



DIRECTORATE-GENERAL FOR INTERNAL POLICIES

**POLICY DEPARTMENT**  
ECONOMIC AND SCIENTIFIC POLICY **A**

**Economic and Monetary Affairs**

Employment and Social Affairs

Environment, Public Health and Food Safety

Industry, Research and Energy

Internal Market and Consumer Protection

**Review of the New European System of  
Financial Supervision (ESFS)**

**Part 1:  
The Work of the European Supervisory  
Authorities (EBA, EIOPA and ESMA)**

**STUDY**







**DIRECTORATE GENERAL FOR INTERNAL POLICIES**  
**POLICY DEPARTMENT A: ECONOMIC AND SCIENTIFIC POLICY**

# **Review of the New European System of Financial Supervision (ESFS)**

## **PART 1: THE WORK OF THE EUROPEAN SUPERVISORY AUTHORITIES (EBA, EIOPA AND ESMA) – THE ESFS'S MICRO-PRUDENTIAL PILLAR**

### **Abstract**

Responding to the challenges of the financial crisis, the European Union (EU) adopted a new financial supervisory framework: the European System of Financial Supervision (ESFS) in 2010. Its new European Supervisory Authorities (ESAs) were established in the beginning of 2011 and are due to be reviewed by the European Commission by January 2014. This report reviews and assesses for the European Parliament the performance of the ESAs. It reasons that the ESAs have been established successfully but need a stronger foundation, in particular enhanced governance when taking decisions on supervisory consistency across the EU. A key conclusion is that the benefits of legal and regulatory harmonisation (Single Rulebook) will be lost without consistent implementation and application. Finally, the report contains recommendations to improve the ESAs' effectiveness and efficiency.

This document was requested by the European Parliament's Committee on Economic and Monetary Affairs.

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## LIST OF ABBREVIATIONS

<b>AIFMD</b>	Alternative Investment Fund Managers Directive 2011/61/EU
<b>AML</b>	Anti-Money Laundering Directive 2005/60/EC
<b>BAC</b>	Banking Advisory Committee
<b>BCBS</b>	Basel Committee on Banking Supervision
<b>BRRD</b>	Bank Recovery and Resolution Directive (proposal COM(2012)280)
<b>BSG</b>	Banking Stakeholder Group
<b>CEBS</b>	Committee of European Banking Supervisors
<b>CEIOPS</b>	Committee of European Insurance and Occupational Pension Supervisors
<b>CEOS</b>	Conditions of employment of other servants of the European Communities
<b>CESR</b>	Committee of European Securities Regulators
<b>Council</b>	Council of the European Union
<b>CCP</b>	Central Counterparty
<b>CDS</b>	Credit Default Swap
<b>CRA</b>	Credit Rating Agency (see also CRA Regulation (EC) 1060/2009)
<b>CPSS</b>	Committee on Payment and Settlement Systems
<b>CRD</b>	Capital Requirements Directive (CRD IV; 2013/36/EU)
<b>CRR</b>	Capital Requirements Regulation (EU) 575/2013
<b>CSD</b>	Central Securities Depository
<b>DG Markt</b>	Internal Market and Services Directorate General (Commission)
<b>DGS</b>	Deposit Guarantee Scheme
<b>EBA</b>	European Banking Authority
<b>ECB</b>	European Central Bank
<b>ECOFIN</b>	Economic and Financial Affairs Council (Council configuration)
<b>ECON</b>	Committee on Economic and Monetary Affairs (Committee of the European Parliament)
<b>EEA</b>	European Economic Area
<b>EFC</b>	Economic and Financial Committee
<b>EIOPA</b>	European Insurance and Occupational Pensions Authority
<b>EMIR</b>	European Market Infrastructure Regulation (EU) 648/2012
<b>ESA</b>	European Supervisory Authority
<b>ESFS</b>	European System of Financial Supervision
<b>ESMA</b>	European Securities and Markets Authority
<b>ESRB</b>	European Systemic Risk Board
<b>EU</b>	European Union
<b>FICOD</b>	Financial Conglomerates Directive 2002/87/EC
<b>FSAP</b>	Financial Sector Assessment Program (IMF)

<b>FSB</b>	Financial Stability Board
<b>IAIS</b>	International Association of Insurance Supervisors
<b>ICAAP</b>	Internal Capital Adequacy Assessment Process (part of CRD 'Pillar II')
<b>IFRS</b>	International Financial Reporting Standard
<b>IMD</b>	Insurance Mediation Directive 2002/92/EC (proposed amendment COM(2012)360)
<b>IMF</b>	International Monetary Fund
<b>IOSCO</b>	International Organisation of Securities Commissions
<b>IOPS</b>	International Organisation of Pension Supervisors
<b>IRSG</b>	Insurance and Reinsurance Stakeholder Group
<b>IORP</b>	Institutions for Occupational Retirement Provision (Directive 2003/41/EC)
<b>ITS</b>	Implementing Technical Standard
<b>JEGR</b>	Joint Expert Group on Reconciliation
<b>LTGA</b>	Long-Term Guarantees Assessment
<b>MAD</b>	Market Abuse Directive
<b>MiFID</b>	Markets in Financial Instruments Directive (2004/39/EC, proposed Recast COM(2011)656)
<b>MiFIR</b>	Markets in Financial Instruments Regulation (proposal COM(2011)652)
<b>NAIC</b>	National Association of Insurance Commissioners
<b>NCA</b>	National Competent Authority
<b>OJ</b>	Official Journal of the European Union
<b>OPSG</b>	Occupational Pensions Stakeholder Group
<b>OTC</b>	Over-The-Counter (Derivatives)
<b>PRIPs</b>	Packaged Retail Investment Products (proposed regulation COM(2012)352 - also called Key Information Document, <b>KID</b> )
<b>Q&amp;A</b>	Questions and Answers
<b>QMV</b>	Qualified Majority Voting (Article 16(4) TEU; Article 3 Protocol (No 36) on transitional provisions based on the rules applicable in the Council)
<b>RTS</b>	Regulatory Technical Standard
<b>SME</b>	Small and Medium-sized Enterprise
<b>SMSG</b>	Securities and Markets Stakeholder Group
<b>SRM</b>	Single Resolution Mechanism (proposed regulation COM(2013)520)
<b>SSM</b>	Single Supervisory Mechanism (proposed ECB regulation COM(2012)511 and amendment EBA Regulation COM(2012)512)
<b>SREP</b>	Supervisory Review and Evaluation Process (part of CRD 'Pillar II')
<b>UCITS</b>	Undertakings for Collective Investment in Transferable Securities
<b>XBRL</b>	eXtensible Business Reporting Language

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## SPECIFICATIONS FOR LOT 1 (ESAs STUDY) - EXCERPT

### 3. LOT 1 - SPECIFICATIONS: SUPERVISORY REVIEW: THE WORK OF THE EUROPEAN SUPERVISORY AUTHORITIES (EBA, EIOPA AND ESMA) - THE EFSF'S MICRO-PRUDENTIAL PILLAR

#### 3.1 BACKGROUND

The financial crisis in 2007 and 2008 revealed important shortcomings in financial supervision, both in particular cases and in relation to the financial system as a whole. Nationally based supervisory models have lagged behind globalisation of financial markets and players and the integrated and interconnected reality of European financial markets, in which many financial institutions operate across borders. The crisis also exposed shortcomings in the areas of cooperation, coordination, consistent application of EU legal framework and trust between national supervisors. Therefore, based on the analysis and proposals of the de Larosière report,<sup>1</sup> and in order to achieve a well-functioning and coherent European System of Financial Supervision (ESFS) with a view to better protecting the citizen, fighting systemic risk and rebuilding trust in the financial system,

- a European Systemic Risk Board (ESRB)

and three new European Supervisory Authorities (ESAs) have been created:

- the European Banking Authority (EBA);
- the European Insurance and Occupational Pensions Authority (EIOPA);
- the European Securities and Market Authority (ESMA).

On 16 December 2010, the three regulations establishing EBA, EIOPA, and ESMA entered into force:

- Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC Regulation (EC) No. 1093/2010 of the European Parliament and of the Council of 24 November 2010;<sup>2</sup>
- Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC;<sup>3</sup>
- Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC.<sup>4</sup>

These three independent EU authorities were established as of 1 January 2011. However, they could build on the foundations of their respective predecessors, i.e. the former Committee of European Banking Supervisors (CEBS), Committee of Insurance and Occupational Pension Supervisors (CEIOPS) and the Committee of European Securities Regulators (CESR). The aim was to bring together the actors of financial supervision at national level and at the level of the Union to act as a network.

**N.B.** At the same time and within the same context, the following regulations and a directive were published:

- Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board;<sup>5</sup>
- Council Regulation (EU) No 1096/2010 of 17 November 2010 conferring specific tasks upon the European Central Bank concerning the functioning of the European Systemic Risk Board;<sup>6</sup>
- Directive 2010/78/EU of the European Parliament and of the Council of 24 November 2010 amending Directives 98/26/EC, 2002/87/EC, 2003/6/EC, 2003/41/EC, 2003/71/EC, 2004/39/EC, 2004/109/EC, 2005/60/EC, 2006/48/EC, 2006/49/EC and 2009/65/EC in respect of the powers of the

<sup>1</sup> Report of 25 February 2009, see [http://ec.europa.eu/internal\\_market/finances/docs/de\\_larosiere\\_report\\_en.pdf](http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf).

<sup>2</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:331:0012:0047:EN:PDF>.

<sup>3</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:331:0048:0083:EN:PDF>.

<sup>4</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:331:0084:0119:EN:PDF>.

<sup>5</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:331:0001:0011:EN:PDF>.

<sup>6</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:331:0162:0164:EN:PDF>.

European Supervisory Authority (European Banking Authority), the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority).<sup>7</sup>

### EBA

EBA acts as a hub and spoke network of EU and national bodies safeguarding public values such as the stability of the financial system, the transparency of markets and financial products and the protection of depositors and investors. EBA is an independent authority and has broad competences, including preventing regulatory arbitrage, guaranteeing a level playing field, strengthening international supervisory coordination, promoting supervisory convergence and providing advice to the EU institutions in the areas of banking, payments and e-money regulation as well as on issues related to corporate governance, auditing and financial reporting.

### EIOPA

EIOPA is an independent authority whose main goals are better protecting consumers, rebuilding trust in the financial system, as well as ensuring a high, effective and consistent level of regulation and supervision taking account of the varying interests of all Member States and the different nature of financial institutions. It is also involved in harmonisation and coherent application of rules for financial institutions and markets across the European Union and strengthening oversight of cross-border groups. EIOPA is commissioned to monitor and identify trends, potential risks and vulnerabilities stemming from the micro-prudential level, across borders and across sectors.

### ESMA

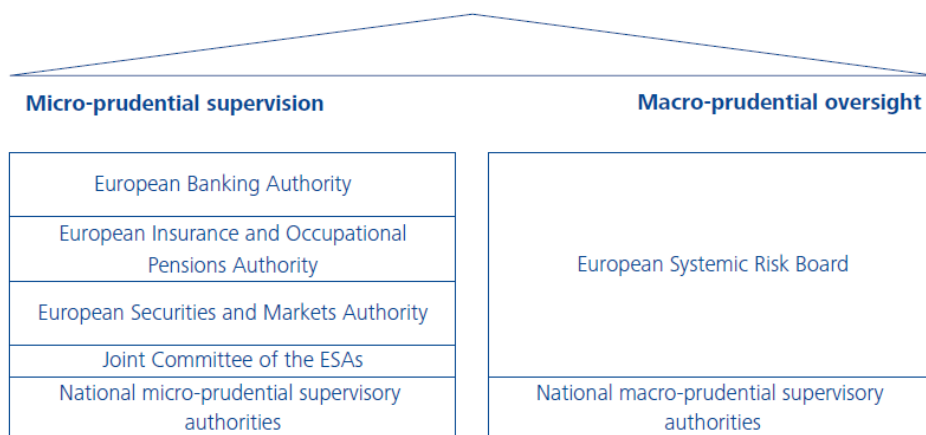
ESMA is an independent authority that contributes to safeguarding the stability of the European Union's financial system by ensuring the integrity, transparency, efficiency and orderly functioning of securities markets, as well as enhancing investor protection. In particular, ESMA fosters supervisory convergence both amongst securities regulators, and across financial sectors by working closely with the other European Supervisory Authorities competent in the field of banking (EBA), and insurance and occupational pensions (EIOPA). ESMA also is responsible for coordinating actions of securities supervisors or adopting emergency measures when a crisis situation arises. In particular, ESMA is also responsible for Credit Rating Agencies active in the EU.

### The ESFS

According to Article 1 of the Regulation (EU) No 1092/2010 the ESRB, the EBA, the EIOPA, the ESMA form together with the Joint Committee of the European Supervisory Authorities (ESAs) and the competent or supervisory authorities in the Member States (as specified in the legislation establishing the three ESAs) the European System of Financial Supervision (ESFS).

Figure 1

#### The European System of Financial Supervision



Source: Annual Report 2011, European Systemic Risk Board

<sup>7</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:331:0120:0161:EN:PDF>.

The three authorities have similar powers and competences in their respective fields. In particular they contribute to the establishment of high-quality common regulatory and supervisory standards and practices, in particular by providing opinions to the Union institutions and by developing guidelines, recommendations, and draft regulatory and implementing technical standards. Furthermore they participate in the consistent application of EU supervisory law and developing a common supervisory culture in the EU. The authorities monitor and assess market developments and cooperate closely with the ESRB. Another task is to foster depositor and investor protection as well as the protection of policy holders, pension scheme members, and beneficiaries. Finally they take over the assignments of the former CEBS, CEIOPS, and CESR.

Article 81 of the three founding regulations<sup>8</sup> calls for a review of the work of the authorities based on a general report drafted by the Commission. This kind of evaluation shall take place every three years; the first report shall be published by 2 January 2014 and forwarded to the European Parliament and the Council. In order to prepare the European Parliament for this review process and the upcoming discussion, the Committee for Economic and Monetary Affairs (ECON) is requesting two studies, namely this one on the work of the ESAs, as well as a twin study on the work of the ESRB.

### 3.2 OBJECTIVE AND DESCRIPTION OF THE STUDY

#### 3.2.1 General context

This study is part of a twin study project to review the establishment and work of the new supervisory architecture. In its macro prudential part, one study will examine the work of the ESRB while **this study** will analyse in detail the work of the **three new European supervisory authorities**. However, already the Larosi re Report states, that '*[m]acro-prudential supervision cannot be meaningful unless it can somehow impact on supervision at the micro-level whilst; micro-prudential supervision cannot effectively safeguard financial stability without adequately taking into account of macro-level developments.*' Consequently the authors of the studies should **work closely together, communicate regularly and share results**.

Both studies are aimed to feed in to the discussions in ECON as well as in the Plenary of the European Parliament. To play an active role in the review process, the European Parliament should be able to base its assessment of the review report on own expertise and data.

<sup>8</sup> See Regulations (EU) No. 1093/2010, No. 1094/2010 and No. 1095/2010 quoted above, in the following named 'founding regulations'.



## EXECUTIVE SUMMARY

**The three European Supervisory Authorities (ESAs), the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA) form - in conjunction with the national supervisory authorities (National Competent Authorities, NCAs) and the European Systemic Risk Board (ESRB) - the new financial supervisory architecture in Europe: the European System of Financial Supervision (ESFS).** The ESFS was developed based on recommendations of the *High Level Group on Financial Supervision* chaired by Jacques de Larosière to address previous shortcomings in the practice of financial supervision and to **enhance cooperation and coordination between NCAs in Member States.** The ESFS came into effect on 1 January 2011. While this study reviews the ESAs, another study on the ESRB has also been carried out for the European Parliament in parallel, entitled '*Review of the New European System of Financial Supervision (ESFS) – The Work of the European Systemic Risk Board – The ESFS's Macro-prudential Pillar.*'

**The study reviews the ESAs by assessing if their establishment has been in line with the ESA Regulations and if their creation and work has delivered the desired results.** To this end, the report assesses the key common features (establishment and internal organisation, governance, institutional profile and positioning, communication and consultation processes) and the key roles the ESAs play (regulatory, supervisory, financial stability, consumer protection; see details on the Assessment Grid in section 1.8).

Less than three years is a short observation period. However, although almost identical Regulations established the ESAs, their scope has evolved very differently. The EBA has had to deal with a severe banking crisis, and its founding legislation has already been modified to take account of the planned Single Supervisory Mechanism (SSM). The EIOPA has been very active but has been hampered in developing the integrated Single Rulebook for insurance by the postponed implementation of the insurance Directive (Solvency II). The scope of the ESMA has been significantly expanded to new areas, including direct EU-wide supervision of credit rating agencies (CRAs); this direct supervisory power is unique among the ESAs.

The main results of the study are as follows:

### **A successful establishment needing stronger foundation in the future:**

**The establishment process has occurred while the ESAs had to meet very material demands using limited resources.** They have successfully built well-functioning organisations. Although they have benefited from significant budget increases, the current resource model is reaching its limits. The European Commission's budget is contracting, and some NCAs face acute cost pressures, meaning contributions from these sources cannot increase sufficiently. Therefore, the ESAs should form an independent budget line in the EU budget. Furthermore, the administrative requirements of the EU staff regulations constrained the ESAs' ability to recruit staff and allocate their budgets independently. More resources and flexibility will be required for the ESAs to evolve further as EU authorities. **Despite the challenging context, the ESAs have made good progress towards being EU authorities recognised in their own right by their stakeholders.** They have gained influence within the financial services community and with NCAs.

### **A need for enhanced governance for decisions on supervisory consistency:**

**The development of the 'Single Rulebook', i.e. a harmonised set of rules based on first level directives and regulations supplemented by second level implementing**

**and delegated acts has dominated the ESAs' workload, and consequently their regulatory role has been to the fore at the expense of other responsibilities.** The ESAs' establishment has occurred during a period of rapid and far-reaching change to legislative acts and regulatory standards for the financial sector in the EU and internationally.

**For decisions on regulatory matters, the Board of Supervisors' governance model strikes an effective balance between the need for an EU-wide view of regulatory matters and the desirability of securing national buy-in to the ESFS.** Although national bias of members of the Board of Supervisors has still been a challenge for both, members and the Chairpersons, allowance should be made for the fact that the governance has evolved during a crisis period when divergent national interests have put pressure on cross-border cooperation on regulatory and supervisory matters. Qualified Majority Voting (QMV) rather than simple majority voting has been an important improvement allowing national preferences to be overcome to a certain extent.

