

## Regulatory and supervisory developments, the challenges ahead – a European perspective

Finanstilsynet 30<sup>th</sup> Anniversary International Conference  
Oslo

Verena Ross  
Executive Director

First of all, let me start by congratulating Finanstilsynet to its 30<sup>th</sup> anniversary and thanking them for inviting me to this international conference - for inviting me to your birthday party if I might say so.

Today's programme is a good reflection of Norway's strong commitment to open capital markets, to strong co-operation with the other Nordic countries, the rest of the world and especially the European Union. It is therefore a particular pleasure to be here with you today, to bring you a European perspective on the capital markets and their regulation. I would like to express my appreciation to the Norwegian FSA and Anne-Merethe Bellamy, with whom we work frequently together in ESMA's Board of Supervisors, for inviting me to speak here today at this international conference.

Norway is not a Member of the European Union. The European Economic Area Agreement exemplifies however the important trading partners we both are. You are part of the EU Single Market and to make sure that both you and the Union benefit as much as possible from that, it is important that we maintain excellent co-operation.

I am really pleased that, after lengthy but good discussions with the Norwegian Ministry of Finance and your Parliament, the legislation the EU introduced after the financial crisis will finally be integrated into Norwegian law.

I can definitely imagine that not all of you might be happy or excited about that. That some might consider the legislation onerous, burdensome or even going beyond what is needed today in Norway. Especially if we look at things through the eyes of where we are today, in a country that did not experience a severe banking crisis, as the rest of Europe did, but where at this moment the focus is more on stimulating growth.

I could give you now a "typical" regulator's response that we should not forget what we have learned from the financial crisis. But I will not do that. I would rather ask you to look at it from a positive angle, and invite you to see the opportunities the new legislation creates for doing business across Europe by promoting further market integration and preparing our markets for



the future.

Norway is an important capital market for Europe and though you might not have a formal vote within the EU, your voice counts. I am therefore happy that we will further strengthen the integration of the EEA-EFTA States into ESMA's governance in the next months. I would also definitely invite you to comment on ESMA's ongoing work, especially our consultation papers.

In any case, it is good that events like this are organised where we can learn from each other, exchange views on the direction of travel, ensure close co-operation and discuss how things can be further improved and fine-tuned.

Today I will speak about the future of our capital markets, including the capital markets union and how important (retail) investors are in that respect. I will use examples of ESMA's work to illustrate this – these examples fall into three areas:

- (i) the role of disclosures;
- (ii) the role of distribution; and
- (iii) the importance of supervisory convergence.

Finally, I also would like to touch briefly on the importance of data in today's capital markets and their regulation and supervision.

Let me start by noting how important capital markets are. Europe learned the hard way that it became very (too) dependent on its banking system – to the point that the banking crisis hurt all of us, losing generations of economic welfare. Therefore, as the Norwegian example confirms, we need to develop our capital markets further as an alternative to the traditional banking system to allow new, young entrepreneurs to start their business, to develop their ideas, and to create jobs and growth.

### **Capital Markets Union – putting investors at the core**

The European Commission launched the Capital Markets Union initiative building further on a history of decades creating welfare by integrating our economies. I wholeheartedly support that initiative and whilst I am very open about the fact that I would have preferred to do this with 28 Member States I think that what we could do with 28, we should definitely do with 27. This is an opportunity for Europe, for its citizens and future generations which we cannot and should not disregard.

I am very happy that the European Commission confirmed last month its commitment to the CMU project through the publication of a progress report accelerating some reforms and highlighting the role ESMA should play in that respect.

There is acknowledgement of what ESMA has already achieved over the last 5 years: amongst others building stronger capital markets through rules and principles contributing to financial stability. But, as ESMA has identified in its strategic orientation last year, there is also a clear need for more consistent implementation and stronger supervision, to support investor

protection, orderly markets and financial stability.

CMU is also about providing investment opportunities, both for professionals and for consumers. At school we all saw in our textbooks that one should diversify one's investment portfolio, but today we learn the hard way. Putting money aside only on a savings account within a low (or even negative) interest rate environment will not allow us to build up sufficient savings or a worthwhile pension. Capital market investment will have to become a key element of a retail investor's portfolio. Providing comfort to them that the rules of the game are clear and fair will be one of the main challenges for the Capital Markets Union to work.

Indeed, the CMU has to take investor protection as one of its main guiding principles. As I mentioned earlier I would like to briefly speak about three ESMA work streams that exemplify this focus.

