

ESMA response to the Commission Green Paper on Building a Capital Markets Union

1. ESMA welcomes the Commission Green Paper on Building a Capital Markets Union¹ (the 'Green Paper') and takes the opportunity of this consultation to share with the Commission its views on this milestone initiative.

I. Introduction

2. Achieving a capital markets union ('CMU'), i.e. an integrated and well-regulated single market for capital, may be considered as the ultimate natural development of the 'free movement of capital' – already foreseen in the Treaty of Rome – which is at the heart of the Single Market and is one of its 'four freedoms'. ESMA considers that this objective should be developed through the following areas of activity in order to have maximum effectiveness:
 - A. *Greater diversity of financing*
3. The integration of capital markets is even more important as gross new bank lending to companies has substantially declined in many parts of the Union since the beginning of the financial crisis in 2008. The development of alternatives to complement traditional bank financing is of utmost importance for Europe's future.
4. Several alternative sources can be identified in order to create a more diversified system of funding with greater involvement of institutional or non-bank investors and a higher proportion of direct capital market financing. Increasing the role of the non-banking sector will not only help in accessing the much needed capital for investments, it should also help in making a shift from debt to equity funding.
5. The more diversified system of funding that CMU could bring does not necessarily mean a smaller role for banks, rather an evolved and slightly different one. Banks will certainly continue to conduct their important lending activities, but a more diversified system of funding should also allow for less bank intermediation. The nature of the funding activities performed by banks of an agency-type will increase, e.g. banks will be involved in equity IPO (alongside other investment firms).
6. In its effort to create greater diversity of financing, the CMU should aim for a high level of investor protection. The greater involvement of investors, including retail

¹ COM(2015) 63 final.

clients, is not only a means of facilitating the diversification of the sources of funding of our economy, but is also crucial in contributing to its stability.

B. Increasing efficiency of EU capital markets

7. Strong progress has been made in the establishment of a Single Market in financial services in the past twenty years. In capital markets, great advances have been made especially in the last few years, in particular with the reforms establishing more robust market infrastructure and practices – such as those on OTC derivatives (EMIR) and central securities depositaries (CSDR) – increasing the transparency of transactions and reinforcing investor protection (MiFID II) or product transparency (PRIIPs). In this context, the progressive shift towards regulations (instead of directives) substantially increased the level of harmonisation of approaches across Europe. A focus on consistent implementation of these rules will help create a level playing field and so help deliver the objectives of CMU. However, even if these measures will greatly contribute to the objective of the CMU, additional steps should be taken towards stronger integration, which is genuinely necessary for deepening the single market in capital, as there are still too many barriers within the Single Market hampering the flow of capital. Some of the areas where these further steps could be taken are described in more detail under sections III and IV of this response.

C. Increasing attractiveness of European Union for investors

8. A European Union with open capital markets which leads global regulatory debates and seeks to reduce fragmentation will attract investment and strengthen Europe as a global financial centre and boost competitiveness of EU firms. Attracting capital to the European Union and strengthening it as a global financial centre is, therefore, a key aspect of the CMU.
9. In order to generate the increased participation of investors and reap the resulting benefits mentioned above, the level of confidence and trust of investors (and especially retail investors) needs to grow, hence the requirements for an efficient and robust framework for investor protection. All CMU initiatives, especially the ones that could give greater access to investors to capital markets, need to embed investor protection objectives to ensure long lasting positive effects of these initiatives.

10. ESMA is pleased to share with the Commission some reflections on ESMA's activities and their contribution to the CMU (section II), answer to a selection of questions in the Green Paper (section III) and give some consideration on other areas affecting the efficiency of the EU capital markets (section IV).

II. ESMA activities and their contribution to the CMU

11. ESMA's main objectives, namely enhancing investor protection and promoting stable and orderly financial markets, are fully aligned with the objectives of the CMU. Through its four activities, which are further described below, ESMA considers that it plays an important role in several dimensions of the CMU and is committed to intensifying its actions in these fields.

1. Completing a single rulebook for EU financial markets

Past and current activities

12. The regulatory agenda for the 2011-2014 period was comprehensive. Major regulatory changes were initiated mainly as a response to the financial crisis but also in the most recent period to stimulate alternative sources of funding for the European economy. These initiatives led to substantial work on developing the single rulebook further. For ESMA this involved drafting technical standards, delivering technical advice on legislation to the European Commission and issuing guidelines on the application of Union law.

13. As far as investor protection is concerned, the revised framework introduced with the MiFID/MiFIR and PRIIPs packages should ensure a significantly safer environment for investors with a more holistic approach to investor protection.

14. We are at present in the midst of an era of implementation and evaluation of the new regulatory framework. The current key priority of ESMA is to ensure a proper implementation of this framework across the EU. ESMA considers that the evaluation of the recent reforms and their implementation may indicate the need for legislative adjustments. This may be the case, for instance, where such an evaluation shows a necessity to better frame certain rules in the interest of the Single Market and always bearing in mind the need to maintain high standards of investor protection.

Future activities

15. While the intensity of the regulatory agenda for the 2016-2020 timeframe can be expected to be much lower, ESMA stands ready for any additional regulatory work that may be requested in the context of the CMU (in particular, in areas such as the review of the Prospectus Directive and any possible upcoming initiatives on securitisation and crowdfunding).