**However, the governance model is cumbersome when much time is spent by the Board of Supervisors processing draft Regulatory Technical Standards (RTSs) and draft Implementing Technical Standards (ITSs) at the expense of discussion of substantive regulatory, supervisory, financial stability and consumer protection issues.** More time should be dedicated to key policy and supervisory issues, e.g. by creating a sub-committee of the Board of Supervisors to filter remaining open issues and to prepare regulatory technical decisions to be formally decided by the Board of Supervisors.

**The ESAs were granted a range of powers to ensure supervisory consistency, avoid supervisory arbitrage and create a level playing field, but the intensity of use has varied markedly, with some powers not used at all.** This has been a result of prioritising work on the Single Rulebook and the existence of legal obstacles for using certain powers. The ESAs' governance, which compels them to be reliant on NCA support in a range of areas, also explains their hesitation to use some powers more actively.

**The unanimous view of stakeholders is that the benefits of legal and regulatory harmonisation will be lost without consistent implementation and application across the EU. To achieve more focus on consistent supervision, an Executive Board (replacing the Management Board) composed of the Chairperson and some full-time members should be created.** The members of such an Executive Board would not necessarily need to be selected among active national regulators/supervisors and would have a seat in the Board of Supervisors and a vote on all issues except those requiring QMV (in particular regulatory work leading to binding implementing rules). The Executive Board would perform direct supervisory functions (like the ESMA's for CRAs) as well as all other functions delegated by the Board of Supervisors.

**In order also to allow the ESAs to have more influence in the EU community, to engage with peers and NCAs on an equal footing and gain the necessary independence to set their own priorities and work programmes, the profile of the positions of Chairperson and Executive Director should be enhanced.** The Chairperson should have an administrative ranking at least as high as that of a Director General of the European Commission and the Executive Director with a ranking of at least a Deputy Director General. The role played by the European Commission in the appointment process (see Box 1) of the first Chairpersons and Executive Directors should not be repeated. The Chairperson should be granted a voting right for decisions on supervisory consistency matters. Furthermore, the Chairpersons should be formally invited to ECOFIN meetings at least twice per year to report on their activities and work programme.



**The ESAs' respective Stakeholder Groups are a work in progress and further changes will be needed if they are to provide strategic input to the ESAs and play a more active role in establishing supervisory consistency.** The groups should have a greater role in informing the ESAs' work, and should take a more strategic approach to identifying priorities for the ESAs to address. To do so, there needs to be greater administrative support for members, especially the Chairpersons. The composition of the groups also needs to change. Consumer representation is too low. There is insufficient representation from those involved in financing the real economy, those who have entrepreneurial experience, or those who require access to finance. The seniority of members should also be encouraged.

**The ESAs have gradually increased their participation in international organisations and discussions with third countries, but there needs to be an increased focus on developing these relationships.** To improve the representation of the EU, the ESAs should be encouraged to participate alongside NCAs with the same membership status.

### **A Structured Single Rulebook:**

**There is support from the financial services industry for the ESAs to always measure the impact of their proposed measures on economic growth and job creation in the EU.** ESAs' regulatory activity should create financial markets that favour long-term investment, economic growth and job creation. A '**Think Small First**' principle should be applied when developing new implementing measures (advice on delegated acts, draft RTSs and draft ITSs, guidelines and recommendations) as well as the application of proportionate rules to small and medium-sized market players.

**The ESAs' ability to contribute more effectively to the drafting of implementing measures has been constrained by their absence from the designing of the EU financial services framework.** The ESAs are typically not consulted on the technical content of legislation. Given their expertise, as well as the challenge they have often faced in drafting implementing measures based on general legislative provisions, there is a strong case for involving the ESAs more in legislative work, yet in a way that respects the institutional legislative process. For that purpose, the ESAs should give a formal opinion on proposed legislation within their respective scope of competence.

**More clarity on the structure of the Single Rulebook would enhance predictability.** The EU should make full use of the EU hierarchy of norms. The legislation by co-decision should focus on the key harmonised provisions leaving practical detail to delegated or implementing acts providing for RTSs or ITSs, possibly supplemented by non-binding measures, and allowing national discretions only in very limited specific circumstances that do not hamper the Single Market. A codification to ensure cross-sector and cross-legislation consistency would help avoiding conflicting legislation. Considering the evolution of the structure of the EU legislation and the scope of action of the ESAs this codification could consist of a Prudential Code and a Consumer/Investor Protection Code.

### **A focus on supervisory consistency:**

**The ESAs have not used their supervisory consistency powers to the extent anticipated by stakeholders.** The ESAs have not played a comprehensive role in identifying divergent applications (peer reviews), tracking (no mediations), policing (opinions or recommendations) or enforcing consistent application of EU law by NCAs (no '*breach of Union law*' case identified). Enhancing the ESAs' governance structures would ease the use of certain supervisory consistency powers. The ESAs' peer review model should be developed to become a more Independent Assessment model, such as that of the IMF (FSAP) and inform the deliberations of the Board of Supervisors.

**Legal conditions to act should be clarified or alleviated.** When the powers to ensure more consistent supervision are not used as a result of restrictive interpretation of the provisions of the ESA Regulations, the European Commission should provide clarification about the conditions to be fulfilled to enable their use, including in particular the ability to prohibit certain activities. When limited use results from restrictive legal conditions, the EU legislators should consider making such powers more operational for the benefit of the stability of the EU financial system. This pertains in particular to action in emergency situations and safeguards and powers requiring an enabling sector specific legislation to be activated (double legal basis).

**The ESAs have played an increasingly active coordination role during volatile market periods.** As NCAs have come to see the value of using the ESAs to coordinate responses to firm specific or market problems, it has become easier for the ESAs to fulfil this role. The ESAs have contributed to the identification of systemic risk and vulnerabilities in the Single Market, in particular through their participation in the ESRB.

**The participation of ESA representatives in colleges of supervisors has improved the functioning of colleges, but the colleges have only made limited progress in enhancing supervisory convergence.** The legal basis for the use of colleges should be significantly expanded in the area of securities markets. A more straightforward '*lead supervisor model*' should be extended to the colleges of insurance groups along with the draft recovery and resolution mechanism. To help provide more harmonised operational supervisory responses, issues identified within colleges should be reported more systematically to the Board of Supervisors for action.

**The ESAs' respective records on consumer protection are mixed.** The ESMA and the EIOPA have made the most progress in this area, the EBA the least. While there are good reasons for these differences, there is now a strong case for greater harmonisation in the substance and intensity of their approach in this important area. There is an opportunity for the Joint Committee's Sub-Committee on Consumer Protection and Financial Innovation to play a pivotal role.

**The ESMAs' direct supervision of Credit Rating Agencies (CRAs) has been successful** and could serve as a model for the direct supervision of other highly integrated pan European entities or activities, such as central counterparties (CCPs). However, as discussion on the SSM showed, changing existing supervisory roles from national to EU level will face obstacles.

**The EBA has been able to make more headway in the area of financial stability than the ESMA and the EIOPA due to market demands.** However, the 2011 stress test proved challenging because the EBA was charged with significant responsibility by the Council without obtaining matching resources or powers. It is broadly acknowledged that the EBA coordinated the stress test effectively in very difficult circumstances. The EBA has clearly identified the issues encountered in the stress test and is currently planning for the next test in 2014 taking these lessons into account. The EBA's work on risk weighted assets is considered valuable by NCAs and the industry. It has also made a positive contribution in the area of recovery and resolution.

#### **Specific priorities for EBA, EIOPA and ESMA:**

**Although the SSM's creation alters the ESFS, the EBA will be a key player in a Single Market context.** The granting of banking supervision responsibilities to the ECB alters the EBA's role, and does so in a way which arguably reduces its influence compared to EIOPA and ESMA. However, since the EBA will act as the 'glue' holding together SSM and non-SSM NCAs, it is important that nothing is done to diminish its standing or effectiveness in delivering on its responsibilities. In particular, a clear position on the development of a

single EU-wide '*supervisory handbook*' should be established between the EBA, ECB and non-SSM supervisors.

The opportunity should be taken as soon as possible to **clarify the respective roles and responsibilities of the EBA in an SSM context, including its responsibilities for stress testing**. The effectiveness of inter-institutional relationships, and in turn therefore supervisory co-operation and harmonisation, will depend in part on a shared understanding of each entity's responsibility in the new banking supervisory architecture. For this reason, it would be preferable for the relevant parties to identify and remove any possible ambiguities before the SSM starts.

**Co-legislators should promptly reach agreement on the implementation and application of the Solvency II insurance framework. This will create certainty for the role of EIOPA.** To ensure efficient decisions by the Board of Supervisors and NCAs' adherence to them, the EIOPA should set more clearly the key objectives, consequences, deliverables, means, and steps leading to the smooth implementation of the framework. In particular, to ensure more consistency for internal model validation under Solvency II, the EIOPA should give high priority to a centre of expertise building on the successful experience of NCAs and in close cooperation with NCAs' experts.

**The ESMA should start stress testing and recovery and resolution planning for trading venues and market infrastructures (in particular CCPs).**

**Meaningful cross-sector work along key supervisory objectives:**

**The Joint Committee is seen by the ESAs as a useful mechanism to ensure cross-sectoral consistency and has provided a valuable contribution in establishing common procedures and rules of the ESAs.** However, it would be more beneficial for work to be structured according to key supervisory objectives and be composed of two major Standing Sub-Committees: one devoted to prudential matters (including financial conglomerates) and the other to consumer protection and financial innovation. The ESAs could delegate to such Standing Sub-Committees some tasks for which they have limited resources or difficulties in establishing them as a priority. The Joint Committee could also be responsible for publishing updates on common findings for better outside communication.

**The Joint Board of Appeal has so far published only one decision.** The first decision of the Joint Board of Appeal creates a precedent in favour of a more active stand of the ESAs on supervisory consistence matters (in particular breach of Union law) and clarifies the status of guidelines and recommendations for the interpretation of the scope of EU law provisions.

**Overall, this review concludes that the ESAs have made good progress and it would be premature to consider redesigning fully the ESAs' structure per sector at this point or changing ESAs' geographical locations. There is no failure or compelling evidence for the creation of a single EU authority covering the three sectors.** There are, however, factors pointing towards the desirability of structuring EU legislation and the ESAs' supervisory roles according to two fundamental supervisory objectives: prudential supervision and consumer/investor protection supervision.

**Priority should be on strengthening the ESAs' ability to use their supervisory consistency powers. Therefore, this report contains 73 recommendations to improve the ESAs' effectiveness and efficiency.**

# 1. INTRODUCTION AND BACKGROUND

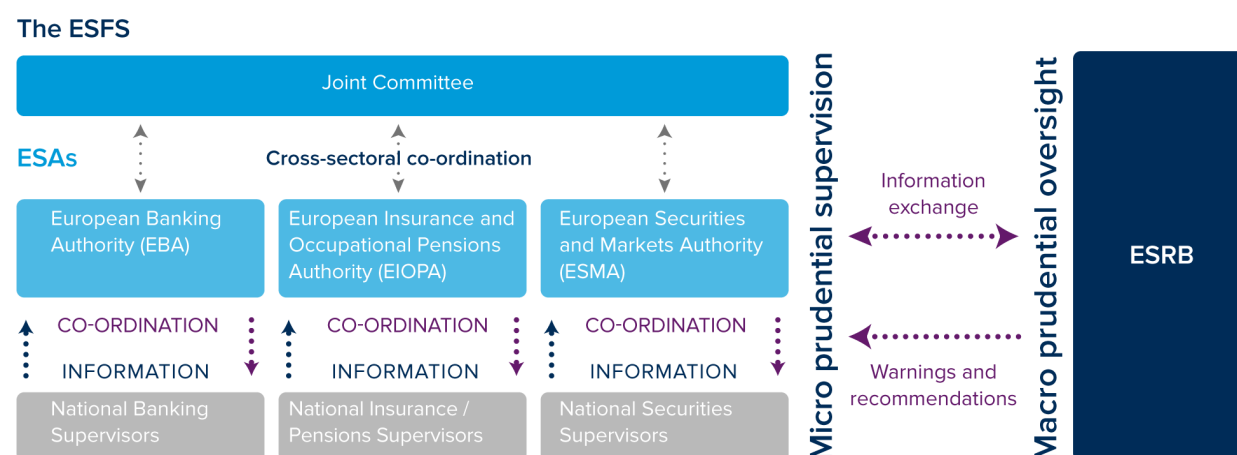
## 1.1. The European System of Financial Supervision (ESFS)

From its onset in 2007, the global financial crisis revealed both gaps in the legislation which governs the financial system and shortcomings in the practice of financial supervision. In the European Union (EU), the crisis additionally highlighted deficiencies in the structures for cross-border crisis resolution; it shed light on the inconsistent application of the EU's legal framework for financial services and it tested supervisory cooperation and coordination between Member States, in some cases affecting the trust between national supervisors.

In order to address these issues and to achieve a more effective system of supervision, a new architecture for European financial supervision was developed based on the recommendations of the 2009 de Larosière Report.<sup>9</sup> This new arrangement, the **European System of Financial Supervision (ESFS)**, was adopted in the form of regulations agreed by the European Parliament and the Council in late 2010<sup>10</sup> establishing:

- the **European Systemic Risk Board (ESRB)** responsible for the macro-prudential oversight of the financial system, focusing on systemic risk;
- three **European Supervisory Authorities (ESAs)** responsible for micro-prudential supervision of financial markets and activities:
  - a) the **European Banking Authority (EBA)**,
  - b) the **European Insurance and Occupational Pensions Authority (EIOPA)**,
  - c) the **European Securities and Market Authority (ESMA)**;
- the **Joint Committee** to foster coordination amongst the three Authorities; and
- with participation of national competent authorities (NCAs) in the three financial sectors.

**Figure 1: Components of the ESFS**



**Source:** Mazars/Oxford Analytica; **Note:** The illustration presents the current structure of the ESFS and does not reflect the introduction of the SSM in the banking sector.

**N.B.** Full details for literature cited as well as for legislative texts, proposals etc. incl. links (where available) are provided in the part 'References' at the end of the study.

<sup>9</sup> The High-Level Group on Financial Supervision in the EU (chaired by J. **de Larosière**), **Report**, 25.2.2009; challenges see Lannoo, K., The road ahead after de Larosière.

<sup>10</sup> **EBA Regulation** (EU) No 1093/2010; **EIOPA Regulation** (EU) 1094/2010; **ESMA Regulation** (EU) 1095/2010, together referred to as the '**ESA Regulations**', as well as **ESRB Regulation** (EU) 1092/2010 and **Specific ECB Tasks Regulation** Council Regulation (EU) 1096/2010.

## 1.2. The ESFS timeline

**Table 1: The ESFS timeline: Key milestones<sup>11</sup>**

Timeline	Milestone
October 2008	The European Parliament called on the European Commission to fundamentally reform the supervisory structure of Level 3 Committees (CEBS, CEIOPS, CESR). <sup>12</sup>
November 2008	The European Commission mandated a high-level group chaired by Jacques de Larosière to make recommendations on how to strengthen European supervisory arrangements with a view to better protecting the citizen and rebuilding trust in the financial system.
February 2009	Publication of the 'de Larosière Report' on financial supervision in the EU setting out a framework for a new regulatory agenda, stronger coordinated supervision and effective crisis management procedures.
May 2009	A conference was held that enabled wide and open discussion on the reform of the European supervisory framework. <sup>13</sup>
September 2009	The European Commission adopted proposals to strengthen financial supervision that would set up the ESFS composed of the ESRB, NCAs and the three ESAs for the banking (EBA), securities and markets (ESMA) and insurance and occupational pensions sectors (EIOPA).
November 2010	The European Parliament and Council adopted the new supervisory framework for financial supervision in Europe.
December 2010	The three founding regulations (ESA Regulations) and the ESRB Regulation were published and entered into force in December 2010.
January 2011	The ESAs started their operations.
June 2011	The adoption of the Alternative Investment Fund Managers Directive (AIFMD) extended the scope of competences of the ESMA to certain tasks regarding alternative investment management.
July 2011	The ESMA became the direct supervisor of Credit Rating Agencies (CRAs). <sup>14</sup>
July 2012	Adoption of the EMIR Regulation (EU) No 648/2012 extended the scope of competences of the ESMA to certain tasks regarding OTC derivatives, central counterparties and (direct supervision of) trade repositories.
September 2012	European Commission proposes to set up a Single Supervisory Mechanism within the ECB and amend the EBA Regulation (see 1.3).
July 2013	European Commission consults (April - July 2013) on the ESFS review. <sup>15</sup>
January / February 2014	European Commission's report on the operation of the ESAs (Article 81 ESA Regulations); European Parliament Report with Recommendations to the European Commission on the ESFS Review (2013/2166(INI)).

<sup>11</sup> See Bartels et al., European Banking and Financial Services Law, p. 61 – 65 for concise history and references.

<sup>12</sup> European Parliament resolution of 9 October 2008 with recommendations to the Commission on Lamfalussy follow-up: future structure of supervision (2008/2148(INI)).

<sup>13</sup> High-Level Conference 'Towards a new supervisory architecture in Europe', Brussels 7 May 2009; documents see [http://ec.europa.eu/internal\\_market/finances/committees/](http://ec.europa.eu/internal_market/finances/committees/).

<sup>14</sup> Regulation (EU) No 513/2011 (CRA II), OJ L 145, 31.5.2011, p. 30, which amends the CRA Regulation 1060/2009/EC.

<sup>15</sup> The contributions received in regard to the consultation are available at [http://ec.europa.eu/internal\\_market/consultations/2013/esfs/contributions\\_en.htm](http://ec.europa.eu/internal_market/consultations/2013/esfs/contributions_en.htm).

