

SMSG contribution to the ESFS Consultation

An SMSG review of the ESA's including a self-assessment

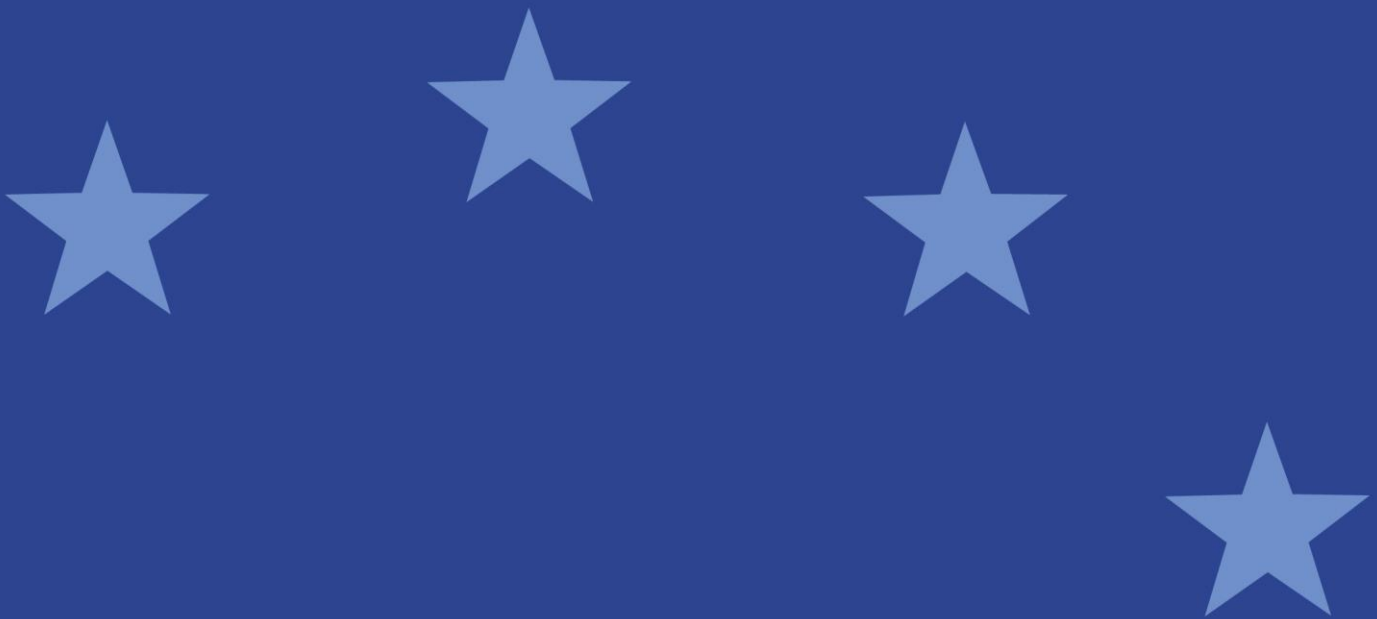


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I. Executive Summary

The SMSG take the opportunity in the following to comment on the review of the European Supervisory Authorities (according to art. 81 of the ESAs Regulations). We make short and long term proposals referred in general to all the ESAs; only in some cases we refer to ESMA. Finally we enclose a self-assessment of our SMSG group.

II. ESAs review: a list of proposals from the SMSG

The three Regulations establishing the European Supervisory Authorities (ESAs) request the European Commission in art. 81 to subject the three Authorities to a general review every three years (the first one will be published by January 2nd, 2014). Among other things the review should also “examine whether:

- (a) it is appropriate to continue separate supervision of banking, insurance, occupational pensions, securities and financial markets;
- (b) it is appropriate to undertake prudential supervision and supervise the conduct of business separately or by the same supervisor;
- (c) it is appropriate to simplify and reinforce the architecture of the European System of Financial Supervision (ESFS) in order to increase the coherence between the macro and the micro levels and between the ESAs;
- (d) the evolution of the ESFS is consistent with that of the global evolution.

In the following document we outline some short-term proposals on the micro organization of ESAs, and some long-term proposals on the governance of the ESAs and a simplification of the structure of the ESAs. The document is structured as follows:

SHORT TERM PROPOSALS:

1. ESMA’s objectives
2. Scope of some ESMA activities: Regulatory and Implementing Technical Standards (RTS and ITS), breach of Union law and settlement of disagreements
3. ESMA’s powers with respect to investor and consumer protection
4. The peer review
5. Emergency situations
6. Fiscal safeguard clauses
7. ESMA support to SMSG

LONG TERM PROPOSALS:

8. Corporate governance of the ESAs
9. Direct supervisory powers
10. Supervisory architecture: from three to two ESAs?
11. ESAs financing
12. SMSG evaluation of ESMA work (attach report by other subgroup)

We focus in the proposals on ESMA even if many of them deal with all the ESAs.

