

**Ms Mairead McGuinness**  
**Commissioner in charge of Financial**  
**services, financial stability, and Capital**  
**Markets Union**  
**European Commission**  
**Rue de la Loi /Wetstraat 200**  
**1049 Brussels, Belgium**

**Ref: ESMA response to the targeted consultation on the functioning of the European Supervisory Authorities**

Dear Commissioner McGuinness,

We would like to take the opportunity of the targeted consultation on the functioning of the European Supervisory Authorities (ESAs) to share our views on the progress made in recent years in strengthening the role of ESMA, and highlight some aspects on which we believe further improvements could be made.

The last review of the ESAs in 2017 represented an important milestone for ESMA. Since its establishment in 2011, ESMA has progressively evolved into an established and recognised European authority, built a reputation in effective supervision, thorough risk analysis and valuable supervisory convergence. That last review provided the opportunity to take stock of the successes of ESMA, while also addressing certain limitations. In order to make ESMA's duties and powers more resilient and fit-for-purpose, a range of changes were agreed by co-legislators.

As that ESAs review only culminated in late 2019, and given that many of those changes have only recently been fully implemented, it remains in our view too early to meaningfully assess the full impact of most of the changes agreed by the co-legislators.

At the same time, the environment in which ESMA operates has also changed dramatically in just a short period of time and presents new challenges for ESMA, National Competent Authorities (NCAs) and market participants. The COVID-19 pandemic brought about new risks for the financial system, while at the same time, the EU financial market landscape was altered on account of the departure of the UK from the EU. These significant events occurred at a time where financial markets are adapting to momentous global changes linked to sustainable and digital finance. These challenges not only give reason for ESMA to continue to self-reflect on the effectiveness of its responsibilities and tools for the present environment, but to also consider how suitable they are to deal with future challenges.

The 2020 Capital Markets Union (CMU) Action Plan describes the ambitions for a deep and efficient single European market for capital for the future. The challenges outlined above also underscore the need to progress urgently on this, in order to rebuild the resilience of the EU economy and expand reliable and competitive sources of funding and investment for the benefit of EU citizens and companies. The Report on the CMU by the High-Level Forum in June 2020, which formed the basis for the CMU Action Plan, highlights how *'high-quality, well-resourced and convergent supervision based on a single rulebook is a pre-requisite for the CMU'* and that the powers of the ESAs need to be commensurate to achieve this. ESMA's mandate must therefore continue to be appraised in order to ensure that it continues to have the appropriate capabilities and tools to drive EU supervisory convergence, to ensure a genuine level-playing field for all market players as well as to enhance investor protection and promote stable and orderly financial markets, in line with its mission and the objectives of the CMU.

Following discussions within the Board of Supervisors, we set forth some general recommendations in the annex, which we believe merit further consideration by the European Commission as part of this review. We stand ready to discuss these in more detail with the European Commission and support its future work of on these matters.

Yours sincerely,

Anneli Tuominen

## Annex

### I. Reinforcing ESMA's approach to supervisory convergence

Building high and consistent standards of supervision throughout the EU remains at the core of ESMA's mandate. It is therefore vital that the tools used to achieve this are regularly appraised and, where necessary, strengthened. Many of the key changes introduced during the last ESAs Review came in the form of new or improved instruments that aim to foster that supervisory convergence. In particular, the ESMA Regulation was revised to establish a new peer review process, Union Strategic Supervisory Priorities (USSP), coordination groups, an EU supervisory handbook, and a new Questions and Answers (Q&A) process.

These new tools were certainly a step in the right direction. In line with [ESMA's Strategic Orientation 2020-22](#), ESMA implemented those changes with a risk-based approach in mind. A structured framework is gradually being put in place in which ESMA, together with the NCAs, proactively identifies supervisory risks and problems that may have an important impact in the EU on investor protection, orderly functioning of markets or financial stability. One of the outcomes was the identification of the [USSPs](#) for the first time in November 2020.

Notwithstanding the recent nature of these convergence powers, it is possible to already see the positive impact in some of their application. For example, the fast-track peer review process proved to be a nimble, efficient and timely convergence tool based on its use in the [Wirecard case](#). At the same time, some less helpful effects in other areas are also evident, for example, complications with the pace of the new Q&A process. Therefore, it is important for ESMA's convergence tools to remain under regular assessment to ensure their appropriateness in line with ESMA's overall objectives.

Recent experiences have illustrated how certain further changes may contribute to more effective convergence efforts by ESMA. At the height of the COVID crisis in 2020, when economic conditions were deteriorating and financial markets were subject to extreme volatility, the emergency coordination role under Article 18 of the ESMA Regulation was not activated based on a Board of Supervisors assessment that an emergency situation did not exist. However, this situation also exposed some fundamental issues regarding a lack of sufficient clarity in the conditions and modalities in Article 18 on how and when to trigger this coordination power. This tool should therefore be assessed further, with a view to clarifying how it can be effectively employed in emergency situations and how it interacts with ESMA's coordination role under Article 31.