### 1.3. New developments: Banking Union and Single Supervisory Mechanism (SSM)

In March 2013 the co-legislators European Parliament and Council agreed on a Regulation amending the EBA Regulation<sup>16</sup> (**EBA amending regulation**) as regards the interaction of the EBA and the European Central Bank's (ECB) prudential supervision powers within the new **Single Supervisory Mechanism (SSM)**.<sup>17</sup> The SSM is a component of the **Banking Union**<sup>18</sup> which will further enhance the supervisory framework in the European banking market. Under the SSM, the ECB will be responsible for specific supervisory tasks related to the financial stability of all euro area banks as well as banks in other (non-euro area) Member States voluntarily joining the SSM. Legislation will be put in place in the coming months which will impact on the work and role of the EBA. This is discussed further throughout this report.

### 1.4. Development of the EU Supervisory Structure - Legal Background and Implications

#### 1.4.1. The Predecessors of the ESAs: Level 3 Committees (CEBS, CEIOPS and CESR)

The predecessors of the ESAs were Level 3 committees: the Committee of European Banking Supervisors (**CEBS**), the Committee of European Insurance and Occupational Pensions Supervisors (**CEIOPS**) and the Committee of European Securities Regulators (**CESR**). The establishment of these committees was already the result of intense discussion and i.a. prepared by the Report of the 'Wise Men Group' chaired by A. Lamfalussy.<sup>19</sup> Besides the aim of developing a more harmonised framework for a Single Market in financial services, a main concern was ensuring more flexible set-up which could act in a faster manner.

#### 1.4.2. Comitology and the new structure of delegated acts, implementing acts and (regulatory and implementing) technical standards, Article 10 - 15 ESA Regulations

The Level 3 Committees were based on **comitology**,<sup>20</sup> a system using delegated powers to the European Commission - which employed committees of different nature - to execute the directives and regulations (Level 1) adopted in co-decision (now ordinary legislative procedure, Article 289 TFEU) by the European Parliament and the Council.

<sup>16</sup> COM(2012)512 final.

<sup>17</sup> The SSM is expected to enter into force on 4 November 2013 after publication of the legal texts end of October 2013; see [http://europa.eu/rapid/press-release\\_MEMO-13-899\\_en.htm?locale=en](http://europa.eu/rapid/press-release_MEMO-13-899_en.htm?locale=en).

<sup>18</sup> See [http://ec.europa.eu/internal\\_market/finances/banking-union/index\\_en.htm](http://ec.europa.eu/internal_market/finances/banking-union/index_en.htm) for more information on the Banking Union.

<sup>19</sup> Committee of Wise Men on the Regulation of European Securities Markets, *Final Report*, Brussels, 15.2.2001; more information on the Lamfalussy process see [http://ec.europa.eu/internal\\_market/securities/lamfalussy/](http://ec.europa.eu/internal_market/securities/lamfalussy/); Alford, D., *The Lamfalussy Process and EU Bank Regulation: Another Step on the road to Pan-European Regulation?*.

<sup>20</sup> For more information on comitology and comitology committees see [http://europa.eu/legislation\\_summaries/glossary/comitology\\_en.htm](http://europa.eu/legislation_summaries/glossary/comitology_en.htm); European Parliament, Legislating more efficiently: questions & answers on new delegated acts, Constitutional affairs, 24.3.2010; <http://www.europarl.europa.eu/sides/getDoc.do?type=IM-PRESS&reference=20100323BKG71187&language=EN>.



Since the Lisbon Treaty entered into force, the legal basis for the new 'ex-comitology' framework is Article 290 TFEU for **delegated acts** and Article 291(2) TFEU for **implementing acts**.<sup>21</sup> Both are 'implementing measures' and non-legislative.

Among the important categories within the financial services legislative framework are **technical standards**. These come in two different formats:

- **Regulatory Technical Standards** - which are delegated acts, Article 290 TFEU;
- **Implementing Technical Standards** - which are implementing acts, Article 291(2) TFEU.

When financial services legislation confers the power to adopt implementing measures, each provision specifies the form it should take: delegated acts, implementing acts, RTSs or ITSs. The process of adoption of delegated acts in the form of RTSs or implementing acts in the form of ITSs is covered in Article 10 to 15 ESA Regulation which oblige the European Commission to justify deviations from the drafts prepared by the ESAs. For the adoption of implementing measures other than RTSs and ITSs, the European Commission may seek advice from the ESAs (in the form of opinions, Article 34(1) ESA Regulations).

#### 1.4.3. ESAs as EU agencies - legal framework and limitations of EU agencies

The 'promotion' from comitology committees (which had no binding powers and had to decide in unanimity)<sup>22</sup> to EU agencies was accelerated by the financial crisis and prepared by the de Larosière Report.<sup>23</sup> While this was an incremental step of the legal environment, being a European Commission agency entails a certain legal framework - as regards e.g. budget and powers - which can not necessarily be extended without changing the legal framework/status.

In the institutional hierarchy of the EU, there are institutions and bodies (e.g. the European Parliament, the Council, the European Commission, the ECB, etc.) with a clear reference in the Treaty, certain powers, tasks, rules to follow and a described level of (i.a. budgetary) independence. Then, there are EU agencies and other EU bodies;<sup>24</sup> EU agency types are mainly decentralised agencies and regulatory agencies.

The ESAs are established as decentralised agencies, i.e. independent legal entities under European public law, distinct from the EU institutions. The draft budget for 2014 gives an **overview on the legal bases, creation, governing and financing structure, discharge procedure, staff policy plans, and resources planning 2014-2020 of these agencies**,<sup>25</sup> see in particular p. 10 on the financing structure:

<sup>21</sup> See e.g. [http://europa.eu/legislation\\_summaries/institutional\\_affairs/treaties/lisbon\\_treaty/ai0032\\_en.htm](http://europa.eu/legislation_summaries/institutional_affairs/treaties/lisbon_treaty/ai0032_en.htm); Stratulat, C. and Molino, E., *Implementing Lisbon: what's new in comitology?*; Clifford Chance, *New EU decision-making landscape: Delegated acts & implementing acts*; O'Leary, *EU Regulatory Affairs: What you should know about implementing and delegated acts*; regarding **'Level'-structure and procedure for adoption of RTS and ITS** see Raptis, *European Financial Regulation: ESMA and the Lamfalussy Process, the renewed European Legislative Process in the Field of Securities Regulation*, p. 61.

<sup>22</sup> Predecessors are the Committee of European Banking Supervisors (CEBS), the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) and the Committee of European Securities Regulators (CESR); see for their set-up previous Directive 2005/1/EC of 9 March 2005, OJ L 79, 24 March 2005, p. 9; and previous European Commission decisions 2004/5-10/EC, all dating 5 November 2003; all superseded by the new ESFS structure.

<sup>23</sup> For more detail, discussion and references see Chatzimanoli, D., *Law and Governance in the Institutional Organisation of EU Financial Services - The Lamfalussy Procedure and the Single Supervisor Revisited*, 2008; brief overview in Speyer, B., *Financial Supervision in the EU - Incremental progress, success not ensured*.

<sup>24</sup> For a systematic overview and link to more details, see for institutions [http://europa.eu/about-eu/institutions-bodies/index\\_en.htm](http://europa.eu/about-eu/institutions-bodies/index_en.htm) and for agencies [http://europa.eu/about-eu/agencies/index\\_en.htm](http://europa.eu/about-eu/agencies/index_en.htm).

<sup>25</sup> See Draft General Budget of the European Commission for the financial year 2014, Working Document Part III, p. 9-12.

## 'Financing structure

Most decentralised agencies are funded entirely by contributions from the EU budget, as described above. Some agencies, however, depend fully or partially on other revenue, such as revenue received from industry (fees):

- Partially self-financed agencies: European Chemicals Agency (ECHA)<sup>4</sup>, European Aviation Safety Agency (EASA) and European Medicines Agency (EMA);
- Fully self-financed agencies: Office for the Harmonisation in the Internal Market (OHIM), Community Plant Variety Office (CPVO) and Translation Centre for the Bodies of the European Union (CdT); and
- Agencies partially co-financed by national public authorities: European Banking Authority (EBA), European Insurance and Occupational Pensions Authority (EIOPA) and European Securities and Markets Authority (ESMA).

The financing structure as outlined above also has an impact on the annual budgetary procedure, in particular as regards two of the fully self-financed agencies: in the case of OHIM and CPVO, the effective control over revenue, expenditure and staffing issues is exercised by their respective Boards, rather than by Parliament and Council. As a consequence, this Working Document mostly presents some general information on OHIM and CPVO in the overview tables for decentralised agencies; no detailed budgetary financial statement is included for these self-financed bodies.'

Notably, while the European Commission plans to implement the 5 % staff cut by 2018 also to the decentralised agencies, it recommends making a distinction between already established agencies with no new duties, those to whom new tasks have been conferred, and newly established agencies. The latter will be allowed to increase their staffing levels.<sup>26</sup>

In regard to budget and the level of flexibility in staffing it is essential to keep in mind that:

- the choice of the legal framework determines the level of flexibility;
- desired changes have to be either compatible with the chosen set-up or alternative legal structures have to be implemented (up to the requirement of a Treaty change - depending on the envisaged status, e.g. 'ECB-like'); and
- just as the budget of most EU institutions, the budget of the agencies is proposed by the European Commission,<sup>27</sup> but altered and adopted by the European Parliament and the Council, in theory thus limiting the power which the European Commission can exercise and enabling the co-legislators to amend/increase the ESAs' budget.

## 1.5. The Role of the ESAs within the ESFS

### 1.5.1. Objectives

The ESAs assumed all tasks of the previous committees on 1 January 2011 supplemented by the additional new tasks set out in the ESA Regulations. The **objective** of the ESAs according to the Article 1(5) EBA and ESMA Regulations (Article 1(6) EIOPA Regulation) is to 'protect the public interest by contributing to the short, medium and long-term stability and effectiveness of the financial system, for the EU economy, its citizens and businesses'. Furthermore, this Article specifies that the ESAs' should contribute to:

<sup>26</sup> See News: *EU Commission proposes 5 % staff cut over 5 years in EU agencies*, 11 July 2013; [http://ec.europa.eu/budget/news/article\\_en.cfm?id=201307111148](http://ec.europa.eu/budget/news/article_en.cfm?id=201307111148); regarding specific issues concerning budgetary procedure for agencies, e.g. fee-collecting agencies/fee setting - partially self-financed agencies see Analytical Fiche Nr. 20: Funding and Budget revenues of agencies, and other Analytical Fiches.

<sup>27</sup> See Draft General Budget 2014, COM(2013)450, Sections 1-10; <http://eur-lex.europa.eu/budget/www/index-en.htm>.



- *'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;*
- *d) preventing regulatory arbitrage and promoting equal conditions of competition;*
- *e) ensuring the taking of related risks are appropriately regulated and supervised; and*
- *f) enhancing customer protection.'*

The ESAs address these objectives through regulatory, supervisory, financial stability and consumer protection roles within the ESFS.

### 1.5.2. Tasks

The **tasks** of the ESAs according to Article 8(1) ESA Regulations can be summarised as:

- *to contribute to the establishment of high-quality common regulatory and supervisory standards and practices, in particular by providing opinions to the EU institutions and by developing guidelines, recommendations, and draft regulatory technical standards (RTS) and implementing technical standards (ITS) in their respective scope of action;*
- *to contribute to the consistent application of legally binding EU acts, in particular by contributing to a common supervisory culture, ensuring consistent, efficient and effective application of the acts in their respective scope of action preventing regulatory arbitrage, mediating and settling disagreements between NCAs, ensuring effective and consistent supervision of financial institutions and financial market participants, ensuring a coherent functioning of colleges of supervisors and taking actions, inter alia, in emergency situations;*
- *to stimulate and facilitate the delegation of tasks and responsibilities among NCAs;*
- *to cooperate closely with the ESRB, in particular by providing the ESRB with the necessary information for the achievement of its tasks and by ensuring a proper follow up to the warnings and recommendations of the ESRB;*
- *to conduct peer reviews of NCAs, including issuing guidelines and recommendations and identifying best practices, in order to strengthen consistency in supervisory outcomes;*
- *to monitor and assess market developments in their areas of competence and to undertake economic analyses of markets to inform the fulfilment of the Authority's functions;*
- *to foster and provide a high level of protection of consumers/investors (investors, depositors, policy holders, pension scheme members and beneficiaries);*
- *to contribute to the consistent and coherent functioning of colleges of supervisors, the monitoring, assessment and measurement of systemic risk, the development and coordination of recovery and resolution plans, and an assessment of the need for appropriate financing instruments; and*
- *to publish on their websites, and to update regularly, information relating to their field of activities, in particular, within the area of its competence, on registered financial institutions, in order to ensure information is easily accessible by the public.*

### 1.5.3. Powers

Article 8(2) ESA Regulations equips each ESA with formal legal **powers** to achieve its objectives and carry out its tasks. These powers are as follows:

- to develop draft RTSs and ITSs, and to issue guidelines and recommendations, the latter also in specific cases;
- to take individual decisions addressed to NCAs in the specific cases;
- in specific cases concerning directly applicable EU law, take individual decisions addressed to financial institutions;
- to issue opinions to the European Parliament, the Council, or the European Commission;
- to collect the necessary information concerning financial institutions and financial market participants;
- to develop common methodologies for assessing the effect of product characteristics and distribution processes on the financial position of institutions and on consumer protection;
- to provide a centrally accessible database of registered financial institutions and other financial market participants in their respective scope of action.

The scope of action of the ESA is presented in detail in the chapters 3, 4 and 5 of the report. The ESAs' scope broadly covers the following market participants:

**Table 2: Market participants within the scope of action of the ESAs**

ESA	Scope of power
<b>EBA</b>	Credit institutions, financial conglomerates, investment firms, payment institutions and e-money institutions
<b>EIOPA</b>	Insurance undertakings, reinsurance undertakings, financial conglomerates, institutions for occupational retirement provision and insurance intermediaries
<b>ESMA</b>	Trading venues and post trading market infrastructures (including direct supervision of trade repositories), credit institutions and financial conglomerates (for their investment services activities), investment and asset managers, listed companies and Credit Rating Agencies (direct supervision).

**Source:** ESA Regulations.

It is important to note that the **responsibility for day-to-day supervision remains with NCAs**,<sup>28</sup> with the exception of the **ESMA's responsibility** for the registration, **direct supervision** and sanctioning of CRAs and trade repositories in the EU.

#### 1.5.4. Administrative Framework

The ESAs comply with the EU administrative rules, as adopted and generally applicable to European entities in accordance with the general EU Framework. This includes:

- Adherence to the **EU Staff Regulations** and the Conditions of Employment of Other Servants of the European Communities (**CEOS**);<sup>29</sup> and
- Adherence to the **Financial Regulation** applicable to the general budget of the European Communities.<sup>30</sup>

<sup>28</sup> Outlined in Recital 8 of EIOPA Regulation, Recital 9 of EBA and ESMA Regulations.

<sup>29</sup> Regulation No 31 (EEC), 11 (EAEC) laying down the **Staff Regulations** of Officials and the Conditions of Employment of Other Servants [**CEOS**] of the European Economic Community and the European Atomic Energy Community, OJ 45, 14.6.1962, p. 1385.

<sup>30</sup> Regulation (EU, Euratom) No 966/2012 on the Financial Regulation applicable to the general budget of the Union.

In addition, each ESA has developed a **Code of Good Administrative Behaviour**<sup>31</sup> to guide their general administrative conduct.

### Adherence to the EU Staff Regulations and the CEOS

According to Article 68 ESA Regulations, the staff arrangements of the ESAs are governed by the Staff Regulations applicable to all European Union institutions. These rules relate to i.a. recruitment, administrative status, promotions and advancements, terminations, working conditions, benefits, and disciplinary actions. The ESAs may not deviate from these rules.

Article 63(1) ESA Regulations sets out the requirement for the drawing up of annual establishment plans by the Executive Director, approved by the Management Board and produced by the Board of Supervisors. The establishment plan indicates the number of posts in each grade and function group. These are appended to the ESAs draft budgets and submitted annually to the European Commission for approval.

Positions at the ESAs are open to nationals of all EU Member States and the countries of the European Economic Area (EEA, Iceland, Lichtenstein and Norway). Staff consists mainly of **temporary agents** covering operational functions and **contract agents** for administration support functions with three-year renewable contracts. The ESAs recruit **seconded national experts** (from the NCAs) who are selected through open selection procedures, and successful candidates are offered positions on secondment for period up to 24 months.

### Adherence to the Financial Regulation applicable to the general budget of the EU

According to Article 62 ESA Regulations, the budgetary arrangements of the ESAs are governed by the Financial Regulation<sup>32</sup> generally applicable to European Union institutions. The revenues of the ESAs are derived from a mixture of:

- **obligatory contributions** from the NCAs;
- a **subsidy**<sup>33</sup> entered in the General Budget of the EU, within the section of the European Commission which explains on one hand that in the first instance, ESAs budgets are subject to the same constraints as that of the European Commission unless European Parliament and Council amend this position, and on the other hand, that full funding in the usual way for agencies might not help the ESAs quest for more flexibility; and
- any **fees** paid to the ESA in the cases specified in the relevant EU law (for example, the ESMA now receives contributions from institutions that it directly supervises, i.e. CRAs and trade repositories).

The **budgetary process** is described in **Article 63 ESA Regulation** and involves the ESAs preparing and sending to the European Commission by 31 March each year an estimate of its revenue and expenditure, including the establishment plan, and its work programme. The European Commission transmits the statement of estimates to the European Parliament and the Council (the 'budgetary authority') together with the draft EU budget. Then, the European Commission has to estimate the subsidy required and enter it into the draft budget. The budgetary authority subsequently adopts the establishment plans for the ESAs

<sup>31</sup> EBA Decision of the Management Board on EBA Code of Good Administrative Behaviour, Decision EBA DC 006, 12 January 2011; Decision of the Management Board on EIOPA Code of Good Administrative Behaviour, EIOPA-MB-11/043, 10 February 2011; ESMA Decision of the Management Board, Code of Good Administrative Behaviour, ESMA/2011/MB/6, 11 January 2011.

<sup>32</sup> The ESAs budgets are established and implemented in compliance with the principles set out in the Financial Regulation: unity, budgetary accuracy, annuality, equilibrium, unit of account, universality, specification, sound financial management which requires effective and efficient internal control, and transparency.