Our overall evaluation on the functioning of ESMA is positive, given also the resource given and the constraints often imposed by the Level 1 players (EU Commission, Parliament and Council). Also the interaction with stakeholders (including with the SMSG) and the consultation process have been quite effective: areas of improvements are possible on bilateral engagement¹, consultation process².

SHORT TERM PROPOSALS

1.1. ESMA's objectives

According to (Article 1 (5), ESMA' overall objective is to protect the public interest. The wording of paragraph (5) focuses primarily on stability and effectiveness of the financial system. Article 1 (5) subsequently lists ESMA's overall objectives³. The group suggests to change the order of these

¹ Bilateral engagement is essential as it allows regulators to source good intelligence and markets expertise and it also allows a wider pool of thoughts to be provided as not all firms will engage with industry bodies on all issues.

² Short implementation timelines (outside of ESMA's control) and lack of resources have made the development of level 2 and level 3 measures complicated and challenging for the industry e.g EMIR where industry is still waiting for clarity on a number of implementation issues (via 'FAQs'). This is delaying the implementation programmes of many firms and increases the likelihood that firms will not meet implementation deadlines. While this issue is being raised with the EC and the EP separately, ESMA can still improve its own process by conducting more early engagement with stakeholder groups and market participants both before the publication of a consultation exercise and after the closure of a consultation – this allows better consideration of possible key challenges that could be expedited for discussion between ESMA, CAs and industry.

It is also unrealistic to completely rely on market participants to conduct market wide impact assessments during an open consultation to prove the unintended and detrimental market impacts from possible requirements - the onus needs to be on the regulators as they have access to market-wide information (e.g. transaction reports, order book data, mandatory requests to regulated firms etc) and generally will have significantly more time to complete this analysis but market participants and SMSG should always be available to provide technical markets expertise to ESMA.

Finally, where legislation contains an obligation for the EC or ESMA to conduct equivalence assessments (EMIR, SSR, MiFID), those assessments must be conducted in a timely fashion so that foreign market participants may ensure that they can fulfil their regulatory obligations and continue to do business in the region particularly as the EU is a global market. A number of equivalence assessments have been delayed or are behind schedule in key dossiers.

³ 5. The objective of the Authority shall be to protect the public interest by contributing to the short, medium and long-term stability and effectiveness of the financial system, for the Union economy, its citizens and businesses. The Authority shall contribute to:

- (a) improving the functioning of the internal market, including in particular a sound, effective and consistent level of regulation and supervision,
- (b) ensuring the integrity, transparency, efficiency and orderly functioning of financial markets,
- (c) strengthening international supervisory coordination,

objectives in order to give better visibility to ESMA's role in enhancing consumer and investor protection.

1.2 Scope of some ESMA activities: Regulatory and Implementing Technical Standards (RTS and ITS), breach of Union law and settlement of disagreements

The lack of clarity with respect to the scope requirements which apply to ESMA's activities should be addressed.

In particular, Regulatory and Implementing Technical Standards (RTS and ITS, respectively art. 10 and 15) may not be proposed by ESMA with respect to the topics indicated in ESMA Regulation Article 1(3) (i.e. corporate governance, auditing, and financial reporting or takeovers) because only the topics listed in Article 1(2) are subject to ESMA's power to propose RTS and ITS where the relevant legislative delegation has been conferred by the co-legislators. This is the case even where legislative measures have been adopted in these areas, and the co-legislators could, accordingly, provide for delegations with respect to RTS and ITS adoption if they were so minded; the ESMA Regulation, however, would seem to present an obstacle to the co-legislators so acting. Similar limitations (to art. 1(2)) deals with the scope of ESMA action with respect to breach of Union Law by national competent authorities (art. 17) and settlement of disagreements (art. 19). Symmetric limitations exist for the other ESAs.

Currently, only Article 16 Guidelines and Recommendations or other forms of soft law can be adopted by ESMA in these areas, despite the efficiencies with respect to supervisory convergence which could follow.

We recognize that there are political complexities in changing ESMA's (and other ESAs) scope of activity. There may be resistance, for example, from Member States which have distinct authorities in charge of, for example, corporate governance issues or takeover matters, and which do not confer these functions on the financial markets authority (ie, in the UK, the Takeover Panel and the Financial Reporting Council and in Austria, the Austrian Takeover Commission), given the potential institutional complexities. Nevertheless, it is important to correct this omission for all three ESAs to ensure that their ability to shape supervisory convergence is not inefficiently restricted referring the scope of ESAs activities in art. 10-15-17-19 also to the topics listed in art. 1(3).

1.3 ESMA's powers with respect to investor and consumer protection

ESMA's powers with respect to investor and more generally consumer protection should be improved.

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- (d) preventing regulatory arbitrage and promoting equal conditions of competition,
 - (e) ensuring the taking of investment and other risks are appropriately regulated and supervised, and
 - (f) enhancing customer protection.