16. The purpose of completing a single rulebook for EU financial markets is to enhance the Single Market by creating a level playing field for investors and issuers across the EU. At the same time, as mentioned above, ESMA considers it essential to reflect on the reforms introduced over recent years and their impact on market participants and investors. In considering future activities on achieving the single rulebook, ESMA

would also like to mention that cross-sectorial considerations, especially in the area of investor protection should be taken into account in the context of the CMU.

2. Assessing risks to investors, markets and financial stability

Past and current activities

17. The purpose of assessing risks to investors, markets and financial stability is to spot emerging trends, risks and vulnerabilities, and, where relevant, opportunities in a timely fashion so that they can be acted upon.
18. ESMA is strengthening its ability to identify and assess risks in the areas of investor protection, the orderly functioning of markets and financial stability in the EU. The risk assessment function provides insight and input to regulatory and supervisory activities, and further develops a distinct EU sectorial perspective. ESMA is given access to unique sets of market data, the use of which is central to meeting its specific operational tasks, including regulatory impact assessments, supervisory stress tests, supervisory convergence, and its sectorial contribution to financial stability in the EU.

Future activities

19. Adequate, forward-looking risk assessment aims at and is essential for an early detection of risks to financial stability, investor confidence, and market integrity, and for the identification and choice of suitable regulatory and supervisory responses to these risks.
20. In recent years, the legal basis has been created for data collection in key markets, and ESMA aims at supporting its regulatory and supervisory activities with the information these unique data contain. ESMA is working on the implementation and realisation of these data collection mandates, and – in close cooperation with NCAs – is committed to developing efficient data collection, management, and analytical approaches going forward. Establishment and operating costs in these areas are high, and resource constraints remain a key obstacle. Obtaining adequate resources for building the necessary capabilities is essential.

3. Direct supervision of specific financial entities

Past and current activities

21. Since its establishment, ESMA has taken on the responsibility for the direct supervision of credit rating agencies ('CRAs') and trade repositories ('TRs'). Stringent supervision of CRAs will be necessary, to support the availability of high-quality ratings, which are expected to continue to play an important role in the EU financial markets in the coming years. TRs play a central role in enhancing the transparency of derivative markets and reducing risks to financial stability. In supervising TRs ESMA's

key regulatory objectives are stability of systems, data quality, confidentiality and regulatory access.

Future activities

22. Fully recognising that CMU is not necessarily about more EU supervision, ESMA is uniquely positioned to develop a European supervisory approach that could have strong benefits for pan-European actors that play an important role in supporting the CMU. While clearly not asking for new areas of direct supervision, ESMA stands ready to assume such news tasks should the co-legislators wish to assign them to ESMA together with the appropriate resources.

4. Promoting supervisory convergence

The functioning of integrated markets requires trust not only in cross-border institutions and cross-border supervision but also in consistent application and supervision of the single rule book across the different countries.

Past and current activities

23. ESMA's overall aim has been to achieve sound, effective and consistent regulatory and supervisory standards and comparable outcomes throughout the EU, in close co-operation with NCAs and smooth co-ordination with the two other ESAs (i.e. EBA and EIOPA) where banking and insurance interact with capital markets.
24. In view of the importance of the workload on the single rulebook, ESMA has focused its supervisory convergence efforts on forging common understanding (through Questions and Answers), common practices (through Guidelines, Opinions or Supervisory briefings) or common enforcement priorities between NCAs. It has also intensified the review of supervisory practices of NCAs.

Future activities

25. For capital markets, ESMA is best placed to support the EU institutions to co-ordinate and ensure that the Single Market perspective is reflected across Europe and that appropriate, consistent implementation and supervisory outcomes are achieved. ESMA is committed to do all it can to contribute to the progress of the Single Market and therefore the progress of the CMU.
26. In this respect, ESMA could play a role in the improvement of the surveillance of financial markets and activities in the EU. Indeed, various reporting obligations stem from different EU regulations but are often processed in silos. A mapping of these reporting obligations should be done with the objective of rationalising their use for supervisory purposes. ESMA could be empowered to put in place common solutions and help optimize the IT tools used by NCAs and ESMA for supervisory purposes.