<sup>33</sup> The EU contribution to the agencies is meant to balance agency revenue and expenditure for that given year (balancing subsidy); see Analytical Fiche no. 20, Funding and budget revenues of agencies.

and authorises the appropriations for the subsidy. However, the ESAs budgets become final only after the final adoption of the EU budget has taken place.

## 1.6. The Purpose of this Study

This study is part of a twin report to review the establishment and work of the new ESFS. This part relates to the ESAs and has been undertaken in view of the European Commission's review foreseen for January 2014 according to **Article 81 ESA Regulations**. It outlines the ESAs' progress since establishment, mentions issues affecting the ESAs' ability to achieve progress, as well as provide recommendations for change or improvement in current processes, structures or regulations. The second study evaluates the functioning of the ESRB and has been carried out separately.<sup>34</sup>

## 1.7. Approach Used

The study is based on the following main information sources:

- the ESA regulations and document review (annual reports, articles, speeches, studies, as well as other documents publicly available or provided by the ESAs);
- the findings of three online consultation via questionnaires<sup>35</sup> to which 105 responses were received from stakeholders (EBA: 24; EIOPA: 38; and ESMA: 43);
- 99 interviews<sup>36</sup> with a wide range of stakeholders and target groups to gather opinions and perceptions of the ESAs' work to date as well as to identify areas for improvement; and
- participation in the European Commission's Public Hearing on Financial Supervision in the EU<sup>37</sup> (24 May 2013, Brussels) where various stakeholders discussed the ESAs.

The fundamental approach used to review the ESAs has been to assess whether the establishment and functioning of the EBA, the EIOPA and the ESMA have had the desired effect as described in the provisions of the ESA Regulations.<sup>38</sup> For that purpose the assessment was structured according to the **key common features of the ESAs**:

- establishment and internal organisation,
- governance,
- institutional profile and positioning within the EU, as well as their
- communication and consultation processes;

and the **key roles** the ESAs play:

- regulatory,
- supervisory,

<sup>34</sup> See Oxford Analytica, *Review of the New ESFS, The work of the ESRB*, PE 507.490, Brussels, October 2013.

<sup>35</sup> The questionnaires were distributed amongst the stakeholder communities via the ECON Committee's website as well as the websites of the EBA, the EIOPA and the ESMA; see Annex for more information providing a summary of the questionnaire responses, as well as a statistical overview of the type and origin of stakeholders that contributed to the analysis.

<sup>36</sup> See Annex for more information providing a summary of the interviews held, as well as a statistical overview of the type and origin of stakeholders that contributed to the analysis.

<sup>37</sup> See [http://ec.europa.eu/internal\\_market/conferences/2013/0524-financial-supervision/index\\_en.htm](http://ec.europa.eu/internal_market/conferences/2013/0524-financial-supervision/index_en.htm).

<sup>38</sup> The fact that **within the ESFS, the day-to-day supervision is carried out by the NCAs** makes the ESAs quite unique when compared to NCAs. Therefore, the ESAs cannot be 'benchmarked' against international principles or standards applicable to NCAs. This is why the review concentrates on an assessment of whether all tasks assigned to the ESAs have been fulfilled.

- financial stability,
- consumer protection.

To understand their individual and collective contributions, the ESAs were considered as a group as well as separate authorities. This methodology has provided to be a good basis to compare and contrast the work of each ESA and in turn make suggestions for possible changes in the ESA Regulations. The impact of the introduction of the SSM within the Banking Union is also discussed and recommendations have been proposed in that regard.

## 1.8. Assessment Grid

For the purpose of the review of the performance of the ESAs, each ESA has been assessed against a grid structured along the key provisions of the ESA Regulations. The outcome of the analysis for features which are common to all ESAs and is presented in chapter 2. The analysis of ESA specific provisions is presented in individual chapters 3, 4 and 5.

### 1.8.1. Assessment of matters common to all ESAs

The ESAs have nearly identical governance and operational arrangements. The areas of common assessment points cover the following:

- **Governance (Article 6, 37, 40 - 53 ESA Regulations):** the governance structures in place in ESAs including the Board of Supervisors, Management Boards, Chairpersons and Executive Directors as well as the important role of the Stakeholder Groups;
- **Establishment and internal organisation (Article 5, 7, 62 - 72, 74 - 77 ESA Regulations):** establishment since 2011, organisation, quantity and quality of resources, funding and budget allocation;
- **Institutional positioning and working relationships (Article 3, 33, 34, 36 ESA Regulations):** establishing positions within the EU institutional framework and developing relationships with the European Parliament, the European Commission, the Council and the ECB as well as positioning within the ESFS and relationship with the NCAs and the ESRB, and including relations with third countries and international organisations;
- **Communication and consultation (Article 73 ESA Regulations):** working language, clarity, timeliness and completeness of communication, consultations and websites.

### 1.8.2. Assessment of the Regulatory and Supervisory Performance of the ESAs

Each ESA has been assessed against four core powers granted under the ESA Regulations:

- **Regulation (Article 10 - 16 ESA Regulations):** contributing to a Single Rulebook in their respective sectors whilst providing advice to the European Commission on delegated acts and developing draft technical standards, guidelines and recommendations;
- **Supervision:** supervising the consistency of supervisory practices across Member States, supervising the daily application of EU law and carrying out direct supervision (ESMA), as follows:
  - **Consistent supervision (Article 21, 28, 29 ESA Regulations):** ensuring consistent and coherent application of EU laws in the respective sectors by coordinating and monitoring the consistent functioning of colleges of supervisors (see Box 1 below) of regulated entities, stimulating and facilitating the delegation of tasks and responsibilities between NCAs or even between NCAs and the ESAs themselves and building a common supervisory culture between NCAs to ensure uniform procedures and consistent supervisory practices and approaches throughout the EU;

- **Implementation supervision (Article 19, 20, 29(1)(a), 30 ESA Regulations):** ensuring the consistent, efficient and effective application of EU law in the respective sectors by preventing regulatory or even supervisory arbitrage, promoting equal conditions of competition (level playing field), conducting peer reviews by which the ESAs and the NCAs assess and compare the degree of convergence reached in the application of EU law, applying a binding mediation mechanism to settle disagreements between NCAs and the capacity to issue opinions to NCAs as a preamble to a formal investigation and breach of Union law procedures;
- **Direct supervision:** only for the ESMA in respect to CRAs and trade repositories;
- **Financial Stability (Article 18, 21(2)(b), 22 - 25, 27, 31 - 32 ESA Regulations):** identification and response to systemic risk and vulnerabilities, stress testing, actions in emergency situations and recovery and resolution planning;
- **Consumer protection (Article 9, 26 ESA Regulations):** identifying consumer trends, carrying out education and training initiatives, issuing consumer warnings, ESA powers and actions to restrict certain activities and work related to compensation schemes.

### 1.8.3. Review of the Joint Committee and Joint Board of Appeal

The ESA Regulations also established two bodies that are competent for all three ESAs:

- **the Joint Committee (Article 54 - 57 ESA Regulations),** a forum for strengthening cooperation between the ESAs for cross-sector matters ensuring consistency of practices, and
- **the Board of Appeal (Article 58 - 61 ESA Regulations),** a joint board in charge of deciding on appeals against decisions taken by the ESAs. The functioning of the Joint Committee, focusing on joint ESA projects, process and usefulness, and the activity of the Board of Appeal to date has also been reviewed (see chapter 6).

Another relevant, but different, issue which the ESAs have to cover are **colleges of supervisors** which are covered in Article 21 ESA Regulations and other sectoral EU legislation.

#### Box 1: Colleges of Supervisors, Article 21 ESA Regulations

*'Enhanced cooperation between supervisory authorities both at EU and global level is key to strengthening the supervision of cross-border banking groups. Colleges of supervisors are the vehicles for the coordination of supervisory activities. Under EU law, colleges of supervisors have to be established for EEA banks with subsidiaries or significant branches in other EEA countries. They may include supervisors in non-EEA countries, where relevant. The colleges allow supervisory authorities to join forces, share knowledge and use skills and resources more effectively and efficiently, regardless of their individual jurisdiction. This requires determination and significant efforts to prompt coordinated approaches among competent authorities. To assist in developing a consistent and effective college framework, the EBA's predecessor, CEBS, published guidelines (i) on the operational functioning of colleges and (ii) on the joint assessment of banks' risks, and joint decisions on the adequacy of cross-border banks' capital within a college setting. With the implementation of the Capital Requirements Regulation and the revised Capital Requirements Directive, these guidelines will be replaced by the directly applicable technical standards covering the functioning of colleges and joint decisions on institution-specific prudential requirements.'*<sup>39</sup>

<sup>39</sup> Taken from the EBA website; <http://www.eba.europa.eu/regulation-and-policy/colleges-of-supervisors>.



## 1.9. Mapping the Review Article 81 ESA Regulations to the Study

Article 81 ESA Regulations also set out the terms of a review process. By 2 January 2014, and every three years thereafter, the European Commission is required to publish general reports on *'the experience acquired as a result of the operation of the Authorities and the procedures laid down in the Regulation(s)'*. The European Commission is required to forward these reports and any accompanying proposals to the European Parliament and the Council.

The table below maps the review points to the sections of this report where they have been addressed.

**Table 3: Mapping: Review Clause (Article 81 ESA Regulation) and Study**

Article 81 paragraph (...) ESA Regulation	Section(s) of this report
(1)(a) Convergence in supervisory practices reached by NCAs: (i) the convergence in functional independence of NCAs and in standards equivalent to corporate governance; (ii) the impartiality, objectivity and autonomy of the ESA	Throughout 2.1
(1)(b) Functioning of the colleges of supervisors	3.3.1, 4.3.1, 5.3.2
(1)(c) Progress achieved towards convergence in the fields of crisis prevention, management and resolution, including EU funding mechanisms	3.4.5, 3.4.6, 4.4.3, 4.4.4, 5.4.3
(1)(d) Role of the Authority as regards systemic risk	3.4, 4.4, 5.4
(1)(e) Application of the safeguard clause of Article 38 ESA Regulation (impinging on financial responsibilities of Member States)	-
(1)(f) Application of the binding mediation role, Article 19 ESA Regulation	3.3.5, 4.3.5, 5.3.6
(2)(a) Appropriateness of separate supervision of banking, insurance, occupational pensions, securities and financial markets	Executive Summary, 6.1, 7.1
(2)(b) Appropriateness of undertaking prudential supervision and supervise the conduct of business separately or by the same supervisor	Executive Summary, 6.1, 7.1
(2)(c) Appropriateness to simplify and reinforce the ESFS architecture in order to increase the coherence between the macro and the micro levels and between the ESAs	Executive Summary, 2.2.2, 6.1, 7.1
(2)(d) Consistency of the ESFS evolution with that of the global evolution	2.2.3
(2)(e) Sufficient diversity and excellence within the ESFS	Executive Summary, chapter 7
(2)(f) Adequateness of accountability and transparency in relation to publication requirements	2.2, 2.2.4, 2.4
(2)(g) Adequateness of resources of the ESAs to carry out their responsibilities	Executive Summary, chapter 7, 0, 2.3.4, 3.1.2, 4.1.2, 5.1.2
(2)(h) Appropriateness of the ESAs' seat to be maintained or to move the ESAs to a single seat to enhance better coordination between them	Executive Summary, 6.1, 7.1

## 2. ASSESSMENT OF MATTERS THE ESAS HAVE IN COMMON

### KEY FINDINGS

- **The ESAs have made good progress towards being recognised by their stakeholders as Authorities in their own right.** The ESAs have gained influence within the financial services industry and with NCAs. But the ESAs lack independence to set their own priorities and work programmes. A higher administrative rank for the Chairpersons would improve their institutional standing.
- **The ESAs have been successfully established from an operational perspective.** The ESAs' staff has built well-functioning organisations while facing very material demands on limited resources.
- **The current ESA apportionment of sector responsibilities remains appropriate, although the creation of the SSM is likely to lead to a debate about the division between prudential and consumer protection tasks within the ESFS.** Stakeholders are aware that the issue is likely to arise once the ECB becomes the prudential supervisor of a large share of the EU banking sector.
- **Although the ESAs have benefited from significant budget increases, the current resource model is reaching its limits.** The European Commission's budget is contracting and some NCAs face acute cost pressures, both resulting in limited funding increases. Thus, the current arrangement is unlikely to provide sufficient future resources. EU administrative requirements constrain their ability to recruit staff and use their resources effectively.
- **When deciding on regulatory matters, the Board of Supervisors membership model strikes the best possible balance between the need for an EU-wide view and the desirability of securing national ESFS buy-in.** It is clear that, at times, members have voted according to national priorities. However, the reality of the ESAs' governance is more nuanced than sometimes portrayed. The new ESAs' governance has evolved during a period when cross-border cooperation on regulatory and supervisory matters has been tested. The result is that the decision making process of the Board of Supervisors is efficient for regulatory matters, but lacks EU impetus for supervisory issues.
- **However, the present governance model is cumbersome, and too much time is spent by the Boards of Supervisors processing draft implementing measures (RTS, ITS) at the expense of discussion of substantive regulatory, supervisory, financial stability and consumer protection issues.** To date, very detailed regulatory matters have dominated the Board of Supervisors' meetings, at the cost of the development of the Boards of Supervisors as strategic and policy contributors to the completion of the Single Market for financial services.
- **The respective Stakeholder Groups of the ESAs are 'work in progress' and further changes will be needed if they are to provide strategic input and play a more active role in supervisory consistency.** Participation of high calibre individuals with global experience and a focus on access to capital would be a real added value. Consumer representation is low compared to industry and the lack of funding and administrative support for members is hindering their ability to enhance their contribution. There is insufficient transparency about the influence of stakeholders on the ESAs' deliberations, but also progress: EIOPA publishes stakeholder meeting calendars and feedback statements.



- **The ESAs have taken the necessary steps to become active counterparts of third countries supervisors and tried to become members, observers or key contributors in key international organisations.** EIOPA is already a member of the IAIS and the exercise of direct supervision (of CRAs by ESMA) makes this international role stronger.

The ESAs' establishment occurred during a period of stress in financial markets and extensive legislative activity. The modernisation or review of existing legislation<sup>40</sup> had and still has a major impact on the ESAs and their activities. So too has the regulation of new, previously unregulated areas<sup>41</sup> to implement the G20 financial services reform agenda.<sup>42</sup>

## 2.1. Governance

### 2.1.1. Board of Supervisors (Article 40 - 44 ESA Regulations)

The ESAs are obliged to act through their respective Board of Supervisors independently and only in the EU's interest. Article 42 ESA Regulations clearly states that members should not seek or take instructions from EU institutions or bodies, from any government of a Member State, or from any other public or private body.

Each ESA established a **Board of Supervisors** in 2011. They are **composed** of

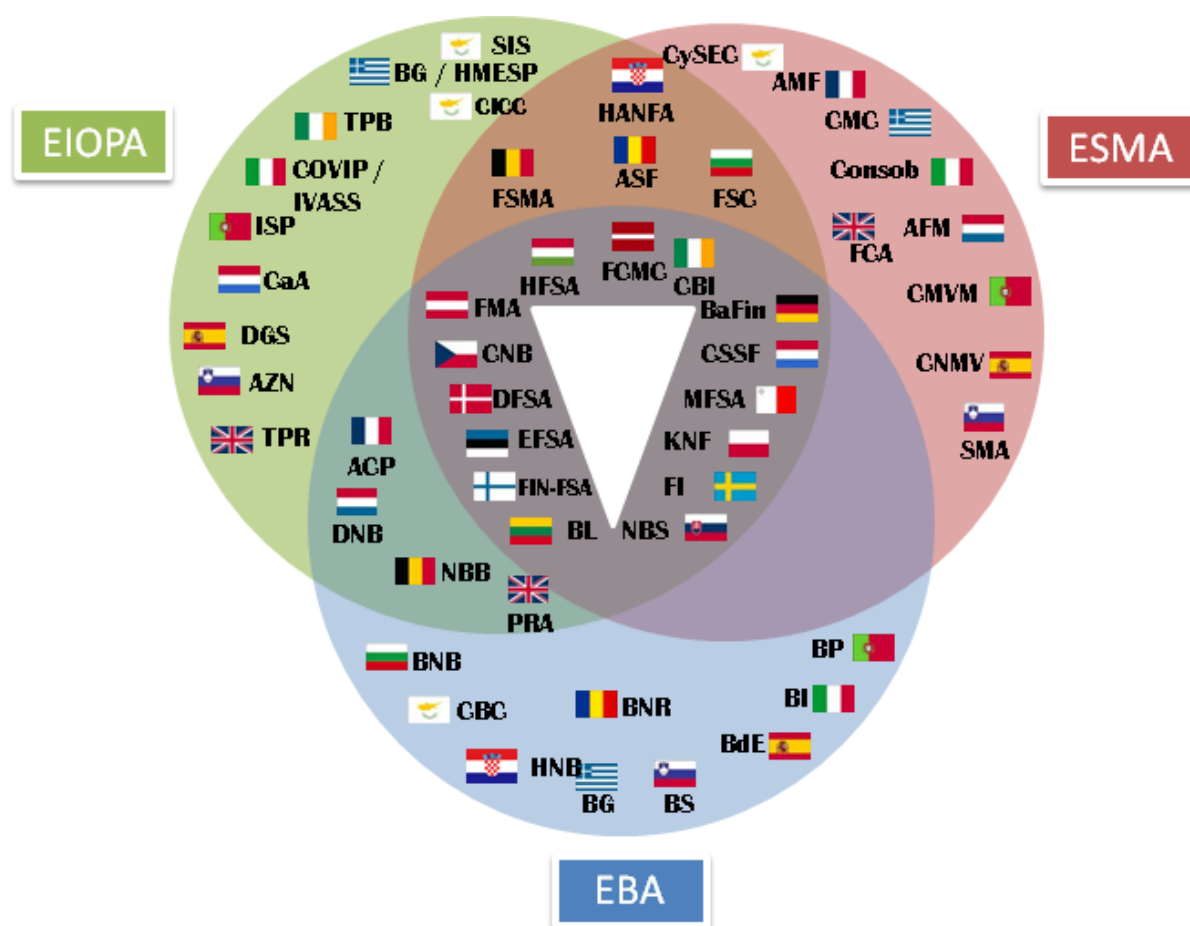
- the ESA (non-voting) **Chairperson**,
- the (voting) **heads of the NCAs** in each of the now 28 Member States, and
- (non-voting) **observers** from the European Commission, the ECB, the ESRB, the other ESAs and NCAs from the EEA.