The ability for supervisory and enforcement information to be shared amongst NCAs and with ESMA is also a fundamental element of effective risk-based supervisory convergence. Where limitations or inefficient approaches to information sharing across the EU exist, it can hamper the effective supervisory or enforcement activity. Decisions may be taken based on limited information, which risks fragmenting the overall supervisory view and hindering efficient supervisory responses in the EU. In addition, it may prevent ESMA being effective in fulfilling its coordination function. Therefore, in order to strengthen the foundation for good information sharing, the legal basis on which NCAs and ESMA can request and share supervisory and

enforcement information, including on entities on a named basis (when justified), should be reinforced in the ESMA Regulation and in sectoral legislation. This would allow us to collectively make our relevant convergence tools work even more effectively.

Another constraint to ESMA's supervisory convergence work is the amount of resources available at national competent authorities. More supervisory convergence activity requires not only additional efforts at ESMA level, but also at national level.

The Q&A tool used by the ESAs is a highly useful and efficient supervisory convergence instrument, designed to provide guidance to NCAs, market participants and other stakeholders on questions relating to the practical application or implementation of the provisions of legislative acts under their remit. The last ESAs Review resulted in the introduction of Article 16b, which adapted and formalised the ESAs' Q&A processes, and also expressly assigned a role to the European Commission for addressing questions that require the interpretation of Union law. However, these changes have not been helpful in practice. In particular for the questions requiring interpretation of Union law for which the process has proven to be extremely inefficient, slow and cumbersome. The strength of the Q&A tool lies in its efficiency, as the importance of timely responses is critical in avoiding divergent or fragmented supervisory, market and industry practices. Therefore, Article 16b of the ESMA Regulation should be reassessed to determine if the underlying objectives of the Q&A tool are being met.

## **II. Considering the merits of EU level direct supervision**

Since its early years, ESMA has established itself as a credible and effective risk-based and data-driven supervisor. This strong reputation is primarily built on ESMA's experience as a direct supervisor and enforcer of EU Credit Rating Agencies and Trade Repositories. ESMA's supervisory responsibilities have since expanded, with the most notable new responsibilities over EU entities in recent years coming in relation to data service providers, critical benchmarks, securitisation repositories and securities financing transactions. Likewise, ESMA's supervisory and monitoring responsibilities over certain non-EU entities has also expanded during this time. ESMA now has supervisory powers over non-EU CCPs and non-EU benchmarks. Depending on when, and to whom, an equivalence decision for the provision of investment services by non-EU firms may be granted, ESMA will also have new monitoring powers over non-EU investment firms.

For many of those new direct supervision responsibilities, it is too early to meaningfully assess the impact of the changes. This is because most of the powers for supervising these entities have only recently, or have not yet fully, taken effect. Nonetheless, the creation of a supervisory regime at EU level for these types of EU entities was an important step.

In ESMA's [response to the last ESAs Review in 2017](#), it outlined some criteria which could also be considered fulfilled in this respect. For example, these entities operate with a strong cross-border dimension across the EU and would therefore present a high risk of regulatory arbitrage. In addition, ESMA was able to capably build expertise centrally for these new areas

and thus bring efficiency gains for both NCAs and market participants. It should be noted that these existing criteria could be further considered and complemented, as the CMU evolves and market developments give rise to new risks or issues at global, national or EU level.

ESMA believes that, where the activity of certain sectors is orientated to domestic EU markets, the best outcomes can be achieved if supervision and enforcement is performed in closer proximity to those entities, in line with the principles of proportionality and subsidiarity. However, in certain circumstances, and taking into consideration criteria such as those mentioned above, there is merit in exploring the benefits of EU level supervision further. This argument is particularly relevant in instances where non-EU entities can access and provide services across the whole European market. The role of ESMA as a gatekeeper to the EU capital market, overseeing and mitigating the potential risks being imported by non-EU entities, could therefore be enhanced.

### **III. Building ESMA's data capabilities**

The swift and continuous evolution of financial markets and underlying technologies presents new risks to the financial system, which requires regulators and supervisors to enhance their data capabilities to ensure the timely detection and mitigation of those risks. The EU approach to risk-based and data-driven supervision must be founded on robust and accessible high-quality data, that is analysed in a consistent manner.

As outlined in ESMA's Strategic Orientation 2020-22, ESMA's aim is to increasingly become a data hub for EU securities markets, in order to enhance the availability of information at EU level for regulators, investors and market participants. Building on ESMA's experience in providing a centralised solution for MiFIR databases, the expansion of ESMA's data capabilities and responsibilities should be recognised in the ESMA Regulation and in relevant sectoral legislation where common reporting requirements already exist, for example, the Short Selling Regulation, the Market Abuse Regulation, and the Money Market Fund Regulation. In addition, as stated in ESMA's [response to the consultation on the European Single Access Point \(ESAP\)](#), ESMA is ready to take up a central role in setting up and running the ESAP, as suggested by the CMU High Level Forum and the European Parliament.