27. ESMA is committed to expanding its focus on supervisory convergence in the coming years, and to adapting its approach to these activities through a greater focus on achieving effective and consistent results *ex ante*, using a wider range of tools within the powers set out in the ESMA Regulation. While continuing to carry out peer reviews, this approach will involve greater emphasis on identifying, supporting and sharing good practices and effective supervisory techniques and enabling sufficient consistency of approaches to ensure that consistent outcomes can be achieved and internal market barriers reduced.
28. This dimension is crucial to progress on the objectives of the CMU, to ensure that the necessary internal market opportunities are available to issuers and financial firms, while ensuring that appropriate investor protection and market integrity are delivered consistently and investor confidence in the capital markets is supported.
29. However, it would not be realistic to aim for full convergence in the short to medium-term and full convergence may not be needed in all areas to achieve the CMU's objectives. NCAs and ESMA have limited resources and need to make choices on where to concentrate their efforts.
30. In connection with the CMU specifically, ESMA has identified several principles which will guide its activities on supervisory convergence, in close cooperation with the NCAs. It will aim at ensuring a consistent approach to authorisation of activity regulated by EU legislation (such as authorisations of collective investment undertakings or investment firms) and contribute to combat unauthorised activity. It will also endeavour to ensure consistent supervision of authorised activity and enforcement of EU regulations in all its fields of competence.
31. It will make sure that all the rules on cross-border and passporting activities are properly applied and actively seek to facilitate effective cross-border supervision and enforcement, so as to exploit the full benefits of the internal market. It will also look for opportunities for supervision to be carried out more efficiently through co-ordinated action, for example through a co-ordinated approach to market monitoring and risk identification, or joint action by some or all NCAs.
32. ESMA will develop this approach working closely with NCAs and supporting them while, where necessary, acting in cases of inappropriate application of EU law; helping NCAs to devise effective and consistent supervisory strategies for new rules and to share experiences of good practice; and looking for opportunities to increase efficiency through common approaches and potentially reduce the cost of achieving supervisory objectives.
33. One area where supervisory convergence will be of crucial importance is investor protection. In order for MiFID II/MiFIR rules, that will play an important part in achieving the required investor protection, to deliver their entire benefits, these texts need to be fully and consistently implemented and enforced all over Europe.

34. In this regard, thanks to the new powers given to NCAs and to ESMA by MiFIR, as well as the coordination of these powers given to ESMA, product intervention at European level will become more efficient and more consistent across the EU.
35. Further progress on the digitalisation of financial services could support both issuer and investor access to capital markets but may also offer specific challenges for supervisory convergence in the area of investor protection and market abuse. This phenomenon offers firms new ways to interact with their clients and trade on markets, could decrease the costs of financial services and could help towards increasing financial awareness and trust in financial products. However, it might also create new challenges for investor protection and monitoring of orderly markets, especially if NCAs develop divergent supervisory responses towards these developments. The pace at which digitalisation initiatives in the financial sector evolve requires ESMA and NCAs to be able to respond quickly to ensure the appropriate and consistent supervisory treatment of these initiatives. Further exploration of the mechanisms available to address these types of challenge may be needed, so that ESMA can ensure convergent and effective action in a quick and timely fashion without preventing potential benefits from digitalisation being realised. Some limited adaptation of the regulatory framework may also be worth considering depending on the pace of progress of digitalisation.
36. Further proposed actions on supervisory convergence are provided under the specific response below to question 25 of the Green Paper.
37. As discussed above, ESMA is conscious that the intense workload linked to the single rulebook is progressively decreasing as the important legislative reforms adopted over the past years are being implemented. However, ESMA would like to stress that other activities – on which ESMA is committed to making further progress – such as risk and data analysis and supervisory convergence (not to mention the ongoing work on supervision) are resource-intensive. Therefore, while ESMA will do its utmost to increase its organisational flexibility, it should be supported by an adequate staffing and funding system. It is essential that the improvement of ESMA's – and, more generally, of the ESAs' – funding model announced in the context of the review of the European System of Financial Supervision is done as quickly as possible, resulting in stable funding sources.

III. ESMA's answers to a selection of questions in the Green Paper

38. ESMA provides below its contribution to a number of questions in the Green Paper.

2) What further steps around the availability and standardisation of SME credit information could support a deeper market in SME and start-up finance and a wider investor base?

Issue at stake

Banks currently represent the main source of financing for SMEs. For their credit assessment, banks rely – besides internal assessment – on external credit scores, which represent a recognised source of creditworthiness information currently provided by both registered CRAs as well as non-registered credit scoring providers. Some CRAs and scoring providers in particular provide extensive coverage on SMEs in specific Member States and/or sectors².

However, according to the World Bank, the availability of financial information and credit history data for SMEs may be uneven across the EU due to different national legislation and, even when available, the financial information provided by SMEs may not accurately reflect their current financial position and overall business performance. Difficult access to information about SME creditworthiness might contribute to explaining why SMEs remain of local/regional interest with credit scores mainly paid for by banks to inform their lending process and risk analysis³.

As mentioned in the Green Paper, in Europe around 25% of all companies and around 75% of owner-managed companies do not have a credit score⁴. Moreover, bank lending decisions have recently become more selective, on the grounds of both banks' balance sheet constraints and the rising default probabilities of borrowers.

At the same time, according to the OECD, EU SMEs have a very narrow investor base as well as limited access to the capital market. The SME bond market is still limited due to higher access and legal costs for the issuance and therefore suited mostly to medium-sized and larger SMEs. At the same time, given the lack of historical data, credit ratings are hard to obtain for smaller companies within the category of SMEs when they need it. Moreover, the cost of credit ratings may also discourage SMEs from seeking them⁵.

² It should also be noted that credit rating agencies have been providing special mid-market enterprises analysis and credit ratings.