The **Executive Director** participates in meetings of the Board of Supervisors. A number of NCAs are represented on more than one ESA, reflecting the integrated nature of their national supervisory authority. Furthermore, some individuals sit on more than one Board of Supervisors. Figure 2 provides an illustration of this composition.

<sup>40</sup> E.g. the Capital Requirements Regulation (CRR) and Capital Requirements Directive (CRD IV), the Solvency II Directive, the Financial Conglomerates Directive (FICOD), or the UCITS V Directive.

<sup>41</sup> E.g. the Credit Rating Agency Regulation (CRA), the proposed Bank Recovery and Resolution Directive (BRRD), the Single Supervisory Mechanism (SSM), the proposed Single Resolution Mechanism (SRM), the European Market Infrastructure Regulation on OTC Derivatives (EMIR), or the Regulation on Short Selling.

<sup>42</sup> See e.g. FSB press release, 19 April 2013, [http://www.financialstabilityboard.org/press/pr\\_130419.pdf](http://www.financialstabilityboard.org/press/pr_130419.pdf).

**Figure 2: NCA representation in the ESAs Board of Supervisors**

Source: Mazars.

<b>ACP</b>	Autorité de Contrôle Prudentiel (French Prudential Supervisory Authority)
<b>AFM</b>	Autoriteit Financiële Markten (Dutch Authority for the Financial Markets)
<b>AMF</b>	Autorité des marchés financiers (French Financial Markets Authority)
<b>ASF</b>	Autoritatea de Supraveghere Financiară (Romanian Financial Supervisory Authority)
<b>AZN</b>	Agencija za zavarovalni nadzor (Slovenian Insurance Supervision Agency)
<b>BaFin</b>	Bundanstalt für Finanzdienstleistungsaufsicht (German Federal Financial Supervisory Authority)
<b>BdE</b>	Banco de España (Bank of Spain)
<b>BG</b>	Τράπεζα της Ελλάδος (Bank of Greece)
<b>BI</b>	Banca d'Italia (Bank of Italy)
<b>BL</b>	Lietuvos Bankas (Bank of Lithuania)
<b>BNB</b>	Българска народна банка (Bulgarian National Bank)
<b>BNR</b>	Banca Națională a României (National Bank of Romania)
<b>BP</b>	Banco de Portugal (Bank of Portugal)
<b>BS</b>	Banka Slovenije (Bank of Slovenia)
<b>CaA</b>	Commissariat aux Assurances (Luxembourg)
<b>CBC</b>	Κεντρική Τράπεζα της Κύπρου (Central Bank of Cyprus)
<b>CBI</b>	Central Bank of Ireland
<b>CICC</b>	Αρμοδιότητα της Υπηρεσίας Ελέγχου Ασφαλιστικών Εταιρειών (Cyprus Insurance Companies Control)
<b>CMC</b>	Επιτροπή Κεφαλαιαγοράς (Greek Capital Market Commission)
<b>CMVM</b>	Comissão do Mercado de Valores Mobiliários (Portuguese Securities Markets Commission)
<b>CNB</b>	Česká národní banka (Czech National Bank)
<b>CNMV</b>	Comisión Nacional del Mercado de Valores (Spain)
<b>CONSOB</b>	Commissione Nazionale per le Società e la Borsa (Italian Securities and Exchange Commission)
<b>COVIP</b>	Commissione di Vigilanza sui Fondi Pensione (Italian Pension Funds Supervision Commission)
<b>CSSF</b>	Commission de Surveillance du Secteur Financier (Luxembourg Commission for the Supervision of the Financial Sector)
<b>CySEC</b>	Επιτροπή Κεφαλαιαγοράς (Cyprus Securities and Exchange Commission)
<b>DFS</b>	Finanstilsynet (Danish Financial Supervisory Authority)

<b>DGS</b>	Dirección General de Seguros (Spanish Directorate-General of Insurance and Pension Funds)
<b>DNB</b>	De Nederlandsche Bank (National Bank of Netherlands)
<b>EFSA</b>	Finantsinspektsioon (Estonian Financial Supervision Authority)
<b>FCA</b>	Financial Conduct Authority (UK)
<b>FCMC</b>	Finanšu un kapitāla tirgus komisija (Latvian Financial and Capital Market Commission)
<b>FI</b>	Finansinspektionen (Swedish Financial Supervisory Authority)
<b>FIN-FSA</b>	Finanssivalvonta (Finnish Financial Supervisory Authority)
<b>FMA</b>	Finanzmarktaufsicht (Austrian Financial Market Authority)
<b>FSC</b>	Комисия за финансов надзор (Bulgarian Financial Supervision Commission)
<b>FSMA</b>	De Autoriteit voor Financiële Diensten en Markten/Autorité des services et marchés financiers (Belgian Financial Services and Markets Authority)
<b>HANFA</b>	Hrvatska Agencija za Nadzor Financijskih Usluga (Croatian Financial Services Supervisory Agency)
<b>HFSA</b>	Pénzügyi Szervezetek Állami Felügyelete (Hungarian Financial Supervisory Authority)
<b>HMESP</b>	Hellenic Ministry of Employment and Social Protection (Greece)
<b>HNB</b>	Hrvatska Narodna Banka (Croatian National Bank)
<b>ISP</b>	Instituto de Seguros de Portugal (Portuguese Insurance and Pension Funds Supervisory Authority)
<b>IVASS</b>	Istituto per la vigilanza sulle assicurazioni (Italian Insurance Supervisory Authority)
<b>KNF</b>	Komisja Nadzoru Finansowego (Polish Financial Supervision Authority)
<b>MFSA</b>	Malta Financial Services Authority
<b>NBB</b>	Nationale Bank van België (National Bank of Belgium)
<b>NBS</b>	Národná banka Slovenska (National Bank of Slovakia)
<b>PRA</b>	Prudential Regulatory Authority (UK)
<b>SIS</b>	Υπουργείο Εργασίας και Κοινωνικών Ασφαλίσεων/Social Insurance Services - Ministry of Labour and Social Insurance (Cyprus)
<b>SMA</b>	Agencija za trg vrednostnih papirjev (Slovenian Securities Market Agency)
<b>TPB</b>	The Pensions Board/An Bord Pinsean (Ireland)
<b>TPR</b>	The Pensions Regulator (UK)

The **tasks of the Board of Supervisors** (Article 43, 45(1), 53(2) ESA Regulations) cover, in particular, the appointment of the Chairperson and the Executive Director, election of the Management Board, adoption of opinions, recommendations and decisions, issuing advice, adoption of the Annual Report and adoption of the annual and multi-annual work programme and of the budget. Although the ESA Chairperson chairs the Board of Supervisors, the NCAs retain full voting rights and decision making responsibilities as the Chairperson has no right to vote.

The Board of Supervisors **structure** creates a formal mechanism for institutionalising the duty of NCAs to take a common European stance on regulatory and supervisory matters. Importantly, the regular meetings of the Board of Supervisors promote multilateral and bilateral cooperation between NCAs.

**Decision-making** (Article 44 ESA Regulations): The predecessor-Committees of the ESAs had to find consensus which is often not an easy and successful task. Now, in general the Board of Supervisors takes **decisions by simple majority** where each NCA has one vote. However, for important regulatory, supervisory or internal matters voting is carried out by **qualified majority** (QMV).<sup>43</sup> For example, QMV is used for decisions relating to RTSs and ITSs, guidelines and recommendations, budget matters, and in instances where the ESA is requested to reconsider a decision to prohibit or restrict certain financial activities (to date no decisions have been taken in respect of the latter). It is important to note that the decision making process of the EBA is modified in conjunction with the creation of the SSM in order to take appropriate account of Member States which will not participate in the SSM: Specified **EBA decisions** will also need to obtain a '**double simple majority**', i.e. that there is at least a simple majority of NCAs participating in the SSM and a simple majority of NCAs not participating in the SSM. As such, this additional condition does not contribute to a more independent and EU interest orientated vote by members.

<sup>43</sup> Article 16 (4) TEU, 238(2) TFEU, 3 Protocol (36) on Transitional Provisions; for explanation and calculation see [http://europa.eu/legislation\\_summaries/glossary/qualified\\_majority\\_en.htm](http://europa.eu/legislation_summaries/glossary/qualified_majority_en.htm).

So an important factor in the development of the ESAs' governance has been the influence of voting procedures. QMV is widely considered to have led to significant improvement compared to the practice at the ESAs' predecessors<sup>44</sup> (full consensus voting). Voting on regulatory matters during Board of Supervisors meetings has become a routine matter that is now well accepted and understood. On occasion, it has also allowed NCAs from large Member States to be out-voted. Voting has thus allowed the governance of the ESAs to develop in line with their purpose.

In practice, discussions and decisions have been heavily influenced by the major NCAs and the European Commission. On some occasions, this has meant that initiatives or actions proposed by the Chairpersons were not endorsed by the Board of Supervisors because they conflicted with NCAs' (national) interests.<sup>45</sup> Critics of the current structure consider that NCA membership works against the ESAs, even with the requirement for the members to shed national considerations in favour of a European view. Others consider that NCA membership is a strength. It creates support amongst NCAs for the ESFS. It gives NCAs a sense of ownership of the ESAs' final decisions. It also reflects the fact that the Single Market for financial services provides the interface between cross-border market players and national supervisory regimes. Several NCAs further consider that, in the majority of cases, there is not a conflict between their respective roles, and the suggested issue of split loyalties is not a real one.

The realities of the current structures also need to be considered. The NCAs are principally accountable to their own national parliaments and finance ministries, and the heads of NCAs are appointed and approved through national processes. NCAs therefore have an unavoidable obligation to act accordingly. But it is also clear that by having these strong accountability mechanisms in Member States, by extension the ESAs obtain greater legitimacy (see Annex, point 5). Furthermore, Member States should exercise their rights in accordance with what is prescribed for in the adopted EU legal framework.

This question of **balance between European and national interests in the ESAs' governance** has attracted significant comment. In its March 2013 Financial Sector Assessment Program (FSAP) report,<sup>46</sup> the International Monetary Fund (**IMF**) repeated its earlier **concerns**<sup>47</sup> **about the composition of the Board of Supervisors**, and noted that national views rather than EU-wide interests continue to dominate the proceedings. The paper reiterated previous IMF recommendations to enhance Board of Supervisors governance. **Alternative governance models** suggested included the provision of voting rights to the representatives of some other EU institutions (except the European Commission), and possibly to the ESA Chairpersons, or further strengthening and delegating more decisions to the Management Board.

While there is validity in these observations, there is neither a fixed nor binary distinction between the national and European interest. At times, NCAs have adopted self-serving national positions which could be said to contradict a wider European interest. Equally, NCAs have taken stances on supervisory issues within their own borders which, although perhaps appearing self-interested, are congruent with the European interest. This is particularly true for those euro area EBA members which have had to deal with severe banking crises. It is

<sup>44</sup> Predecessors are the Committee of European Banking Supervisors (CEBS), the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) and the Committee of European Securities Regulators (CESR); see previous Directive 2005/1/EC of 9 March 2005, OJ L 79, 24 March 2005, p. 9; and previous European Commission decisions 2004/5-10/EC, all dating 5 November 2003; all superseded by the new ESFS structure.

<sup>45</sup> Discussed in chapters 3, 4 and 5.

<sup>46</sup> IMF Country Report No. 13/65, March 2013, p. 11.

<sup>47</sup> Earlier concerns were expressed in IMF Country Report No. 11/186, July 2011, p. 33.

demonstrably the case that supervisors in Ireland, Greece, Portugal, Spain and latterly Cyprus have taken positions at the Board of Supervisors which, had they been pursued, could have lessened both domestic and euro area stresses. The opposition of Cypriot supervisors to a haircut of insured depositors in early 2013 is one such example. In each case, the question of the national versus European interest was fluid.

However, there is frustration amongst NCAs about the content of the Board of Supervisors agenda, in particular the **lack of focus on policy issues** where the Board of Supervisors can contribute an experienced supervisory point of view. Many meetings have been devoted to the adoption of draft RTSs and ITSs and other technical regulatory matters. There have been few strategic or policy discussions, and little focus on the architecture and functioning of the Single Market. Most important, there has been little attention to supervisory matters.<sup>48</sup> Even if there is a wide range of views amongst NCAs, there is a desire amongst them for the Board of Supervisors to spend more time on policy and strategic matters.

In the same way, the bi-annual meetings of the Board of Supervisors with their respective Stakeholder Groups have rarely engaged in substantive, high quality discussions. This has been to the frustration of both sides.

### 2.1.2. Management Board (Article 45 - 47 ESA Regulations)

The Management Boards of the ESAs are comprised of their respective Chairpersons and six other members elected by the Board of Supervisors. The Management Board is responsible for ensuring that ESAs perform their mission and assign **tasks**<sup>49</sup> which include:

- the proposal of an annual and multi-annual work programme,
- the adoption of a staff policy plan, and
- the exercise of budgetary powers of the ESAs.

Each member of the Management Board has one vote. The Executive Director and a representative from the European Commission also sit on the Management Board in a non-voting capacity (the representative from the European Commission has a right to vote on budget related matters).

The Management Board of all three ESAs have focused on **administrative responsibilities**. Yet there are also important differences in the way each ESA has operated its Management Board. At one end of the spectrum, the EBA Management Board has attempted to steer the priorities and resulting work of the EBA, including the agenda for Board of Supervisors meetings. In this respect, the EBA Management Board can be said, broadly, to be fulfilling the role of an executive body within an NCA. At the other end, the ESMA's Management Board focuses strictly on what is required by the Regulation. For the EIOPA, the Board of Supervisors' agenda is part of the Management Board discussion. Contrary to the EBA, within ESMA and EIOPA the Management Board is not a preparatory body for the decisions of the Board of Supervisors.

The experience of the ESAs suggests that the Management Board can have an important influence on an ESA's decisions, and notably that it can bring coherence to its work. There are, though, a number of **obstacles to this model** as listed below:

- Evolution of functions, such as coherence and preparatory work; was not envisaged in the founding regulations. As such, any innovation in the Management Board's role has occurred with an uncertain legislative foundation.

<sup>48</sup> The conduct of supervisory work is analysed in chapter 3, 4 and 5.

<sup>49</sup> All tasks of the Management Board are set out in Article 47 ESA Regulations.

- The opinion has been expressed that voting for the membership of each Management Board reflects national priorities and preferences rather than a view on the suitability of the candidate regardless of national origin.
- There is a view that the rotation of membership of the Management Board every 2.5 years (one extension possible) hinders the emergence of a coherent executive function.
- Membership of the Management Board requires a material time commitment. Typically, members of the Management Board also have large roles in NCAs. This is a particular issue for officials from integrated regulators who are required to attend a minimum number of meetings of each of the ESAs.

Finally, NCAs that are not Management Board members consider that there is little scope to amend preliminary decisions, or even to oppose them, at Board of Supervisor meetings where key decisions have been 'pre-approved' in the Management Board. Such ambiguity cannot be a firm basis for ESA governance. The study makes several recommendations to improve the governance of the ESAs (see chapter 8).

### 2.1.3. Chairperson and Executive Director (Article 48 - 53 ESA Regulations)

The Board of Supervisors of each ESA completed the appointment of the Chairperson and Executive Director soon after the Authorities were established.<sup>50</sup> They were confirmed by the European Parliament after a hearing of its Committee on Economic and Monetary Affairs (ECON).

The **Chairperson is the key representative of the ESA**, and accordingly prepares the work of the Board of Supervisors while also chairing all Board of Supervisors and Management Board meetings. In addition, the Chairperson can be called in front of the European Parliament to provide an update on ESA progress.

The **Executive Director** is responsible for the management of the ESA i.e.:

1. developing and implementing annual and multi-annual work programmes (under the guidance of the Board of Supervisors and the control of the Management Board);
2. developing internal administrative instructions;
3. drafting and implementing the budget of the ESA;
4. annual reporting to the European Commission and European Parliament, and;
5. Human Resources management.

The full time Chairpersons are unanimously seen as a significant improvement compared to predecessor Committee arrangements. Equally, the ESA Chairpersons are widely regarded as having executed their duties to a high standard.

This was particularly evident during the most difficult times of the crisis and when the ESAs were publically asked to intervene without having the authority or means to do so (for example, during the period of the EBA stress tests and ESMA short selling restrictions – see sections 3.4.2 and 5.4.3 for more details). In these instances, the Chairpersons sometimes felt exposed (if not isolated) while the ESAs were expected to be authoritative. The Chairpersons did not always have the support of the Board of Supervisors as a whole, or the backing of individual members. As with any regulatory authority, at times the identity of the senior leadership of an ESA will be associated with the ESA itself. As such, the

<sup>50</sup> In line with Article 48 and 51 ESA Regulations.



Chairpersons would greatly benefit from operating within a governance structure which gives them greater authority.

A number of stakeholders therefore emphasise the need to **enhance the standing of the Chairpersons position through a higher administrative ranking**. This could ensure that they have a maximum possible standing and influence, and the ability to speak on a more equal basis with the heads of the NCAs, EU officials and foreign counterparts. This is also supported by the IMF as well as the Chairpersons and senior management of the ESAs.

## **Box 2: The appointment of the first ESA Chairpersons**

In accordance with Article 48 ESA Regulations, the Chairpersons of the ESAs shall be appointed by the Board of Supervisors following an open selection procedure. The European Parliament may, after having heard the candidate selected by the Board of Supervisors, object to the designation of the selected person. However, for the **designation of the first Chairpersons, the European Commission was in charge of drawing-up a short list of candidates**. On this occasion the European Commission added several criteria not contemplated by the ESA Regulations for the selection of candidates (e.g. age limit, administrative ranking, etc.). The process has been criticised, notably by the European Parliament, for its lack of transparency and ability to select a sufficient number of candidates (for some ESAs, the short list was made of one name).

Recital 55 ESA Regulations **calls for a review** of the opportunity of having a shortlist drawn by the European Commission for subsequent designations. A process, in line with Article 48 ESA Regulations, without the administrative criteria and process of the European Commission would significantly enhance the capacity to attract high profile candidates.

