority solely for guidelines that are within the scope of the „comply or explain" procedure.* [22]*All other guidelines still require the two-thirds majority.*

Last, we are rather skeptical as to the extend the EP draft report intends to involve the SMSG in the operative business of ESMA: this relates in particular to the assessment of Q&As[23] *and the request for information from NCAs and market participants*[24]*. Q&As are very detailed and given the limited frequency of SMSG meetings, we guess it might not be practical to involve the SMSG on every Q&A to be issued. This would clearly overstretch the role as well as the resources of the SMSG with regard to ESMA's activities. The same goes for the request for information, which requires sufficient background information for the members of the SMSG to being able to assess its necessity.*

2.3 Guidelines and Q&As

2.3.1 ESMA guidelines

Although guidelines are legally not binding, the past has shown that 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 and therefore a significant impact on market participants.

Against this background, the ESAs regulations should be altered in some respects to ensure that guidelines cannot be used for standard stetting "through the back door" without a clear legal mandate on level 1, as we have for example seen in the efforts of EBA to erase the corporate exemption to CVA in CRD IV.

- First, the competence to issue guidelines should be stated in a less general manner, so that ESAs make restrained use of guidelines and, if they are issued, take a rather principle based approach. 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

[21] EP draft report, Regulation (EU) No 1093/2010, Article 16 – Paragraph 5a (new), amendment 39.
[22] See above.
[23] EP draft report, Regulation (EU) No 1095/2010, Article 37 – Paragraph 1, amendment 268.
[24] EP draft report, Regulation (EU) No 1095/2010, Article 37 – Paragraph 5 – Subparagraph 1, amendment 272.

practice. We would therefore prefer that guidelines are issued only on the basis of clear mandate within the level 1-regulation.

- Second, to prevent/remedy potential discrepancies in the implementation of EU legislation in the various Member States that are harmful for European Capital Markets, we suggest ESMA collects information on differences that occurred- rather than issuing guidelines. The compilation could be published subsequently in order to increase transparency on interpretations that have disrupted the markets which in turn will likely help National Competent Authorities to refrain from such interpretations in the implementation process of EU legislation. This would not require any additional competences for ESMA and would at the same time be more appropriate for market participants. It would help to focus on the most relevant individual cases instead of NCAs and market participants having to cope with extensive guidelines that might not take into consideration national market specifics.

- *Third, greater stakeholder engagement needs to be guaranteed. We are pleased to see that according to the EU Commission's proposal, ESAs shall as a general rule conduct open public consultations regarding guidelines.It is also positive noting that following the EP draft report, ESAs shall provide reasons when they do not conduct open public consultations or do not request advice from the Securities and Markets Stakeholder Group.*[25]

- *Last, we are also pleased that the EP draft report foresees a procedure that allows the EP and the Council, together with the EU Commission to be involved in withdrawing unlawful guidelines.*[26] *The involvement of the EP and the Council enhances scrutiny as opposed to the EU Commission proposal that only saw it as a task reserved for the EU Commission.*

2.3.2 Q&As

Besides guidelines, we would also 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.

Deutsches Aktieninstitut demands that Q&As are issued cautiously and on a principle based approach, for the same reasons as guidelines (see above).[27]*Therefore, we are critical as to the EP draft report stating that any natural*

[25] EP draft report, Regulation (EU) No 1095/2010, Article 16 – Paragraph 2, amendment 259.
[26] EP draft report, Regulation (EU) No 1093/2010, Article 16 – Paragraph 5b (new), amendment 40.
27 E.g. under EMIR, market participants faced huge administrative burdens to implement the respective compliance processes due to frequent updates of the ESMA Q&As. The same problem arised recently under MiFID II/MiFIR.

or legal person may submit questions to ESMA and that ESMA is required to publish respective answers on the ESMA homepage[28]. We fear that such a process might deter ESMA to provide principle based guidance and it might be at the same time overburdening for ESMA.

Nevertheless, we welcome that the issue of Q&As has been raised by the EP to become part of the political discussion. In this context, the following topics should be addressed:

- Improvements regarding market consultation is needed having in mind that the Q&A – though non-binding – will have an impact on the behavior of market participants. Currently, market participants have no possibility to comment on the ESMA Q&As with regard to their practical feasibility.
- In the same vein, it is problematic that the implementation periods for changes of the Q&As are not clearly defined. It is very challenging for market participants to apply the updates immediately, lacking other timing information. This should be remedied accordingly.

[28] EP draft report, Regulation (EU) No 1093/2010, Article 16b (new), amendment 43.

3 Financing of ESAs

3.1 Retain EU budgetary contributions

Deutsches Aktieninstitut welcomes the EU Commission's proposal to maintain the principle that up to 40 % of the annual funding of the ESAs stem from the EU budget. We strongly oppose changing the current ESAs funding model to a system fully funded by the NCAs or the private sector.