³ http://siteresources.worldbank.org/EXTFINANCIALSECTOR/Resources/2828841395933501015/Facilitating_SME_financing_rough_CR_public_comments_web.pdf

⁴ http://ec.europa.eu/finance/consultations/2015/capital-markets-union/docs/green-paper_en.pdf

⁵ http://europa.eu/efc/working_groups/hleg_report_2013.pdf

Proposed actions

One of the difficulties faced by SMEs when trying to access both bank financing and capital markets is insufficient credit information. A possible approach could consist of increasing the availability and standardisation of credit information concerning SMEs in the Union either by stimulating a market led initiative or adopting regulatory measures, at least for SMEs that are ready and interested to disclose such information. This could be achieved via further harmonisation of the national accounting standards which are based on the Accounting Directive and the introduction of specific requirements for disaggregated information in the financial statements which are imperative in the process of establishing scoring. It should be noted that, while the recent amendments to the Accounting Directive had the aim of reducing the regulatory burden for SMEs, measures proposed above would have the benefit of facilitating the access to financing at national level and potentially remove barriers to cross-border financing. Please note that these proposals would not influence issuers preparing IFRS financial statements according to the IAS Regulation or common EU level accounting standards for SMEs listed on MTFs as proposed in the answer to question 8 below.

Increasing the availability of credit information through the harmonisation suggested above would benefit not only scoring providers – that are currently not regulated – but also other providers of creditworthiness assessment (for instance, credit rating agencies and banks performing internally the creditworthiness assessment of their clients). Finally, it should be noted that there is no level playing field between rating and scoring providers and credit scores are not regulated. As such, a careful approach should be considered given the necessity to avoid encouraging the creation of rating-like instruments.

8) Is there value in developing a common EU level accounting standard for small and medium-sized companies (SMEs) listed on MTFs? Should such a standard become a feature of SME Growth Markets? If so, under which conditions?

Issue at stake

ESMA notes that MTFs are perceived differently across Member States (MS). While in some MS listing on an MTF is perceived as an entry point for listing on a regulated market, in other MS they are seen as a separate trading platform on which issuers are listed for an indefinite period of time.

In most MS companies listed on MTFs are required to use the national accounting standards, but in some MS issuers have the option to use IFRS as endorsed in the EU. From the evidence gained by securities regulators, it seems that this option is not extensively used, but that there is a correlation between their use and the market capitalisation. The fact that requirements for calculation of income taxes and profit

distribution are often linked to the national accounting standards seems also to play an important role in the choice of the accounting standards.

While no comprehensive study has been conducted on the causes of this limited use of IFRS, some refer to the perceived complexity and significant pace of changes in the standards which would most likely imply the need to use consultants, with resulting impacts on the costs of compliance. Consequently, some MS have developed a specific accounting standard for these companies on the basis of the IFRS requirements but with a reduced disclosure regime (e.g. in the United Kingdom).

The lack of a common EU level accounting standard for SMEs listed on MTFs does not seem to be the key barrier to accessing financing by these companies at national level; however, use of a common accounting standard might help companies become more attractive for cross-border investors.

Proposed actions

On the basis of the above considerations, ESMA believes that it would be beneficial if companies listed on MTFs in all MS would be allowed to use IFRS for their consolidated accounts as an alternative to the national accounting standards, as this might avoid the double cost of conversion should issuers consider listing on regulated markets in the future.

At a later stage, improvement in access to cross-border financing might be facilitated by developing a common specific EU level accounting standard for SMEs listed on MTFs. Those standards should be in line with the accounting principles for recognition and measurement included in the IFRS, potentially simplified for disclosure requirements. In terms of the legal tool, ESMA believes that the introduction of common accounting standards for SMEs on MTFs should be introduced through an EU Regulation.

9) Are there barriers to the development of appropriately regulated crowdfunding or peer to peer platforms including on a cross border basis? If so, how should they be addressed?

Please note that ESMA's focus is on crowdfunding which involves investment, as distinct from donation, non-monetary reward or loan agreement. As such, the response below covers investment-based crowdfunding only.

Issue at stake

The regulation/supervision of crowdfunding platforms varies across the EU, due to differences in the interpretation of EU rules likely to apply and national regimes. In addition, there are gaps and issues in the current EU framework, which may raise investor protection concerns and prevent crowdfunding from reaching its full potential.

These include: the perceived regulatory burden of the current legislative framework, the ease with which one can structure business models that fall outside of EU regulation (e.g. through the use of financial instruments which are not regarded as transferable securities and hence fall outside the scope of MiFID), the different thresholds that apply to the obligation to produce a prospectus across Member States, the capital requirements likely to be imposed on platforms and the use of the MiFID optional exemption.

A more appropriate legislative framework, which would address the gaps and issues discussed above and provide more consistency across the EU, would enhance investor protection and help encourage the development of a pan-European crowdfunding market. A sound and robust pan-European crowdfunding sector has the potential to provide an alternative source of funding to businesses and the EU economy, in particular for SMEs. It also has the potential to offer an attractive investment proposition to investors, including a sub-set of retail investors, provided the right safeguards are in place.

Proposed actions

In order to address gaps and issues in the current EU framework, ESMA would recommend (i) investigating measures to reduce the incentives for platforms to use non-transferable securities and/or fall outside of the existing framework, for example by considering whether some or all of the MiFID provisions should be applied to such securities and (ii) exploring options for the application of tailored, harmonised and proportionate disclosure requirements for the raising of capital where the obligation to publish a prospectus, as prescribed by the Prospectus Directive, do not apply.