### 2.1.4. ESA Stakeholder Groups (Article 37 ESA Regulations)

The Stakeholder Groups of the ESAs are an additional important component of their governance. They were established to facilitate consultation with consumers, users and providers of financial services. Input is requested, particularly in respect of draft RTSs and draft ITSs, guidelines and recommendations, and in addition, the groups can submit opinions and advice to the ESAs on any issue related to the tasks of the Authorities. The Stakeholder Groups may request investigations of alleged breaches or non-application of EU law. The Stakeholder Groups are highlighted below.

**Table 4: ESA Stakeholder Groups and Chairpersons** (July 2013)

ESA	Stakeholder Group	Chairperson
<b>EBA</b>	Banking Stakeholder Group (BSG)	Mr David Llewellyn (Loughborough University, Vienna University of Economics and Business)
<b>EIOPA</b>	Insurance and Reinsurance Stakeholder Group (IRSG)	Ms Michaela Koller (Director General Insurance Europe)
	Occupational Pensions Stakeholder Group (OPSG)	Ms Chris Verhaegen (Secretary-General Pensions Europe)
<b>ESMA</b>	Securities and Markets Stakeholder Group (SMSG)	Mr Guillaume Prache (Managing Director European Federation of Financial Services Users/EuroFinuse)

It is interesting that the Stakeholder Groups elected Chairpersons with very different profiles and backgrounds: an academic, a top ranking representative of an EU association of the specific sectors and a representative of financial services users. Each Stakeholder Group is composed of 30 members appointed by the Board of Supervisors and representing market participants, relevant sectors, and their employees' representatives as well con-

sumers, users of financial services and representatives of SMEs. Members of the stakeholder groups are appointed for a 2.5 years cycle which is renewable once.<sup>51</sup> In 2011, the ESAs received a significant number of applications, leading to a challenging selection process in which they sought to achieve a balanced composition while respecting the requirements of the ESA Regulations.

It has taken the Stakeholder Groups time to establish and to define an operating model that allows them to contribute to the ESFS. Their **main challenge** has been to decide how to approach the **consultation processes** of the ESAs when drafting RTSs and ITSs. Should they be consulted for all consultations? Should this occur before or during the consultation? At the request of the Group members, a *modus operandi* seems to have been found that uses the expertise of the Stakeholder Groups to discuss key market issues and the issues the ESA should consider when developing their work programme ahead of consultations. It is in this role that members consider that their input adds value. Furthermore, some Stakeholder Groups have succeeded in organising working sub-groups, establishing their own priorities and contributing high quality policy papers to the ESAs on an *ad hoc* basis, of which some have been published.<sup>52</sup>

A number of suggestions have been made to **improve further the functioning of Stakeholder Groups**. For example, Stakeholder Groups are considered difficult to manage as a consequence of their **size**. One option would be to shrink<sup>53</sup> the groups. Another would be to segment their membership, possibly using a division between industry and consumer representatives. However, on balance there is no strong call to change the current formula at this juncture. But there are at least **four issues that deserve political impetus**.

- **Composition.** The Stakeholder Groups' membership is diverse, and there are notable differences in the members' financial sector experience and knowledge. This can impact the stakeholder groups' ability to have informed discussions and thus to inform ESA decisions and hold them to account. **Senior individuals** with experience gained outside Europe, or who have been involved in corporate finance, as well as global institutional asset managers and retail investors, **are underrepresented**. Shorter meetings focused on fewer issues would favour the active participation of high calibre senior experts.

**Financial services users and consumers are poorly represented.** After the announcement of the selected candidates in 2011, a number of complaints were raised by consumer representatives about the composition of the EBA, EIOPA and ESMA groups. The main concerns expressed were in relation to the over-representation of financial industry interests and the under-representation of financial user representatives on the group, as well as gender balance and incorrect adoption of the definition of difference stakeholder categories provided for in the ESA Regulations. Complaints were received directly by the ESAs and by the **European Ombudsman**.<sup>54</sup>

At a minimum these various criticisms should be taken into account during the current appointment process. **Improving the compensation of not-for-profit associations of consumers** could make a marked difference for all of the ESA Stakeholder Groups.

<sup>51</sup> The first 2.5 year cycle has been completed and the ESAs recently called for candidate's applications.

<sup>52</sup> Published opinions and letters on the EBA's website <http://eba.europa.eu/about-us/organisation/banking-stakeholder-group/publications>, the ESMA's website <http://www.esma.europa.eu/page/SMSG-advice-and-letters> and the EIOPA's website <https://eiopa.europa.eu/about-eiopa/organisation/stakeholder-groups/sgs-opinion-feedback/index.html>.

<sup>53</sup> However, this would require a change of the ESA Regulations.

<sup>54</sup> Decision see <http://www.ombudsman.europa.eu/activities/visitreport.faces/en/52209/html.bookmark>.



- **Resources.** There is a **recognised shortage** of resources provided by the ESAs to their Stakeholder Groups, limiting their ability to challenge the ESAs. While the ESAs have provided resources and support to its Stakeholder Groups to the best of their ability, a modest increase in administrative and research resources, as well as the allocation of more senior ESA staff time to Stakeholder Group issues would enhance their effectiveness.
- **Supervisory consistency role.** To date, most of the Stakeholder Groups' activities have been devoted to **regulatory issues**. On a few occasions, the Stakeholder Groups tried to use their ability to submit opinions on problems of level playing field or even request an ESA to investigate alleged breaches of Union law. The responses of the ESAs have not been satisfactory. In accordance with the ESA Regulations, the Stakeholder Groups should be allowed to play an active role in pursuing consistent **supervisory matters** (subject to controls to address the fact that representatives of regulated entities are members of Stakeholder Groups).
- **Term.** The 2.5 year term of the groups may be too short to add long-term value. It took some months for the members to determine their role and where they could best contribute. In addition, the diversity in membership meant that it also took time to develop a common culture. There would be significant merit in **maintaining a number of existing members** in the next cycle to keep momentum and reduce the challenges of starting afresh with new groups.

Overall, the ESAs are generally satisfied and supportive of the initial role of the Stakeholder Groups. Amongst stakeholders more generally, there is strong support for the proposition that the Stakeholder Groups need to make a greater contribution to the ESFS through their interaction with the ESAs (see Annex, point 21).

## 2.2. Institutional Positioning and Working Relationships

As newly established Authorities, an important aspect of the ESAs' evolution is their position relative to other EU institutions and the nature of the associated working relationships. The working relationship between the ESAs is discussed in chapter 6 on the Joint Committee.

### 2.2.1. Relations with EU Institutions (European Parliament, Council, European Commission, ECB)

**General:** The ESAs fit into a complex set of existing institutional relationships. Importantly, the **ESAs are accountable to the European Parliament and the Council**. This accountability includes the transmission of the ESAs work programme for the next calendar year (before 30 September of each year) and a multi-annual work programme as well as their annual report on their activities (including the Chairperson's performance). Regarding **budget**, the ESAs also transmit their final accounts by 1 July following the completion of the financial year (accompanied by the opinion of the Management Board) - the European Parliament grants a discharge to the ESAs for the implementation of their budget, following a recommendation from the Council. The European Parliament and the Council may also invite the Chairperson or their alternate to make a statement.

Furthermore, the ESAs serve as **independent advisory bodies** and can **issue opinions to the European Parliament and the Council**. The ESAs monitor and assess developments in their respective areas of competence and, where necessary, inform the European Parliament or the Council about the relevant micro-prudential trends, potential

risks and vulnerabilities on a regular and, if necessary, on an *ad hoc* basis.<sup>55</sup> The European Parliament and the Council may request an ESA to conduct an inquiry into a particular type of financial activity, or type of product or conduct, to assess potential threats to the stability of the financial system. The ESA can subsequently make appropriate recommendations for action to the NCA concerned. They may also request an ESA to investigate an alleged breach or non-application of Union law by NCAs.

The European Parliament and the Council are involved in the process of adopting **RTSs** (Articles 11 - 14 ESA Regulations).<sup>56</sup> The delegated power to the European Commission to adopt RTSs may be revoked at any time. The European Parliament and the Council may object to RTSs developed by the ESAs and adopted by the European Commission, in which case the standard does not enter into force. In case of non-endorsement or amendment of draft RTSs, the European Parliament and the Council may invite the responsible Commissioner, together with the relevant ESA Chairperson, for an *ad hoc* meeting of the competent committee of the European Parliament or the Council to present and explain their points of disagreement. However, the European Parliament and the Council also have a **scrutiny right as regards ITSs**, see Article 11 Regulation (EU) No 182/2011.

Finally, the **review** by the European Commission on the experience acquired as a result of the operation of the ESAs (by January 2014 and every three years thereafter) and any accompanying **proposal** must be forwarded to the European Parliament and the Council.

It should be noted that the European Parliament has additional specific rights: after having heard the candidate selected, it can **object** to the designation of the **Chairperson**, **confirm** the extension of a mandate or **remove** the Chairperson following a decision of the Board of Supervisors and; the European Parliament shall **confirm the appointment of the Executive Director**.

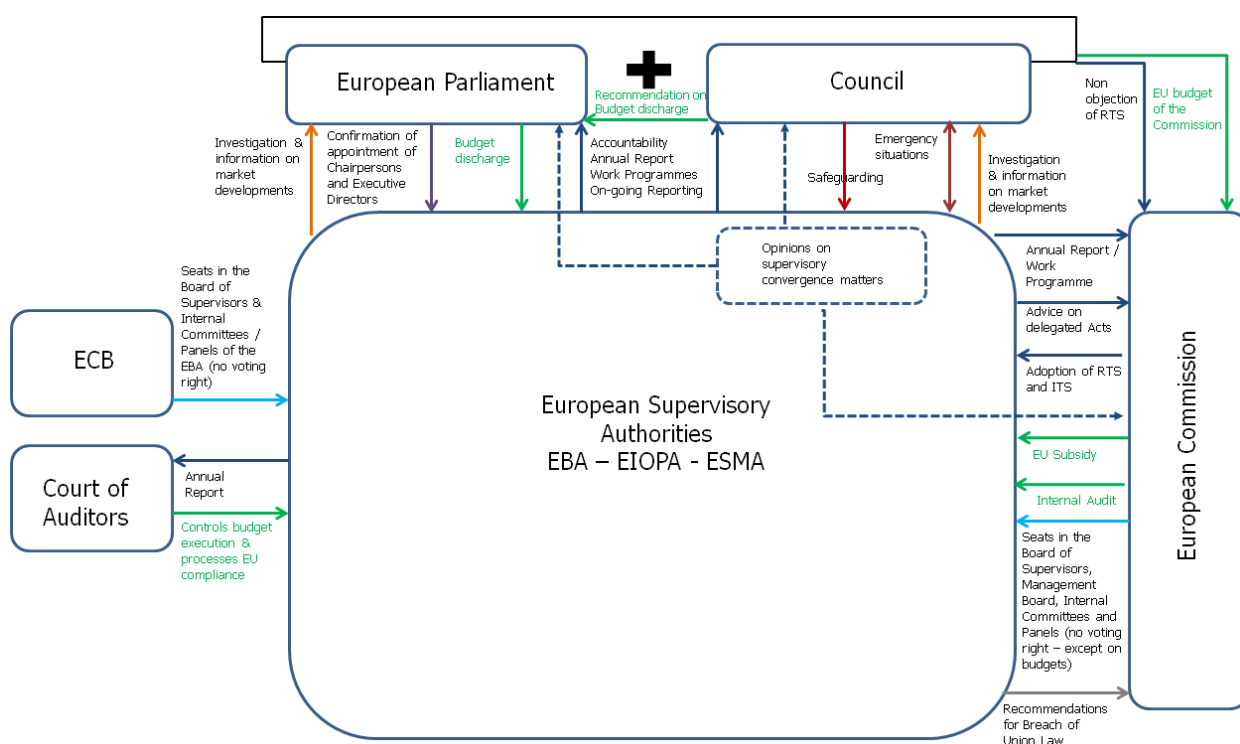
The **Council** has a more formal operational relationship with the ESAs:

- The Council has the power to determine the existence of an emergency situation, following a request by any ESA, the European Commission or the ESRB. Declaration of an emergency situation is a necessary precondition for use of the ESAs' emergency powers (including banning or restricting a financial activity that is not foreseen in the EU legislation);
- the Council is involved in the safeguard mechanism, established under Article 38 ESA Regulations, with the aim of ensuring that decisions by the ESAs in emergency or settlement situations affecting the stability of a financial institution do not impinge on the fiscal responsibilities of Member States. Member States may invoke this safeguard and ultimately bring the matter before the Council for a decision and;
- if an ESA does not act on a recommendation of the ESRB, it shall explain to the ESRB and the Council its reasons for not doing so.

In addition to the relationship with the European Parliament and the Council, the ESAs have complex institutional, operational and budgetary relationships with the European Commission as well as relationships with the ECB and the Court of Auditors. These key relationships are broadly illustrated in Figure 3 below.

<sup>55</sup> The ESAs share their reports on Risks and Vulnerabilities prepared for their dedicated committees with all relevant EU Institutions, Article 32(3) ESA Regulations, see section 3.4.

<sup>56</sup> See section 1.4.2; for the process of adoption of RTS and ITS see Raptis, p. 64 ff.

**Figure 3: Positioning of ESAs in the EU institutional framework**

Source: Mazars.

**Relationship with the European Parliament:** Since the publication of the de Larosière Report, the European Parliament has sought the creation of an integrated supervisory framework for financial activities in the EU. The European Parliament has been keen to see strong institutions constructed within the ESFS, and this ambition was reflected both in the amendments to the proposed ESA Regulations<sup>57</sup> and the interpretation of the ESAs' objectives. Following the adoption of the ESA Regulations, in addition to its role in the process of RTS adoption and the formal links described above, the European Parliament has had a very keen interest in the ESAs' performance. The ECON Committee has held a number of hearings with the Chairpersons. It has sought to ensure that the ESAs have the ability to deliver their objectives. It has rigorously granted a discharge to the ESAs for the implementation of their budgets. **Our research has not identified any major shortcomings in the relationship of the European Parliament to the ESAs.**

**Relationship with the Council (FSC and EFC):** In addition to formal links described above, the relationships of the ESAs with the Council are more operational and happen at three different levels. The **ESAs (the Executive Directors) are permanent observers of the Financial Services Committee (FSC)**<sup>58</sup> where they provide assessment of financial markets developments at each meeting. The annual report is also presented in the

<sup>57</sup> See documents in the procedure files of the ESAs Regulations; e.g. for EBA: establishment <http://www.europarl.europa.eu/oeil/popups/ficheprocedure.do?id=580463>; discharge 2011 [http://www.europarl.europa.eu/oeil/popups/ficheprocedure.do?lang=en&reference=2012/2207\(DEC\)](http://www.europarl.europa.eu/oeil/popups/ficheprocedure.do?lang=en&reference=2012/2207(DEC)); SSM adjustment [http://www.europarl.europa.eu/oeil/popups/ficheprocedure.do?lang=en&reference=2012%2F0244\(COD\)](http://www.europarl.europa.eu/oeil/popups/ficheprocedure.do?lang=en&reference=2012%2F0244(COD)).

<sup>58</sup> The FSC was set up to provide for cross-sectorial strategic reflection separate from the legislative process; to help define the medium- and long-term strategy for financial services issues; to consider sensitive short-term issues; to assess progress and implementation; and to provide political advice and oversight on both internal and external issues. The FSC works closely with the Economic and Financial Committee (EFC), especially as regards preparing meetings in the Economic and Financial Affairs Council (ECOFIN); see [http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/misc/75677.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/misc/75677.pdf).

FSC along with the priorities of the work programmes. The content of these FSC discussions and any key points resulting from such discussions are conveyed to the **Economic and Financial Committee (EFC)**<sup>59</sup> of the Council. Deliberations on the budget and control of execution are less intense as this main role lies with the European Parliament. The ESAs are **ad-hoc observers of the EFC** and **active members of the bi-annual 'Financial Stability Table'**.<sup>60</sup> In addition to bi-annual risk assessment reports per sector prepared by the ESAs, the Joint Committee produces a policy-focused Report on Risks and Vulnerabilities for the EU Financial Sector for discussion.<sup>61</sup> The most active discussions were focused on the EBA's stress testing of banks and the recapitalisation exercise as well as the ESMA's supervision of rating agencies and the impact of low interest rates on the insurance sector monitored by the EIOPA. This work prepares the informal ECOFIN<sup>62</sup> where the three Chairpersons are invited on an *ad-hoc* basis. They have sometimes been invited to **ECOFIN** meetings, in particular for discussions on the banking stress test and the recapitalisation exercise. As regards the non-objection to the endorsement of RTS, the process is generally conducted by written procedure or in COREPER<sup>63</sup> if there are issues for discussion. Finally, it should be recorded that the Council has not declared an emergency situation during the financial crisis nor it has used its safeguard mechanism.

**Relationship with the European Commission:** The European Commission has played a determining role in proposing the creation of the ESAs, supporting their establishment and active role. But on an on-going basis, the relationship with the European Commission is complex. The ESAs are not accountable to the European Commission, but they do have a close working relationship with its DG Markt. Subject to the agreement of the European Parliament and the Council, the European Commission is the EU institution that adopts and, therefore, gives the force of law to RTSs and ITSs developed by the ESAs. The ESAs provide advice to the European Commission, either in response to a Request for Advice from the European Commission, or on the ESAs' own initiative. As such, the regulatory roles of the ESAs are fully dependent on successful cooperation with the European Commission. This gives the European Commission significant influence in the ESAs' fulfilment of their regulatory responsibilities.

The European Commission also plays a significant role in the ESAs' budgetary processes, not only because it has a voting right in the Management Board on budgetary matters, but because it contributes to the ESAs' funding and carries out internal audits. While there is a clear basis for the European Commission's involvement in this area, the administrative rules applying to the ESAs,<sup>64</sup> and at times the European Commission's interpretation of these rules, impact the operational freedom of the ESAs.

<sup>59</sup> The EFC's preparatory work for the Council of the European Union includes the economic and financial situation, the euro exchange rate and relations with third countries and international institutions. The EFC is an advisory committee that also provides the framework for preparing and pursuing the dialogue between the Council and the ECB; see <http://europa.eu/efc/>.

