

## **FESE Position Paper Amendments to the European System of Financial Supervision and the Review of the European Supervisory Authorities**

### **1. Introduction**

The Federation of European Securities Exchanges (FESE) represents 35 exchanges in equities, bonds, derivatives and commodities through 19 Full Members from 28 countries, as well as 1 Affiliate Member and 1 Observer Member.

FESE is a keen defender of the Internal Market and many of its members have become multi-jurisdictional exchanges, providing market access across multiple investor communities. FESE represents public Regulated Markets. Regulated Markets provide both institutional and retail investors with transparent and neutral price-formation. Securities admitted to trading on our markets have to comply with stringent initial and ongoing disclosure requirements and accounting and auditing standards imposed by EU laws.

At the end of 2016, FESE members had 8,982 companies listed on their markets, of which 6% are foreign companies contributing towards European integration and providing broad and liquid access to Europe's capital markets. Many of our members also organise specialised markets that allow small and medium sized companies across Europe to access the capital markets; 1,291 companies were listed in these specialised markets/segments in equity, increasing choice for investors and issuers. FESE is registered in the European Union Transparency Register with number 71488206456-23.

FESE supports efficient, fair, orderly and transparent financial markets that meet the needs of well protected and informed investors and provide a source for companies to raise capital and for investors to hedge their portfolios. Through their RM and MTF operations, FESE members are regulated by their NCAs which implement the rules and standards agreed by ESMA.

### **2. Summary of FESE position**

In considering the proposals from the European Commission on the ESAs Review, FESE believes the focus should be on the following high-level principles and objectives:

- Strengthening supervisory convergence within ESMA's current tools and structures
  - The proposals for new direct supervision are not justified
  - NCAs competence and knowledge needs to be utilised in European supervision
  - ESMA should have a stronger role in third country issues
- **Strengthening supervisory convergence should be achieved within ESMA's current tools and structures**
- FESE has a very positive view of the overall workings of ESMA. Therefore, we are not in favour of radical changes to ESMA's role that could disrupt the market.
  - Given ESMA's increased workload and the recent application of new markets regulation such as MiFID II/MiFIR, the ESAs review provides an opportunity to ensure that ESMA can continue to fulfil its current function properly and strengthen its role.
  - While FESE believes that ESMA already has the correct range of tools to be able to deliver supervisory convergence, **we also broadly support the package of measures to strengthen supervisory convergence**: a single rulebook for financial services is incomplete without greater consistency and convergence of supervisory practices.
  - The adoption of the proposals for reform of supervisory convergence would allow ESMA to reinforce the EU's Single Market and contribute to the delivery of the Capital Markets

Union (CMU), while utilising National Competent Authorities' (NCAs) knowledge in terms of local rules, practices and business models.

➤ **FESE does not support extending direct supervision by ESMA for Prospectus Approval, Data Publication Services and Benchmark Administrators**

- ESMA should not take a direct supervisory role in areas where NCAs perform these roles effectively, as this has not been sufficiently justified by the Commission's impact assessment. Before any consideration of transferring these tasks to ESMA, it must be demonstrated that supervisory coordination via ESMA, supervisory colleges and supervisory convergence (both current and strengthened as proposed by the European Commission) across the NCAs has not achieved its objectives.
- In contrast to measures to improve supervisory convergence, direct supervision runs the risk of undermining key elements of the Single Market's regulatory and supervisory structures.
- Proposing changes to legislation that has not yet been implemented introduces uncertainty and unpredictability and is likely to drive business outside the EU.
- The Commission proposals for direct supervision would lead to counter-intuitive outcomes, such as fragmented supervision of trading venues' infrastructure as well as a duplication of responsibilities and costs:
  - **Prospectus Approval:** NCAs have already developed the experience and expertise to review the prospectuses which are within the remit of the proposal and local ecosystems have evolved around these markets; this efficient and effective approach cannot be easily replicated. If approved, this proposal would jeopardise the EU's firmly established position as a leading market in listing the corresponded securities, as it would create disruption and confusion in a well-functioning market, which is not in line with the objectives of the CMU. Lastly, the final Prospectus Regulation was only published in 2017 and full implementation will only take place by mid-2019 and therefore, there has not been any possibility at this stage to assess the functioning of the incoming regime. For this reason, the proposal appears premature and is not in line with the principles of subsidiarity and proportionality according to Article 5 of the Treaty on the European Union.
  - **Data Publication Services:** The introduction of direct ESMA supervision over Data Publication Services would lead to a fragmentation of supervision. While ESMA would be responsible for the authorisation and supervision of APAs, ARMs and CTPs, NCAs would retain responsibility for the authorisation and ongoing supervision of the rest of trading venues' businesses. Additionally, MIFID II has only become effective on 3 January 2018, we believe it is premature to be considering such radical changes to supervision at this stage. Alongside being inefficient and potentially confusing, it would not reduce costs for NCAs in any way.
  - **Benchmark Administrators:** The proposed transfer of supervisory powers from the national level to ESMA appears premature and is not in line with the subsidiarity principle according to Article 5 of the Treaty on the European Union. The EU Benchmark Regulation (BMR) has only become effective on 1 January and has hence not yet been tested in practice.
- Instead of direct supervision, the focus should be on strengthening ESMA's role in supervising and co-ordinating supervision to ensure there is a level playing field across the EU. Therefore, developing the tools set out for supervisory convergence should be the way forward to enhance CMU targets and objectives.

