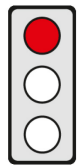


KEY ISSUES

Objective of the Regulation: The responsibilities and powers of ESMA are to be significantly widened.

Affected parties: ESMA, investment funds, investment firms, trading venues, data reporting services, benchmark administrators and contributors, issuers, investors.



Pro: –

Contra: (1) A centralised EU securities supervision of EuVECA, EuSEF and ELTIF funds by ESMA is not useful unless the applicable law is also harmonised.

(2) Centralised supervision of securities prospectuses by ESMA is disproportionate with respect to the Member States. ESMA only needs to take on a purely coordinating function such as by providing guidelines for the national supervisory authorities.

The most important passages in the text are indicated by a line in the margin.

CONTENT

Title

Proposal COM(2017) 536 of 20 September 2017 for a **Regulation** of the European Parliament and of the Council amending Regulations

- (EU) No. 1095/2010 establishing the **European Securities and Markets Authority (ESMA)**,
- (EU) No. 345/2013 on **European venture capital funds (EuVECA)**,
- (EU) No. 346/2013 on **European social entrepreneurship funds (EuSEF)**,
- (EU) No. 600/2014 on **markets in financial instruments (MiFIR)**,
- (EU) 2015/760 on **European long-term investment funds (ELTIF)**,
- (EU) 2016/1011 on **indices** used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds, and
- (EU) 2017/1129 on the **prospectus** to be published when securities are offered to the public or admitted to trading on a regulated market

Brief Summary

Note: Unless otherwise indicated, article numbers refer to the Proposal for a Regulation COM(2017) 536.

► Background

- The Regulation amends the provisions on the three European Supervisory Authorities (ESAs). These are:
 - The European Securities and Markets Authority (ESMA, in Paris; this [cepPolicyBrief](#)),
 - the European Supervisory Authority for Insurance (EIOPA, in Frankfurt; see [cepPolicyBrief](#)), and
 - the European Banking Authority (EBA, currently still in London, soon to move to Paris; see [cepPolicyBrief](#)).
- By amending other Regulations, it accords ESMA additional supervisory powers.

► Provisions similar to those of the EBA and EIOPA Regulations

- The ESMA provisions on governance, on the relationship with national supervisory authorities, on the withdrawal of guidelines, on the financing of the agency, on stress tests, on establishing a Union supervisory handbook, on consumer protection, on the consideration of ecological, social and technological factors and those relating to governance, as well as provisions on the tasks in relation to third countries, are similar to the provisions applicable to the EBA and EIOPA (cf. therefore [cepPolicyBrief](#) on the EBA and [cepPolicyBrief](#) on EIOPA).

► Main difference to the EBA Regulation and EIOPA Regulation

- Unlike the EBA and EIOPA, ESMA is given direct supervisory powers; specifically those applicable to certain investment funds, securities prospectuses and benchmarks as well as to data reporting services. ESMA is also granted product intervention and investigatory powers.
- ESMA's Executive Board will propose decisions to the Board of Supervisors in this regard. The Board of Supervisors decides by way of a simple majority. Each national supervisor has one vote. [Art. 47 (4) in conjunction with Art. 44 (1) ESMA Regulation]

► **Authorisation and supervision of selected investment funds**

Exclusive competence of ESMA

- In future, it will be ESMA – rather than the national supervisory authorities (NSAs) – that is responsible for the authorisation and supervision of [Art. 4, 5 and 7]
 - European long-term investment funds (ELTIF) [Art. 5 et seq. ELTIF Regulation (EU) 2015/760, see [cepPolicyBrief](#)],
 - European venture capital funds (EuVECA) [Art. 14 et seq. EuVECA Regulation (EU) No. 345/2013] and
 - European social entrepreneurship funds (EuSEF) [Art. 15 et seq. EuSEF Regulation (EU) No. 2015/460].

Joint competence of ESMA and the national supervisory authorities

- ESMA is jointly responsible together with the NSAs for the supervision of alternative investment fund (AIF) managers authorised by the national authorities under the AIFM Directive [Directive 2011/61/EU, see [cepPolicyBrief](#)], that have fund assets of € 500 million and above, where the managers in addition to the AIF also operate a EuVECA or EuSEF [Art. 4 (1); Art. 14a EuVECA Regulation and Art. 15a EuSEF Regulation].
- ESMA only supervises compliance with requirements relevant to EuVECA and EuSEF pursuant to
 - EuVECA and EuSEF Regulations and
 - national transposition provisions for the AIFM Directive.

► **Regulatory and implementing standards under ESMA**

- ESMA develops uniform technical regulatory and implementing standards for a whole range of provisions contained in the EuVECA, EuSEF and ELTIF Regulations [e.g. Art. 7 (3) EuSEF Regulation].