In addition, ESMA believes that consideration should be given to the possible development of a specific crowdfunding EU-level regime, in particular to mitigate the risks arising when platforms are regarded as outside the scope of MiFID, which would allow for more proportionate requirements imposed on platforms, appropriate investor protection and the use of a EU passport. Consideration should also be given to whether some AIFMD requirements, which might in theory be applicable in some cases, are appropriate for the use of collective investment structures used in crowdfunding or whether any adaptations would be needed bearing in mind that AIFMD was not originally designed to capture those activities.

Further details about those gaps and issues and possible ways to address them are provided in the crowdfunding Advice that ESMA published on 18 December 2014. In addition, ESMA carried out a survey of National Competent Authorities ('NCAs') in December 2014 on regulated platforms in the EU, including the rules under which they are regulated, the type of services that they offer, the capital requirements that are imposed on them and the investment instruments, structures and remuneration models that they are using, whose findings are presented in appendix. In particular, the survey highlights the disparity in the extent to which platforms are currently

regulated in different member states and the challenges it poses for a level playing field and regulatory/supervisory convergence.

11) What steps could be taken to reduce the costs to fund managers of setting up and marketing funds across the EU? What barriers are there to funds benefiting from economies of scale?

17) How can cross border retail participation in UCITS be increased?

ESMA identified the following possible barriers to setting up and marketing funds across the EU and to cross-border retail participation in UCITS. For each of these barriers ESMA has identified some of the actions that could be envisaged.

i. UCITS notification procedure

Issue at stake

The UCITS IV Directive simplified the procedure for cross-border marketing of UCITS by introducing regulator-to-regulator notifications and clarifying the role of each NCA. This procedure has proved to be a success. However, under the UCITS IV Directive, any updates to the documentation provided to the NCA of the host Member State at the time of the notification of marketing have to be communicated by the UCITS itself and not by its NCA. The Commission consultation document of 26 July 2012 recognised that it could be considered whether to introduce a regulator-to-regulator notification for any changes to the notification file, including the information on arrangements for marketing or marketing of a new share class.⁶

Proposed actions

ESMA believes that the notification procedure would be even more efficient if the NCAs of the home Member State of the UCITS were in charge of transmitting the updates of the documents. Indeed, this would make the procedure much easier for UCITS managers.

ii. UCITS/AIFMD – home/host competencies

Issue at stake

Both the UCITS Directive and the AIFMD provide for detailed rules on the division of competences between home and host NCAs. However, there may be a need for further clarity on the scope of competences of the home/host NCAs under both directives as well as on the extent to which additional

⁶ See section 9.4 of the consultation document.

national requirements are allowed for the purpose of the cross-border marketing of funds.

Proposed actions

Introducing additional clarity on the split of competences between home and host NCAs and clarifying the types of additional requirements that are permitted at national level for the cross-border marketing of UCITS/AIF would further incentivise passporting activities and simplify their functioning. In particular, consideration may be given to further clarifying the division of competencies under the UCITS Directive with regard to rules of conduct in situations where UCITS management companies establish branches in a host Member State to manage UCITS.

iii. UCITS – harmonisation of cost disclosure

Issue at stake

The UCITS framework provides for a detailed set of rules on cost disclosures (namely, through the KIID provisions) and on remuneration rules. However, there is currently a lack of harmonisation on the substantive rules governing costs and expenses in a UCITS product.⁷ This may hamper the comparability of different product offerings and thereby reduce the attractiveness of UCITS to retail investors.

Proposed actions

In line with the abovementioned mandate under the UCITS V Directive, the Commission could analyse what the common costs and expenses of retail investment products across Europe are, and consider whether further harmonisation of the disclosure of those costs and expenses, with a view to bringing new competitive pressures, is needed, while taking into account all the specifics and differences between the offered products.

iv. UCITS – KIID

Issue at stake

In relation to cost and risk disclosure under the UCITS KIID, more consistency could be achieved. It has indeed been the case that managers in different Member States apply slightly differently the requirements of the CESR guidelines on i) the methodology for the calculation of the ongoing charges

⁷ Recital 8 of the UCITS V Directive recognises this issue by providing that “The Commission is invited to analyse what the common costs and expenses of retail investment products in the Member States are, and whether further harmonisation of those costs and expenses is needed, and to submit its findings to the European Parliament and to the Council”.

figure in the KIID and ii) the methodology for the calculation of the synthetic risk and reward indicator in the KIID.

Proposed actions

ESMA sees merit in further harmonisation of the requirements on cost and risk disclosure under the UCITS KIID, and stands ready to modify the aforementioned guidelines as appropriate, or to clarify the interpretation of the guidelines in corresponding Q&As.

While the MiFID and PRIIPs provisions will apply at the end of 2016, further harmonisation efforts should be aimed not only at UCITS, but also at all substitutable investment products (including insurance-based investment products). For that purpose, ESMA suggests aligning as much as possible the UCITS and PRIIPs cost and risk and reward disclosure regimes.

v. UCITS – fund calculators/central databases

Issue at stake

Investors may have difficulties in comparing the costs of different investment products as there are currently no fund calculators or central databases on costs publicly available across Europe.