This is why we also welcome the EP draft report stating that at least 35 % of the funding shall stem from the EU budget.[29] By setting this fixed threshold, efficient budgetary control by the EU Institutions is guaranteed. This means also ultimately democratic control. It is thus on the one hand an improvement to the EU Commission proposal, where the EU contribution could also be well below 40 %. On the other hand, a higher threshold would be preferable, as it would enhance budgetary control and would ensure that ESAs are better being held accountable.

3.2 Issues regarding funding by the private sector (financial institutions)

Deutsches Aktieninstitut has serious misgivings about changing the current ESAs funding model to a system (partly) funded by the private sector in place of NCAs.

3.2.1 Importance of EU budgetary contribution and issues related thereto

First of all, we strongly reject any change regarding the contribution of the general EU Budget (40%) for the reasons stated above under No 1.

3.2.2 Distinction between financial and non-financial sector

Deutsches Aktieninstitut welcomes that the Commission distinguishes between financial and non-financial companies. The same goes for the EP draft report. In the further legislative process, it must be ensured by a clear wording that non-financial companies are not inadvertently drawn into the financing of the ESAs. But also for financial companies we believe that participation in the financing of the EU supervisory authorities is not appropriate or should at least be kept to a minimum.

[29] EP draft report, Regulation (EU) No 1093/2010, Article 62 – Paragraph 1 – Point a, amendment 209.

Supervision is the primary responsibility of the state and its costs shall be borne by revenues stemming from taxes.

As for non-financial companies, the mere circumstance that securities of non-financial companies are traded on capital markets does not turn non-financial companies into active market participants.[30] 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 issuer-related measures. Such matters only form a minor part of the ESAs´ activities and expenditure and, therefore, cannot be compared with those for really active market participants. Furthermore, the ESAs´ activities regarding non-financial companies clearly have the character of a public good which cannot be financed according to the causation principle. Consequently, it does not seem proportionate to burden the funding obligation on non-financial companies.

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 regulations. This contrasts 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.

3.2.3 Governance consequences of a shift of funding to the financial sector

Furthermore, it would be necessary that the financial companies are part of a representative body of each ESA. The more the funding obligation is shifted to the financial companies the more the involvement and competences of the NCAs have to be shifted to the financial companies too (see, e.g., the administrative council of the German NCA).

In addition, more transparency about the cost structure and cost allocation of the ESAs is needed. The higher the burden for financial companies, the higher need to be the requirements regarding transparency, cost structure and cost allocation of the funding model (see more above under 4.1, third bullet point).

30 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.

3.3 Distribution regime

Deutsches Aktieninstitut recommends retaining the distribution key of the ESAs' funding model. There are no valid reasons for changing the current system.

3.3.1 Current distribution

Deutsches Aktieninstitut opposes to change the distribution between the member states. The current distribution is easy to handle and does not incur significant costs. *We therefore applaud the EP draft report requiring obligatory contributions of up to 65% of the estimated revenues of the Authority from the national public authorities competent for the supervision of financial institutions.*[31] *It at least partly ensures that the current distribution regime is maintained.*

3.3.2 Adequate criteria for the distribution

In order to allow distribution of the costs to the financial institutions the Commission would like to be empowered to determine how these contributions be calculated. The Commission, i.a., wants to establish "appropriate and objective criteria" to determine the annual contribution payable by individual financial institutions. As regards to the establishment of "appropriate and objective criteria" we stress that a few criteria do not seem appropriate to make 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. *In this regard, the EP draft report can be at least in parts be seen as an improvement as funding shall be dependent on the evolution of the scope of institution-specific supervision.*[32] Furthermore, the beneficiaries of a financial market may also be investors from other countries. There are so many criteria and all of them must be evaluated and put into relation.

A more proportionate division than the current cost distribution (which is measured by 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 few criteria would only give the impression of a fairer financing, but would, in reality 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

[31] EP draft report, Regulation (EU) No 1093/2010, Article 62 – Paragraph 1 – Point ab (new), amendment 210.

[32] EP draft report, Regulation (EU) No 1093/2010, Article 62 paragraph 1 point b, amendment 211.

German NCA (BaFin). But such a complex key has the disadvantage that it needs a lot of time, very high introductory costs and increased administrative burdens and costs for the ESAs (compare under No 1 c).

3.3.3 Consequences for the distribution of voting rights

The markets of the Member States and their companies vary in size and, from the point of view of the Commission, therefore also benefit differently from the EU regulations of the market and the indirect supervision of the ESAs. However, in the event of any changes in the distribution of costs among 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 by the regulations of the market and indirect supervision by the ESAs 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.

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