- **NCA's are necessary for further development of European capital markets**
  - FESE wishes to strongly underline the need to recognise the importance of supervisors' understanding of the stakeholders under supervision and the markets they operate in. The right balance must be struck within the European supervisory system, between a centralised European approach and the role of NCAs. NCAs are necessary for further development of European capital markets due to their wealth of experience supervising their local markets and adapting the regulatory environment to best suit the local ecosystem, taking into account local habits, culture, historical solutions. This is the best way to achieve the objective of CMU while still ensuring the diversity of markets in the EU can be nurtured and prosper in the future.
  - Enforcing supervisory convergence should mean ensuring that legislation is implemented as intended by the legislator to establish a level playing field, while importantly identifying and recognising any situations in which there may be more than one way to achieve these objectives.
  
- **Third Country issues and Europe's role in Global Markets need to be part of ESMA's mandate**
  - FESE supports measures to strengthen oversight over third country market participants, via: (i) an extension of ESMA's powers to monitor on an ongoing basis regulatory and supervisory developments in third countries deemed as equivalent, (ii) a new ESMA monitoring role when it comes to effective supervision by NCAs of outsourcing or delegating activities outside the EU to resolve forum shopping concerns.
  - In addition, FESE proposes for ESMA to play a broader role in assisting the European Commission in preparing equivalence decisions as well as in their implementation. ESMA should closely involve NCAs in assessment of equivalence, given NCAs know best the practical consequences of such decisions on the markets they supervise.
  - In general, the coordination of supervision both within the EU and with third countries is important to ensure a global level playing field. A guiding principle in this context must be the assurance of reciprocal market access under equivalent conditions.
  - The ESAs, and in particular ESMA, should always consider the international dimension, such as the work of IOSCO to ensure that EU guidelines do not significantly differ from international standards.
  - There is a need to recognise that capital flows are global and that the European market should fit into a globally competitive model. Therefore, the Commission should focus on providing a vision for Europe on a global stage.

### 3. Detailed position on the Commission proposal

#### a. Increase in ESMA powers to deliver supervisory convergence

##### **Strengthening supervisory convergence should be achieved within ESMA's tools and current structures**

FESE strongly supports the ESAs objective to promote a common supervisory culture and foster supervisory convergence across the EU given its importance to establishing a level playing field and ensuring that legislation is implemented as intended by the legislator. Accordingly, FESE supports the majority of the measures included in the proposal to strengthen supervisory convergence as described below.

FESE agrees that there have been challenges to the delivery of supervisory convergence to date and that a more effective framework is required in the EU, particularly to address the risk of diverging supervisory practices across Member States.

The impact of diverging supervisory practices tends to be particularly significant in areas where there is a move towards high-levels of EU regulatory harmonisation, underpinning cross-border business and competition, for example in the area of secondary trading. For example, under MiFID I there have been situations in which differences of views across NCAs, combined with a lack of coordination at ESMA level, have led to differences in the approvals of pre-trade transparency waivers across the EU. FESE welcomes the introduction of provisions, under MIFID II/MiFIR, by which ESMA is required to issue non-binding opinions on proposed transparency waivers and play an important role in ensuring that markets and supervisory practices are aligned across the EU. Such mechanisms are an important part of delivering supervisory convergence, especially where the goal is high-levels of EU regulatory harmonisation.

However, we consider that, in seeking greater supervisory convergence, efforts should focus on those areas which can bring the greatest value without creating unnecessary additional duplicative burdens on either exchange services or NCAs. Enforcing supervisory convergence should mean ensuring that legislation is implemented as intended by the legislator to establish a level playing field, while identifying and recognising any situations in which there may be more than one way to achieve these objectives. At the same time, FESE wishes to strongly underline the need to recognise the importance of supervisors' understanding of the local or regional cultures and habits as well as regulatory frameworks and business models which may have been developed, benefitting market players and the CMU as a whole.

We believe that the ESAs – and ESMA in particular – already have a sufficient range of tools, which can be strengthened, to be able to deliver increased supervisory convergence. FESE believes that the focus should be on maximising the effectiveness of the tools ESMA currently has at its disposal as opposed to introducing new ones. Critically, greater supervisory convergence should not automatically undermine local competencies and expertise, particularly within NCAs. It is vital that supervisors' understanding of practical operation of the exchange deriving from their direct supervision as well as the regulatory frameworks and business models which have been developed should be maintained.

##### **FESE views on the specific proposals**

###### **(i) Current role of Peer Reviews and proposal for Independent Reviews**

In respect of the current tool of peer reviews, we note that the ESA rules provide for ESMA to undertake periodic reviews of the NCAs focused on, *inter alia*, the degree of convergence reached in application of EU law and in supervisory practice. In respect of the activities of FESE Members, we do not believe that

these peer reviews have been used extensively<sup>1</sup> and would strongly support an increase in their use in order to deliver strengthened supervisory convergence and cooperation.

In principle, we welcome the proposal to review supervisory practices via the ‘Independent Reviews’. While today the primary focus of the current peer reviews appears to be on the application of EU law, we would welcome a strengthened focus of the new review system on differences in supervisory practices. These Independent Reviews should take into account best practices and recognise the need for NCAs to have the flexibility to achieve the same outcomes by different means.

#### **(ii) Role of Strategic Supervisory Plans and Annual Assessments**

Enhanced coordination between the ESAs as well as between the ESAs and the NCAs is much appreciated by FESE for fostering consistent supervisory approaches. Nonetheless, setting strategic targets and priorities in context of the strategic supervisory plan should be closely monitored since it should not lead to de facto binding standards for NCAs, but should rather leave enough flexibility for national best practices and particularities (no “one size fits all” approach).