<sup>60</sup> 'The EFC meets in a specific format, the "Financial Stability Table" twice a year; its composition is then that of a full EFC, "enlarged" to include non-member participants, such as the presidents of Committees specialising in the supervision of the financial sector.', see [http://www.banque-france.fr/fileadmin/user\\_upload/banque\\_de\\_france/Eurosystème\\_et\\_international/04-416\\_Comite\\_economique\\_et\\_financier-GB.pdf](http://www.banque-france.fr/fileadmin/user_upload/banque_de_france/Eurosystème_et_international/04-416_Comite_economique_et_financier-GB.pdf).

<sup>61</sup> For latest report see <http://www.eba.europa.eu/documents/10180/16145/JC-2013-010-JC-RSC-Joint-Risk-Report.pdf>.

<sup>62</sup> See <http://www.consilium.europa.eu/policies/council-configurations/economic-and-financial-affairs.aspx>.

<sup>63</sup> The Permanent Representatives Committee (**Comité des représentants permanents - COREPER** - Article 240 TFEU) consists of the head or deputy head of mission from Member States in Brussels and is responsible for preparing the work of the Council of the European Union, see [http://europa.eu/legislation\\_summaries/glossary/coreper\\_en.htm](http://europa.eu/legislation_summaries/glossary/coreper_en.htm).

<sup>64</sup> In particular the Staff Regulations and the CEOS.

The European Commission also played a crucial role in the selection of the first Chairpersons and EDs of the ESAs. Stakeholders have clearly perceived such close relationship between the ESAs and the European Commission (see Annex, point 7).

**Relationship with the ECB:** The ECB's main relationship is with the EBA, where it attends various meetings, including the Board of Supervisors. The relationship between the ECB and EBA is considered to be constructive.

**Conclusion:** After almost three years, it can be said that the ESAs have progressively found their place in the EU institutional framework, but without yet having fully been able to set their own priorities or allocate to their priorities with complete freedom the resources required to address them.

## 2.2.2. Relationship with the European Systemic Risk Board (ESRB) and the NCAs

**Relationship with the ESRB:** The ESRB is a core component of the ESFS and is responsible for macro-prudential oversight of the financial system within the EU.<sup>65</sup> The ESRB and the ESAs are required to **cooperate with each other and share information of importance to systemic risk across sectors**. To date, the **EBA has had the most active relationship with the ESRB**, reflecting the impact of the banking crisis on both institutions. It is expected that the ESRB will have to broaden its coverage to reflect the need for more analysis of systemic risks in other parts of the EU's financial system.

As members of the ESRB General Board and Steering Committee, the ESA Chairpersons are actively involved in ESRB meetings and decision making. In addition, **ESA staff participates in various ESRB Committees** and working groups at times taking a leading role of specialist subjects. The ESRB Secretariat also participates in the ESA Board of Supervisors meetings and in Standing Committees and Sub-Groups as well as the Joint Committee. In addition to the on-going cooperation via meetings and groups, a key task for the ESAs in the area of **risk and vulnerabilities assessment** is the production of micro-prudential risk assessment reports which are shared with the ESRB to support risk analysis of the wider financial sector.

The ESAs are also **obliged to follow up on warnings and recommendations issued by the ESRB** in relation to systemic risks. The ESRB Secretariat provides specific follow up/progress reporting templates when a recommendation or warning is issued, that ESAs are required to complete and return regularly. To date, ESRB issued five Recommendations, only **three recommendations** have been published affecting an ESA (the other ESRB recommendations addressed NCAs and the European Commission) and **no warnings**. One of the recommendations was issued confidentially to the EBA. All recommendations addressed to the ESAs relate to the banking sector demonstrating the ESRB's work has been dominated by banking issues to date. This is also the perception of stakeholders (see Annex, point 10). A summary of the recommendations and the EBA's response is included in Table 4 below; the full list is provided in the References section. However, the ESAs also have other ways of cooperating and working together with the ESRB beyond their responses to formal recommendations.

<sup>65</sup> See part II study by Oxford Analytica, 'Review of the New European System of Financial Supervision ('ESFS'), The work of the European Systemic Risk Board – the ESFS's macro prudential pillar'.

**Table 5: ESA responses to the formal ESRB recommendations<sup>66</sup>**

ESRB Recommendation	ESA response
<b>ESRB Recommendation of 21 September 2011 on lending in foreign currencies (ESRB/2011/1): Recommendation E, Paragraph 2: Capital Requirements</b> - EBA to address guidelines to national supervisory authorities regarding the capital requirements	The EBA has developed Guidelines on capital measures for lending in foreign currency. <sup>67</sup>
<b>ESRB Recommendation of 22 December 2011 on US dollar denominated funding of credit institutions (ESRB/2011/2):</b> no specific recommendation to the EBA	The EBA has worked to receive further notifications of the data collection funding.
<b>Confidential Recommendation on US-Dollar denominated funding to credit institutions:</b> EBA to engage with NCAs for harmonised reporting of key liquidity ratios of US-Dollar funding (net stable funding ratio and liquidity coverage ratio) ahead of proposed binding technical standards for key liquidity ratio	The EBA has engaged with NCAs and launched a voluntary monitoring of Liquidity Coverage Ratio and Net Stable Funding Ratio in 2011.
<b>ESRB Recommendation of 20 December 2012 on funding of credit institutions (ESRB/2012/2):</b>	
- <b>Recommendation A (paragraph 4 and 5)</b> regarding monitoring and assessment of funding risks and funding risk management by supervisors	Currently working on this recommendation. Guidelines are being produced with the intent that the EBA launches a consultation by end of 2013.
- <b>Recommendation B (paragraph 3 and 4)</b> regarding risk management of asset encumbrance by institutions.	<b>Recommendation B3</b> fulfilled by an ITS under CRD IV/CRR. <b>Recommendation B4</b> will be fully enacted with new reporting templates at a later date.
- <b>Recommendation D (paragraph 1, 2 and 3)</b> regarding Market transparency on asset encumbrance.	Linked to CRR, work starting in the second half of 2013.
- <b>Recommendation E (paragraph 2, 3 and 4)</b> regarding covered bonds and other instruments that generate encumbrance.	The EBA is starting work on this issue with discussion to be launched in the coming months.

**Relationship with the NCAs:** Within the ESFS framework, the NCAs play a significant role. They are in charge of day-to-day supervision of individual financial institutions and securities markets at national level. They also interact extensively with the ESAs: the NCAs hold decision-making authority within the ESAs' Boards of Supervisors, participate and contribute actively in all standing committees, sub-groups and task forces, they second staff or provide temporary staff to work on *ad-hoc* projects (such as the EBA stress test in 2011) and are the **main source of information for the ESAs** for supervisory and oversight matters (such as colleges of supervisors or peer reviews). In summary, the **NCAs exercise key influence on the conduct of the ESAs** (see section 2.1.1) and their participation within the ESAs has improved cooperation between NCAs (see Annex, point 9).

<sup>66</sup> This table relates to formal ESRB recommendations and does not include other types of work between the ESRB and the ESAs.

<sup>67</sup> Consultation closed, see EBA/CP/2013/20, 23 May 2013; [http://www.eba.europa.eu/news-press/calendar?p\\_auth=ePW09UBJ&p\\_id=8&p\\_lifecycle=0&p\\_state=normal&p\\_mode=view&8\\_st\\_ruts\\_action=%2Fcalendar%2Fview\\_event&8\\_eventId=204634](http://www.eba.europa.eu/news-press/calendar?p_auth=ePW09UBJ&p_id=8&p_lifecycle=0&p_state=normal&p_mode=view&8_st_ruts_action=%2Fcalendar%2Fview_event&8_eventId=204634).



Some NCAs consider that the ESAs have lost some of the benefits which accrued from the less formal approach of their predecessors. For example, the CEBS but more especially its predecessor '*Groupe de Contact*' allowed for much **less formal discussion on sensitive issues**, in part because the group had **no decision making or mediation role**. While the NCAs understand the different role of the ESAs, and therefore the need for greater formality, it is thought that the Board of Supervisors in particular has become mechanistic, with the consequence that there is less substantive discussion of supervisory issues.

**Box 3: Access to NCA data, Article 35 ESA Regulations**

Under Article 35 ESA Regulations, an ESA may request an NCA to provide all information necessary to carry out its duties. This information can be requested as required or periodically and in specified formats. In doing so the ESA must take into account any relevant existing statistics produced and sent to the European statistical system and the European System of Central Banks (ESCB). Where the information is not available or not made available by an NCA, the ESA may request this information from other relevant authorities in the Member States or even directly from a financial markets participant. Obligations of professional secrecy apply to such exchanges of information. The ESAs have requested specific data for two main reasons: to assess market developments and systemic risks and to conduct stress tests.<sup>68</sup>

**The main difficulty the ESAs face is the significant differences in quality and consistency of the information received** (provided that information is passed on). This is compounded by the **ESAs lack of ability to validate or challenge key components** of such information. This is due to restrictions on the ESAs powers in the area as well as resource constraints. Significant work to harmonise formats and enhance a common understanding of relevant information is still necessary to enhance the usability of data. So far, dedicated IT systems between the ESAs and the NCAs have been developed only where explicitly requested by sector specific EU legislation.

It should be noted that **NCAs have also challenged the legitimacy of some ESAs requests for information** on the grounds that day-to-day supervision is the responsibility of NCAs. In addition, the interaction between the confidentiality provisions of the ESAs and their obligations to grant access to documents has inhibited NCAs willingness to provide confidential information. ESAs should develop a common understanding with NCAs on these issues to encourage trusted flows of information.

For their part, the **ESAs have not challenged the supervisory or oversight decisions of NCAs**, partly due to limitations in access to data. Naturally, there is a widely shared view amongst NCAs that this is not the ESAs' role. The ESAs are also clear that they were not tasked with this role, unless there is an alleged breach of Union law by an NCA.<sup>69</sup> It does mean, though, that any expectation that the ESAs would become equals, possibly first among equals, with NCAs in the ESFS has not been realised. Instead, a workable balance between the role of the ESAs and NCAs in the oversight of individual financial institutions and securities markets was found within the framework for the current ESA Regulations.

The one exception is Credit Rating Agencies (CRAs). Their direct supervision by ESMA has reduced duplication between Member States and consequently the administrative burden they would otherwise have faced. However, the small number and previous level of national supervision of CRAs might have facilitated this approach.

<sup>68</sup> See sections 3.4.2 and 4.4.1 for details on EBA and EIOPA stress tests.

<sup>69</sup> Although they do have the task to ensure consistency and a level playing field (Recital 11 ESA Regulations).

So far, the **NCA**s have delegated only one task to the **ESA**s under Article 28 of the **ESA Regulations** - the **negotiations of a framework agreement with third country authorities** on a very specific sector (see chapter 5 on the **ESMA**, section 5.3.3).

### 2.2.3. Relation with Third Parties and International Organisations (Article 33, 75 **ESA Regulations**)

The **ESA Regulations** allow for the **ESA**s to enter into administrative arrangements with supervisory authorities, international organisations and administrations of third countries. These arrangements do not create legal obligations in respect of the EU and its Member States. Within the college of supervisors framework, **ESA** representatives have an opportunity to work together with supervisors across the world.

The **ESA**s contribute to the equivalence decisions on third countries regulatory and/or supervisory regimes and have therefore engaged in regular contact with third countries' regulatory and supervisory authorities. Within the **CRA** direct supervision framework, the **ESMA** has formally concluded administrative arrangements with third country counterparties and the **EIOPA** has signed a cooperation agreement with the **World Bank** to foster risk based supervision in the field of insurance. A number of regulatory and supervisory contacts or discussions are held by the three **ESA**s with third country supervisors with a clear priority given to US, Switzerland and China as well as countries subject to a formal **equivalence test**, in particular, Japan, Hong Kong, Singapore, Korea, Australia, United Arab Emirates, Brazil, Mexico, Argentina, Canada, Israel, and Bermuda. In addition, the **ESA**s participate in the European Commission's **Financial Markets Regulatory Dialogue**,<sup>70</sup> including dialogues with the United States, Russia, Japan, Switzerland and Brazil. The **ESA**s have worked with Croatia in the preparation of its formal accession to the EU in July 2013. Representatives of Croatia were invited to the **ESA** Board of Supervisors meetings as observers, and included in the contact list for receiving discussion documents and were also part of selected **ESA** groups and institutional substructures.

Importantly, the **ESA**s have been able to **participate** in a number of working groups or formal or informal international groups of **NCA**s where key policy issues and international standards are discussed (**FSB**, **IOSCO**, **IAIS**, **CPSS**, **BCBS**). **EIOPA** has become a member of the **IAIS** in its own right; the **ESMA** is an associate member of **IOSCO** and **EBA** an observer in the **BCBS**. Such working relationships are crucial to ensuring that the regulatory work of the **ESA** is consistent with global benchmarking and does not create competitive disadvantages for the Single Market. It also contributes to an efficient implementation in the EU of the G20 conclusions and recommendations. More recently, the **EBA** has become directly involved in the oversight of Member States either in the Troika's work on Programme countries, or where specific banking sector measures have occurred under some form of external oversight.

The international profile of the **ESA**s is so far limited to technical and operational matters. **ESA**s have gained a right to contribute alongside the European Commission or **NCA**s in dialogues with key bilateral countries or international organisations. Direct supervisory powers are a key factor which makes it both possible and necessary to more formally establish relationships with third countries and international organisations.

The **ESA**s have therefore taken the necessary steps to become active regulatory and supervisory counterparts of third country supervisors in the global context and tried to become members, observers or contributors in the key international organisations of the

<sup>70</sup> See [http://ec.europa.eu/internal\\_market/ext-dimension/dialogues/index\\_en.htm](http://ec.europa.eu/internal_market/ext-dimension/dialogues/index_en.htm).

respective sectors and scope of action. At this juncture and with the exception of EIOPA (in IAIS), the participation of the ESAs in international organisations are mostly pragmatic and too informal.

When considering the participation of the ESAs in international organisations, one of the key discussion points is how the ESAs would operate compared to NCAs. A shared view is that the ESAs should not replace the NCAs within such organisations, notably because the day-to-day supervision is conducted by the NCAs.

So far, a preferred approach is for ESAs to participate in those international organisations with a different membership status (with the exception of EIOPA that is a full member of IAIS) alongside the NCAs. There is no particular reason for the ESAs to have a different membership status. On the contrary, a participation of the ESAs, on an equal footing, including within the key decision bodies of such international organisations, would reinforce the influence of the EU as a whole.

#### 2.2.4. Accountability, Independence and Transparency

The ESAs are accountable to the European Parliament and to the Council.<sup>71</sup> This accountability is described in detail in section 2.2.1. The ECON Committee is the competent Committee to exercise the accountability role of behalf of the European Parliament. The ECOFIN fulfils this role for the Council. No significant concerns about the capacity of the European Parliament and the Council to exercise their role have been highlighted during research. The ESAs have been transparent and responsive to accountability requests. The accountability regime is well understood by stakeholders (see Annex, point 8).

The ESAs are not defined in the ESA Regulations as independent EU authorities despite their name and have been formally established as EU agencies.<sup>72</sup> The independence of the ESAs is a result of the combination of several provisions of the ESA Regulations.<sup>73</sup> Generally, stakeholders consider that the ESAs are independent from the European Parliament and the Council but not from the European Commission (see Annex, point 5, 6 and 7). When discussing independence, it might be useful to distinguish between budgetary, accountability and tasks-related independence.

Measured against their objectives in the founding ESA regulations, the ESAs have shown a capacity to act with independence. In part, this is a result of their success in navigating complex accountability arrangements - at times when parties to the ESAs decision making process have themselves held conflicting views. It is also a result of the legitimacy that the ESAs have achieved amongst the NCAs. While it is true that this inserts national priorities into the ESAs' decision making processes, it is hard to imagine that the ESAs could achieve a similar measure of independence without the NCAs' support.

It is unanimously considered that the Chairpersons and Executive Director have clearly acted independently and objectively and that the ESAs are progressively finding their place in the EU institutional framework. However, the role of the NCAs in the decision making process in the Board of Supervisors, the role of the European Commission in the definition of the work programmes and regulatory priorities and the budgetary and administrative process have not allowed the ESAs to appear yet as fully independent Authorities.

<sup>71</sup> Article 3 ESA Regulations.

<sup>72</sup> See section 1.4.3. For a detailed description of the application of the Meroni doctrine to agencies as part of the Commission's policy to control their powers, see Kull, D., *Legal Implications of the Establishment of the European Securities and Markets Authority*, Queen Mary, University of London, 8 August 2011.

<sup>73</sup> Articles 1 (5) EBA, ESMA/(6) EIOPA last sentence, 42, 46, 49, 52 and 59 ESA Regulations.

**Independence from the European Commission:** The European Commission funds 40 % of the ESAs's running costs. In addition, the ESAs are required to comply with administrative requirements applicable to all EU institutions. The European Commission is also a source of much of the ESAs' regulatory workload as a consequence of the ESAs' role in the rulemaking process. The volume of requests from the European Commission makes the ESAs effectively sets their priorities and prevents them using resources differently (see Annex, point 7).

Another important issue arising from this relationship is how the European Commission does, or does not involve itself in policy and regulatory decisions. The European Commission's role in the legislative process is unambiguous. However, there have been instances since 2011 when the boundary between the respective roles of the European Commission and ESAs in regulatory and supervisory matters could have been blurred. For example, the EIOPA received a letter from DG Markt raising questions about the calibration of Solvency II draft implementing measure.<sup>74</sup> During the EBA stress test, the European Commission became involved in discussions at the Board of Supervisors about the construction and publication of the test.

**Independence from NCAs.** This is discussed in detail in section 2.1.1.

## 2.3. Establishment and Internal Organisation

### 2.3.1. Organisation of the ESAs

Upon establishment, the ESAs replaced their predecessor bodies and continued the work originally carried out by the Committee of European Banking Supervisors (CEBS), the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) and the Committee of European Securities Regulators (CESR). The newly designed Authorities were built on an already existing, coordinated network of NCAs but it is clear that, from the outset, the ESAs have obtained a status as recognised Authorities and are today much more than a Committee or a network of NCAs.

