January 23, 2018

European Commission Feedback request on the legislative proposals for reforms to the European system of financial supervision

Final Response

FIA and ISDA (together the Associations) welcome the opportunity to provide feedback on the European Commission's (Commission) published Draft Implementing Regulation on the operations of the ESAs and the proposed supervisory framework. The joint response is particularly focused on ESMA, given the nature of our memberships.

The Associations support the overall goal of the ESAs review package aimed at (i) reinforcing coordination of supervision across the EU, (ii) extending direct capital markets supervision by ESMA where appropriate, but only where ESMA has built up the necessary expertise and capacity to take over new supervisory powers, (iii) increasing engagement, enhancing consultation processes and creating a culture of continuous dialogue with market participants, (iv) improving governance and funding of the ESAs, and (v) promoting sustainable finance and FinTech.

The current European supervisory set-up for both banking and capital markets has proven to be efficient, maintaining market stability and integrity in times of market stress. The Associations believe that increased supervisory convergence would help to deepen capital markets in Europe, key to a more diversified source of funding for European companies. In addition to increased convergence, there is an opportunity to increase the efficiency and competitiveness of Europe's capital markets through initiatives to streamline and simplify supervisory processes and remove duplication. The proposed recalibration of supervisory structures should be considered carefully, to ensure structural stability, given that relevant EU legislation is still in the process of implementation.

We have the following comments:

Executive Summary

The Associations support the overall goal of the ESAs review package.

1. The governance structure should provide for independent, objective supervisors accountable to legislators but operationally independent. It is important to recognise the very different nature of capital market supervision (which tends to be varied by product and participant, as well as global in nature) versus bank supervision (which typically involves more similar institutions doing a smaller set of activities which are often more locally oriented) and ensure an

appropriately differentiated policy approach at each ESA. Supervisory convergence should be the primary focus of the ESAs;

2. We welcome the introduction of an independent Executive Board with full-time members replacing the current Management Board but **recommend** that further clarification should be provided regarding the role of the full-time members of the Executive Board in the management of the ESAs. We agree that the Board of Supervisors should continue to be the main decision-making body of the ESAs;
3. We **recommend** further clarifications as to how the proposed Executive Board would work with the proposed CCP Executive Session on the authorisation of CCPs (EMIR Part 2.2);
4. We **recommend** that ESMA and NCAs take a differentiated approach to supervision with regards to wholesale and retail customers;
5. Given the need to increase resources of the ESAs, we accept a funding system partly funded by the industry, subject to a dedicated industry consultation and within certain parameters. There is a need for fees and contributions to be commensurate as a reasonable level of fees will ensure that the provisions of financial services remains cost effective and that the competitiveness of the EU market place is not affected. Further clarification is required on the collection mechanism;
6. Fees should be fairly allocated across the regulated population. It would be inappropriate to carve-out specific categories of entities just because they are smaller in size than the largest financial institutions. We recognise that proportionality should be at the heart of the allocation;
7. We **recommend** increased engagement between the ESAs and the industry and support the creation of a more robust consultation culture with increased transparency around policy decisions;
8. New powers for the ESAs: any consideration to expand ESMA's direct supervisory powers should respect the subsidiarity principle according to Article 5 of the Treaty of the European Union and would first require in-depth assessment, including corresponding cost/benefit analysis and ideally also preceding consultation of concerned entities. In this context, the value of supervision by national authorities should be recognised, given their strong knowledge of local markets, with their particularities (specific products, client base, and tax regimes), best practices and national legal frameworks. National supervisors also have the best understanding of practical operations and business models of supervised entities and have established networks of coordination between regulators;
9. Regulatory forbearance: we believe that the ESAs should be provided with powers to temporarily suspend the application of certain regulatory requirements in certain circumstances and within a reasonable timeframe - effectively relieving firms from enforcement action during that time period;
10. Amendments to timeframes: the implementation of significant regulatory reform has highlighted the importance of providing the ESAs, NCAs and market participants with adequate timelines to deliver financial reform;
11. ESA involvement in the Level 1 process: we believe it is important to give the ESAs observer status for Level 1 negotiations, at least at the stage of trilogies;
12. Reform of the Q&A process: we support the proposal that the ESAs should conduct public consultations on guidelines and recommendations, and believe this should extend to Q&As; and
13. We support ESMA supervision for pan-European crucial IBOR benchmarks (i.e. Euribor, Eonia, which have already been determined critical by the Commission). National competent authorities should retain the supervisory authority over Benchmarks at national level and retain the ability to determine if their local benchmarks are critical.

I. Governance

As part of the Capital Markets Union (CMU), the Five Presidents' Report on Completing Europe's Economic and Monetary Union of June 2015 highlighted the need to strengthen the EU supervisory framework, leading ultimately to a single capital-markets supervisor.

Effective supervision requires clear responsibilities, rules for decision-making and procedures that avoid redundancies and allow for efficient processes with regard to market participants, as time matters when it comes to financial stability, especially in market stress situations.

When considering the current political and regulatory desire to accelerate the integration of supervision of certain sectors of the financial industry, the question is how should supervisory structures be designed and who should be in the driving seat in order to ensure both financial stability and legal certainty as well as operational functionality of the supervised entities concerned. The governance structure should provide for independent, objective supervisors accountable to legislators but operationally independent. It is important to recognise the very different nature of capital market supervision (which tends to be varied by product and participant, as well as global in nature) versus bank supervision (which typically involves more similar institutions doing a smaller set of activities which are often more locally oriented) and ensure an appropriately differentiated policy approach at each ESA. Supervisory convergence should be the primary focus of the ESAs.

