

Summary of Conclusions

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

Date: 12 July 2019
Time: 9:00 – 12:30
Location: ESMA, CS60747 – 103, rue de Grenelle, 74345 Paris
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1. Opening remarks

The ESMA Chair welcomed all to the meeting noting the good turn-out of board and SMSG members and the importance of the topics on the agenda.

2. ESMA strategic orientation

The ESMA Chair noted that the current ESMA Strategic orientation for 2016-2020 relate to a period where the focus of ESMA's activities had been on the single rule-book work and intensifying work on supervisory convergence. The environment for ESMA is now shifting involving important legislative developments, new mandates and Brexit. The ESMA Board has therefore found it relevant to develop a new strategy for the years to come.

The ESMA Chair high-lighted data and risk analysis as key components to drive ESMA's activities, like supervisory convergence and direct supervision. Areas of focus will also be CMU, sustainable finance and financial technology. ESMA will aim for an outcome-oriented focus.

ESMA will continue to work on supervisory convergence as a key priority while also direct supervision will become a more important element for ESMA in particular in relation to the supervision of 3rd countries CCPs.

Three SMSG members made a presentation in order to raise a number of recent challenges. Giovanni Petrella mentioned, among other things, sustainable finance and cyber risks, but

also stability issues relating to demographic change. He also referred to new tools in the form of AI and big data. He considered market structure issues to remain high on the agenda and also mentioned cooperation issues in the EU and beyond among key points for attention.

SMSG member Guillaume Prache noted that investor protection – also a CMU goal – should remain a key priority, especially given the low and often negative returns for investors, including on pensions where in assessing the risk profile of the client the time-horizon of the investment should play a more prominent role. ESMA should continue to work on enhanced transparency of performance and fees in the PRIIPs and MiFID II review, and should continue to use its banning powers where necessary. He further raised that only 20% of products are under ESMA's remit, and that ESMA should ideally also be involved in the PEPP L2 and L3 work.

SMSG member Alexander Schindler mentioned as key aspects CMU, the post-Brexit need to strengthen EU capital markets in consolidating the financial services industry, PRIIPs and the whole value chain of sustainable finance, as well as important issues due to lack of data.

Members of the SMSG and Board members mentioned several market developments which should be decisive for the establishment of ESMA's course of action.

- Brexit, which increases the urgency of a CMU,
- Input of SMSG in direct supervision by ESMA, which requires greater agility
- ESMA's role in relation to other regulators will gain in importance
- Data issues - GDPR being insufficient for big data – the need to understand algorithms.
- Need for non-financial institutions not under ESMA's remit should at least be monitored
- Compliance by SMEs – proportionality
- Regulatory tools to take into account increased use of smartphones
- Robo-advice models should be monitored with mystery shopping. Robo-advice is for the happy few: fee based and access to low-cost ETFs.
- Libra currency and AI machine learning (also for market surveillance)
- Cloud Risks
- Distribution and tokenisation to escape regulation
- MiFID II framework for secondary trading, speed bumps and data
- Access to data and transparency
- Need for more regulatory convergence
- Need for an interactive rulebook.
- Need for competition between different platforms; need to examine who is trading where; risk that many investors are pushed out because they cannot compete with algorithmic traders.

The ESMA Chair thanked all participants for the very useful input and summarised key elements of the discussion like CMU, sustainable finance, responding to new financial technology and a request for proportionality.

3. Sustainability

SMSG member Michael Nietsch gave a presentation covering the wide area of Corporate social Responsibilities (CSR) and sustainability work, including initiatives at EU and UN level in relation to taxonomy and the green bond standard. He noted as main challenges: the speed of the developments, the multitude of initiatives, the problem in attaining reliable data, the high risk of fraud and varying reporting standards.

Ana Martínez-Pina García, CNMV, Chair of the ESMA Coordination Network on sustainability, made a presentation covering the EU Action plan and the work that ESMA is undertaking as a result of this, covering corporate reporting advice in relation to MiFID II, AIFMD and UCITS, short-termism and investment firm disclosures.

Gerben Everts, AFM, gave a presentation of the work undertaken by the Dutch Authority in relation to sustainable finance.

SMSG members high-lighted the urgency of the matter and that capital markets are waiting for the legislators to finalise the legislative framework and pointed to the issue of lack of data (no ESG equivalent to IFRS). They also mentioned the need for retail investor education in view of transition challenges.

Members also mentioned green washing risks at fund level or at issuer level. There is still a weak framework on social and governance issues.

The ESMA Chair thanked all for the useful input on the topic and mentioned the extensive mandated provided to ESMA in this area.

4. Closet indexing

ESMA Board Member Derville Rowland, Central Bank of Ireland, explained that the CBoI has been working on the issue of closet indexing, using among other the ESMA closet indexing study of 2015. The CBoI had undertaken a study covering all their funds (2550 actively managed funds) in order to find out how funds described their investment strategy and whether the fees aligned with a passively managed fund. She described how the CBoI now is following-up the funds suspected of being closet index funds, and that 50 such cases were under investigation.

ESMA Board Member Andrew Bailey, FCA, presented the work his authority had undertaken to assess how far funds' objectives were clear to investors. 96 funds had been identified for closer scrutiny of which 25 did have adequately described their fund strategy, while 71 had not. He noted a new type of active management, and the purpose of price formation that active management entails.

ESMA Board Alternate Françoise Kauthen, CSSF, presented some of the work that they had been undertaking in relation to closet indexing and mentioned that they have investigations ongoing.

SMSG member Guillaume Prache noted that the topic had been on the agenda for a few years and accounted for the work that Better Finance had done. He regretted that, apart from sanctions in the UK, no other EU authority had issued sanctions for closet indexing.

ESMA Board member Robert Orphèle mentioned that they were doing a study on closet indexing.

SMSG members made various comments in relation to i.a. benchmarks used, investor objectives. The ESMA Chair concluded the discussion noting the complex measurement issues which warrant a careful approach regarding enforcement and sanctions.

The SMSG Chair stressed the importance of the SMSG being able to discuss topical issues of securities regulation with the Board and expressed gratitude to everyone present at the meeting for their engagement in the discussions.