#### **(iii) Role of ESMA in Settlement of Disagreements**

We welcome the Commission proposal to give ESMA further powers to intervene on *its own initiative* in respect of resolving disputes between NCAs in cross-border situations in cases of a disagreement based on objective criteria, complementing the current situation where ESMA involvement is subject to NCAs requesting it. We note that the deployment of this tool today has been rather limited<sup>2</sup>. While we believe that an explicit mandate at Level 1 should be maintained, greater consideration by the Level 1 legislator to its deployment should be given, particularly in areas where there is a clear consensus on the need to achieve high levels of consistent regulatory and supervisory approaches across the EU.

#### **(iv) Role of ESMA in Collection of Information**

ESMA already has a strong role in the centralisation of trading data under MiFID II/MiFIR for the purposes of transparency calculations, tick size determinations and reporting. FESE considers that these trading data submissions from the industry and NCAs will give ESMA a definitive data set from which they can draw objective conclusions on the functioning and impact of the legislation on European markets.

FESE agrees that without good quality data it is not possible for ESMA or NCAs to perform their tasks. However, the task of day-to-day market supervision rests with the NCA for the relevant market which indicates that the NCA should be the main requester of additional data directly from entities.

In the context of breach of law investigations, we believe it is important that the proposed extension of ESMA powers to request information directly from market participants is clearly limited in scope to this area only. Any extension of powers to request information directly from market participants by ESMA going beyond breach of law investigations would likely complicate information requests venues receive from regulators, via duplication. FESE considers that, outside the changes in the context of breach of law investigations, the focus should instead be put on ensuring that the lines of communication between ESMA and NCAs are enhanced.

#### **(v) ESMA powers to recommend that NCAs investigate cross-border orders, transactions & activities that are a threat to financial stability and/or the orderly functioning of markets**

We consider that giving powers to ESMA to recommend NCAs undertake investigations presupposes that the body will have the requisite monitoring resources to cover markets (both in terms of

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<sup>1</sup> One recent exception to that has been the ESMA peer review of the NCA processes for prospectus approval

<sup>2</sup> NCA cooperation covering supervisory activity and information exchange under MiFID II, critical benchmarks under the Benchmarks Regulation and potentially in respect of Resolution Colleges determination of CCPs’ resolution plans under the proposed CCP Recovery and Resolution Regulation.

technology and people). This appears to be a duplication with current NCA responsibilities and would merely increase costs and blur respective responsibilities. FESE does not therefore support this proposal.

#### **FESE proposal**

In seeking greater supervisory convergence, efforts should focus on those areas which can bring the greatest value without creating unnecessary additional duplicative burdens on either exchange services or NCAs. Enforcing supervisory convergence should mean ensuring that legislation is implemented as intended by the legislator to establish a level playing field, while identifying and recognising any situations in which there may be more than one way to achieve these objectives.

- **Independent Reviews**: Support an increase in their use in order to deliver strengthened supervisory convergence and cooperation, while there is the need for NCAs to have the flexibility to achieve the same outcomes by different means.
- **Strategic Supervisory Plans and Annual Assessments**: Enhanced coordination between the ESAs as well as between the ESAs and the NCAs is much appreciated by FESE for fostering consistent supervisory approaches. Nonetheless, setting strategic targets and priorities in context of the strategic supervisory plan should be closely monitored since it should not lead to de facto binding standards for NCAs, but should rather leave enough flexibility for national best practices and particularities (no “one size fits all” approach).
- **Settlement of Disagreements**: Support proposal to give ESMA further powers to trigger the settlement between NCAs in case of a disagreement based on objective criteria or on NCA request, when mandated at Level 1.
- **Collection of Information**: Rather than additional powers, the focus should instead be put on ensuring that the lines of communication between ESMA and NCAs are enhanced. The parameters governing ESMA’s right to request information directly from market participants in the context of breach of law investigations should be well-defined and the outcome should not be an increase of ESMA requests to market participants for information above and beyond the scope of breach of law investigations.
- **ESMA power to recommend NCA investigations**: FESE does not support this proposal as it presupposes that ESMA would require duplicate resources to those of NCAs to able to monitor markets in order to make recommendations for investigations.

#### **b. Risks and unintended consequences of Direct Supervisory Powers**

##### **ESMA should not take on Direct Supervision in areas where NCAs perform these roles effectively**

FESE considers that there needs to be a compelling rationale for proposing a radical change from the current supervisory set-up to direct supervision by ESMA. FESE believes this rationale has not been provided by the Commission and we would question whether these proposals aimed at direct supervision meet the principles of subsidiarity and proportionality. In our view, the focus should be on strengthening ESMA’s role in fostering supervisory convergence and co-ordinating local NCAs to ensure there is a level playing field across the EU, rather than directly supervising certain activities/entities while other related activities/entities would still be supervised by NCAs. This can be delivered by adopting the majority of the Commission’s proposals on strengthening supervisory convergence.

In contrast, FESE considers that the Commission’s proposals to increase the Direct Supervisory Powers for ESMA would have the largest impact on market infrastructures, in particular services offered by exchanges, and would also lead to a duplication of responsibilities and costs. In principle, FESE is concerned over the direction of the proposed direct supervisory powers and as to whether these

proposals will achieve the stated aim of greater supervisory convergence. We are concerned that the proposed measures risk undermining key elements of the Single Market's regulatory and supervisory structures, introduce uncertainty and unpredictability and is likely to affect the EU's competitiveness in a global market.