Establishment of the Executive Board and clarifying the role of the CCP Executive Session

We welcome the Commission proposal for a more effective governance structure for the ESAs by introducing an independent Executive Board with full-time members, which are selected on their merits and competencies - replacing the current Management Board.

However, we believe further clarification should be provided on what the role of the full-time members of the Executive Board will be in the management of the ESAs. It should be made clear whether the Executive Board members would be given management responsibilities for divisions of the ESAs (akin to the BaFin or ECB Executive Boards), or if they would sit on top of the existing management structures and not have management responsibilities (akin to the US independent regulatory agencies such as the SEC and CFTC). It should be made clear whether the Executive Board members would simply replace existing management positions, or if they would add to them.

Board of Supervisors and CCP Executive Session

We agree that the Board of Supervisors should continue to be the main decision-making body of the ESAs and support the proposal to include full time members of the Executive Boards to the Boards of Supervisors.

For CCPs, the supervisory college structure functions well and the lead NCAs for the affected entities have been fulfilling their critical role in this context adequately. They have been very useful in terms of knowledge sharing and fostering cooperation between regulators.

We would question how the proposed Executive Board would work with the proposed CCP Executive Session in the Commission proposal on the authorisation of CCPs and requirements for the recognition of third-country CCPs (EMIR Part 2.2). Having both an Executive Board and CCP Executive Session may be duplicative

and result in substantial organisational overheads within ESMA. There should be further consideration as to how these bodies can be streamlined while still ensuring the operational independence of the CCP Executive Session.

Creating a culture of consultation and transparent policymaking

Level 3 Measures

Consultation on guidelines and recommendations

This proposal presents an important opportunity for a step-change in the approach to industry consultation by the ESAs, with increased transparency of the policy decision process coupled with robust information sharing and communication arrangements with financial market participants (as well as between rule makers/ supervisors within the EU and beyond).

We support the Commission proposal that the ESAs should conduct public consultations on the guidelines and recommendations they issue, particularly given that Level 3 instruments can provide important clarifications on implementation matters. Generally, we encourage the ESAs to engage in continuous discussions with industry and other stakeholders throughout the Level 3 process.

The proposal should be amended to also cover Level 3 Q&As. Q&As are considered to be Level 3 instruments that provide important clarifications and/or interpretations on implementation matters. However, they do not have a legal status in the ESAs Regulation. This lack of clarification means that these instruments are not binding unless communications from NCAs indicate otherwise.

The Q&A process should therefore be made more transparent, with increased visibility as to the areas of interpretation that ESMA is working on. Stakeholders should be provided with opportunity to input into the development of the ESA Q&As before they are finalised, as they are well positioned to provide views on the likely impact of any draft guidance, which should help to inform the development of a fully considered Q&A. This could also be achieved by increased use of stakeholder groups. In addition, impactful Q&As should be accompanied by reasonable implementation timelines to allow for sufficient time for the industry to comply with these new Q&As.

Cost benefit analyses of recommendations

We welcome the proposed reforms requiring the ESAs to carry out cost-benefit analyses on guidelines and recommendations.

Stakeholder groups

Consulting with market participants, professional users of markets and consumers is the bedrock of effective rulemaking. While the consultative working groups/ stakeholder groups are an important component in ensuring a formal consultation process, consultation should not be restricted to the individuals who are members of these groups. With capital markets rulemaking in particular, it is vital that there is an ongoing process of engagement with interested parties to enable ESMA to fully understand sometimes nuanced and complex issues. Such an approach would be more aligned with the Commission's Better Regulation philosophy. Moreover, active ongoing engagement with market participants would assist ESMA in identifying potential issues at an early stage.

We feel that there is a need to instil a culture of 'soft' consultation at the ESAs that is not limited to formal published consultation and stakeholder groups, but which would consist of and include broader ongoing informal dialogue with the industry and consumer alike. Engaging in continuous and more frequent discussions with stakeholders throughout would assist the ESAs in providing effective and efficient supervision. We strongly believe that the ESAs should be required to organise on a periodic basis roundtable discussions, in order to benefit from discussions with the industry on latest market practices and

developments. This channel of open dialogue would also bring transparency to the policy making process and help stakeholders understand the ESAs policy decisions. We **recommend** making improvements to enable the consultative working groups to feed into the ESAs' processes more efficiently and ahead of the publication of each relevant technical standard and Q&As.