### **Disclosure - PRIIPs**

The first one, disclosure, will take an important step forward with the implementation of PRIIPs next year. The so called Packaged retail and insurance-based investment products (PRIIPs) is probably one of the most important projects ESMA has been working on in close co-operation with EBA and EIOPA (and of course all national competent authorities). It is one of the most visible projects for the end investor that ESMA is working on: retail investors will physically be able to see a Key Investor Information Document (KIID) bringing together the key information about potential investments.

ESMA together with EBA and EIOPA has been working hard over the last years in finding a suitable cross-sectorial approach for PRIIPs and their manufacturers, working closely with the European Commission that did some important consumer testing work. We believe that the standards we have proposed to the European Commission represent a balanced compromise between the different interests. They are built on considerable stakeholder consultation – three separate consultations and including the input of an expert group.

It seems that some market participants are not convinced by our suggested way forward, probably also because there might still be some concerns related to the implementation of the Insurance Mediation Directive (IMD). Indeed, given the timing of the PRIIPs work, there was a clear need for alignment with MiFID 2 but we also had to look at the UCITS KID in this context.

As you know, the European Parliament's ECON Committee expressed concerns which were followed by the Parliament when deciding to reject the RTSs prepared by the ESAs and to ask for a delay of the implementation deadline.

The Parliament's concerns are four fold:

1. How credit risk should be treated within the risk calculation and categorisation of insurance products?
2. How multi-option products should be treated?
3. Whether the proposed method for performance scenarios reflect accurately potential losses investors could suffer; and

4. How the comprehension alert, which informs an investor that she/he is about to buy a product that is not simple and may be difficult to understand, will be applied across the different EU countries.

I still believe that the RTS proposed by the three ESAs and supported by the respective NCAs represents a balanced compromise between the different interests, fully taking into account the breadth of PRIIPs covered and aimed to ensure better comparability between them. Of course these RTS – as with any technical instrument – can always be improved and refined. But they represent a good and sound foundation in our view.

It is now up to the European Commission – who is in the lead – to find a common way forward together with Parliament and Council in the next months. There is no formal role for the ESAs, but we will assist the Institutions wherever possible. Rest assured that I am fully convinced about the need for clarity both for investors and market participants on what the world will look like on 1 January 2017, when the Regulation is supposed to come into effect which as I mentioned earlier is another topic the Institutions are currently discussing.

We are also conscious that further guidance might need to be provided by the ESAs and we stand ready for that. In fact, we are already preparing some Q&As or guidelines which might help the industry in its implementation of the PRIIPs regulation.

### **Distribution – MiFID**

But it would be wrong to portray investor protection as an issue of disclosure only. Yes, increasing the transparency of financial instruments will improve the functioning of securities markets. However, more is needed to support capital markets playing a more central role in the financing of the economy. We need to have a well-functioning intermediation process ensuring that financial instruments, find their way properly into the portfolios of asset managers and end-investors. MiFID II very much recognises that this process is still distorted and further improvements are needed in the way investment advice on financial instruments is provided.

So, distribution plays an important role as well. And MiFID 2 will have a big impact on the distribution landscape including:

- (i) the need for retail investors to seek advice in order to access financial instruments deemed complex;
- (ii) the cost of investment advice;
- (iii) more transparency on fees; and
- (iv) a ban on inducements in the event of *independent advice*.

I know that many of you, at the business side, are concerned about how this will impact your business model. But I am convinced that this an important step change in the interest of the investors. It is true that the impact is difficult to predict. Will there be new market entrants in this new environment? Will there be new products and services embracing the new regulatory principles, or perhaps trying to circumvent them?

I think it is quite likely that some of the advice will become more standardised and generic, and as such hopefully contribute to lower costs for investors. In that respect, I also believe that

Europe should embrace the positive side of technology.

Just imagine what could be the impact of automated advice on the retail market? Where young people, who do not want to go to their local branch anymore, or who do not know their 'account manager', will buy products with a few clicks.

And I see some people already looking at me, is ESMA really promoting people buying products quickly without due diligence or care? No, advice should be provided, but I believe that for simple products we can better structure and standardise advice. And for those that believe every client is different (even in respect of buying of simple products) and needs personal care, I would dare to ask the question: that is the system we currently have, and why did it go wrong so many times? I am not saying that automated advice is the answer to all our issues. Far from it. But we should look carefully how new technological developments in this area – also in combination with existing advice channels - can provide better customer experiences and better advice at the same time.

### **CFDs – a good example of supervisory convergence on the ground**

Thirdly, I would like to talk about supervisory convergence – a term which has a bit of dry connotation at the start but which is much more important than you think.

Over the last months' regulators all across Europe were overwhelmed by investors complaining about so called contracts for differences they had bought, often cross-border and mainly from companies based in one jurisdiction.

I know this was also the case here in Norway – and I believe that it is fair to mention how Anne-Merethe has taken care of the interests of Norwegian investors in the debates on this issue around the ESMA table.

