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Key Note Address

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Chair

It is a pleasure to be here in Frankfurt at the sixth BWF/ICMA Capital Markets Conference where so many representatives of the financial community are present to get updated on the regulatory changes in European securities markets and to discuss such issues as EMIR.

For many people the lack of transparency – and, by consequence, the lack of understanding on what was going on – in relation to the so called over-the-counter derivatives is the symbol of the urgent need for more adequate regulation after the financial crisis. The EU's response to that concern, EMIR, became quickly an important backbone of European financial markets regulation and for ESMA. Today I would like to guide you through the past, the present and future of EMIR and ESMA.

Considering the audience here today, the focus on EMIR is warranted, however, I will make side-steps covering all main objectives of ESMA. Just to recap, ESMA's objectives include responsibility for:

- creating a Single Rulebook;
- ensuring supervisory convergence in the application of EU securities law across the 28 Member States;
- the supervision of Credit Rating Agencies and Trade Repositories;
- contributing to the financial stability of the EU; and
- investor protection.

These objectives apply to a broad range of financial activities in Europe's securities markets, from trading complex derivatives to high frequency trading, the supervision of key financial market players – such as credit rating agencies and trade repositories – to the management of investment funds and how these are sold to the public. In essence ESMA's work, in all its various guises, contributes to investor protection and stable financial markets in the EU.

While to many people this may seem a daunting task, I believe that ESMA has risen to the

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challenge and has performed well in delivering work of high quality since its inception.

The past

In that context, let me start by going back. Back to September 2009, four years ago. The G20 leaders agreed in Pittsburgh that “all standard OTC derivative contracts should be traded on exchange or electronic trading platforms and, where appropriate, cleared through central counterparties; OTC derivative contracts should be reported to trade repositories.”

One year later, in the autumn of 2010, one year after Pittsburgh and today three years ago. Europe was in still full in discussions, ESMA did not yet exist, and the United States had already adopted the Dodd-Frank Act. The European Parliament, the Council and European Commission were discussing how to set up three European Supervisory Authorities that could become central pillars for maximum harmonization as suggested by Jacques de Larosiere in February 2009. ESMA, the European Securities and Markets Authority, became operational only a few months later on 1 January 2011 together with its sister organizations: the European Banking Authority (EBA) and the European Insurance and Occupational Pensions Authority (EIOPA).

The ambitions were and are high. The European Commission, with Commissioner Michel Barnier at the forefront, is one of the main drivers in the development of European level regulation for the financial markets and European level supervision of credit rating agencies. In addition, this regulation and supervision needed to be closely aligned internationally, based on the G20 commitments.

It is therefore no surprise that ESMA performed well the last two years in connection with both ambitions through the development of the single rulebook and the direct supervision of credit rating agencies. Regarding credit rating agencies, all the important elements required for effective supervision have been established in less than two years. In total 22 CRAs are now supervised by ESMA and we have conducted significant on-site supervisory work on such issues as internal controls in CRAs, their governance and bank rating methodologies. Considering the nature of supervision and the level of confidentiality required, the achievements are less visible to the outside world compared to other ESMA activities. However, seeing the activities close up, I am confident that direct supervision at EU level by ESMA is effective and achieves benefits by improving the functioning of CRAs.

In the past two years, ESMA has contributed extensively to the creation of a single rulebook for the European Union’s securities markets with a large number of draft technical standards, guidelines and technical advice in such areas as OTC derivatives, hedge funds and private equity, UCITS funds, short selling and financial and prospectus information for investors. The new powers provided to the ESAs to achieve maximum harmonization were required to achieve this clear and substantial improvement in the EU single rulebook. This has however taken so much of our work that for some stakeholders ESMA is primarily seen as a regulatory authority. The preparation of 38 draft technical standards making the EMIR-Regulation operational in such a short time frame and in close co-operation with regulators outside the European Union – and the United States in particular – was a real challenge. I think we may say that we have been successful. ESMA delivered the technical standards ready for adoption within seven months after finalizing the European legislation, and just 6 weeks after it entered into force, which has allowed to catch-up most of the delay the EU had compared to the US.

That ESMA was able to speed up its work does not mean that I believe it is a best practice for upcoming legislation. Sufficient time is essential to develop sound and consistent implementing rules. Considering the topics of today's conference, I would like to particularly mention MiFID and MiFIR. The complexity surrounding some of the issues and the fact that some rules will impact markets and instruments that were previously unaffected by regulation and the interplay with Member State legislation clearly ask for due consideration and sufficient time. We will for instance need to properly fine-tune and balance transparency with liquidity when extending pre and post-trade transparency to bond and derivatives markets. We are aware that this will be a delicate issue but are convinced that we will succeed. But to do so, we need the support of stakeholders, your support, ICMA's support – who can provide us with data, expertise and evidence on what is the actual relative liquidity of every corner of those markets and what characteristics should be taken into account when defining that regime.