Proposed actions

Progress has been made on improving cost disclosures for investors through recent initiatives such as MiFID, UCITS and PRIIPs. However, experience has shown the difficulties of disclosing comprehensive and relevant information on costs in one table or one summary cost indicator. As such, it might be useful to complement the information on cost disclosure mandated by the aforementioned legislation via the setting up of reliable on-line calculators or central databases on the costs of these products. Consideration should be given to whether this would be best achieved through voluntary industry or consumer-led initiatives, or on the basis of legislative requirements.

vi. UCITS – improvements on the fund offering

Issue at stake

One way that cross border retail participation in UCITS could be increased is by encouraging providers of financial services to offer investors ready access to a wider choice of funds at competitive prices. The MiFID II framework already goes some way to encourage the offering of increased choice of financial instruments, including UCITS, whilst ensuring increased investor protection. First of all, MiFID II requires investment advisers who provide advice on an independent basis to assess a sufficient range of financial instruments for their clients. The increased development of open architecture

advice models may increase cross border retail participation in investment markets, including UCITS. Furthermore, MiFID II permits investment firms that provide services other than advice on an independent basis or portfolio management to receive third-party payments and benefits only where the payment or benefit is designed to enhance the quality of the relevant service to the client and does not impair with the investment firm's duty to act in the best interest of its clients. In its Technical Advice to the Commission on MiFID II and MiFIR, ESMA advised that the quality of an investment service should be considered enhanced if an additional or higher level service is provided to the client. For the service of advice (on a non-independent basis) this could mean, inter alia, providing access to a wide range of suitable financial instruments. For other financial services this could mean providing access to a wide range of financial instruments at competitive prices, including an appropriate number from third party providers having no close links with the investment firm together with the provision of added-value tools.

On a related topic, given the fragmentation in the processing of investment funds, particularly the lack of common communication channels and standardised format for order placements, investment fund processing may be inefficient and the operating costs, shared between the investor and the fund or its management company, are not neutral.

Proposed actions

It should be noted that the regulatory incentives to increase investor choice as discussed above may still leave room for differentiated application at national level. The Commission could therefore consider further refining the meaning of 'sufficient range of financial instruments' as indicated in ESMA's Technical Advice on the MiFID II delegated acts currently being drafted (including the possible consideration of the element of internationally diverse offerings) or rely on possible ESMA "Level 3" measures, as suggested in ESMA's Technical Advice.

Ensuring compatibility across the European settlement platforms would help standardising and automating the complex and fragmented processing of orders for investment fund subscription, redemption or switching. It would also strengthen the operational settlement process, shorten the settlement cycle which may under certain circumstances, such as IPO or financial crises situations, be crucial and reduce the costs to both the investor and the fund or its management company.

vii. UCITS fund mergers – different tax regimes

Issue at stake

Notwithstanding the progress made through the UCITS IV Directive in the simplification and harmonisation of the procedures for cross-border fund mergers, feedback from stakeholders shows that a major obstacle to this type of activity seems to be the different tax treatment of mergers across the EU.

Proposed actions

The Commission could launch an exercise to identify more precisely the tax-related obstacles to cross-border fund mergers in order to ascertain if there is any scope to try resolving these. Subject to the outcome of that analysis, consideration should be given to harmonising the different tax regimes across Europe governing cross-border fund mergers. This would introduce clarity and incentivise this type of activity by creating economies of scale for asset managers.

14) Would changes to the EuVECA and EuSEF Regulations make it easier for larger EU regulated funds to run these types of funds? What other changes if any should be made to increase the number of these types of fund?

Issue at stake

The figures available on the usage of the EuVECA (European Venture Capital Funds) and EuSEF (European Social Entrepreneurship Funds) labels show that there is still limited interest from the industry in these vehicles.⁸ A potential barrier to the take up of EuVECA and EuSEF activities by fund managers is the lack of clarity on whether or not managers whose portfolios exceeds EUR 500 million can apply for authorisation under the EuVECA and EuSEF Regulations. In order to deal with this issue, on 11 November 2014 ESMA issued a Q&A (ESMA/2014/1354) clarifying that AIFMs above the threshold of Article 3(2)(b) of the AIFMD can manage and market EuSEF and EuVECA and specifying which provisions should apply to these managers for the performance of these activities.⁹

Proposed actions

While the ESMA Q&A already clarified the types of manager authorised to manage and market EuSEF and EuVECA, a possible legislative amendment of the EuVECA and EuSEF Regulations reflecting such a clarification would help in providing asset managers with further legal clarity and certainty on the matter. This may help in

⁸ As of 16 March 2015, there were 15 authorised EuVECA managers managing 25 EuVECA funds and 2 EuSEF managers managing 3 EuSEF funds.

⁹ See Questions and answers 1b and 1c of the Q&A.

fostering the take up of EuVECA and EuSEF activities also by bigger asset managers. This would be in line with the provisions of the review clauses under Article 27 of the EuVECA Regulation and Article 28 of the EuSEF Regulation which both foresee that, by 22 July 2017, the Commission shall gather data for assessing the necessity to extend the scope of the Regulations in that direction.

16) Are there impediments to increasing both bank and non-bank direct lending safely to companies that need finance?