The centralisation of this role at EU level must bring clear benefits and efficiency gains for both NCAs and reporting entities. The streamlining of reporting and data collection will ultimately result in a cost and burden reduction for NCAs and market participants, whereby centralised databases utilising latest technologies (for example, Regtech and Suptech) and providing mutual access to NCAs (and the public where relevant), would allow for the reduction in duplication of data collection, processing and analysis by multiple authorities. The extensive availability of data in a single digital location, for which the quality of that data is ensured by ESMA with the support of NCAs, enhances the consistency in the interpretation and use of that data, which will lead to a better, common understanding of risks in EU markets. This inextricably links the aims of an EU data hub with ESMA's supervisory convergence objectives. A thorough Cost-Benefit Analysis should be conducted in order to explore these ideas further,

and to determine the most relevant reporting regimes which would benefit from such centralisation.

Finally, building ESMA into a robust and capable EU data hub ultimately requires a substantial amount of effort, and will require ESMA to strengthen its capacity to manage and analyse growing volumes of data. Therefore, the ambition must be supported by the necessary financial and human resources.

#### **IV. Ensuring the single rulebook remains fit-for-purpose**

Continued harmonisation of the single rulebook is an essential pre-requisite to building an effective CMU. Over the last 10 years, significant progress has been achieved on the development of a comprehensive EU single rulebook. However, further reinforcement and harmonisation of the legislative framework in some areas is still needed.

As already highlighted in [ESMA's letter to the European Commission](#) on the improvement of the Transparency Directive after the Wirecard case in March 2021, reducing the options provided for in the directive and addressing divergences in its implementation are essential to further foster supervisory convergence in the area of supervision and enforcement of financial reporting. Similar considerations might apply also to other areas where the single rulebook is based on minimum harmonisation directives that provide a number of different implementation options. This could be achieved through review of specific sectoral legislation, for example, the upcoming reviews of MiFID and UCITS Directive and by ensuring better alignment across different sectoral legislation, both within the securities markets sector (for example, MiFID and UCITS – where ESMA has previously highlighted areas where divergences could be reduced) and across different sectors (for example, in the area of disclosure between insurance and securities sectors).

The COVID crisis illustrated the importance of having an EU regulatory framework that is sufficiently flexible to react in a timely manner to international and EU market developments and has the capability to adjust detailed requirements in an efficient way. Making changes to the single rulebook to address such market developments can currently be onerous, requiring a complete Level 1 legislative process that can often take several years to complete. In particular, when detailed granular technical aspects are governed by Level 1 requirements directly, rather than by supplementary Level 2 requirements in technical standards or delegated acts, necessary regulatory adjustments cannot be made swiftly. When designed and used properly, respecting the principles of proportionality and good governance within the framework for the development of technical standards, the Level 2 process can be more efficient and flexible, to be able to respond to rapidly changing circumstances. Therefore, further consideration should be given to the possibility to delegate technical rulemaking to ESMA via Level 2 mandates, instead of maintaining detailed requirements within the Level 1.

Finally, while the last ESAs review introduced so called 'No-Action letters' (Article 9a of the ESMA Regulation), which can be used under specific circumstances, ESMA's experience in responding to the COVID crisis in 2020 illustrated the limitations to their usage under the

current legal framework. Consequently, ESMA had to use non-prioritisation supervisory statements to achieve the same objectives. Therefore, the creation of a more effective tool that allows ESMA to react to changing market situations or international developments would provide a higher degree of legal certainty to the market. Such a tool would also match better the toolbox of securities regulators in other major jurisdictions that can provide such relief in specific circumstances, in response to sudden market developments or crisis situations.

## **V. Alleviating funding issues**

In the last ESAs Review, while the European Commission had proposed to revise the funding of the ESAs, the ESAs' funding set-up was eventually not adjusted. As a result, ESMA and the NCAs are still faced with significant impediments and burdens in their ability to allocate resources effectively.

The current funding system is particularly inflexible and increasingly complex as regards the financing of direct supervisory mandates. ESMA will soon have eleven different funding sources, which are not fungible, forcing ESMA to effectively manage eleven different budgets prepared on an annual basis. This inflexible and strictly annual budgeting system limits ESMA's capacity to attain economies of scales and prevents ESMA from reallocating resources on the basis of identified risks, which a risk-based supervisor ought to be able to do. This is especially critical for the direct supervision tasks (for example Benchmarks and Securitisation Repositories) which are related to important sectors for the EU financial sector but are characterised by a small number of small entities which struggle to cover the fees for the minimum level of ESMA's direct supervision cost.

Finally, NCAs of varied sizes have been experiencing resource constraints as the financing needs of ESMA has grown in parallel with its responsibilities, and furthermore as their own resource needs increase in line with ESMA's enhanced supervisory convergence efforts. This has been exacerbated by the withdrawal of the UK from the EU, which has increased the individual NCAs' contributions.

While acknowledging that any fundamental change in the financing of the ESAs is unlikely at the current juncture, in the short term, the European Commission should reassess the structure of ESMA's budget and increase the flexibility of appropriations across both time and mandates. Such budgetary flexibility would allow ESMA to focus and prioritise resources in a risk sensitive manner – putting additional emphasis on the most relevant priority areas during a given period, at the same time fully respecting the principle of sound budget management and budget discipline.