II. Funding

Given the need to increase resources of the ESAs, we accept a funding system partly funded by the industry. It is clear that efficient supervision requires adequate resources. If competencies are shifted from NCAs to the ESAs, then this needs to be reflected in the funding system. Any further decisions about how the ESAs' costs are recovered from the industry should be subject to a separate consultation. We **recommend** that the following points are considered when specifying details of industry funding via the required Delegated Act:

- Fees and contributions need to be commensurate: a reasonable level of fees will ensure that the provisions of financial services remains cost effective and that the competitiveness of the EU market place is not affected.
- The proposal by the Commission points to the fact that the current funding framework "seems to lead to uneven contributions by NCAs which are not easy to justify." Moving to contributions by the industry could make the whole process fairer, but is also likely to change the weight of each country in the funding process.
- The funding arrangement for ESMA should take into account the heterogonous nature of its indirectly regulated population. Unlike EBA or EIOPA, which have a relatively homogeneous group of banks/insurers, ESMA, within its remit, indirectly or directly regulates a wide range of firms including corporate issuers, commodity companies, asset managers, principal traders, investment firms, financial markets infrastructures and banks. For this reason, fees should be fairly allocated across the regulated population. It would be inappropriate to carve-out specific categories of entities just because they are smaller in size than the largest financial institutions. We recognise that proportionality should be at the heart of the allocation.
- We agree with the Commission proposal that annual contributions by the private sector should be collected by NCAs and that entities will not be charged twice when directly supervised by NCAs and indirectly supervised by the ESAs. However, we believe that there should be further clarification on how this will work in practice. For example, to the extent that ESMA responsibilities will replace NCA responsibilities, would there be a commensurate reduction in full-time employees (FTEs) at the NCAs?
- Since there should be a clear split within ESMA between direct and indirect supervisory staff, consideration should be given to how the contributions will be split between those entities directly and those not directly supervised.
- A move to majority industry funding for ESMA should be accompanied by increased accountability for ESMA to its stakeholders and regulated population. The Associations **recommend** increased transparency in how supervisory and policy decisions of the ESAs are made, and to give stakeholders increased opportunity to provide input prior to ESMA's decision making process.
- The proposal would see 146 additional FTEs added at ESMA, an increase of over 80% compared to end-2016 headcount (181 per 2016 ESMA annual report) together with an additional 49 staff as proposed under the EMIR Review Part 2 proposal[1]. Combined, the Commission is proposing to nearly double the size of ESMA. At the same time, by introducing an industry-funding model, financial institutions would be required to fund 60% of ESMA's annual budget. While the proposal does provide additional supervisory responsibilities to ESMA, it does not appear that an increase of this

[1] See European Commission's proposal (2017/0136 (COD) published on 13 June 2017, page 16 (impact assessment).

size is justified. For example, 9 FTEs to provide an annual report to the EC on third-country regulatory developments appears to be disproportionate and 7 FTEs to manage the industry-funding model is a significant increase. We **recommend** that the Commission more carefully consider the staffing needs of the ESAs under this proposal, and ensures that any increases are gradual to allow the organisations to grow at a reasonable pace.

- Consideration should also be given to the impact of Brexit on the ESAs. Given the UK constitutes a significant portion of the EU's financial markets, the UK leaving the EU should result in the need for a reduction in the size of the ESAs. This change has not been incorporated into the Commissions' estimates of the ESAs funding needs. Instead' the proposal would result in EU financial institutions having to provide funding for a regulator that will have jurisdiction over a smaller market. The ESAs will also need to consider the impact of losing the ability to employ UK experts, we **recommend** an openness to employing international staff including UK citizens, to ensure that the ESAs have access to a wide-ranging pool of talent.

III. New powers for the ESAs

The current European system of financial supervision following the subsidiarity principle has proven to be efficient and effective. As a guiding principle, supervisory structures should be re-calibrated carefully and gradually, and only when significant benefits can be achieved. The ESAs already have a broad range of tools to be able to deliver strengthened supervisory convergence – in this regard, the EU Commission's proposals to grant ESMA additional and far reaching direct supervisory powers appear premature.

Any consideration to expand ESMA's direct supervisory powers should respect the subsidiarity principle according to Article 5 of the Treaty of the European Union and would first require in-depth assessment, including corresponding cost-benefit analysis and ideally also preceding consultation of concerned entities. In this context, the value of supervision by national authorities should be recognised, given their strong knowledge of local markets, with their particularities (specific products, client base, and tax regimes), best practices and national legal frameworks. National supervisors also have the best understanding of practical operations and business models of supervised entities and have established networks of coordination between regulators.

ESMA direct supervision of MiFIR data reporting service providers

Given that MiFID II application will start in January 2018, we do not believe that changes to the envisaged supervision of data reporting services providers (DRSP) are necessary at this point in time.

Considering the significant recent changes to the reporting landscape, from an organizational perspective, it is preferable that NCAs act as relevant supervisors of DRSPs as set out by MiFID II: direct supervision by ESMA would require adaptations to MiFID II, where NCAs are identified as the competent supervisors of DRSPs. Before changing the new supervisory structure within the regulatory reporting landscape, it would seem sensible to go step by step' gaining first experience with the implementation of the new MiFID II regulatory requirements and related tools (such as the Financial Instrument Reference Data System (FIRDS)) first. In addition, the Commission should consider whether such a significant supervisory change of reporting might be better considered in the context of its recent 'supervisory reporting' consultation, which aims to evaluate and assess the effectiveness of reporting to supervisors in the EU.

ESMA to be granted temporary intervention powers:

Temporarily banning the ability of fund managers to sell their products would lead to a publicly imposed 'gate' on new subscriptions. This could impact the ability of fund managers to manage the liquidity of their funds, the pricing of the product and have negative implications for existing investors in the fund. Fund managers have tools, such as gates, to manage fund liquidity when circumstances require. We think that regulators should focus on improving the effectiveness and consistent use of those tools, rather than overriding them with a new intervention power that will likely be counter-productive.