But ESMA cannot only rely on data provided by market participants. We have therefore increasingly stepped up our research capacity over the last months and our Trends, Risks and Vulnerabilities Report is a good example of that. We closely monitor the EU financial markets, and increase our understanding of specific market phenomena. One example close to today's agenda concerns the frequently debated issue of short selling. We have conducted extensive empirical analyses, also considering the evaluation of the Short Selling Regulation that we delivered earlier this year to the European Commission. We found that hedge funds account for most of the short positions reported on EU equities, with the top ten holders accounting for around 30% of all reported positions. Looking at the temporary short selling restrictions, they appear to have limited impact on markets, both in terms of liquidity and volatility. Finally we found no evidence of a significant deterioration in liquidity in the sovereign CDS market.

In addition to our work on the single rulebook and CRA supervision, we have also undertaken various other activities contributing in our opinion to our main objectives of investor protection and stable financial markets. On the first, I would like to specifically mention the investor warnings that we have published, including one together with EBA on Contracts For Differences (CFDs), and the collection and analysis of data on consumer trends.

The present

It is no surprise that the G20 commitments steered ESMA's agenda in its pioneering years towards the completion of the single rulebook and supervising CRAs. Talking about the strong focus on the G20, there is a concern that I would like to share with you. I believe that we need to ensure the right balance between regulation and supervision. Regulation is only credible when it is effectively supervised. We cannot have a model where a strong increase in the regulation of financial markets is without an accompanying increase in supervisory activity and the availability of adequate resources to supervise and enforce the new rules.

Over the last years ESMA has built up its capacity as a supervisor and will, without losing the completion of the single rulebook out of sight, increase further its supervisory activities. This concerns both direct supervision and supervisory convergence. Let me explain that a bit more.

Already today ESMA is not only directly supervising credit rating agencies but is, as you will know, also responsible for the registration and direct supervision of trade repositories. Trade repositories are relatively new market infrastructures which, once registered, will play a crucial role in ensuring the transparency of derivatives markets. Under EMIR, counterparties and central counterparties will have to report all the details of their derivatives contracts as well as the modification and termination of these contracts. It is clear that the data gathered on derivatives contracts will play an important role for the supervision and oversight of all regulators.

ESMA opened recently the registration process for trade repositories. This is a challenging process for all of us as these new market infrastructures are often still defining their own business model, elaborating their pricing policy, recruiting their staff, adopting their internal policies and procedures and setting up IT infrastructure.

ESMA is currently assessing the half dozen applications it received so far – often containing thousands of pages. Many of the potential trade repositories are part of existing international market infrastructure groups (such as central depositories for securities, clearing houses and exchanges) which can leverage upon their existing know-how. With the information we have now, and assuming everything goes well at both sides (the applicants and ESMA), we would expect to grant the first registrations in November 2013. It is very likely that it will concern a few trade repositories and all derivative asset classes (commodities, credit, foreign exchange, and interest rates) both exchange-traded and over-the-counter.

This means that the obligatory reporting to trade repositories would start around February 2014 since the legislation foresees a 90 calendar day phase-in between the registration of the repository and the reporting start date. This phase-in should allow counterparties sufficient time to contract with their trade repository and adjust IT systems.

It will be of no surprise that this new reporting will need some adjustments and fine tuning. We are already working closely with the entities that have applied for registration as trade repositories and national competent authorities to ensure that all counterparties know how to report and how to meet the obligations in this respect. We are particularly looking at the consistency in reporting between EMIR and MiFID and the reporting of Exchange Traded Derivatives (ETDs), which needs further clarification. ESMA has been working on both issues and proposed in August 2013 to the European Commission to delay the reporting date for ETDs with one year to January 2015. This delay would give ESMA time to develop guidelines for the reporting of ETDs. However, the European Commission signaled last week that it does not intend to support such a delay. While far from ideal, if the delay is not endorsed by the European Commission, ESMA intends to provide some Questions and Answers on ETD reporting before the start of the reporting obligation.

I think you all will agree with me if I say that EMIR already had an impact on the market and made markets more robust, more transparent and safer. That most of the technical standards have been finalized and published does however not mean that it is time for ESMA to take a rest. No matter how carefully legislation is drafted there will always be questions about its practical application.