### **Concerns with the Commission's Impact Assessment**

The Commission states there are concerns that the *incentive structure in ESA decision-making process leads to a lack of decisions in particular in the area of regulatory convergence and supervisory convergence, or decisions that are overly oriented towards national instead of broader EU interests*. We consider that the Commission has not given any concrete examples of which legislative files have been purposefully not fully implemented to the benefit of one Member State over another. The Commission would need to assess the actual impact of such regulatory divergence and whether this possesses an actual risk of arbitrage.

Furthermore, the Commission states that *the risks of regulatory arbitrage and regulatory or supervisory race to the bottom, notably in the context of possible relocations of financial firms following the United Kingdom's exit from the EU, increases the need for enhanced supervisory convergence across the EU*. FESE agrees that the ESAs have not fully used their powers and therefore, before centralising the supervisory power with ESMA and removing the local NCA, we would suggest that ESMA review of supervisory practices be strengthened first in order for them to be allowed to address any perceived regulatory arbitrage. Only after there has been full experience of these powers would the Commission be able to conclude on the necessity of moving towards a more centralised structure.

Finally, the Commission argues that *in order to deepen market integration and ensure more consistent supervisory practices and implementation of EU rules a more integrated .... supervisory framework ensuring common implementation of the rules for the financial sector and more centralised supervisory enforcement has been identified as key to the completion of the CMU*. FESE fully supports the CMU Action Plan and has worked closely with the Commission on initiatives to increase funding to the real economy. However, we firmly believe that the CMU will flourish based on the adoption of rules regarding access to market and funding sources, and not changes to supervisory structure. Moreover, the ESAs Review will not take effect for a number of years and NCAs will take the supervisory lead in the interim in capital markets. In order to provide certainty in the long term, we advise against a radical overhaul of the European supervisory structure.

FESE also wishes to highlight its support for the conclusions of the European Parliamentary Research Service (EPRS) in its initial appraisal of a European Commission Impact Assessment.<sup>3</sup> In this appraisal the EPRS states that *"The IA does not provide a thorough assessment of the economic, social and environmental impacts of the policy options to tackle current problems, but rather a description of their respective advantages and disadvantages, based on internal desk research and quite varied feedback from stakeholders"*<sup>4</sup>. As we have stated, there needs to be further analysis on the significance of the proposals and the impact they would have on European market functioning. This is also noted by the EPRS which states that more analysis is needed on the areas of ESMA governance and powers: *"There seems to be an imbalance in the IA, with the analyses on the funding of the ESAs much longer and more consistent than the ones on their powers and governance, even though the latter have the most complex set of options"*<sup>5</sup>.

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<sup>3</sup> [http://www.europarl.europa.eu/RegData/etudes/BRIE/2017/615634/EPRS\\_BRI\(2017\)615634\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2017/615634/EPRS_BRI(2017)615634_EN.pdf)

<sup>4</sup> Initial Appraisal of a European Commission Impact Assessment: Review of the European supervisory authorities, European Parliamentary Research Service (EPRS), December 2017, p. 8.

<sup>5</sup> Initial Appraisal of a European Commission Impact Assessment: Review of the European supervisory authorities, European Parliamentary Research Service (EPRS), December 2017, p. 5.

## **FESE views on the specific proposals**

Please find below the detailed comments that challenge the logic that direct supervisory powers will lead to greater supervisory convergence.

### **(i) Proposal for ESMA to be central approval authority for certain types of Prospectuses**

#### **There is no evidence that NCAs have failed in their role as supervisors**

The Commission Impact Assessment states that they have *identified certain types of prospectuses which, due to the nature of the securities and issuers concerned, involve a cross-border dimension within the Union, a level of technical complexity and potential risks of regulatory arbitrage which are such that their centralised supervision by ESMA would achieve more effective and efficient results than their supervision at national level.* Moreover, they state that *the centralisation of their approval, as well as all related supervisory and enforcement activities, at the level of ESMA will enhance the quality, consistency and efficiency of supervision in the Union, create a level playing field for issuers and lead to a reduction of the timeline for approvals. It will eliminate the need to choose a 'home Member State' and prevent forum-shopping.*

The final Prospectus Regulation was only published in 2017 and full implementation will only take place by mid-2019. Indeed, the topic of prospectus approval was fully debated during the negotiations on the final Regulation and it was concluded that no changes regarding responsibility for scrutiny and approval should be made. Therefore, there has not been any possibility at this stage to assess the functioning of the incoming regime and we consider that there is no rationale or legal foundation to support amending the approval procedure. There is no robust evidence provided by the Impact Assessment to support this proposal. We understand that the motivation to transfer prospectus review and approval powers from NCAs to ESMA is to address concerns regarding “potential” – according to the Commission explanatory note – regulatory arbitrage. However, we are not aware, anecdotally or otherwise, of any regulatory arbitrage relating to prospectus review and approval.

Furthermore, there is no evidence provided by the Commission as to how the proposal will “achieve more effective and efficient results than their supervision at national level” and “lead to a reduction in timeline for approvals”. There are concerns that any changes to the current approval process may hamper efficiency for markets participants which could jeopardise fund raising in the EU.

#### **Policy makers must consider the current role of EU listing venues in the global market**

The EU is currently a leading jurisdiction for the origination, distribution and listing of certain types of securities. Any disruption to the status quo would be to the detriment of the European capital market as originations and listings would be likely to migrate outside of the Union to jurisdictions that are perceived to better support issuers seeking to raise capital. Indeed, we are concerned that the Commission’s proposals significantly increase the risk of business moving outside the EU and damaging European capital markets which is completely at odds with CMU. If such a proposal is adopted, Europe stands to lose its competitiveness to other financial centres, e.g. in Asia and the US. This risk is heightened further in a post-Brexit environment.