Pending the required delegation in a legislative measure, the ESMA Regulation Article 9(5) power with respect to product intervention cannot be used by ESMA (or the other ESAs as well). ESMA does not accordingly have, at the moment (pending the outcome of the MiFID II/MiFIR negotiations) any power to ban any product, or to suspend its distribution. We are of the view that such a power is important and should be conferred on ESMA.

We also suggest the language of the Article 9(5) enabling power be refined. Although the title of Article 9 refers to “*tasks related to consumer protection*”, the Article 9(5) product intervention powers as currently drafted cannot be activated for consumer and investor protection reasons, but can only be used where so required by “*the orderly functioning and integrity of financial markets or the stability ... of the financial system*”. Financial stability is a different goal than consumer protection and should not control the application of these powers. This is all the more the case as we understand the MiFID II/MiFIR proposals are likely to provide for product intervention powers for ESMA where so required on investor protection grounds. The Article 9(5) language should accordingly be corrected to refer to investor protection.

On consumer trends as mandated by Article 9.1 (a), while ESMA has recently (2013) published its first “Trends Risks and Vulnerabilities” report, hardly anything is mentioned therein on consumer trends.⁴

The power given to ESMA to investigate alleged breaches or non-application of EU law (ESMA Regulation, Article 17) has not been used to date by ESMA or – to our knowledge – by the two other ESAs. The SMSG has made a request in this regard to ESMA, but this request has remained inconclusive as of today (see the SMSG own initiative paper on its own self-assessment in the context of the ESAs Review). This issue may be related to the issue of the ESAs’ governance raised below (Para. 7), as it may be challenging for the Authority to launch an investigation against one or several of its own board members.

1.4 The peer review

The peer review foreseen in ESMA Regulation Article 30 is very important, particularly as it can be made public and ‘peer pressure’/ ‘name and shame’ dynamics can accordingly come into play. But the result of the evaluation process may be disclosed publicly only with the agreement of the competent authority that is the subject of the peer review: this limitation, which was proposed by the Council, is likely to affect negatively the ‘name and shame’ dynamic which is implicit in the public disclosure of bad peer review results.

⁴ ESMA has recently (2013) published its first “Trends Risks and Vulnerabilities” report (attached), but actually only one page addresses retail investors (p 21). Of the two tables presented in this regard one deals with “portfolio returns” but what is shown are actually not retail portfolios but rather capital market indices, i.e. excluding manager’s impact and all fees and expenses supported by retail investors, not mentioning taxes and inflation. In addition showing a 5 Y average seems a rather short timeframe; 10 year and more will be more meaningful for long term and retirement savings. The other table is supposed to reflect retail investor sentiment using a “sentix” index from Datastream: retail investor representatives of the SMSG are not familiar with this index, nor do they know of any individual investor organization which has submitted data.

1.5 Emergency situations

Regarding the power to act in possible emergency situations (ESMA Regulation, Article 18), which possibly may arise all of a sudden, a critical issue is the lack of possibility for an ESA (and the European Systemic Risk Board (ESRB)) to declare the existence of an emergency: the ESA should rather ‘issue a confidential information to the Council ... The Council shall then assess the need for a meeting’ and then inform the Commission and EU Parliament (Art 18). While this cumbersome process may be appropriate for the evaluation of a structural macro-systemic emergency, it is obviously incompatible with the timing of a micro-emergency situation which may require ESMA, for example, to decide on a Sunday night to suspend trading on certain classes of financial instrument or to limit short selling.

1.6 Fiscal safeguard clauses

Regarding the fiscal safeguard clauses (ESMA Regulation, Article 38), the ESAs shall ensure that no decision adopted in the case of an emergency situation and settlement of disagreements impinges in any way on the fiscal responsibilities of Member States: the concept of ‘fiscal responsibility’, seems vague and potentially too extensive, thus it could generate controversies. We appreciate the sensitivities associated with the allocation and location of fiscal responsibility for decisions taken by ESMA; however, we recommend that consideration be given to the exact nature of the circumstances which allow Member States to disregard and ultimately veto action by ESMA. Furthermore, in the case of ESMA, the typical decisions in case of an emergency situation are likely to relate to the suspension of trading or to short selling; the fiscal implications of these decisions are not likely to be material and thus we recommend that these decisions be excluded from Article 38.

1.7 ESMA support to SMSG

A possible revision deals with art. 37 of ESAs Regulations which do not explicitly foresee for a secretarial support to the work of the SMSG. In spite of that, ESMA provided on a voluntary basis part time resources which dedicated a great effort in assisting the Group: SMSG benefited from it. At this point, though, SMSG suggests the Regulation requests ESMA to provide for full-time dedicated resources to assist SMSG in all its work.

