MORE EUROPEAN SUPERVISION AND BETTER REGULATION ARE KEY ELEMENTS TO BUILD A TRUE CAPITAL MARKETS UNION

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The completion of the European **Capital Markets Union** is, alongside the Banking Union, an indispensable building block of a Single Market in financial services. It is also **a prerequisite to a strong and autonomous European Union capable of competing at the global level**. This is even more so as the post-Brexit EU is now a multipolar financial market and European businesses dramatically need market-based equity financing to recover from the health crisis.

Efficient European supervision is a cornerstone of the Capital Markets Union, together with the establishment of **an effective Single Rulebook**. However, previous legislative attempts towards more integrated European supervision have regrettably not received enough political backing from Member States, despite a broad consensus on the need for a consistent implementation of rules across the EU.

As efforts were made to promote supervisory convergence with existing tools, the French AMF believes that there is clear evidence that convergence exercises are now reaching their limits, in particular as they largely depend on national authorities' resources. The EU capital market needs a harmonised and unified supervision that ensures a level playing field for all market players and eliminates arbitrage opportunities. **It is high time Member States transformed declarations of intent into a tangible political support for a harmonised EU supervision of capital markets.** It is also time to draw lessons from recent legislative experiences and address the shortcomings that undermine nimble law-making and thwart the delivery of better regulation in the EU.

The AMF very much welcomes the fact that the European Commission has identified 'supervision' as a top priority for action in its renewed CMU Action Plan, and has responded to the related public consultation on 21 May 2021 [https://ec.europa.eu/info/consultations/finance-2021-esas-review_en]. The present paper summarises the main messages contained in the AMF's response to the Commission.

☐ Some of ESMA's convergence tools fall short of delivering on their objectives

There is no questioning that ESMA strongly contributes to establishing a common supervisory culture and convergent supervisory practices, through the use of convergence tools and powers attributed by Regulation (EU) 2010/1095 (e.g. Union strategic supervisory priorities, peer reviews, common supervisory actions, coordination functions…). However, **several tools have proved unsuitable and should be reviewed**, among which:

- T**he procedure for Q&As**: the new process for Q&As introduced by the recent reform is not efficient and significantly hinders the ability of ESMA to foster convergence amongst national authorities and a harmonised understanding of EU law among market participants. This is the result of the new requirement whereby ESMA must forward to the European Commission those questions that require an interpretation of Union law. This has created a bottleneck, causing major delays in the delivery of responses, which is counterproductive and goes against the primary goal of Q&As to swiftly address practical questions of implementation raised by market players.

- The so called ***no action letters***: the provisions of the ESMA Regulation in this respect are not those of a real no action letter as it exists in other jurisdictions; it is hence of very limited interest when a need for forbearance arises. A proper power to issue *no action letters* should equip ESMA with the ability to temporarily suspend the applicability of rules when they can have harmful consequences. ESMA needs a legal tool to avoid the deadlock which may occur when specific Level I or II provisions are unenforceable or require international coordination;

the ability to issue so-called no-action letters, with a European scope, similar to those used in the US for instance, would provide targeted and legally sound responses in those specific instances and offer European players a level playing field with their competitors across the world. A concrete proposal [https://www.banque-france.fr/sites/default/files/rapport_24_a.pdf] was put forward by the French *Legal Comity for Financial Markets of Paris* in 2018, which should deserve consideration by colegislators.

☐ Supervisory convergence is a valuable exercise but it will soon be reaching its limits

Absent any political support for centralising more supervisory powers in the hands of ESMA, the EU has chosen supervisory convergence as the 'by default' approach to foster a harmonised European supervision and support the building of a CMU. Owing to the fragmentation of supervision across national authorities and to the various domestic implementations of EU rules, ESMA and national authorities now spend considerable resources and efforts carrying out time-consuming exercises to foster convergence among themselves (e.g. peer reviews, common supervisory actions).

Still, supervisory convergence, although positive and useful in some specific situations, is no panacea and **cannot be the EU's only way to reach harmonisation of supervision at European level** in the long term. In practice, it can only be carried out efficiently on a small number of selected themes, because national supervisors have limited resources and time to devote to those exercises and cannot let themselves be diverted from their statutory missions. Supervisory convergence is by nature extremely time and resources consuming, for NCAs as well as for ESMA. With the continued legislative inflation in financial services regulations, relying solely on supervisory convergence will therefore quickly reach its limits, unless NCAs' resources are significantly increased.

The AMF believes that supervisory convergence is a second-best option which is not sustainable in the long run, that its limits should be acknowledged, and that, instead of relying solely on such approach, **the EU should seriously consider a shift towards a truly centralised supervision of certain categories of entities and activities.**

☐ European supervision makes sense for a number of entities and activities

Considering the limits of supervisory convergence amongst 27 jurisdictions, **it would be commendable to give more powers of supervision to ESMA, for certain categories of entities that display a significant / systemic importance and carry out cross-border activities in the EU**. ESMA should also be the prime candidate to directly supervise previously unregulated actors or activities, which EU law covers for the first time. This is the more straightforward way to ensure harmonised supervision at EU level for entities operating in different Member States.