We consider that the proposed amendments to the Prospectus Regulation, if adopted, will:

1. **Decimate the position of EU leading centres for the listing of specialist non-equity securities issued by EU issuers.** Given the specialist nature of these product types, it is crucially important that EU issuers can choose jurisdictions where the regulatory regimes reflect a deep understanding of specialist non-equity securities and have developed the experience and expertise to review the prospectuses relating to such securities in a competent manner, all of which is a necessary pre-cursor to listing these securities on regulated markets in these jurisdictions;



2. **Stifle competition, drive business away from EU regulated markets and annihilate EU's leading position** in the issuance of debt securities and consequently in the global listing market, as many non-EU issuers might choose alternative jurisdictions to issue their international debt instruments. This completely undermines the ambitions of CMU and will serve to discourage non-EU issuers, in particular, from seeking to raise capital and list their securities in the EU, known as the home for international capital markets.

#### **The proposal creates many operational difficulties**

NCA's have developed the experience and expertise to review prospectuses and have established very efficient and effective approval processes. We consider that these established approaches cannot be easily replicated. This work necessitates that the supervisor understands different legal structures, languages and has knowledge of various local sectors from every jurisdiction. In addition, it is not always clear if the issuance is "specialist" or not until the prospectus review process has commenced, so we consider that it would not be reasonable to transfer the approval process mid-way through a review. This will only make the approval process less efficient and creates risks in terms of market opportunities which is crucial for issuers. Furthermore, there are many important legal issues that do not appear to have been considered (for example, how can decisions be appealed? How can ESMA challenge NCA activities when still overseeing local NCA's carrying out the same activities?). Given the regime currently works extremely well, we would strongly caution against implementing these changes which are likely to significantly disrupt the market.

#### **FESE proposal**

- **There is no evidence or regulatory foundation to demonstrate a need for ESMA to have a formal role in the approval process for certain prospectuses.**
- **ESMA's role should focus on supervising the approval process of NCA's and ensuring a level playing field.**
- **Issuers should continue to be able to choose their jurisdiction for listing and apply for approval of their prospectuses through the NCA's in order to ensure there is no negative disruption to an already established and well-functioning market.**

- (ii) **Proposal for ESMA to be the central supervisor for all Approved Reporting Mechanisms (ARMs), Approved Publication Arrangements (APAs) and Consolidated Tape Providers (CTPs)**

#### **Data publication services are only one part of data providers' business that needs to be considered holistically in terms of supervision**

The Commission's starting point is that NCA authorisation and supervision of Data Reporting Services Providers (DRSPs)<sup>6</sup> will not be fully effective since the business is predominantly cross-border. The Commission argues that, as APAs and CTPs are designed to overcome market fragmentation by consolidating data, it is not consistent to supervise them in a fragmented (i.e. nationally based) way. In a similar vein, the Commission believes that there is no need for NCA's to be close to DRSPs as the business is cross-border in itself. Overall, the Commission argues that ESMA direct supervision would spare NCA's the responsibility of supervising a small number of entities across countries, implying more efficient processes and positive cost implications.

MIFID II provides the regulatory framework for the emergence of APAs, ARM's and CTP's within the EU. With the framework having only become effective on 3 January 2018, we believe it is premature to be considering such radical changes to supervision now. In addition, we are not aware of any extensive impact assessment nor cost/benefit analysis having been performed in this area that would legitimise a

<sup>6</sup> DRSPs include Approved Publication Arrangements (APAs), Approved Reporting Mechanisms (ARMs), and Consolidated Tape Providers (CTPs).

transfer of supervisory powers from the national to the EU level. Thus, the proposed radical overhaul of the supervisory regimes set out in MiFID II might infringe the subsidiarity principle. In view of the absolute need for market operators to be supervised by a supervisor having a deep knowledge of the eco-system in which they operate, market operators will under MiFID II/MiFIR continue to be supervised by their respective NCA and it is only natural that these NCAs also supervise the provision of data considering that this is an integral part of the operators' ecosystem that should not be supervised in isolation.

We are concerned that the introduction of direct ESMA supervision over DRSPs would lead to a fragmentation of supervision: while ESMA would be responsible for the authorisation and supervision of APAs, ARMs and CTPs, NCAs would retain responsibility for the authorisation and ongoing supervision of the rest of trading venues' businesses, including the market data franchise.

Such a fragmentation of supervisory responsibilities is problematic given that the provision of DRSPs and publication / reporting services for trading venues are generally fully operationally integrated. Commonalities across FESE Members include:

- From a service point of view, clients benefit from a one-stop-shop approach where **access to trading services also provides access to reporting services** without the need to setup additional connectivity.
- From an operational point of view, APAs and ARMs are both fully integrated in **trading venue systems for data collection**. The same operational setup and IT interface is therefore used to collect data for a range of purposes including, inter alia, for APAs, ARMs, order record keeping and position reporting for commodity derivatives.
- From a **data processing** point of view, eligibility checks for deferred publication are performed across trading venues and the APA. Similarly, controls on ARM data are integrated within broader trading venue checks.
- Lastly, **data dissemination** is handled both for the APA and trading venues via integrated systems.

In its Impact Assessment, the Commission **acknowledged the risk of parallel ESMA and NCA supervisory responsibilities for trading venues' market data businesses**. However, the Commission stated that this would not be a problem as they believe the activities would be located in different entities. This is not in line with how FESE members organise their market data businesses, as outlined above.