Issue at stake

As outlined in the Green Paper, the European Commission put in place in 2013 the EuVECA and EuSEF Regulations. These Regulations aim at facilitating the financing of start-ups and social businesses. These two Regulations have been supplemented by the ELTIF (European Long-Term Investment Funds) Regulation, the purpose of which is to channel investments by funds into long-term projects such as infrastructure.

The EuVECA, EuSEF and ELTIF Regulations are an important step forward but ESMA believes that the collective investment industry can play a much bigger role in the financing of companies. Since funds authorised under the aforementioned Regulations have to respect specific requirements in terms of eligible investments, it may be the case that companies that need finance cannot benefit from this alternative source of financing. It is for this reason that ESMA is of the view that direct lending by funds to companies that need finance should be further facilitated and not restricted to certain types of business.

Proposed actions

In some Member States funds that are not authorised under the EuSEF, EuVECA and ELTIF Regulations can already grant loans to a large spectrum of companies. The legislation governing these activities varies among Member States, which could act as a barrier to the development of a pan-European market for such activities.

Mindful of financial stability issues, ESMA believes that the development of harmonised rules, whether as an opt-in regime or as a mandatory regime for all funds originating loans at European level should be explored with the aim of creating more favourable conditions for the cross-border marketing of these funds in Europe, while ensuring at the same time an appropriate level of investor protection including the absence of marketing of these funds to retail investors and mitigating risks to financial stability.

25) Do you think that the powers of the ESAs to ensure consistent supervision are sufficient? What additional measures relating to national or EU level supervision would materially contribute to developing a capital markets union?

Issue at stake

Delivering a sustainable CMU in practice requires effective and consistent supervision in order to achieve the necessary investor protection and orderly markets, while avoiding undue risks to financial stability and market distortions from regulatory arbitrage. While ESMA's focus on this aspect of its work is set to increase in the coming years, experience to date already suggests that some enhancements would make it easier for ESMA and NCAs to deliver effective and convergent supervision of capital markets.

Proposed actions

Even if no significant difficulties have so far emerged, it would help to clarify and adapt certain aspects of the existing ESMA Regulation, in order to ensure that the powers already available to ESMA can be better used to improve outcomes in practice, such as the following:

- Clarifying NCAs' obligations to respond to requests for information made by ESMA in order to carry out its supervisory convergence mandate pursuant to Article 35 of the ESMA Regulation and align them further with article 17 of the same regulation. To ensure a timely response to emerging supervisory convergence issues, the right of initiative to collect information on an emerging supervisory convergence issue could be delegated to a panel of the Board of Supervisors or the Chair.
- Seeking the full public disclosure of the outcome of peer reviews where agreed by the Board of Supervisors, and maintaining the subjects' right of public response to the findings.
- Giving ESMA the ability to recoup the cost of specific activities, by agreement, from participating NCAs, to make it easier to deliver tailored training or other professional development activities to supervisors from relevant NCAs, and facilitate the delegation by NCAs to ESMA of certain activities where agreeable to both parties.
- Under its new strategy, ESMA will be seeking to provide ex ante assistance where possible. However, in certain cases it will need to consider whether to use its powers under Article 17 of the ESMA Regulation to determine whether an NCA has breached Union law. Were it to make such a finding, it would be important to ensure that the problem is rectified effectively. In the first instance, it would be for the NCA concerned to take the necessary action. However, in case it did not do so, there are powers in Article 17(6) for ESMA to address market participants

directly where the relevant requirements of the acts referred to in Article 1(2) are directly applicable to financial market participants. It would be useful to clarify that these powers relate to those provisions of Directives that establish unconditional obligations that are sufficiently clear and precise to be directly effective.

Moreover, in order to further develop the efficiency of the CMU, the ESAs and NCAs could benefit from having the possibility to suspend temporarily the application of a particular rule if its application could lead to unintended consequences or its application requires guidance or technical specifications that are not yet available, without the application of the relief itself leading to consequences unintended by the law.¹⁰ For example, the clearing obligations laid out in EMIR or the trading obligations laid out in MiFID II could have detrimental effects in case of a sudden drop in the liquidity of a product.

Therefore, consideration should be given to providing ESMA with the legal possibility to suspend certain obligations, suspend their enforceability or to provide further guidance, in well-defined situations backed up by specific provisions in the sectorial legislation covering the field in which these actions would apply. Of course, these new powers would have to be subject to strict democratic control by the European Parliament and European Council.

The suggestions above are made fully recognising that a broader evaluation of the ESFS is planned and such evaluation may also address the issues mentioned.

28) What are the main obstacles to integrated capital markets arising from company law, including corporate governance? Are there targeted measures which could contribute to overcoming them?

Issue at stake

Several problems can be identified in the current mechanics of the voting infrastructure, particularly at a cross-border level. Prominent issues include ensuring easy access to information (e.g. the distribution of proxy materials), effective voting in absentia and reliable vote confirmation systems.

Inefficiencies in the voting chain should be addressed at the EU level for the following main reasons: i) international institutional investors suffer high operational costs from engagement due to different national regulatory frameworks, ii) local differences in standards within the EU are a barrier to foreign capital and do not always seem justified by domestic financial market structures, iii) solutions cannot be effectively sought at domestic level only.

¹⁰ Please note that already in its letter to Commissioner Barnier dated 31 October 2013 (ESMA/2013/1561) ESMA argued for the possibility of such temporary relief.