LONG TERM PROPOSALS

1.8 Corporate governance of the ESAs

The main threat to the ESAs’ efficiency relates to their governance. Today, the Board of supervisors and the Management Board are composed of national competent authorities (plus the Chairman and some non-voting members). This kind of composition does not necessarily guarantee the efficiency of ESAs decisions, or ensure the requisite degree of independence, as it embeds the interests of national authorities. This governance may be a factor which makes it more difficult to take action in sensitive areas, particularly with respect to Article 17 enforcement

action. The mandatory review of ESA includes in fact (article 81-1-a-ii): “the impartiality, objectivity and autonomy of the authority”.

When the ECB was created, the choice was made to add six ‘other’ members to the Governors of Central Banks in the Governing Board and in the General Council: the six independent members, appointed by the European Council, constitute the executive board of the ECB.

The SMSG thinks that a similar choice should be made for the ESAs⁵. The Management Board should be composed of six independent and highly-qualified individuals, including the Chairman, appointed by qualified majority of the Council and a non-binding opinion of the European Parliament. The Board of Supervisors should be composed of the head of the national competent authorities plus the 6 members of the Management Board⁶. This new framework would lead to more effective ESA governance, and may overcome the natural resistance of some national competent authorities to promote, through a central body, convergence in regulation and supervision - particularly given the radically different powers which the ESA can exercise as compared to the precursor Level 3 Committees.

Furthermore, members of the Supervisory Board should be appointed in the first instance with different mandates (50% for three years; and 50% members, including the chairman, for six years) in order to have *de facto* a staggered and more independent board. The ESA Chairman should also have a casting vote both in the Management Board and in the Board of Supervisors⁷.

1.9 Direct supervisory powers

Regarding direct supervisory powers on entities with EU-wide reach or economic activities with EU-wide reach (as was originally foreseen for all the ESAs in the Commission proposal (Proposal, Article 6(3)), only ESMA was conferred with these powers, with respect to rating agencies initially and trade repositories subsequently. ESMA has also been conferred with direct intervention powers with respect to short selling.

It is our view that ESMA should be conferred with a wider range of direct supervisory powers where such a transfer of function brings material supervisory efficiencies. ESMA could accordingly be conferred with supervisory competence with respect to systemically important financial institutions (SIFIs) where a clear case has been made, market infrastructures such as trading platforms, central securities depositories, or index providers. The principle of direct supervision by ESMA has already been conceded. ESMA has also been empowered to engage in a range of operational supervisory convergence tasks, including with respect to information gathering (ESMA Regulation, Articles 21-35). At the same time, ESMA should be given additional powers or responsibilities in a progressive way because significantly extending its responsibilities in such a new organisation greatly increases the risk of regulatory failure. It is also unrealistic to expect ESMA can handle any additional and significant increase in responsibilities simply by an imme-

⁵ A similar view has been expressed by Jacques de Larosière at the Public hearing on Financial Supervision in the EU, Brussels, 24 May 2013.

⁶ The Board of Supervisors should be attended, as non-voting members, by the representatives of the Commission, the ESRB, the other ESAs and the chairman of the banking supervisory Board of the ECB.

⁷ In any case the voting status of the Chairman should be changed. The Chairman currently cannot exercise a vote on the Supervisory Board although the Chairman can vote in the Management Board; this asymmetry should be corrected.

diate increase in resources (many things can take years to develop especially in new organisations e.g. back office/IT functions, learning and development of its staff etc).

A future step (and real milestone) would be to attribute supervisory and non-exclusive competence on all entities with EU-wide reach in order to have a truly European System of Financial ‘Supervisors’.

The Group appreciates that a reform of this nature represents a very significant change to financial market governance in the EU, and that the location of fiscal responsibility, and compliance with the European Court’s *Meroni* doctrine with respect to which powers can be transferred to EU agencies, must be carefully considered. It also understands that the conferral of direct supervisory power on the European Central Bank (ECB) under the Single Supervisory Mechanism (SSM) is taking place within a distinct legal framework, reflecting the ECB’s particular legal status under the Treaty. It considers, however, that given that ESMA has shown itself to be a capable supervisor with respect to rating agencies, given the pan-EU systemic risk that certain cross-border actors can generate, and given that the ESA review provides the opportunity to engage in ‘blue-sky’ thinking, that more consideration should be given to how such a transfer of competence might be achieved. Consideration could, for example, be given to whether, given the increasing demands of EU financial market governance, the ESAs should be constituted as EU bodies under the Treaties (necessitating a Treaty amendment).

1.10 Supervisory architecture: from three to two ESAs?

In each country, financial markets regulation has been affected by the structure and the evolution of the domestic financial system as well as by the legal system in place. The different objectives of regulation, the different markets, and intermediaries have been assigned to one or more authorities.

Financial regulation aims to correct market imperfections and unfair distribution of the resources, while pursuing four general objectives: macro-stability of the system, micro-stability of the intermediaries, market transparency and investor protection, and, last but not least, efficiency.