Furthermore, **FESE does not agree with the implied premise that ESMA supervision would reduce supervisory costs** given that NCAs would be spared the responsibility of supervising a small number of entities across Member States. FESE Members provide APA and ARM services on the basis of home state authorisation and supervision, on a pan-EU level on the basis of the passporting arrangements. Placing the supervision of these services under the responsibility of ESMA would have no significant impact on the supervisory costs of NCAs in this area as they would still be in charge of the supervision of trading venues for the rest of their businesses.

On the contrary, **economies of scale** for the NCAs in supervising both the DRSPs and the broader trading venue business would disappear, alongside the risks of fragmentation and duplication costs as noted above. The Commission argues that ESMA direct supervision of DRSPs would improve the quality of data collection as it would remove the risk of data being stored in different formats across entities and Member States.

FESE questions the degree to which this is an issue given that the existing EU legislative framework, MIFID II in particular, already lays out very detailed and harmonised standards covering data collection.

In the event that - notwithstanding these clear harmonised rules - divergences emerge across Member States, we believe ESMA would be able to resolve them, even with its existing powers and definitely in the context of a strengthened convergence framework.

Moreover, the Commission states that NCAs might not have the necessary capacity to detect, assess and monitor potential problems which might emerge in other Member States in relation to the activities of DRSPs. The introduction of direct supervision would, in the Commission's view, allow ESMA to better compare business and best practices, while ensuring that the users of data can also rely on fully harmonised approaches to supervision.

The exact nature of the 'problems' referred to by the Commission is not made at all clear. Under the model where APAs and ARMs will be authorised and supervised by the home Member State, other authorities would be able to raise issues in the event they arise. Moreover, coordination within ESMA via (strengthened) convergence would also be an option. On the contrary, direct ESMA supervision is not required to achieve this objective, certainly not in respect of facilitating better comparisons of business and best practice.

FESE strongly believes that it would be more prudent to allow the emergence of APAs, ARMs and CTPs to be developed within the framework of existing regulatory and supervisory provisions in the interests of providing all participants with a degree of stability going forward. It is also worth noting that final MiFID II rules will put in place the provisions for an industry led solution for a CTP. Moreover, supervisory responsibilities will be unclear if certain parts of the business are supervised by NCAs and others by ESMA.

#### **The proposal does not recognise value of local NCAs in developing the supervisory structure**

FESE believes that policy makers should value the development of supervision at a national level given the influx of new regulation. This development includes not only data analysis, but also increased access to information about markets and companies and the preservation of invaluable local expertise. Moreover, enforcement will initially need to be at a national level and this should not be abruptly removed.

#### **FESE proposal**

- **There is no evidence to demonstrate a need for ESMA to have a formal direct supervisory role in data publication services.**
- **ARMs, APAs and CTPs should continue to be supervised by NCAs.**

**(iii) Proposal that for any benchmark administrator that has a 'Critical Benchmark', ESMA will become the central supervisory authority for all benchmarks offered by that administrator.**

#### **The BMR has only become effective on 1 January 2018, therefore we do not support radical changes to the supervisory structure at this stage.**

There is no evidence at this point in time that supervisory colleges would not be in the position to effectively authorise and supervise administrators of Critical Benchmarks. As such, the proposed transfer of supervisory powers from the national level to ESMA appears premature and is not in line with the subsidiarity principle according to Article 5 of the Treaty on the European Union. The BMR has only become effective on 1 January 2018 and the supervisory structure contained in it has hence not been tested in practice.

Any consideration to expand ESMA's direct supervisory powers would again require in-depth assessment first, a cost/benefit analysis and preceding consultation of the affected entities to provide

evidence on the effectiveness of the envisaged supervisory structure to justify and legitimise a transfer of supervisory powers from the national to the EU level. Any evaluation of the supervisory regime for Critical Benchmarks should be undertaken within the foreseen BMR review and take into account the BMR transitional provisions. We understand that this constitutes a new regulatory responsibility for all NCAs and they will need to build up expertise and knowledge on these services. In order to achieve an efficient regulatory outcome, both NCAs and benchmark administrators will work closely together with respect to the application of the BMR. Therefore, we caution against any proposal that would undermine this work in the future and undo the cooperation between benchmark administrators and NCAs which is working efficiently.

Furthermore, FESE observes that material changes to the criteria for designating a Critical Benchmark as defined within the BMR are proposed. The originally envisaged criteria has not even been tested in practice, let alone proved inefficient. Thus, FESE is of the opinion that the de minimis threshold for Critical Benchmarks should remain in place as lined out in the BMR. Such material changes to the BMR are not in line with the purpose of the ESAs Review. Therefore, the ESAs Review should focus on the details of powers to authorise and supervise administrators of Critical Benchmarks and of all benchmarks that are used in the Union but administered outside.

### **Positive Experiences of Supervisory Colleges as an example**

Regarding supervisory colleges, it should be considered that the current EMIR college structure functions well and the lead NCAs have been fulfilling their critical role in a sound manner and have been very useful in terms of knowledge sharing and fostering cooperation between regulators. The supervisory college structures are best suited as a tool to exchange information and to align, if necessary, participating NCAs on best practice in other colleges. While supervisory colleges do indeed increase supervisory cross-border cooperation and have the potential to ensure appropriate supervisory convergence, there is always room for improvement, e.g. as regards current structure and working methods. There are concerns that supervisory colleges as currently functioning, may not guarantee the achievement of a level playing field. For example, the number of representatives in a college makes it virtually impossible for it to carry out efficient supervision. Regarding the number of representatives, there are also concerns that discussions in college meetings often do not contribute to bringing issues forward or towards a solution. A suggested way to address such inefficiencies may be to clarify the working methods and the roles of each participant. In particular, it is important that the lead supervisor has a clear role and drives the work in the college.