ESMA has received more than one thousand questions covering around 50 topics on how to read, how to apply or how to comply with EMIR. We have provided the market and public with responses mainly in the form of three sets of so called Questions and Answers. Getting an answer might in some cases take time, as we need to converge 28 Member States on complex requests, but the market clearly benefits from consistent application throughout the entire European Union. I know that in some cases our answer might not be the one you were hoping for but a converged response holds in my opinion a value on its own.

And that brings me to what we call supervisory convergence. Though more and more securities markets legislation is developed at EU level, its supervision and subsequent enforcement is mainly the task of the national regulators. The uneven supervision and application of EU law across the Member States could however result in regulatory arbitrage within the Internal Market. ESMA will therefore launch new activities in the near future to further strengthen consistency in supervisory outcomes. To improve the organization and governance of our convergence work, we will introduce changes aimed at strengthening our peer review tool with more on-site visits, targeting of topical supervisory matters and more independent assessment teams. Indeed, this means that a group composed of representatives of national competent authorities and ESMA staff will be visiting a selection of national regulators to interview employees but also to review supervisory files.

The future

Let me now have a look at the future without starting to dream. I will talk about the imminent future and things that concern all of us: practice, regulators and legislators.

I am sure that many of you will have heard about the Opinion of the Advocate General before the Court of Justice (ECJ) of the European Union on the Short Selling Regulation and the emergency powers assigned to ESMA. I believe that you, like me, might have some questions on this but you will understand that I will not comment on that. We follow closely the developments in this area but are waiting for the final ECJ decision.

There are however other legal and organizational issues that will require legislators' and regulators' attention. Let me start with the legal instruments that we are using to build the single financial market within the European Union. We need to ask the question whether we have all the legal tools needed for the increased role of the EU in financial market regulation and supervision. Let me explain this a bit more with the example of the clearing and trading obligations. We recently consulted on the preparatory work we are doing for the clearing obligation determinations. Once CCPs get authorized under EMIR, ESMA has to assess whether the over-the-counter products they clear should be mandatorily cleared across the EU. This determination is important to reduce systemic risk.

We should however avoid that CCPs are presented with products with risks they cannot manage properly. When derivatives lose liquidity they cease to be fit for central clearing and trading in a matter of weeks. In those cases, and in order to avoid increasing risks that CCPs cannot longer manage, or to impact liquidity further by forcing trading, regulators need to act swiftly. We currently lack those "express" measures in the EU financial markets, since the full legislative process of technical standards has to be applied.

Adopting mechanisms to suspend temporarily an obligation that could increase risk of reducing them or that would start to run contrary to the objective of a Regulation is a need that the European System of Financial Supervision should get sooner than later if we want EU markets to be properly regulated and supervised.

Another challenge I would like to mention is ESMA's funding, both the level and the model. In terms of staffing we are still a relative small organization and we need to plan carefully the best use of our resources. It is fully understandable and justified that within the current economic environment all public expenditures – including those of EU authorities – should be considered carefully. However, with the current regulatory agenda as it looks, severe cuts would require severe re-prioritization. If you then know that ESMA asked, on the basis of careful considerations, 27 additional staff members to meet its objectives in 2014 but was only allocated 7 additional members of staff in the Commission proposal, you will not be surprised that I am getting worried. ESMA has already indicated to the European Parliament and the Council that a substantial increase in resources is necessary to fulfill the EMIR requirements. If those resources are not granted, ESMA will have to reschedule its priorities including not doing some of its envisaged tasks.

And that brings me to my concerns on the funding model. The way we are now funded appears to have become an important problem for the development of ESMA. The current model where National Competent Authorities partly fund the ESAs implies that more funding for the EU supervisors means less funding for the national supervisor. This results in tensions as it is inconsistent with the current regulatory reform agenda which requires the strengthening of regulation and supervision both at EU and national level.

Possible solutions to consider here are decreasing the level funding by NCAs and increasing funding from the EU budget, or from market participants. On the latter, while we are already partly funded by market participants, not all ESMA activities directly related to market participants are yet funded by them. To give an example, this could be the case where an infrastructure requests an ESMA decision that will allow it to operate in the EU single market. For instance, recognition of foreign infrastructures could be paid by the CCPs when applying to operate in the EU market, instead of the European taxpayers.

Ladies and gentlemen, I am coming to the end of my speech. The implementation of EMIR has kept all of us – the financial community, the legislators, ESMA – busy and will continue to do so. I am sure that MiFID 2 and MIFIR will do so as well. I am however convinced that the different initiatives at global, European and national level will enhance investor protection and make financial markets more transparent, safer and well-functioning. And that is the most important.

Thank you for your support, input and for your attention. Thank you.