ESMA direct supervision of certain types of prospectuses

We do not support the Commission proposal that ESMA becomes the direct supervisor of certain prospectuses. We believe that NCAs deal with the supervision of prospectuses sufficiently and are concerned that the proposals could hinder market efficiency. A move to direct supervision by ESMA would also require provisions to manage the grandfathering of previously granted derogations.

Proposed Amendments to the Benchmarks Regulation

Regarding the proposed amendments on new powers for ESMA under the Benchmarks Regulation (BMR), please see the specific BMR section below.

IV. Regulatory Forbearance/ delayed enforcement of rules

Although the Commission is not proposing anything to this effect, we believe that the ESAs should be provided with powers to temporarily suspend the application of certain regulatory requirements in certain circumstances and for a reasonable timeframe - effectively relieving firms from enforcement action during that time period.

The Associations attach to this response a legal analysis that they have commissioned, jointly with the Association for Financial Markets in Europe (AFME), the European Banking Federation (EBF) and the European Fund and Asset Management Association (EFAMA), in order to suggest practical solutions to allow regulatory forbearance where appropriate.

Since their creation in 2011, the ESAs have played an important role in the regulatory response to the financial crisis in particular through their role in producing Technical Standards, developing the single rulebook and non-binding Q&As.

However, it was also noticeable that all stakeholders, including market participants, NCAs, the ESAs, and particularly ESMA, have faced challenges on multiple occasions in view of tight timelines and effective dates, which have proven extraordinarily difficult to meet in a number of areas (EMIR, MAR, MiFID II/R and PRIIPs). Under these circumstances, the industry as well as national regulators have felt that the lack of flexibility in the timelines and the implementation dates could lead to market and supervisory disruption. There have been numerous examples of European lawmakers setting strict requirements in line with the G-20 commitments (the EU notably was not able to meet the deadline set by the G20), only to find other jurisdictions' regulators having the ability to provide relief when implementation challenges emerged. This has left European regulators hamstrung, doing everything to prevent market disruption, but being legally constrained to signal flexibility, while legislative fixes (where deemed appropriate) often could not be enacted timely enough for legally tidy solution.

In the US, in circumstances where the industry may be unlikely to meet a regulatory deadline or otherwise where it does not make sense in the circumstances to enforce a particular rule for a period, US authorities are able to issue 'no action relief', a form of regulatory affirmation that firms will not face enforcement due to lack of compliance for the period of the relief. Currently, no similar power exists in the EU. In such a scenario, the EU institutions are forced to rush through changes to the legislation to amend the application dates. This creates significant market uncertainty as to whether dates will be changed, and if so, whether they will be changed in time. When such changes are supported by a flexible approach to enforcement expressed in the ESAs' statement (like those which were published under EMIR for the Variation Margin 1 March 2017 big bang and the 3rd of January deadline for the application of mandatory variation margin rules to FX Forwards), the fact that these statements do not constitute forbearance and are not binding is considered problematic for most non-EU market participants.

The only alternative route available in the EU is for the EU institutions to encourage all NCAs to announce a period of forbearance for their jurisdiction. However, this creates significant risk of lack of harmonisation in the approaches taken by NCAs.

There has been significant industry discussion on the need for the EU authorities to have some form of direct no action relief / forbearance powers similar to those held by authorities in the US.

For these reasons' market participants, NCAs and the ESAs have recognised that the capacity to delay the enforcement of rules when it appears that the application date is unworkable would provide significant relief. The capacity to grant 'no-action relief', a concept derived from the US and a concept used in EU national regimes and to which the Associations would prefer the use of the term "regulatory forbearance", would enable, where necessary' the industry and regulators to have more time to fully prepare for the implementation of the new framework.

The Commission proposal on the ESAs review however does not include a tool that provides for the concept of regulatory forbearance. With the absolute deadlines of EU legislation and rule making often late in the process, ESAs would benefit from forbearance tools – this should by no means mean that legislators are giving up their policy sovereignty but provides for a practical supervisory tool to ensure markets operate efficiently and effectively.

The Associations fully appreciate that there are strict limits to the powers which can be granted to the ESAs as a result of the Meroni doctrine[2] and the European Court of Justice judgement given on 22 January 2014 about the ESMA powers to adopt legally binding measures upon financial institutions of EU Member States in the event of a threat to the proper functioning of the financial market or to the stability of the financial system of the EU in the context of the Short Selling Regulation[3].

The Associations nonetheless strongly feel that the effectiveness of EU financial rules would immensely benefit from a mechanism allowing flexibility in the timelines (for the benefit of regulators and market participants) in order to avoid the critical situations as recently experienced, where neither the market participants – particularly the small financial counterparties, small buy-side firms and corporates which are less equipped to prepare to regulatory changes – nor the regulators were ready to fully comply with a

[2] Judgment of the Court of 13 June 1958. Meroni & Co., Industrie Metallurgiche, SpA v High Authority of the European Coal and Steel Community. Case 9-56: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:61956CJ0009; Case 9-56

[3] Case C-270/12, United Kigdom v Council & Parliament.

number of provisions under European directives or regulations that are at the heart of the EU framework, e.g. MiFID II/R and EMIR.

We **recommend** the EU co-legislators to consider an alternative approach to grant regulatory forbearance. In this respect, the attached legal analysis aims at considering all possible existing tools and suggests changes to legislative texts which may be required to reach the objective.

Introducing a formal "regulatory forbearance" regime would improve the regulatory process, help the ESAs in their implementation work, and consequently make them more effective.