#### **FESE proposal**

- **There is no evidence to demonstrate a need for ESMA to have a formal supervisory role for non-critical benchmarks.**
- **Non-critical benchmarks should be supervised by local NCAs as agreed in the BMR.**

### c. Role for ESMA in Third Country Equivalence and International Convergence

#### **Further recognition of Third Country issues and Europe's role in Global Markets**

FESE proposes for ESMA to play a broader role in assisting the Commission in preparing equivalence decisions as well as in the implementation of such decisions. For ESMA to deliver fully informed advice to the Commission in respect of equivalence, FESE considers that ESMA should closely involve NCAs in the process of assessing equivalence, given NCAs know best the practical consequences of equivalence decisions on the markets they supervise.

Convergence and harmonisation in relation to third country aspects are important in order to maintain a level playing field and financial stability in global capital markets. This is valid for matters within the EU as well as for matters which include any type of third country aspects. A general guiding principle in this context must be the assurance of reciprocal market access under equivalent conditions.

Moreover, delivering these objectives, FESE would recommend that the ESAs, and in particular ESMA, always consider the international dimension, such as the work of IOSCO to ensure that EU guidelines do not significantly differ from international standards. We would urge ESMA to advocate that EU wide legislation follows its own previous guidance or international guidance to avoid legal uncertainty and avoid unnecessary compliance costs.

#### **FESE supports role for ESMA in Third Country equivalence monitoring**

FESE supports the Commission's proposals to strengthen oversight over third country market participants, via: (i) an extension of ESMA's powers to monitor on an ongoing basis regulatory and supervisory developments in third countries deemed as equivalent, (ii) a new ESMA monitoring role when it comes to effective supervision by NCAs of outsourcing or delegating activities outside the EU to resolve forum shopping concerns.

Equivalence regimes across EU legislative texts differ. FESE believes that an appropriate mechanism at EU level is important to ensure that third country standards are equivalent to European ones and that equivalence decisions can be assessed on a recurring basis. Therefore, FESE welcomes the proposal to extend the ESAs' role in ensuring constant monitoring of third country regulation and supervisory standards and to develop administrative arrangements with third countries.

Regarding a new ESMA monitoring role when it comes to effective supervision by NCAs of outsourcing or delegating activities outside the EU to resolve forum shopping concerns, we consider that such a mechanism would prevent firms based in the EU from potentially undercutting EU regulation by outsourcing their activities to jurisdictions with a lighter regulatory regime. This can serve to strengthen the EU by ensuring a consistent approach to outsourcing and delegating activities.

In addition, Brexit will have a fundamental impact on financial markets and their regulatory frameworks. In the light of Brexit, thought could be spent to review EU files and third country equivalence provisions that were designed under the premise that the UK as the biggest European financial market is part of the EU sample. We would urge ESMA to advocate that EU wide legislation follows its own previous guidance or international guidance to avoid legal uncertainty and avoid unnecessary compliance costs.

#### **FESE proposal:**

- (i) Support enhancing and clarifying ESMA's power in assisting the Commission to prepare equivalence decisions;**
- (ii) Support an extension of ESMA powers to monitor on an ongoing basis regulatory and supervisory developments in third countries deemed as equivalent; and,**
- (iii) Support a new ESMA monitoring role when it comes to effective supervision by NCAs of outsourcing or delegating activities outside the EU to resolve forum shopping concerns.**

## d. ESMA Governance & Decision Making

### **ESMA decision-making process must reflect the competence and expertise of NCAs**

In principle, FESE supports the Commission's aim to improve the decision-making processes within ESMA. The competencies and expertise of NCAs, however, need to be effectively reflected in the proposed Executive Board composition and decision-making procedure. In order to achieve the Commission's aims, we would caution against creating an overly complex relationship between the Executive Board, the Board of Supervisors and the Executive Session for CCPs, otherwise there would be serious concerns as to whether a new structure would function efficiently in a crisis. Interaction and responsibilities of these bodies might therefore need clarification.

In addition, the governance arrangements of ESMA are key to ensure an effective and efficient supervisory convergence. In this respect, FESE considers that the newly proposed Executive Board should have a composition ensuring that this body is in a position to fully comprehend the diversity of the various European financial ecosystems and take decisions that are relevant and executable in the whole of the EU. This is paramount to ensure that the Executive Board fosters convergence without taking a "one-size fits all" approach which will damage European financial markets. Hence, it would seem sensible to consider the impact of decisions on the various financial markets within the EU. Subsequently, thought could be spent if this circumstance should be reflected in the weight of votes within the governance bodies.

FESE would welcome more transparency on the internal working structure of ESMA Working Groups, as well as periodic feedback from the decision taken by the various ESMA departments before the decision is taken by the ESMA Board of Supervisors. FESE would also ask the ESAs to consider adopting better procedures for instances when deadlines included in Level 1 cannot be fully met. In recent years, many pieces of legislation have been subject to delay and/or Level 2 and 3 have not been finalised in time to allow the industry to prepare for correct, timely implementation. A new procedure could allow regulated entities to ask a supervisor for clarity regarding conflicts with implementation timelines. FESE considers that legal clarity should be provided as early as possible to promote efficiency and correct implementation.

### **Need for more prominent role for Stakeholder groups**

A pre-condition for a more prominent and consulting role for the ESMA Securities and Markets Stakeholders Group (SMSG) should be clear rules to ensure balanced representation on the group in terms of its composition. Subject to such rules being adopted, FESE would welcome a role of the stakeholder groups to potentially raise concerns when they consider that an ESA has exceeded their competences and submit their opinion to the Commission.