Both the original Shareholder Rights Directive (SRD) and its proposed revision address these issues mainly at a high level¹¹ and other initiatives¹² have not yet produced all the envisaged results in terms of widely implemented and ambitious best practices. While this is naturally a very complex and long-term process, there is a need for further improvement.

Proposed actions

It is therefore proposed to further harmonise and streamline general meetings' operational processes based on a joint public/private initiative¹³ so as to ensure that voting-related information from the issuer reaches the shareholders¹⁴ and vice versa in a timely and cost efficient manner. These objectives could be facilitated in particular if jurisdictions and/or companies were to promote the enlarged use of information technology in voting, including secure electronic voting in listed companies.

Potential actions to achieve these results should be subject to a thorough cost-benefit analysis and minimum harmonisation should be preferred when there is a risk of undermining good practices at national level. Specific targeted actions may include the following:

- Promoting standardised electronic communication systems and forms for uniform use across the voting chain, facilitating the flow of information on meeting notices, agendas, votes and entitlements or notifications of participation.
- Promoting more uniform and transparent record dates, cut-off dates and other deadlines in the voting process, at least where compatible with national laws.
- Promoting minimum voting services to be provided (with transparent costs, if any) to clients by custody banks or other entities in the chain (possibly including confirmation of vote delivery). Coordinated ways to implement these services would also maximise the benefits arising from increased automation of general meetings.

IV. Other areas affecting the efficiency of the EU capital markets

39. In the course of its reflections on CMU, ESMA encountered some additional areas that it considers important for the functioning of the EU capital market and thus the

¹¹ The proposed Securities Law Legislation (SLL) aims to address some of these goals but the legislative process has not been finalised yet.

¹² See - for example - the work of the European Post Trade Group (EPTG), which addresses the broader item of "cross border shareholder transparency and registration procedures", as well as the work of the Broad Stakeholder Group (BSG) on "market standards for corporate actions processing and general meetings".

¹³ This initiative should be consistent with any possible implementing acts adopted by the EC on the basis of Art. 3 of the revised SRD.

¹⁴ The proposed actions should not impact national laws defining the concept of shareholders.

CMU. We identify those areas below, without making proposals as they are, for example, not in the remit of securities regulation or further analysis is needed before making any proposals.

1. Company and insolvency law

40. As recognised in the Green Paper, notwithstanding several directives on company law and progress made in the area of conflict-of-laws rules for cross-border insolvency proceedings, differences in company laws and national insolvency frameworks may jeopardise the cross-border activities of companies and investors.
41. ESMA provided above¹⁵ some input focusing on corporate governance also related to benefits coming from increased use of technology. Moreover, ESMA agrees that inconsistencies across the EU on company and insolvency law may have an impact on both the decision to invest and the value of the investment made, especially in the case of an investor considering an investment for his own account or on behalf of a third party outside its country of origin.

2. Securities law

42. The Commission has been reviewing securities laws for several years and has identified significant barriers to the safe and efficient functioning of the Single Market. The existing legal gaps and inconsistencies reduce transparency in terms of 'who owns what' and can create legal risks in cross-border securities holding and dispositions.
43. With increasing cross-border investment and the use of securities as collateral, the legal gaps and different approaches across Member States create legal risk and increase costs for intermediaries and investors. This reduces efficiency, favours opacity and could increase systemic risk.

3. Taxation

44. Taxation at both corporate and individual level is having an impact on the attitude of issuers and investors. Equity investments are typically more heavily taxed than debt investments. Tax incentives applied at retail level can strongly impact on the saving attitude of individuals. Moreover, investors do not always have clear information about the taxation applicable to their investments, especially in case of investment abroad, which creates information asymmetries.

¹⁵ See the response to question 28.

4. Compensation Schemes/Out of court dispute settlement

45. Only when investors feel sufficiently protected will they be willing to enter the capital markets and participate in them. In ESMA's view there are two topics that can affect the consistent level of investor protection across the EU and thus the functioning of the CMU.
46. The first one is the current EU legislation on investor compensation schemes (Directive 97/9/EU, 'ICSD'). The ICSD leads to divergent compensation schemes across the EU countries since it is a minimum harmonisation directive which, inter alia, does not harmonise the funding systems of compensation schemes (e.g. ex-ante or ex-post). This hampers the efficiency of the capital markets.
47. The second topic is the extra-judicial system for consumer complaints. MiFID II (in conjunction with the Alternative Dispute Resolution Directive) introduces a high-level framework for out of court settlement of disputes between investment firms and their clients. It is very likely that this has led or will lead to divergent systems and frameworks in the various Member States. This could create barriers for cross border investments, and there may be scope to minimise some of these divergences.

5. Sanctions in EU financial services legislation

48. Not all the provisions on sanctions in the existing legislation are aligned with the more detailed provisions which have been included in more recent legislation on the minimum type and level of sanctions which need to be available under national law.

49. For the two other consultations launched by the Commission on 18 February 2015¹⁶, reference is made to the two separate ESMA responses 2015/ESMA/857 and 2015/ESMA/858.

¹⁶ Consultations on "Review of the Prospectus Directive" and "An EU framework for simple, transparent and standardised securitisation".