Naturally, such regulatory forbearance decisions will have to be supported by economic/ impact analysis undertaken by the ESAs after consultation with the industry. Over the past years and in light of regulatory reforms underway, a number of regulators both inside and outside of the EU (for example the SEC/CFTC) have strengthened their resources in the area of economic/impact analysis and it would be appropriate to give the ESAs such capacity to produce economic/ impact analysis.

We **recommend** the Commission and the ESAs to strengthen their capacity in this area and develop their own impact assessment frameworks for evaluating the implementation costs of secondary legislation and the appropriate timeline necessary to comply with the rules. This can be implemented without changing the existing legal framework.

ESA involvement in the Level 1 process

It is critical to provide the ESAs with adequate timelines and resources to enable the institutions to deliver financial reform and rules of the highest standards. We consider that the following elements are vital to enable the ESAs to fulfil their duties successfully and efficiently on an on-going basis:

- Mandates should require the ESAs to draft technical standards within a reasonable timeframe. The industry's experience is that timeframes are often too short, particularly when ESAs have to consider more complex issues. For the Market Abuse Regulation, the RTS dealing with inside information was available after the application date of the regulation; in MiFID II, the RTS on trading obligation was published in the EU Official Journal (OJ) on 22 December 2017 with the application date of MiFID II/R on the 3 January 2018. Another example is the late adoption by the European Commission of the indirect clearing RTS both under EMIR and MiFIR, which requires the industry to implement significant system and legal documentation changes. The RTS were only published in the Official Journal on 21 November 2017 with insufficient time left for firms to achieve compliance by 3 January 2018.
- Timelines for Level 2 implementation should specify a period for ESA drafting rather than define an absolute date. The timelines should be appropriate and proportional to the complexity of the task to be accomplished and the field to be regulated, and also take into account the quantity of information to be gathered and analysed by the respective ESA. A combination of 2 timelines is recommended, such as a 9 to 18 month period from the finalisation of Level 1 to the finalisation of Level 2 (depending on the complexity of the implementing rules), and subsequently another 6 to 12 month time period from the finalisation of Level 2 rules and Level 3 Q&As to final rule application dates. This would allow sufficient time for the ESAs to draft Level 2 measures as well as allowing sufficient time for national regulators and the industry to implement the regulatory changes. EMIR (i.e. margin rules), CSDR, PRIIPs or MiFID II/MiFIR have proved how challenging, and sometimes impossible it is to meet absolute application dates. The implementation of the Market Abuse Regulation (MAR) is another example that demonstrates the negative impacts on implementation

for both the industry and NCAs when Level 2 rules are finalised after the application date of the Level 1 Regulation.

- New Regulations/Directives that require a large amount of changes (operational changes, complex IT systems, extensive training) to be implemented should be applied in a phased-in approach to avoid the numerous challenges of a big-bang implementation. Principles of prioritisation should be incorporated in Level 1 mandates in particular for legislation requiring a high number of Regulatory Technical Standards (RTS) (e.g. MiFID II/MiFIR).
- Level 1 requirements should only come into effect after the effective dates of the more prescriptive Level 2 details to avoid legal uncertainty.
- In order to avoid inconsistencies as a result of translating legislation that was initially drafted in English, we **recommend** the establishment of an advisory entity/body/jurist linguist (also at ESMA level) that could interpret legal concepts that may differ between the civil law and common law.
- ESAs should have the opportunity to participate in the Level 1 discussions as an observer. They should in particular be allowed to provide opinions on Level 1 provisions that could contradict or affect the application of other insurance/banking/financial legislation or that raise legal or technical issues (e.g. extra-territoriality, privacy issues). The privacy issues under the EMIR and MiFIR reporting regimes could have been properly dealt with through the use of such a mechanism.
- To avoid uncertainties around the entry into force of provisions, the Level 1 text should clarify that delegated/implementing acts may have a delayed application date, or that these acts provide for possible phase-in periods of the obligations.

V. Third-country equivalence

We agree that it would be beneficial for the ESAs to be involved in the monitoring and implementation of equivalence decisions, which should be achieved by establishing strong and continuous engagement with third country regulators. Regulatory and supervisory coordination and cooperation within the EU and with third countries is important to ensure a robust and coherent global regulatory system. Possible divergence from standards agreed at a global level, particularly where the EU is applying more stringent requirements could undermine the attractiveness of Europe as a place for international investment. A general guiding principle in this context must be the assurance of reciprocal market access under the same conditions.

Capital markets are global markets, benefiting greatly when open markets access is ensured. Ongoing dialogue with third countries should have the objective of ensuring openness to wholesale business.

The Associations believe, when recognising the diversity of third country provisions under different EU legislative texts and the lack of an equivalence regime in some of them, there is the need to ensure a consistent supervisory approach at EU level.

ESMA already supports the European Commission in the equivalence assessments of third country regimes, and is involved in the work following an equivalence decision (recognition of third country CCPs and certification of third country CRAs) as well as in supervisory cooperation agreements with third country authorities. Given this, the Associations welcome the Commission's proposal to extend the ESAs' role in assisting the Commission preparing equivalence decisions, to ensure monitoring of third country regulation and supervisory standards and to develop supervisory arrangements with third countries.