Stakeholder group Members have a significant contribution to make to the discussions with a view to providing relevant input to the ESAs. However, often there is no introduction of who is present in the meetings and it is difficult to identify the individuals participating from the ESA secretariats and NCAs. Clearly, more structured transparency in the meetings should enable the sharing of relevant experiences and contribute to a useful discussion. Moreover, improvements on the structuring of the meetings, in terms of providing regulatory/institutional context would be useful for those individuals appointed as a result of their practical industry experience, and who may lack an understanding of the exact mechanics of the regulatory process.

#### **FESE proposal**

- **Proposed changes to ESMA's governance and decision-making procedure must not add any further complexity to the current procedures and should respect the diversity of the various European financial ecosystems.**
- **Adopt clear rules to ensure balanced representation on ESMA SMSG.**

- **Support the role of the stakeholder groups to potentially raise concerns when they consider that an ESA has exceeded their competences and submit their opinion to the Commission.**

#### **e. Level 3 Guidelines and Q&As**

FESE's experiences of ESMA's work in respect of providing Level 3 clarifications on key elements of the MiFID II regime have been positive, particularly in the context of ESMA providing a form of ex ante approach for supervisory convergence. We welcome the fact that, during the process of finalising the rules and standards for implementation, ESMA is generally open to stakeholder input and, where possible, provides helpful feedback. However, we would warn against supervisory convergence being used as an argument for the ESAs to move into *de facto* policy making.

FESE has contributed to the work of ESMA on guidelines and recommendations, and in many instances these guidelines provide useful guidance for NCAs to supervise the application of the relevant legislation. We also support the work that ESMA has done providing guidelines ahead of legislative proposals, such as 'Microstructural Issues'. However, we would ask the ESAs to consider the timing between the issue of pre-legislation guidelines and the proposal and application of the fixed rules.

FESE considers that the ESAs could be involved earlier on in the Level 1 negotiations, perhaps in an observer capacity. This may facilitate and assist the articulation between the legislative and rule making process, especially at Levels 2 and 3. In addition, Level 1 could benefit from technical experts being involved at an early stage to provide expert advice and present reliable data on which to base assessments. Therefore, we would encourage ESMA to be more vocal in expressing its views on the structure and content of Level 2 legislation implied by the co-legislators already during Level 1 discussions, in order to avoid unnecessary difficulties in preparing Level 2.

In respect of the Level 3 tools, overall, we believe that they constitute a useful mechanism to provide clarity on the way NCAs will interpret and implement, on a consistent basis, the Level 1/2 provisions. At the same time, we note the differences in approach in respect of the drafting of guidelines and recommendations on the one hand – requiring a formal process of consultation – and Q&As on the other, which do not. While we appreciate the need for flexibility in respect of the drafting of Q&A, specifically in order to address issues as they arise, we believe the process by which industry and stakeholders can provide input to the process could be strengthened. FESE suggests that the process for developing Guidance becomes more transparent. For the Level 2 rulemaking, the ESAs are obliged to, and indeed do, conduct consultations as well as hearings. FESE welcomes the proposal to strengthen the role of stakeholder groups and the industry within the process of issuing guidelines and recommendations. It needs to be considered to expand the consultation process for guidelines and recommendations to Q&As, in order to ensure that decisions are based on the broadest possible input and expertise. Especially as Level 3 tools are sometimes used in areas where full harmonisation is not sought, and where on the contrary it is intended to facilitate implementation of rules where there is indeed room for flexibility and adaptation to local habits and business models, input from industry across the whole of EU may be no less useful than when it comes to rules where harmonisation and convergence is the main goal.

#### **FESE proposal**

- **Level 3 Guidelines and Q&As: Support strengthening and formalising the Level 3 process to enable input from stakeholders.**

## f. ESAs Funding

Currently the vast majority of NCAs in the area of financial services are funded through industry contributions. FESE understands that efficient fulfilment of supervisory tasks requires adequate resources for the ESAs. However, this must be considered in line with the final direct supervision roles that ESMA may take up with the caveat that an increase of industry funding of ESMA should be met by a corresponding reduction of the fees exchanges pay to their NCAs. It needs to be avoided that entities affected would be directly contributing both to NCAs' funding and to ESAs' funding, which would result in cost inefficiencies and duplication of the financial burden for supervised entities. Additionally, in introducing partly industry financing, our Members believe that the framework should impose an explicit requirement on NCAs to demonstrate that domestic supervisory fees no longer cover any indirect funding requirement from industry for the ESAs.

Overall, FESE welcomes the proposal that existing national structure should be used to collect the fees, within a common methodological framework. In principle FESE supports the structure of the Commission proposal to retain the current public funding and combine this with contributions from the industry.

We consider that a reasonable level of fees and contributions will have to be found to keep costs of financial services down and ensure competitiveness of the EU market place. Procyclical effects might be taken into account, since in times of a crisis, an increase in the burden on supervisors will likely be matched by a weakening of industry's capacity to pay fees. Moreover, the impact of Brexit on staffing and funding needs of the ESAs needs to be considered, since the UK currently provides a significant portion of the EU's financial markets. It should be ensured that the envisaged increase in staff and funding would not lead to further increase in their mandate.

### **FESE proposal**

- **Support partial industry funding for ESMA but believe existing national structures should be used to collect the fees, within a common methodological framework, in line with the final direct supervision roles that ESMA may take up.**
- **It is important to ensure a reasonable level of fees and contributions and avoid cost inefficiencies and duplication of the financial burden for supervised entities.**