► **ESMA powers regarding prospectuses**

- In future, it will be ESMA – rather than the NSAs – that is responsible for approving prospectuses drawn up in the EU which [Art. 31a Prospectus Regulation (EU) 2017/1129]
 - are necessary for the admission of non-equity securities - i.e. securities that are not shares - to a regulated market to which only qualified investors have access,
 - relate to asset backed securities or “ABS”,
 - relate to securities issued by property companies, mineral companies, research companies or shipping companies.
- Prospectuses that have been approved by an authority in a third country are deemed to have been approved EU-wide if the Commission has classified the legal position in that country as “equivalent”. ESMA works together with the authorities in the third country and is officially responsible for supervision in the EU [Art. 29 Prospectus Regulation].
- ESMA is responsible for notifying the competent supervisory authorities in the host Member State of the said securities if they are to be offered there or admitted to trading on a regulated market (“pass notification”) [Art. 31a Prospectus Regulation].
- In future, ESMA “shall have the power” to exercise control over the advertising of securities whose prospectuses it has itself approved. At the request of the competent authority, ESMA shall exercise control over “all or some categories” of these securities. [Art. 22 (6a) Prospectus Regulation]

► **ESMA powers regarding benchmark administrators and contributors**

- “Benchmarks” are indices used to determine inter alia the value of a financial instrument. “Contributors” are persons who provide data for determining benchmarks. “Administrators” control the provision of benchmarks. [Art. 3 (1) paras. (3), (6) and (9) Benchmark Regulation (EU) 2016/1011]
- “Critical benchmarks” are those from administrators in the EU which are used as a reference for financial instruments or -contracts [Art. 20 Benchmark Regulation]
 - with a value of at least € 500 billion;
 - with low relevance insofar as there are no “market-led substitutes” for the values.
 The Commission decides on classification by way of implementing acts and this is examined by the Member States [Art. 20 (5) Benchmark Regulation].
- In future, it will be ESMA – instead of the NSAs – that is responsible for the supervision of [Art. 40 Benchmark Regulation]
 - administrators of critical benchmarks,
 - administrators based in third countries who provide benchmarks in the EU,
 - contributors to critical benchmarks and
 - contributors who provide input data to administrators based in third countries who provide benchmarks in the EU.

► **ESMA powers regarding data reporting services**

- In future, it will be ESMA – rather than the NSAs – that is responsible for the authorisation and supervision of “data reporting services” [Art. 27a et seq. MiFIR Regulation (EU) 600/2014].

- “Data reporting services” are persons who [Art. 2 (1) paras. 34–36 and 36a MiFIR-Regulation]
 - publish trading information on behalf of investment firms (“approved publication arrangements” or “APA”) or
 - obtain trading information from stock exchanges and APAs and consolidate it in a “continuous electronic real-time data stream” (“consolidated tape provider” or “CTP”) or
 - report details of transactions to ESMA or the responsible supervisory authorities on behalf of investment firms (“approved reporting mechanism” or “ARM”).
- **Additional product intervention and investigatory powers of ESMA**
 - In future, ESMA and the NSAs will be able to prohibit or restrict certain financial activities as well as the marketing, distribution and sale of financial instruments by managers of UCITS investment funds (see [cepPolicyBrief](#)) and alternative investment funds (AIF, see [cepPolicyBrief](#)), such as where this is necessary a.o. for the protection of investors or for market stability [Art. 1 (5a) MiFIR Regulation]. Until now, they could only do this in the case of banks and investment firms [Art. 1 (5a) MiFIR Regulation].
 - ESMA has extensive investigatory powers, e.g. to issue a summons or carry out on-site searches [Art. 19a–21c EuVECA Regulation, Art. 20a–22c EuSEF Regulation, Art. 34–35g ELTIF Regulation, Art. 48a–48l Benchmark Regulation, Art. 43b–43l Prospectus Regulation].

Statement on Subsidiarity by the Commission

Amendment of the ESMA Regulation and the other Regulations serves the “consistent functioning” of the internal market. This requires EU action.

Policy Context

The Commission held a consultation in spring 2017 on the activities of ESAs.

Legislative Procedure

20 September 2017	Adoption by the Commission
Open	Adoption by the European Parliament and the Council, publication in the Official Journal of the European Union, entry into force

Options for Influencing the Political Process

Directorates General:	DG Financial Stability, Financial Services and Capital Markets Union
Committees of the European Parliament:	Economic and Monetary Affairs (leading), Rapporteur: Ohmar Karas (EVP Group, AT) and Pervenche Berès (S&D Group, FR)
Federal Ministries:	Finance
Committees of the German Bundestag:	Finance Committee
Decision-making mode in the Council:	Qualified majority (acceptance by 55% of Member States which make up 65% of the EU population)

Formalities

Competence:	Art. 114 TFEU (Internal Market)
Form of legislative competence:	Shared competence [Art. 4 (2) AEUV]
Procedure:	Art. 294 TFEU (ordinary legislative procedure)

ASSESSMENT

Economic Impact Assessment

As with banking supervision, which was extensively centralised at the European Central Bank (ECB) in the wake of the banking crisis, the Commission - now in light of Brexit - proposes partial centralisation of securities supervision in the EU. There are however major differences between the two cases: Firstly, common banking supervision is limited to the eurozone whereas ESMA’s powers will apply throughout the EU. Secondly, the banking sector is characterised by a pronounced level of cross-border interconnection between the banks as well as large-scale interdependence between banks and governments. This interdependence has cast doubt over the creditworthiness of several eurozone countries and led to the establishment of bailout funds - in particular the ESM for governments and the SRF for banks. As these bailout funds ultimately involve a mutualisation of risk and even of costs, centralised banking supervision by the ECB was introduced in order to minimise moral-hazard risks arising from the opportunistic behaviour of national bank supervisors.