However, the equivalence process should be significantly improved and reviewed to ensure decisions are taken in a more transparent manner. It is important that there are appropriate parameters in place

surrounding any ESMA assessment of ongoing equivalence. In line with the Commission's Better Regulation agenda, the Associations **recommend**:

- To establish appropriate transparency provisions to ensure industry is sufficiently aware of assessments made in time before changes are required in practice;
- To implement appropriate transitional periods following any withdrawal of an equivalence decision, to avoid a cliff edge effect;
- To conduct any assessment based on an equivalent outcomes basis, rather than a 'line-by-line' equivalence basis with an increased use of deference to third-country legislation to avoid excessive multiplication of laws and supervisory bodies governing global markets;
- To give due consideration to the treatment of legacy positions in the case of any change in equivalence determination; and
- To ensure that equivalence decisions are properly monitored and enforced.

Regarding the proposed amendments on third country regimes under the Benchmarks Regulation (BMR), please see the specific BMR section below.

VI. Technological innovation

The Associations strongly support the Commission's desire to establish technology-neutral regulation with a view to removing potential barriers to innovation. We encourage co-operation and information sharing between ESMA and NCAs. Given diversity of thought is a crucial ingredient of innovation' it will be important for NCAs to continue to develop so called regulatory sandboxes at the Member State level. That of course does not preclude ESMA from developing its own regulatory sandboxes where it has a specific responsibility or expertise.

However, we believe the detail and scope of FinTech work that the ESAs intend to undertake should be further defined and consulted on. In addition to promoting convergence of frameworks, the ESAs should develop frameworks that aim to both support financial innovation and address the consumer risks and potential stability implications of new technologies and services. It is important to recognise that:

- A one-size-fits-all regulatory approach is not conducive to technology innovation – any new regulatory framework should be flexible, graduated and principles-based, and oversight should be tied to scale and the risks presented.
- New rules or guidance should take into account banks' existing authorities to develop, test and launch innovative products and services. It's also important that regulators do not implicitly limit the ability to experiment.
- There are specific activities that do warrant careful attention by regulators, regardless of who is engaging in the activity – namely payments, lending activities, and data storage – as the risks associated with these activities have far reaching impacts on consumers and the broader financial system (i.e. money laundering, terrorist financing, disparate impact, fraud, identity theft, unauthorized transfers, etc.).
- Regulators/ supervisors should develop expertise, engage both banks and non-bank innovators, and focus frameworks on functions, not specific technologies or companies.

FinTechs have the ability to operate across jurisdictions, as the new technologies they are implementing are not limited by geographic boundaries or a single legal and regulatory regime. New regulatory and

supervisory frameworks promulgated by local and regional authorities to address FinTech innovation should strive to be harmonious with existing innovation frameworks in order to mitigate against regulatory arbitrage and conflicting rule sets that stymie the development of innovative products and services

Sustainability

We support ESA-led research initiatives and cost-benefit analyses on how climate, environmental, social and governance (ESG) factors can be integrated into potential policy initiatives. However, we would caution against the Commission's proposal that the ESAs should provide guidance to the Commission on how sustainability considerations can be embodied in relevant financial legislation. Premature policy initiatives have the potential to impede the growth of green finance initiatives, especially given the lack of consistent and generally accepted definitions and taxonomies in this area.

We **recommend** that any decisions regarding the incorporation of sustainability considerations are subject to a separate consultation. The ESAs should engage actively with market participants and industry bodies to keep on top of market practices and developments in this rapidly changing area. This will allow Regulators to achieve their objectives and help to ensure that potential issues are identified at an early stage.

VII. Outsourcing/delegation issue and risk transfer arrangements

We are supportive of the retention by national regulators of control with respect to outsourcing and delegation requirements, and would not be in favour of any move by the ESAs to infringe upon the functional independence of NCAs in this respect.

Outsourcing arrangements are an essential part of efficient business models, and any significant restriction to the ability to outsource to non-EU entities could detrimentally impact the market by providing less competition and by doing so driving down standards.

As a principle, we are concerned that singling out third country outsourcing and delegation procedures as an activity that needs enhanced scrutiny and oversight may send a negative message to third country jurisdictions and operators about the openness of Europe's financial markets.

There are a number of important existing tools to ensure supervisory convergence for the purposes of delegation and outsourcing; not all of these tools have been tested yet. For example, just this summer ESMA set up a new Supervisory Coordination Network. In line with the principle of subsidiarity, we **recommend** that supervisory convergence is properly pursued before considering whether the NCAs should be stripped of their powers.

VIII. Requests for information from the ESAs

Whilst we appreciate the need for the ESAs to obtain information in relation to the market participants they regulate, we are concerned that these requests could be duplicative of information that market participants already provide to their NCAs. In particular, were the ESAs to request information from market participants that has already been provided to the NCAs, that request could be made in a different format requiring the data to be cut in different ways, which would increase the burden on market participants for little discernible

benefit. We therefore **recommend** that the ESAs be required to cooperate with NCAs to determine whether the data has already in fact been provided before making binding requests on market participants.