In order to pursue these four objectives, there is neither a single theoretical model nor just one practical approach to the regulation and supervision of financial markets. Pros and cons have been extensively discussed by many studies and significant differences are found in the literature in terms of both definition and classification of regulatory models and techniques. And it is difficult to observe in reality the adoption of regulatory schemes that are fully consistent with one theoretical model.

We think that the appropriate solution for EU financial system governance is the ‘twin-peaks model’ which was also envisaged by de Larosière Report, according to which the regulatory framework should evolve ‘towards a system which would rely on only two Authorities: The first would be responsible for banking and insurance issues, as well as any other issue which is relevant for financial stability (e.g. systemically important hedge funds, systemically important financial infrastructures). The second Authority would be responsible for conduct of business and market issues, across the three main financial sectors. Combining banking and insurance supervisory issues in the same Authority could result in more effective supervision of financial conglomerates and contribute to a simplification of the current extremely complex institutional landscape’ (de Larosière Report, point 216, p. 58).

Our proposal assigns the distinct objectives of prudential regulation and conduct regulation (which would encompass consumer protection and the remaining market regulation elements not covered by prudential regulation) to two new ESAs (which would replace the current 3 ESAs): the micro stability for all entities, where needed, based in London, and the conduct regulation for all entities based in Paris.

1.11 ESAs financing

A further topic deals with the funding of ESAs. If the function of ESAs increases, the budget of the ESAs needs to be strengthened, without harming its independence.

1.12 Role of ESMA in relations with third countries

We support that ESMA receive more powers and competences in relation with third countries. This would be in line with the development of the single Rulebook for the development of which ESMA plays a major role. It is important that ESMA be associated by the European Commission to international negotiations, be empowered in directives and regulations to negotiate with third countries regulators either in its own name or in the name of national regulators (MoU), and to participate in the recognition of third country standards.

As a consequence, we support the view expressed in the March 2013 FSAP of the IMF on the European Union, and more precisely on ESMA⁸, that :

"In the medium term, it would be worth exploring whether further centralization of supervisory functions in ESMA is desirable. There are a few areas where such centralization would be desirable (below). (...)

Facilitating cooperation in connection with third country regimes. Given the global nature of financial services, global regulatory convergence is key. Regulatory convergence does not necessarily mean that all countries should have the same regulation rather more and more the trend is to go toward mutual reliance. In this context, ESMA could play a role in helping to set up these systems of mutual reliance (for example, through the determination whether the frameworks are “equivalent” enough or facilitating the execution of MoUs) ».

⁸ European Union: Publication of Financial Sector Assessment Program Documentation—Technical Note on European Securities and Markets Authority, March 2013 IMF Country Report No. 13/69, Point 101, page 30.



III. SMSG self-assessment report

2.1 Executive Summary

The conclusions of the SMSG on its self-assessment are that overall the Group has functioned well and has been an active contributor to the work of ESMA. This has manifested itself in both engaged discussions on current market developments, in 14 public opinions, advices and reports as well as some self-initiative reports.

The SMSG further believes that the composition of the Group, where the professional experiences of the members cover several areas of the financial services sector, and the team spirit in which it has operated, has been an important and contributing factor.

In the below the SMSG sets out the role of the SMSG, analyses its composition, its achievements, its effectiveness and remaining challenges with a view of how the SMSG can continue to provide ESMA with the best value added.

2.2 Outline of ESMA SMSG Self-Assessment

2.2.1 What is our role?

- a. Our audience: ESMA; above all we are a source of internal support
- b. ‘Involvement’ in a broad sense (not just consultations)
- c. An independent representative of stakeholders way
- d. Timing: Early/‘upstream’ - for provision of better value-added to ESMA
- e. Level: More high level, less technical
- f. Requests to investigate breaches of EU Law
- g. Scope: Proactive; own initiative also possible, but targeted to be of use to ESMA
- h. Support accountability: challenge ESMA in an effective and constructive manner

2.2.2 Who are we and how have we worked?

- a. Diversity: collective diversity of professional experiences from different sectors/fields
- b. Independence: Each member acting in a personal capacity
- c. ‘Team Spirit’: Acting collegially and constructively

2.2.3 Summary of what we have done

- a. Rules and procedures / establishing good governance
- b. Advice:
 - i. In response to ESMA’s requests
 - ii. Own initiative



- c. Requests to investigate potential breaches of cases of non-implementation of EU Law (Article 17(2) of REGULATION (EU) No 1095/2010 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL)

2.2.4 How effective have we been?

- a. Where we have made a difference
- b. What areas have we not covered?
- c. Interaction with other groups

2.2.5 What do we need in order to be able to fulfil this role in the future?

- a. Objective: To reinforce our current role, not to deviate from it radically
- b. Relationship with ESMA
 - i. Must continue to have feedback from ESMA on what advice is/is not followed
 - ii. Must retain a role of acting on own initiatives
- c. Administrative support: Significantly more needed to support the Group's effectiveness
- d. Continuity/length of mandate:
 - i. Introducing the principle of rolling mandates of 5 years recommended; half of the group renewed at a time
 - ii. At end-2013, we recommend that approx. 50% of the current members are retained (those willing to stay) and renewed for another 2.5 years, while new members are appointed to make up for the other half, with the intention of keeping them for 5 years
- e. Composition: As presently, relevance of background to be supplemented by diversity
- f. Rules and procedures: Successors of current SMSG encouraged to endorse them
- g. Visibility/communication: We would like to work with ESMA on how to make the Group publicly more visible thus adding to the value it provides to ESMA
- h. Funding of expenses and compensation:
 - i. Overall
 - ii. Specific for non-industry members.