Across the ESMA community, we have noted an increase in the offer of speculative products such as financial contracts for difference (CFDs), binary options and rolling spot forex to retail clients, often on a cross-border basis across Europe.

The proliferation of these types of risky and speculative products gives rise to investor protection concerns. Supervisors have also observed that they are often marketed and sold in an aggressive manner, and that some firms fail to comply with their regulatory obligations under MiFID, which creates the conditions for retail investors to suffer detriment (e.g. in the form of unexpected losses).

ESMA already issued in 2013 an investor warning on CFDs, together with the EBA, highlighting some of the main risks of investing in CFDs and describing some poor practices observed in this sector of the market.

In 2014, we published an opinion on MiFID practices for firms selling complex products and an accompanying investor warning on the risks of investing in complex products.

Recently we have been focusing more on promoting common supervisory approaches and practices across Europe (on the basis of what we have published earlier) and have been

encouraging the dialogue between home and host supervisors.

Since mid-2015, ESMA has been coordinating the activities of a group of NCAs and the Cypriot regulator which has been focussed on issues relating to a number of Cyprus-based investment firms offering these types of products across Europe. In the context of this group, CySEC has so far imposed administrative fines on a number of firms and suspended the license of one firm (which has since withdrawn its license).

Also in July 2016, we published a further warning on these products.

It really shows the practical added value ESMA can have when an issue is persistent across Europe. We will continue monitoring this area and continue with our supervisory convergence work, including by coordinating the ongoing cooperation work of the group of NCAs and by continuing our related policy work (e.g. issuing more Q&As on what is expected of firms in the coming months). ESMA will also consider whether in light of the new MiFID II requirements and particularly the product intervention powers that will be entering into application in 2018, further work will be necessary.

I think this is a perfect example that a true Capital Markets Union is not only about making more rules but even more about applying those consistently in practice. That's what we call supervisory convergence. Supervisory convergence has increasingly become one of ESMA's core activities. It will help us to achieve a level-playing field (including on the important investor protection issues) both within the EU and the EEA-EFTA States.

### **High quality data – prerequisite to ESMA's and NCA's risk analysis and supervision**

Having talked respectively about ESMA's rule making and supervisory convergence activities so far, I finally would like to say a few words about the need for high quality data to assess risks to investors, markets and financial stability.

This is an area where we are gradually stepping up but where we are starting from a much lower base than other regulators, especially our colleagues dealing with banking supervision. We need to have better data on (and developments in) securities markets. ESMA has already taken first steps to improve the EU-wide data and risk analysis on securities markets as part of our trends, risks and vulnerabilities reports.

Data to assess risks and allow the focus of our limited regulatory and supervisory resources is essential, at both national and European level. In some areas, national authorities already have relevant data, which we can aggregate and benefit from at EU level, in a way that does not create additional burdens for market participants. In other areas national level data is either non-existent or it is not possible to aggregate and use the various pieces of data collected at national level. Here convergence will again be essential. Finally, some data we need to collect ourselves, especially from entities supervised directly by ESMA such as trade repositories and credit rating agencies.

In one area we are entering completely new ground to improve data quality. In the context of the MiFID II implementation, national competent authorities (including the Norwegian FSA) have delegated to ESMA for the first time two major data related IT projects (which are legally

under MiFID a national competence). ESMA will provide a central facility in relation to reference and trading data and the calculation of the comprehensive MiFIR transparency parameters. This project will allow us to collect data in a more efficient and harmonised manner across Europe, thereby achieving important economies of scale and lowering costs for industry and taxpayers, and publish all transparency parameters and reference data on financial instruments in a one-stop shop.

The project which requires ESMA to connect to hundreds of trading venues across the EU is on track and is planned to go live at the same time as the application of MiFID II in January 2018.

This should contribute to market transparency and data quality across Europe in this important area. It will make ESMA a key part of European market infrastructure, as firms will need to consult regularly the data and information published on ESMA's website for the whole of the EU.

## **Conclusion**

That brings me to the end of my talk during which I have focused on how important capital markets will be to finance our future. A Capital Markets Union needs to centre around the investor. The aim has to be to achieve for the investor a modern, state-of-the art, genuinely European approach towards disclosure, distribution, data-collection, and cross-border supervisory issues. ESMA will continue its efforts across its four activities of rule-making, supervision, convergence and risk analysis to contribute to a strong investor focus and to sound financial markets in general.

ESMA will continue to work with stakeholders across the different sectors and across the whole of Europe. In particular, we look forward to further building on the already strong cooperation with our Norwegian supervisory colleagues and the Norwegian financial market and investor community.