IX. Other Comments

Proposed amendments to the Benchmarks Regulation (BMR)

We support ESMA supervision for pan-European crucial IBOR benchmarks, like Euribor or Eonia (that have already been determined critical by the Commission). For local currency IBOR benchmarks that are important at national level, e.g. WiBOR, we strongly believe that the national competent authorities are the best placed to carry out their supervision. National Competent authorities should retain the power to determine if their local benchmarks are critical (if they wish to take such a determination decision in the future). Therefore we agree with the Commission proposal for direct ESMA supervision, but only for such benchmarks as Euribor and Eonia. We strongly oppose to the Commission suggestions to completely remove from the BMR the possibility for national authorities to determine that a local benchmark is critical and to supervise it. Our remarks below on critical benchmarks supervision, determination of criticality and national versus ESMA supervisory powers should be considered in this context. Regarding third country benchmarks we support supervision at the ESMA level. Concerning the timing and impact assessment of the potential changes, we would like to highlight that conclusive evidence on the functioning of supervision under the current BMR rules should be gathered, taking into account the BMR transitional period (which ends on 1 Jan 2020) and the BMR review.

Critical benchmark supervision

In general we recognise the benefits of a more integrated supervision for administrators of critical benchmarks. We believe that more integrated supervision may improve transparency and market confidence and achieve supervisory convergence across the EU in the area of benchmarks supervision. In particular, it could make the application process for administrator authorisation more efficient, as compared to the current college arrangements for critical benchmarks. This would be the case, however, only provided that the application and supervision process is appropriately designed and implemented in practice in order to (i) achieve the objective of effective supervision, (ii) to be time efficient and (iii) to take into account the potential impact on all the relevant EU countries and stakeholders groups, (for instance from the market, operational and compliance risks perspectives). Moreover, ESMA's new powers should not unduly increase the administrative burden on market participants.

We also note that supervisory colleges may authorise and supervise administrators of critical benchmarks for the period starting on 1 January 2018, when the BMR became applicable, until the ESAs review proposal has been adopted and entered into force. Conclusive evidence on the functioning of supervision should be gathered during this time to determine and legitimise the process of the regulatory review of the EU supervisory framework of critical benchmarks. It would be important to ensure that any changes of the framework are coordinated with the current BMR transitional provisions and the envisaged BMR review.

Determining criticality

The Omnibus Regulation proposes several changes to the way a benchmark can be determined critical under the BMR. The Omnibus retains the BMR's first criterion that has to be met for a benchmark to be considered critical, namely the minimum EUR 500 billion reference value. We believe that this brings relatively minor modifications in practice. We are concerned, however, that the proposal actually removes from the BMR legislation other avenues for determining certain 'national' or 'smaller' cross-border benchmarks as critical and replaces them with a set of new conditions that have important consequences, e.g. delegating NCAs

powers to ESMA and modifying de minimis thresholds. While this may seem to be done for simplification purposes, these are material changes to the BMR that do not regulate the details of powers to authorise and supervise administrators of critical benchmarks only. Therefore, the Commission proposals appear to go beyond the changes required to reflect the new supervisory environment and cannot to be considered in line with the purpose of the ESAs Review.

National versus ESMA supervisory powers

In particular, the proposal makes ESMA the direct supervisor of national critical benchmarks if they have a total reference value of less than EUR 500 billion (but do qualify for any of the conditions as set out in Article 20(2)). The Commission text removes important national powers to determine criticality where the national impact may be significant from the local or cross-border perspective. We are concerned that ESMA would lack the in-depth understanding of local market conditions and specificities when exercising supervisory powers. We do not believe that there are significant concerns about the current supervision of such benchmarks by NCAs, which would justify this change in supervisory responsibilities (nor would such change create any significant efficiency gains in terms of more effective, coordinated and consistent supervision). The Commission's Impact Assessment does not sufficiently justify the proposed change, as it does not show a clear benefit of shifting such responsibilities from NCAs to ESMA. Moreover, Recital 49 of the proposal does recognise the importance of the closer market proximity of an NCA to a national critical benchmark compared to ESMA by suggesting that ESMA delegates, entirely or in parts, the supervision of that benchmark to the relevant NCA where the administrator is based. Therefore, we would be cautious about granting ESMA direct supervision of national critical benchmarks as NCAs are better placed to supervise benchmarks critical for their markets.

Any consideration to expand ESMA's direct supervisory powers should respect the subsidiarity principle according to Article 5 of the Treaty on European Union and would first require in-depth assessment, including corresponding cost/benefit analysis and ideally also a prior consultation of concerned entities. In this context, factors should be taken into account such as the value of supervision at national level by authorities that know best the local markets with their particularities (specific products and client base), best practices and national legal frameworks. National supervisors have the best understanding of practical operations and business models of supervised entities and have established the networks of coordination between regulators.

Furthermore, the BMR already provides for such an assessment of the supervisory regime: According to Art. 54(1)(b) BMR, a review by the EU Commission of the functionality and effectiveness of the supervisory regime for critical benchmarks is foreseen for 2020. Market participants are currently implementing the legislation to ensure long-term compliance with the BMR.

Thresholds

Moreover, for critical benchmarks the Omnibus Regulation modifies the EUR 500 billion de minimis thresholds under Art. 20(1)(a) BMR and removes the EUR 400 billion de minimis thresholds under and (c)(i) BMR. This would mean that benchmarks having a total value of less than EUR 500 billion might be considered as a critical benchmark under different conditions and by a different authority. Benchmark providers might also risk legal uncertainty as to whether benchmarks having a total reference value of less than EUR 400 billion would continue to be considered as non-critical benchmark under the current conditions. Moreover, the originally envisaged criteria has not even been tested in practice yet, let alone proved inefficient. We are of the view that the de minimis thresholds for critical benchmarks as set under the BMR should remain in place. It would be preferred to assess their usefulness as envisaged in the BMR Review in 2020 at the earliest.