2.3 Detailed views

2.3.1 What is our role?

- Recital 48 and Article 37(1) of REGULATION No 1095/2010 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL, that establishes ESMA (ESMA Regulation) clearly states that the SMSG is of service to ESMA to facilitate consultations with stakeholders and express opinions before the adoption of draft regulation or implementing technical standards, guidelines and recommendations. Therefore the SMSG is above all a source of internal support to ESMA. It is also provided that the Group should work as an interface with other user groups. Although ESMA is the addressee of the SMSG's work, its opinions and advices shall



be made public by ESMA to inform the debate on financial market regulation generally.

- The involvement of SMSG should not be limited to consultations. It is supposed to advise on future public consultations and as the representative of stakeholders in a broad sense to facilitate the consultation of others. Subjects to be submitted to SMSG by ESMA are not limited to the ones which ESMA will submit to public consultations but include the full scope of ESMA activities.
- The SMSG should be involved at an early stage of the process. Given the extensive expertise of its members and the fact that they are subject to confidentiality with regard to their activities for the SMSG, it is in the best interest of ESMA to seek advice from the SMSG on subjects before they are submitted to the ESMA Board of Supervisors. This gives ESMA an initial consolidated opinion of market stakeholders.
- Given the profile and diversity of the SMSG, the Group believes that it should focus more on high level subjects and less on technical details. Some members are certainly qualified to assess detailed rules; whereas others, who have no background in finance, may not be able to comment on technical details, whilst having an opinion on a high level.
- Article 17(2) of ESMA Regulation⁹ also provides that the SMSG is one of the institutions that can request ESMA to investigate the alleged breach or non-application of Union law.
- It is important that the SMSG is able to make its own initiative on subjects that it thinks are of importance to ESMA. As financial market professionals, but also consumers, savers, entrepreneurs, etc. SMSG members bring together not only a broad experience of capital markets but also of the interaction between the capital markets, the investors and the issuers. As a permanent witness of the financial markets and the “real economy”, SMSG can act as early warning to ESMA.
- The SMSG also fulfils an accountability function. ESMA exercises a wide range of powers over the financial markets and its legitimacy must be supported by a strong accountability structure. The SMSG forms part of this structure by challenging ESMA in a constructive and effective manner.

2.3.2 Who are we and how have we worked?

a. Diversity: collective diversity of professional experiences from different sectors/fields

- Recital 48 of ESMA Regulation states that “for reasons of efficiency, a Securities and Markets Stakeholder Group should be used for that purpose, and should represent, in balanced proportions, financial market participants, small and medium-sized enterprises (SMEs), academics and consumers and other retail users of financial services”.
- The Group noted that the SMSG is formed of 6 groups i.e. “Financial Markets Participants”, “Users of Financial Services”, “Representatives of Financial Services

⁹ « Upon a request from one or more competent authorities, the European Parliament, the Council, the Commission or the Securities and Markets Stakeholder Group, or on its own initiative, and after having informed the competent authority concerned, the Authority may investigate the alleged breach or non-application of Union law”



Employees”, “Consumers”, “Small and Medium Size Enterprises”, and “ Academics”.

- When the Group was set up, a number of complaints were filed as some stakeholders felt that they were under-represented. Given the diversity, competence and independence of the members, members believe that they were able to take into account and reflect in their advice the views of most parts of the capital market participants.
 - The Group also noted that in several cases the professional experiences of the members cover several areas of the financial services sector including their experience as investors and consumers which give them a wider view of the subjects under discussion. This should be considered as a plus.
 - It was also necessary for all sub-working groups to ensure that they were well balanced in terms of representation. This has at times been challenging in particular for more technical issues like EMIR, where we could not involve any consumer/retail user representatives. This is because there are few of them (six), and they do not always have the technical support and resources from their own organizations that some other members have.
- b. Independence:** Members are asked to and do serve in a personal capacity. It is key for ESMA that the opinions expressed by the members reflect only their experience and personal opinions. However, inadequate support to the SMSG and its working groups may lead to conflicts of interests.
- c. ‘Team Spirit’:** One characteristic of the SMSG as of today is the team spirit which underpins its work. This team spirit has allowed the SMSG to work cooperatively and productively, seeking consensus whilst allowing all opinions to be expressed freely.