- When it comes to **regulated entities whose activity features a strong cross-border dimension and whose size is beyond a certain level**, experience shows that potential supervisory divergences between EU jurisdictions are likely to have an adverse impact on the global efficiency of supervision, undermining the European level playing field and affecting market efficiency. It would be beneficial and justified to transfer authorisation and supervisory powers from national authorities to ESMA for such entities (e.g. EU CCPs, CSDs, market operators).

- Direct supervision should also be granted to ESMA whenever the EU decides to regulate **a financial activity, profession or type of product that was previously unregulated**. In such case, it makes sense to build regulatory expertise at ESMA level from the outset. For instance, should an EU framework be established to regulate providers of non-financial data, ratings and services in the future, it would be legitimate to entrust ESMA with authorisation and supervision tasks in relation to the entities covered by that framework. Likewise, granting ESMA the power of direct supervision of public offers of crypto-assets in the EU (scrutiny of white papers) and of crypto-asset service providers would create obvious economies of scale for all national supervisors and concentrate expertise in an efficient way, for the common European benefit.

While national options could be justified in some cases, it should be highlighted that reducing them at a minimum in the relevant regulatory framework is a prerequisite for transferring the direct supervision of entities or activities to ESMA.

☐ The governance of ESMA needs revisiting to allow for a more European dimension in the decision-making process

The current governance framework of ESMA does not allow for full objectivity, efficiency and independence, as the governance structure is composed mainly of national authorities, both at the Board of Supervisors and Management Board levels; and the decision making process involves only national authorities, most decisions being taken at the Board of Supervisors level and by simple majority voting.

Although some aspects of ESMA's governance have been rightly adjusted by the ESAs Review in 2019 (Chair person voting right; Board members' abstention from participating in the discussion and voting in relation to issues that might be considered prejudicial to their independence; specific procedure for peer reviews…), there remains a strong **need to improve this governance in order to enhance the European dimension** in the decision-making process. It is a matter of credibility for the European authority.

Reinforcing the role of the Management Board, and its independence, is essential in this perspective. Depending on the decisions to be taken, different decision-making settings could be established:

- ↗ Decisions on supervisory convergence should be taken by an independent Management Board composed of permanent members (while preparatory work could be undertaken by committees composed of representatives of national authorities). Decisions concerning entities under direct supervision by ESMA should also be taken by the Management Board under such new setting after having heard the views of the home competent Authority.

- ↗ All other strategic decisions should remain in the hands of the Board of Supervisors, and be taken by weighted majority voting: this would cover all normative or interpretative work (RTS/ITS, technical advice requested by the Commission as a basis to draft delegated acts, guidelines, Q&As).

Finally, the structure and source of ESMA's financing should remain closely linked to its governance, in particular as regards voting modalities (for instance, if weighted voting is generalised at Board level as advocated, then participation to financing obligations should not be as stringent for members having a lesser vote). It is also important to ensure sufficient flexibility, so that ESMA is able to adapt quickly to external/market developments and finance important new projects, in order to properly fulfil its missions and cope with increased supervisory powers.

☐ In parallel, completing a true Single Rulebook requires simplification and more coherence

The work carried out by ESMA when developing technical standards, guidelines and recommendations, has contributed very positively to harmonising the EU Single Rulebook, and ESMA deserves credits in that respect. However, recent practical experience shows that such record is undermined by unreasonable deadlines set by co-legislators at Level I when laying down Level II empowerments, a tendency to accumulate excessive details in EU law, as well as a lack of proper sequencing between the application of Level I and II provisions that would ensure smooth appropriation by regulated entities.

More generally, it is important to **simplify the European normative process and rationalise financial regulation**. It is a condition of efficiency for the Single Market and for the EU's competitiveness globally. In practice, this would mean transferring from Level I to Level II certain quantitative provisions, to allow for a more flexible recalibration should the need arise in the future. Level I should focus on general principles of regulation, while specific details in relation to those principles should be developed at Level II. At the same time, co-legislators should strive to contain unnecessary inflation of Level 2 empowerments, and no work should be undertaken at Level II unless it is clearly mandated by the Level I. Besides, the agility of EU law would be greatly enhanced if the application of Level I provisions were made conditional on the prior adoption of related Level II provisions. This would spare regulated entities from having to apply requirements for which Level II specifications are still missing (as has occurred lately).

It would also avoid the need to perform quick-fixes when the delegated acts are not ready in time (cf. MiFID II & PRIIPS precedents).

Finally, it is essential to **aim for maximum harmonisation of texts**, and to minimise opportunities for diverging national interpretations. Indeed, directives (especially those of minimum harmonisation) leave large possibilities for national authorities to adopt autonomous supervisory stances. National options should be reduced to the bare minimum and maintained only if duly justified (e.g. irreducible specificities of national law). Overall, the presence of options in EU acts whereby Member States may decide whether or not to opt for a particular regime may represent barriers to a maximum harmonisation in the EU, thus creating potential forum shopping for market players. The choice of regulations rather than directives should be systematised by the Commission in the future, especially where financial products benefitting from a European passport are involved, since diverging implementations by Member States have the potential to harm the European Single Market (e.g. UCITS product rules).

The above proposals are consistent with the principles of better regulation and, if endorsed and implemented with diligence and care by European institutions, would greatly contribute to enhancing the EU Single Market's competitiveness, and the EU's sovereignty and autonomy.