None of this provides grounds for centralising securities supervision in the EU. Firstly, cross-border interconnection in the securities sector is not comparable to that of the banking sector and secondly there is no large-scale interdependence between investment firms and eurozone governments.

Theoretically, centralised securities supervision may result in the uniform treatment of similar cases EU wide, which prevents regulatory arbitrage and distortions of competition. The requirement for this, however, is EU-wide harmonisation of the regulatory provisions applied by the central authority. **Standard EU securities supervision for EuVECA, EuSEF and ELTIF funds by ESMA is not useful unless the applicable law is also harmonised.**

Only a few provisions are harmonised by the EuVECA, EuSEF and ELTIF Regulations. Many provisions are still regulated at national level and will only be harmonised with the Regulation - by way of ESMA's technical standards. Firstly, the fact that supervision is to be centralised prior to further harmonisation gives cause for concern. Secondly, the supervisor should not at the same time set the supervision rules. In the case of alternative investment funds, there is also a risk of conflicts of jurisdiction with the national supervisory authorities (NSAs). It is in any case doubtful whether ESMA is technically better qualified than the respective national authority to apply the various national implementation rules of the AIFM Directive.

Prospectus rules are extensively harmonised - even if a range of national regulatory exceptions still exist. **Centralised approval of prospectuses by ESMA is not necessary because closer coordination of the activities of national authorities is also possible** without centralised supervision, such as **by way of ESMA guidelines**. ESMA can already take action against breaches of law by the NSAs. It is odd that prospectuses from third countries with an equivalent supervisory system can be used without further assessment in the EU. Why authorities in third countries are considered capable of appropriate supervision, when national authorities in the EU are not, is unclear.

Centralised, uniform EU supervision of critical benchmark administrators and contributors and of data reporting services is quite understandable in view of the cross-border relevance of these services. The existing national supervision has not however resulted in any serious problems which might need remedying. In view of ESMA's ability to take action against breaches of the law by NSAs and to settle conflicts between the NSAs with binding effect, centralised supervision by ESMA is not superior to national supervision.

Legal Assessment

Legislative Competency

The measures serve the functioning of the single financial services market. The relevant legislative basis is therefore Art. 114 TFEU, as also confirmed by the CJEU (Case No. C-270/12, para. 102 et seq.).

Subsidiarity.

Unproblematic.

Proportionality with respect to Member States

Centralised supervision of securities prospectuses by ESMA is disproportionate with respect to the Member States. Although it is generally appropriate for preventing significant national differences in dealing with prospectus approval, this aim can also be achieved by way of a less intrusive encroachment upon the sovereignty of Member States. **ESMA only needs to take on a purely coordinating function such as by providing guidelines for the national supervisory authorities.**

Compatibility with EU Law in other Respects

The Regulation is contrary to the case law of the European Court of Justice (CJEU) as established in the Meroni case (CJEU, case no. C-9/56). A delegation of power by the EU legislator in favour of ESMA, as an organ which does not belong to an EU institution, is only permissible where the associated executive powers are clearly defined. In a later judgement (CJEU, case no. C-270/12, para. 45-53) the CJEU clarified that the delegated powers must not include any margin of discretion. It is however permitted for the organ to weigh up conflicting public interests insofar as there is an appropriate system "of procedural and substantive limitations" to prevent any shifting of responsibility for strategic political decisions. This is not the case here because, in the context of the supervision of funds via EuVECA and EuSEF, ESMA has the power - previously held by the national authorities - to demand more own funds in the event of a "significant change of business activity" (Art. 10 (3) and (4) EuVECA and Art. 11 (3) and (4) EuSEF). This provision permits ESMA to make policy decisions because no regulatory or implementing standards exist or are planned which restrict ESMA's margin for discretion. Thus there are no sufficient "procedural and substantive limitations".

Impact on German Law

The German Capital Investment Code ("KAGB") will have to be amended.

Conclusion

Standard EU securities supervision for EuVECA, EuSEF and ELTIF funds by ESMA will not work unless the applicable law is also harmonised. Centralised supervision of securities prospectuses by ESMA is disproportionate with respect to the Member States; ESMA only needs to take on a purely coordinating function such as by providing guidelines for the national supervisory authorities.