2.3.3 Summary of what we have done

a. Rules and procedures / establishing good governance

- The Group spent quite some time in the beginning on rules and procedures and on the election of the chair and the vice-chairs. The Group considers that the time was well spent and that it has contributed to the efficient functioning of the SMSG.
- Some rules have been more difficult to follow. In particular it has sometimes been difficult to keep the deadlines (i.e. minimum time required for approval and sending of documents). However members of the Group agreed to handle the rules flexibly when necessary. ‘Learning by doing’ has proved effective.

b. Advice:

- i. In response to ESMA**
- ii. Own initiative Reports**

Since its launch, the Group has produced 14 public opinions, advice and reports over only 1.5 years of effective activity. The Group has also delivered a number of informal feedback documents to ESMA. More detail about these activities is provided in the SMSG Annual Report 2011-2012. The Group’s ambition is to deliver advice at the earliest upstream stage possible and to focus on strategic issues. This means that the SMSG has tried to get involved at an early stage, often by responding to “discussion papers” rather than by tak-



ing part in ESMA's later Public Consultations on standards or guidelines. In this context, the Group welcomes the fact that ESMA is developing and formalizing its feedback on Group advice. In addition to its advice to ESMA, the Group also started working on a number of own initiatives outside of ESMA's Annual Work Programme. In this context, it set up specialized working groups which examine the impact of regulation on the access of SMEs to capital markets, on Investor Protection and on Credit Rating Agencies.

Following discussions with the Board of Supervisors, the Group set up two horizontal work-streams on covering investor protection and SMEs access to capital market funding. The aim is to analyse the impact of any Level II measures on investor protection and SMEs. The Group published its SME report in 2012.

c. Requests to investigate potential breaches of cases of non-implementation of EU Law (article 17(2) of ESMA Regulation)

In November 2011¹⁰, the SMSG asked ESMA to investigate a potential case of non-implementation of EU law regarding the lack of distribution of index ETFs to retail investors in Europe. As of today, this initiative remains inconclusive. The provisions of article 17 of the ESAs Regulations are a challenge as – to our knowledge – none of the ESAs has made any use of it to this date (see the SMSG own initiative paper on the review of the ESAs for more analysis of this issue).

2.3.4 How effective have we been?

a. Where we have made a difference

Generally, the group considers that it was able to respond to ESMA's request for advice in a timely and comprehensive manner. In addition to the Group's advice, members believe that the high-level exchanges with ESMA management and Board of Supervisors on recent market developments were particularly fruitful.

b. What areas have we not covered

SMSG has made use of its power to request for investigation by ESMA of potential breaches of EU law under Article 17 of ESMA Regulation in the distribution of ETFs.

c. Interaction with other groups

SMSG should work as an interface with other user groups in the financial services area established by the Commission (recital 48 of ESMA Regulation). While initial contacts were taken with the EBA and EIOPA Stakeholders Groups, these have until now (due to work loads and lack of resources) not really materialised themselves into on-going working relationships.

2.3.5 What do we need in order to continue to be able to fulfil this role in the future?

a. Objective: To reinforce our current role, not to deviate from it radically

¹⁰ In its advice on UCITS Exchange-traded funds dated 29/11/2012, the SMSG wrote: "ETFs are a low cost and straightforward investment proposition for investors, and as such, ESMA should investigate how to make indexed ETFs more offered to retail investors... This points to potential problems regarding ETF distribution."



b. Relationship with ESMA

i. Must continue to have feedback from ESMA on what advice is/is not followed

The effectiveness of the Group's advice is related to the extent to which it is taken into account by ESMA. ESMA has increasingly provided feedback on what was taken into account and what was not and explaining why. This process could be more systematic and further improved for example in an annual assessment that SMSG could include in its annual report.

ii. Must retain a role of acting on own initiatives

The Group's broad experience and diversity is a particularly useful asset especially when trying to take a cross-sectoral and holistic view of matters in order to assess side-effects and unintended consequences as was manifested in the SME Financing Report.

c. Administrative support: more needed

- According to article 37(4) of ESMA Regulation, the Authority shall ensure adequate secretarial support for the Securities and Markets Stakeholder Group.
- Going forward, ESMA will need to dedicate more resources to provide proper administrative support to our work. Resources currently dedicated to the SMSG are very insufficient considering the amount of work being undertaken.
- The Group understands that the lack of resources dedicated to the SMSG is linked to the relative scarcity of resources available for the functioning of the Authority itself. However, the Group considers that this situation risks damaging the quality of the advice given and its usefulness to ESMA, and undermines the SMSG in carrying out the tasks with which it has been charged under the ESMA Regulation.
- In particular, the work of the Chair is particularly demanding and in the case of the SMSG would not have been possible without the active support of the Vice-Chairs.
- Furthermore there is a clear conflict of interest if members and especially the Chair and vice-Chairs have to use employees of their organization to do work for the SMSG. The same applies for members who take on the responsibility of chairing a working group

d. Continuity/length of mandate:

- i. Introducing the principle of rolling mandates of 5 years recommended with half of the group being renewed at each time.**
- ii. At end-2013, we recommend to keep approx. 50% of the current members (those willing to stay) and renew them for another 2.5 years, while hiring the other half with the intention of keeping them for 5 years.**
- The 2.5 years mandate is considered by the Group as too short to be fully efficient compared to the time it takes to complete a project under the EU working process. Some members considered that a 5 year non-renewable mandate would be better as it would match that of the president of the Authority.
- The present mandate of the members of the SMSG will expire on December 31, 2013, end of the first 2.5 years period.
- There was unanimous agreement amongst the members of the Group that the collective end of mandate was a sub-optimal solution. It took the Group approxi-



mately 6 months to be up and running (including the drafting and completion of internal rules). After an initial starting phase, the efficiency of the Group increased substantially. Since most of the comments and the drafting of papers is done by mail and in phone conferences it is important that the members know each other well. Starting again with a completely newly formed group will consequently cost time and deprive ESMA from very useful experience considering the substantial expertise around the table.

- Members therefore suggest that there should be a more fluid rotation of the members of the Group. One proposal was to follow the French AMF procedure where the mandate of the Board members lasts 5 years but with a renewal of half of the group every 2.5 years. For the initial term, 50% of group would start with a 2.5 year term. Renewable mandates could come from the alternate group although this could also be counter-productive since there is a relatively big turn-over in the securities industry. It's good to bring in new talents and to rejuvenate the pool of expertise.

e. Composition: As presently: relevance of background to be supplemented by diversity:

The Group believes that the selection of members should be based on several factors including the balance between the various stakeholders, diversity of experiences and countries of origin. It is the combination of the diversified background that allows the fair representation of the various stakeholders as well as the team spirit.

f. Rules and procedures

- i. We recommend that the group who will follow this acting SMSG takes over our rules and procedures
- ii. A few remaining issues (e.g. quorum) may need to be clarified.

In cases where the currently stipulated quorum at meetings has not been met due to last minute cancellations etc., the SMSG has, rather than postponing decisions as time seldom allows for this, recirculated the voted papers to the full group immediately after the meeting to allow non-present members to voice any objections they may have. A non-reply has been considered as an approval. An alternative to this pragmatic approach, for consideration by the next SMSG, would be to lower the numbers present required for a quorum.

g. Visibility/communication: We would like to work with ESMA on how to make the Group publicly more visible

A number of members considered that despite the excellent work undertaken by the Group, the opinions lacked visibility. It is rather difficult to find the SMSG when consulting ESMA's website. A number of proposals were made to give the Group's work better visibility including adding ESMA SMSG advices into the ESMA 'News' section on the website and allowing for RSS feeds. Another proposal to enhance the visibility would be to encourage ESMA to answer our papers i.e. give us more detailed feedback. One member considered that the format of our advice was a bit boring and needed some 'prepping'! Interested parties could also be provided with the option of subscribing to the SMSG public papers and opinions via a website "click" option.



In addition the Group believes that it is important that preferably ESMA communicates SMSG's analyses and recommendations to EU policy-makers (the European Commission, Council and Parliament) in order to better inform them and potentially enable SMSG's findings to have more impact on level 1 text.

h. Funding of expenses and compensation:

- i. Overall: Contradiction between Art 37(3) which requests that “the Board of Supervisors shall, to the extent possible, ensure an appropriate geographical ... balance and representation of stakeholders across the Union” and ESMA’s policy to reimburse travelling expense only to academics and consumer representatives.**
- ii. Specific for non-industry members:** Current remuneration levels offered by ESMA are not adequate (art 37(4) of ESMA Regulation) and below the current practice of other EU organizations.

Annex to the Self-Assessment Report

Job description - Secretary to the ESMA SMSG

Principal function

1. Support the SMSG Steering Committee i.e. Chair and Vice-Chair(s)
 - Prepare Steering committee meetings
 - Support Chair in chairing meetings
 - Report back to members, ensure follow-up
 - Support SMSG in developing Annual Programme
 - Support SMSG in drafting Annual Report
2. Organise SMSG meetings
 - Prepare agenda and meeting documents in line with Internal Rules
 - Draft summary of minutes
 - Ensure swift and transparent follow-up
3. Organize joint meetings of the Board of Supervisors and the Securities and Markets Stakeholder Group
 - Prepare agenda and meeting documents in line with internal rules
 - Help SMSG to bring all questions of relevance to the attention of the Board of Supervisors
 - Prepare meeting documents
 - Draft summary of minutes
 - Ensure swift and transparent follow-up
4. Organize conference calls and meetings of the ESMA SMSG sub-working groups
 - Prepare agenda
 - Prepare list of participants
 - Provide meeting documents
 - Ensure swift and transparent follow-up (collect input and recirculate amended draft)
5. Ensure proper visibility of SMSG
Coordinate of SMSG public image (website, documents, publications, data)