

SUMMARY OF CONCLUSIONS

Joint meeting of the Board of Supervisors and the Securities and Markets Stakeholder Group

Date: 24 May 2017
Time: 13:30 – 17:00
Location: ESMA, CS60747 – 103, rue de Grenelle, 74345 Paris
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1. Opening remarks

The ESMA Chair welcomed all SMSG members and all ESMA Board of Supervisors' members to the meeting. He emphasised the high importance that ESMA places to being able to hold these meetings with the SMSG and he thanked all board members and stakeholders present for their time and effort dedicated to the meeting.

The SMSG Chair also welcomed participants of the meeting. He informed the Board of Supervisors on the SMSG's own initiative work carried out since the joint meeting in November 2017, in particular on cost and past performance and sustainable finance.

2. Brexit: a) Risk management in the period around 30 March 2019 in the area of financial services; and b) Supervisory convergence regarding relocation

The SMSG member Eric Litvack held a presentation on contract continuity in the context of the UK leaving the EU. He mentioned among others the work on a master agreement regarding the clearing of OTC derivative contracts under French and Irish law.

SMSG Member Mark Hemsley presented some aspects of derivative contracts and Brexit, high-lighting that the potential legal framework fragmentation into the various EU 27 legal frameworks is a major risk in itself given the diversity of laws, the appropriateness of the legal framework, case law, procedures and interpretations. Risks apply to cleared and un-cleared contracts, both of which may amount to very large sums. Regarding uncleared derivatives:

UK and EU-27/EEA parties need the ability to service existing contracts and potentially enter into new agreements in a reciprocal manner (Bank of England estimated that the issue concerns a notional value of £26tn). Cleared – UK and EU-27/EEA parties and CCPs need to be able to access each other (Bank of England estimates that the issue concerns £70tn with £27tn maturing after Q1 2019).

Robert Ophèle, AMF and Chair of the PTSC presented his observations on the work that needs to be undertaken as regards contract continuity. He remarked that preparing for a hard Brexit is a shared responsibility between the private and public sector. Even if a general grandfathering clause seems very challenging in the context of a hard Brexit, several options remain on the table in making sure that securities contracts can continue to be honoured: (i) apply the reverse solicitation exemption to lifecycle events for OTC non-cleared derivative contracts, but there is need of a homogenised guidance on this topic, (ii) move those contracts to an EU27 firm part of the same group and limit in the same time the unintended consequences of such moves of contracts in clearing obligations and collateral margining, (iii) have a transitional period, which would be the easier way but is politically uncertain. These different options need to be clarified as rapidly as possible, as well as the amount of contracts really at risk.

Edwin Schooling Latter, Head of Department Market Strategy at FCA, noted that authorities and market participants need to prepare for the worst and hope for the best. He assured that the UK does prepare for implementation of the EU laws like MiFID II/MiFIR, MAR, etc. He stated that he does not expect that the private sector will and can solve all the issues. The best way in his view would be to make a solution part of the withdrawal agreement. EU law will remain available to future contracts.

Comments were made on the costs that renewal of contracts might bring for retail investors.

The ESMA Chair noted that under the withdrawal agreement, if there will be one, the problem of cliff-edge effects will be postponed as during the transition the UK will apply all EU legislation while at the end of the transition it will become a third country. He noted that for UCITS there is no third country regime.

ESMA Board of Supervisors member João Sousa Gião, CMVM, Chair of the SCSC, presented the work undertaken in the Supervisory Convergence Network (SCN) in the last year. The group meets monthly to discuss real cases and horizontal issues such as outsourcing, delegation and the like. The National Competent Authorities share experiences and views but remain fully responsible for their respective individual cases. They present cases to the SCN early on in the process, sometimes even before there have been formal applications. The SCN can escalate matters to the Board of Supervisors. The issues discussed often relate to matters in the cross roads between banks and investment firms. An increase in the number of requests can be noted from a few countries while it could also be noted that a number of firms do not yet have plans for the time after Brexit.

SMSG members also commented on, inter alia, trading obligations, data needs and the need for EU27/UK cooperation MOUs. The Executive Director confirmed that ESMA is indeed

conducting internal preparations for possible MOU(s) with the UK authorities, just as there are MOUs in place with other third country authorities around the world.

3. MiFID II implementation

SMSG member Kerstin Hermansson presented a note of the SMSG outlining a number of issues in relation to MiFID II implementation, such as:

- Market standards for target market information.
- Trading flows seem to have moved slightly to trading venues, while noting a decrease in trading.
- There is a need to have more data on post-trade transparency for equity. APAs have no common standards.
- Data is not correct as regards SIs and their market share statistics should be higher.
- The tick size regime for SIs is not working correctly.

SMSG members made the following remarks:

- One SMSG member noted that it is currently difficult to interpret the market and that market participants still face the same issues as before
- One SMSG member noted that research for SMEs tends to be less available.
- One SMSG member made the point that there are some actions to be taken which are relatively straightforward like cleaning up data standards.

ESMA noted that further Q&As will soon be finalised which should be able to help market participants and that ESMA works on issues like enhancing the quality of data. As regards LEI for issuers, ESMA continues to encourage market participants.

The ESMA Chair noted as regards target markets that manufacturers and distributors need to provide more information and that it is not the role of ESMA to pre-approve any particular standard. ESMA is monitoring the developments vis-à-vis availability of research.

4. PRIIPS implementation

SMSG member Georg Baur presented some of the SMSGs observations in relation to PRIIPs, noting that there is a reluctance by corporates to issue bonds due to unclarity of regulatory scope, there are differences in nomenclature (e.g. between MiFID and PRIIPs), leading to

retail clients being overloaded with or misled by information and possibly liability issues for firms and investors.

He noted that, because of the now required determination of future performance scenarios based on historical data, and a lack of correspondence between recommended holding period/duration and annual approach, some scenarios show far too positive performance and by that may mislead retail investors. Solutions to the problem could be flexibility, a disclaimer, warning or extension of the UCITS/certain AIF exemption deadlines. Furthermore, he noted that the SMSG favours a targeted early review of the PRIIPs regulation and reminded that the SMSG already has expressed its support for having past performance scenarios instead of artificial future performance scenarios.

SMSG Vice Chair Jarkko Syyrila presented some observations on the issue of transaction costs for PRIIPS, where he stated that the current market consensus is that more precise market data (i.e. mid-market prices) will not solve the fundamental problem of over- and underestimation of transaction costs because the methodology as such is flawed. A solution would be to remove market impact from cost calculations, and to work at technical level with market participants to better understand the problem. He stated that a solution cannot await the PRIIPS review and in the meantime an extension of the deadline for UCITS KIIDs could be a solution.

Martin Moloney, Central Bank of Ireland, Chair of the IMSC, stated that he had sympathy with the argument that extension of the UCITS KIID deadline should be considered if the problems with PRIIPS were fundamental, but he said he would be cautious about the idea of bringing the PRIIPs review forward. At the same time, there is a strong merit in moving from the UCITS KIID to the PRIIPS KID as soon as practical. He acknowledged that aspects of the problem arose because dates and certain parameters are hardwired in ways that are not easy to change.

The ESMA Chair noted that, depending on the assessment of the issues, there may be a mix of level 1, 2 and 3 solutions needed. More evidence on transaction costs would be required as there is no clarity yet to what extent positive transaction costs are the result of inappropriate application of the methodology or the result of issues with the methodology itself. More generally, not looking into market impact would underestimate the net transaction costs.

The ESMA Chair closed the meeting thanking all for a high-quality discussion.