Third country benchmarks

In general, we welcome many aspects of the proposed changes for third country regimes. While the conditions for granting third country benchmarks a qualification for the use in the EU are being adapted to the new supervisory structure and in many instances improved, we would also welcome the effective recognition of the ISOCO principles on the provisions of equivalence decisions This would be a crucial element to ensure that after the end of the BMR transitional period, EU users retain uninterrupted access to non-EU benchmarks, for instance while hedging their global investments and foreign trade activities. The impact on relations and cooperation with third country regulators and supervisors would also have to be taken into account.

Conditions for qualification

Regarding the conditions for qualification, we believe there are benefits for ESMA to take over the role of NCAs with respect to the recognition and endorsement of benchmarks provided by non-EU administrators for use in the EU. This would mean, amongst other things that, under the recognition regime, there would no longer be a need for non-EU administrators to identify a "Member State of reference" for the purposes of an application for recognition. The non-EU administrator could appoint a legal representative anywhere in the EU for the purposes of the application and there would be no delay to an application resulting from the need for NCAs to refer the application to ESMA for an opinion on the significance of the benchmark (since ESMA would handle the whole application process). These changes appear to bring positive effects on an efficient application of these third country regimes in practice. We also note that supervised entities that endorse third country benchmarks would potentially be subject to dual supervision in that they would be subject to supervision by their home state NCA with respect to their other supervised activities (and any benchmarks provided by them directly) and supervision by ESMA with respect to any third country benchmarks endorsed by them. We believe that any potential interdependencies and synergies should be analysed, inter alia from the administrative burden point of view.

We also note that there would be changes to the regime under which third countries can be treated as equivalent for the purposes of the BMR. In particular, the Commission could grant equivalence on a conditional basis. Obviously there should be requirements to monitor equivalence on an ongoing basis and ESMA would be prohibited from concluding cooperation agreements with third countries with strategic deficiencies in their national anti-money laundering and counter-terrorism finance regimes. In principle' we welcome the proposed changes. The assessment of a third country's equivalence cannot be an one off decision but needs to be undertaken periodically, in order to make sure that third country regulatory and supervisory frameworks are at least as prudent as in the EU and to ensure a level playing field.

A broader concern at the moment is how exactly the EU BMR third country regimes (equivalence, endorsement and recognition) will operate in practice and there is still a lot of uncertainty around whether third-country administrators will indeed be authorised in time for 1 Jan 2020. This uncertainty may be a reason for considering pushing any BMR review and ESAs review work back until we can gather evidence on the functioning of the BMR in its current form.

IOSCO principles

Regarding the effective recognition of the ISOCO principles, the Commission suggests that the IOSCO principles 'may' be taken into account while assessing third country regimes' equivalence with the BMR. This seems to be weakening the current language which does not appear to leave such optionality.

This is extremely important because as it currently stands, the equivalence based on the assessment of a third country national regulatory and supervisory regime for benchmarks with the EU BMR works only for

very few benchmark administrators. This is because today few countries have an authorization regime for local critical benchmarks (i.e. Singapore and Japan). This is not the case for the U.S or Switzerland. Third countries authorities and market participants rely today to a large extent on IOSCO principles.

Furthermore, we would like to reiterate our position as highlighted in the past that the equivalence judgment framework (as well as the recognition or endorsement authorisation) should be made such that the administrator's governance should follow the core elements of IOSCO Principles and the overall framework established by the BMR rather than prescriptively meet each detailed requirement of the Regulation on a line-by-line basis.

Supervision of contributors

According to the Commission proposal, ESMA would also have supervisory powers with respect to supervised contributors to critical benchmarks and to third country benchmarks qualified for use in the EU under one of the third country regimes. It is essential to consider whether such ESMA supervision, even though limited to the BMR purposes, would have any implications for national markets or prudential supervision and supervision under SSM/ECB for other purposes, inter alia from the supervisory co-operation, legal certainty, potential duplication, and administrative burden point of view. We strongly believe that there should not be a direct ESMA supervision of contributors to critical benchmarks, as national competent authorities are best placed to supervise financial institutions they are usually responsible for and can oversee in a holistic way. It is also important to clarify that if a benchmark has not qualified for the use in the EU, the EU based contributors to these benchmarks would not be covered by an EU supervision. This would be in line with the interpretation brought by ESMA in its 9 November Q&As update under the BMR (QA 4.3.).

Stability of the legal framework

On another topic concerning the stability of the legal framework, we note that the Omnibus Regulation itself would enter into force 20 days after its publication in the Official Journal but would only apply two years after entry into force. Nevertheless, the powers over benchmark administrators would only transfer to ESMA three years after the Omnibus Regulation enters into force, but there would be transitional arrangements for existing administrators and applications in process at that time. It would be also important to ensure that any changes of the framework are coordinated with the current BMR transitional provisions and the potential BMR review.

Reviewing the BMR in areas other than supervision

As a more general matter, another proposal in the draft Omnibus Regulation is that the Commission would be given additional powers to adopt delegated acts to define certain aspects of the requirements under the BMR, e.g. governance, methodologies, systems and controls. While the link with the changes to the new supervisory environment is not entirely clear, it may open a venue to further potentially useful clarifications enhancing legal clarity in other areas of the BMR, e.g. possibly regarding outsourcing of certain administrator functions.

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