The ESAs have devoted much of their first two years to developing their internal organisation to carry out their mandate. They subsumed a number of staff members from the predecessor agencies, but new structures articulated around the ESAs' responsibilities required a number of key appointments to lead the key divisions and units. For most of these positions, new persons were recruited, which in itself, reflects the willingness to create *new entities*.

The organisation charts of the three ESAs do not show significant differences apart from the fact that the **EBA and the EIOPA are entrusted with prudential supervisory consistency tasks under their scope of action**. This 'oversight' function is a visible structuring factor. The organisation structure of the ESMA is more open and less hierarchical, reflecting the more varied scope of action with a department exclusively dedicated to direct supervision of CRAs. A detailed presentation of the organisational charts is included in sections 3.1.1, 4.1.1 and 5.1.1 of the ESA chapters below.

<sup>74</sup> Letter from Jonathan Faull of DG Markt, European Commission, addressed to Gabriel Bernardino Chair of EIOPA, 26.09.2012 [http://ec.europa.eu/internal\\_market/insurance/docs/solvency/letter201202\\_en.pdf](http://ec.europa.eu/internal_market/insurance/docs/solvency/letter201202_en.pdf).

### 2.3.2. Recruitment and Staffing

The ESAs follow the employment and Human Resources practices of the **EU Staff Regulations**<sup>75</sup> applicable to European institutions. Positions at the ESAs are open to nationals of the 28 EU Member States and the countries in the European Economic Area (EEA). The ESAs have recruited heavily since their establishment in 2011 and display similar staff structures with the workforce comprised of Temporary Agents,<sup>76</sup> Seconded National Experts (SNEs)<sup>77</sup> and some Contract Staff.<sup>78</sup> The ESAs rely on NCAs' experts to carry out much work through Working Group structures (Sub-Committees, Panels, Groups and Task Forces) (see section 2.3.3. below). There is no particular evidence or opinion to suggest that the location of ESAs negatively impacts on recruitment. So far, positions advertised have always attracted candidates, on average approximately 41 applications are received per position with some differences between the three ESAs, EBA (31), EIOPA (45) and ESMA (46).<sup>79</sup> The ESAs consider, however, that the quality of these applicants varies markedly.

On an annual basis, the ESAs update Establishment Plans (in line with European Commission requirements) estimating the number of additional staff needed to fulfil upcoming tasks set out in the work programmes. The Establishment Plans are appended to the budget submitted to the European Commission each year. An evolution of the headcount in the respective ESAs is illustrated below which is linked with the increase in responsibilities assigned to the ESAs since 2011 and their workload. The table below provides figures for all ESA staff, including temporary agents, SNEs and contract staff (temporary agents in brackets).

**Table 6: ESA head count**

ESA	As at 1.1.2011	As at 31.12.2011	As at 31.12.2012	Planned for 31.12.2013	Planned for 31.12.2014
The EBA	31 (31)	52 (40)	94 (68)	123 (93)	154 (120)
The EIOPA	27 (24)	56 (43)	91 (69)	114 (80)	120 (84)
The ESMA	35 (11)	56 (50)	99 (75)	160 (121)	195 (148)

**Source:** Annual Reports 2011/2012, and Establishment Plans 2013/2014 after submission to the European Commission; in brackets (...): number of temporary agents; **N.B.** 'planned' not necessarily identical to 'draft budget (DB)' requests, see tables below from the Draft General Budget 2014 for the decentralised agencies.

With a few exceptions, market participants consider that the staff recruited by ESA during their first two years of existence have a good level of expertise on regulatory and supervisory matters but are insufficient in terms of numbers. Several NCAs have highlighted the fact that ESAs' staff lack enough seniority.

But beyond the figures, across all three ESAs, staffing issues are a common concern for the following reasons (albeit being common for most institutions within the EU framework):

- **An inflexible administrative framework.** The ESAs observe that their need to follow EU staff regulations hinders their recruitment options. For example, the ESAs must plan their headcount for the coming year via an establishment plan which is submitted to the

<sup>75</sup> Regulation No 31 (EEC), 11 (EAEC), laying down the Staff Regulations of Officials and the Conditions of Employment of Other Servants (CEOS); see link in references; **N.B.** the **CEOS are part II at the end**.

<sup>76</sup> Temporary Agents are employed on the basis of the Article 2 CEOS.

<sup>77</sup> For information on the Seconded National Expert Framework see [http://ec.europa.eu/civil\\_service/job/sne/](http://ec.europa.eu/civil_service/job/sne/).

<sup>78</sup> Contract Agents are employed on the basis of Article 3a CEOS.

<sup>79</sup> Based on number of recruitment campaigns and number of applications received throughout 2011 and 2012.

European Commission for approval. Headcount is based on an estimation of the tasks to be completed i.e. the work programme.

- **Timing mismatch.** The establishment plans constitute an absolute limit for each ESA; no appointment may be made in excess of the limit set. At times this strict limit is difficult to manage within rapidly growing ESAs and has become a problem especially when new tasks and requests are added to the ESAs during the year. It is also at times difficult to estimate the number of staff required early on in the year. During the course of a budgetary year, ESAs have seen their scope of action increased or been confronted with a high number of requests from the EU institutions leading to the need for additional resources not originally contemplated in the establishment plans. In addition, there is often a significant timing gap between the agreement of new tasks and the concrete establishment of a new operational team to carry out this task.
- **Attracting specialised skills and experience from NCAs.** Recruiting expert staff has been difficult due to the fact that the NCAs need similar profiles and, under the Seconded National Expert framework, it is not always attractive for those experts if their own conditions of employment are more favourable. In this case, an ESA is not considered as a significant step in their career and is reflected in their remuneration when they return to their original NCA. At the same time, some NCAs note that ESAs staff recruited directly in the private sector for supervisory purposes is not ideal as it can create a clash of cultures with NCAs experienced supervisory teams.
- **Secondment contracts.** A number of secondment contracts are due to expire in 2013 with renewal subject to confirmation of the long-term need for the job as well as past performance of the individual. Headcount could potentially be reduced and become a problem if the long-term needs for positions do not match headcount.
- **Mix of staff challenge.** The three ESAs have tried to combine staff experience coming from various origins and with different contractual clauses. Broadly speaking, temporary agents were recruited for areas of work that form the core task of the ESAs, the secondment of staff from the NCAs is generally more temporary and related to regulatory activity. Finally, a search for staff from the private sector was conducted for highly technical areas or for newly regulated activities (for which there was no competencies available in the NCAs).
- **EU Human Resources policies.** The ESAs have developed specific Human Resources policies in compliance with the current EU Staff Regulations and procedures. As regards payment and compensation schemes, the ESAs have applied the European Commission rules on payroll and individual rights. However, a general lack of flexibility of the staff Regulation. Such procedures leave limited room to improve efficiency and personnel management. This creates, for example, difficulties where cost of living is not adequately calculated in the EU Rules.
- **Uncertainty.** The future development of tasks and budget is to a certain extent uncertain for the ESAs, especially for the EBA in the context of the SSM (where the ECB has greater budgetary freedom for staff costs) and for the EIOPA in the absence of implementation and application of Solvency II. This is considered to impact the attractiveness of ESAs as places to work.
- **Shortage.** All commentators agree that the ESAs lack the resources to carry out their increasing number of tasks and that this may have inhibited their ability to carry out certain tasks. The solution to this shortage of resources relies fundamentally on the adequacy of the budgetary measures and their expanding role. This issue is analysed further in section 2.3.4.



### 2.3.3. Work Planning and Establishment of Working Groups

The ESAs' activities are driven by the annual work programmes usually agreed in Q3 of the previous year. Multi annual work programmes are also developed covering the two years ahead. The agreed ESA annual Work Programme drives the establishment of a Working Group or the allocation of work under the remit of an established Standing Committees. The objective of a Committee is to assist, advise and support the ESA work in fulfilling their mandates and to contribute to work programmes in specific areas.

#### Work Planning

The annual work programmes of the ESAs describe and summarise the main objectives and deliverables for the forthcoming year. Broadly speaking, the work programmes are structured in a similar manner: a descriptive section describing the key priorities, and a more detailed action plan highlighting the work area, resources and deadlines. Key priorities are based around the regulatory, supervisory, financial stability and consumer protection roles as well as priorities to develop the internal organisation of the young organisations. The ESAs are responsible for developing the work programmes under the leadership of the Executive Director.

The plans are based on tasks specified in the ESA Regulations and in the other relevant EU sector legislation, some of which is still being shaped. Therefore, the majority of the tasks outlined are directly linked to external requests, especially requirements of the European Commission. The ESAs do have the ability to include their own initiatives in the plans, but it is uncertain whether these initiatives will receive proper focus.

The ESAs' work programmes include a long list of actions. For example, the 2013 the work plans include the following number of tasks and priorities: the EBA (91 priority tasks), the ESMA (75) and the EIOPA (150+).<sup>80</sup> It is likely that this extensive number of tasks will be unachievable given the lack of sufficiently available resources, and the likelihood of receiving other ad hoc requests to complete work throughout the year. Concern is expressed amongst the stakeholder community that the ESAs are and will be unable to deliver important work that will benefit the financial services community such as supervisory and financial stability tasks.

#### Standing Committees, Groups, Panels and Task Forces

The work of the ESAs, from development of internal procedures to regulatory and other technical work are carried out through a working group structure made up of Standing Committees, Groups, Panels and Task Forces. These groups report directly to the Board of Supervisors and are comprised of primarily NCA experts, ESA staff and in specific cases, representatives of other ESA staff, the European Commission, the ESRB, the ECB or even third country supervisors. These working groups are generally chaired by the head or a high ranking official of an NCA.

The ESAs have created both permanent and ad-hoc Committees, Groups, Panels or Task Forces. Permanent groups are designed and established for the core regulatory and supervisory areas included in the scope of action of each ESA. Ad-hoc groups are dedicated to specific temporary work and are generally disbanded once their task has been achieved. When establishing permanent groups, the ESAs have tried to mirror the manner in which international organisations in their sector have allocated responsibilities between working groups. In addition, for regulatory work, some committees or groups have created technical consultative groups of stakeholders. There is only one committee whose establishment is

<sup>80</sup> It is difficult to compare the ESAs number of tasks against each other due to differing level of granularity required by mandates. These figures are for illustrative purposes only.

set out in the ESA Regulations, the Committee on Financial Innovation.<sup>81</sup> The three ESAs have also established Review Panels<sup>82</sup> (further discussed in the context of peer reviews in the ESA chapters below).

The technical drafting or preparations of decisions of the Board of Supervisors are elaborated in these groups. The composition of Committees, Groups, Panels or Task Forces reflects therefore the composition of the Board of Supervisors where NCAs play a predominant role. The decision making process of these groups is closely connected to the one of the Board of Supervisors: only contentious issues where no agreement could be reached are elevated for final decision in the Board of Supervisors – without excluding a vote. The specific Committees Groups, Panels or Task Forces and their organisation and functioning are described and discussed further in chapters 3, 4 and 5 below.

#### 2.3.4. Financial Transparency and Budget

The financial positioning of the ESA Regulations<sup>83</sup> is fully in line with the Framework Financial Regulation applicable to EU agencies. This includes the applicable financial transparency rules in particular vis-à-vis the budgetary authorities (the European Parliament and the Council), the Court of Auditors and the general public.

The ESAs' revenues are based on 60 % contributions from the NCAs (with a formula based on the weightings of votes)<sup>84</sup> and 40 % contribution from the general EU budget of the European Commission established for agencies. In addition, the ESMA receives part funding from firms it directly supervises i.e. CRAs, and - in the near future - trade repositories.

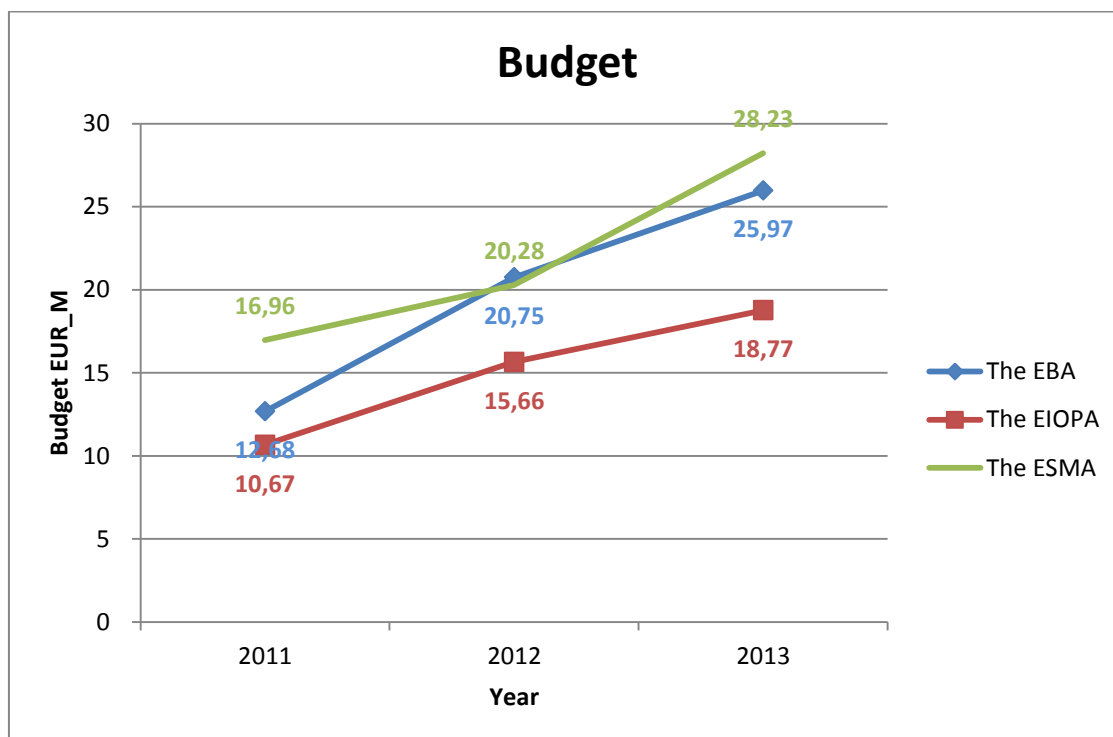
As a general point, it can be noted that the ESAs budgets have been significantly increased during their first three years of existence. In terms of size, the ESMAs budget has increased most significantly over the period (EUR 28.23m in 2013). The EBA budget has doubled in the period and the EIOPA's increased by 75 %.

<sup>81</sup> Article 9(4) ESA Regulations; the aim of the Committee is to '*bring together all relevant NCAs with a view to achieving a coordinated approach to the regulatory and supervisory treatment of new or innovative financial activities and providing advice for the Authority to present to the European Parliament, the Council and the Commission*'.

<sup>82</sup> In the context of Article 30 ESA Regulations, to conduct peer reviews of NCAs.

<sup>83</sup> The budgetary requirement of the ESAs is set out in Article 62 ESA Regulations.

<sup>84</sup> Obligatory contributions by NCAs are calculated in accordance with Article 62(1)(a) ESA Regulations and represent 60 % of the total an ESA annual budget. The amount due is distributed between the NCAs in accordance with a formula based on the weighting of votes of the Member States as set out in Article 3(3) of Protocol (No 36) on transitional provisions. In other words, the NCAs from Member States that have more votes in a Qualified Majority vote under the TFEU are those who contribute more to the financing of an ESA. Across Members States there is variety of models for the financing of NCAs combining contributions (fees) from market participants and/or a contribution from the national budget. This is the reason why national budget restrictions affect the ability of some NCAs to pay their ESA obligatory contribution.

**Figure 4: ESAs budget figures (2011 – 2013)**

**Source:** ESA 2011, 2012 and 2013 budget figures.

With the current funding mechanism any funding increase for the ESAs translates into a funding reduction for the NCAs (in particular for those NCAs that are integrated supervisors contributing to two or three ESAs) and for the European Commission. In light of the increasing number of tasks devoted to ESAs, the current funding arrangement seems to have reached its limit. A number of NCAs have raised the issue of increasing difficulties contributing to ESA budgets due to national austerity measures in some Member States. In addition, the fact that the contribution from the EU is extended from the General budget<sup>85</sup> drafted by the European Commission adds a significant layer of complexity and bureaucracy but could also undermine the independence of the ESAs. For all of these reasons, the ESAs advocate a budget 100 % funded by the EU budget with a distinct budgetary line. It would have the merit of making the ESAs defend their own budget and not the European Commission. The figures for the ESAs as decentralised agencies in the Draft General Budget 2014 part III are as follows:<sup>86</sup>

<sup>85</sup> See European Commission, Draft General Budget 2014, Working Document Part III, p. 9: '*Furthermore, the Board plays a central role in the adoption of the **agency's budget, which is independent from the EU budget. As the decentralised agencies have a separate legal personality, their budgets are published separately in the EU Official Journal, under their own responsibility.***'; [http://ec.europa.eu/budget/library/biblio/documents/2014/DB2014\\_WD\\_III\\_en.pdf](http://ec.europa.eu/budget/library/biblio/documents/2014/DB2014_WD_III_en.pdf).

<sup>86</sup> See [http://ec.europa.eu/budget/library/biblio/documents/2014/DB2014\\_WD\\_III\\_en.pdf](http://ec.europa.eu/budget/library/biblio/documents/2014/DB2014_WD_III_en.pdf); p. 158ff.

**Budget line** 12 03 02 — European Banking Authority

## • Human Resources

Human Resources	2012		2013	2014
	Authorised under the EU Budget	Actually filled as of 31/12/2012	Authorised under the EU Budget	DB request
Establishment plan posts: AD	57	61	84	94
Establishment plan posts: AST	11	7	9	9
<b>Total Establishment plan posts</b>	<b>68</b>	<b>68</b>	<b>93</b>	<b>103</b>
Contract Agents	12	12	15	15
Seconded National Experts	15	14	15	26
<b>Total staff</b>	<b>95</b>	<b>94</b>	<b>123</b>	<b>144</b>

## • Financial Resources

Revenues	2013	2014
	Revenues estimated by the agency	Budget Forecast
EU contribution	10 386 944	11 303 791
Other revenue	15 580 416	16 955 687
<b>Total revenues</b>	<b>25 967 360</b>	<b>28 259 478</b>

Expenditure	2013		2014	
	CA	PA	CA	PA
Title 1	15 277 408	15 277 408		
Title 2	5 608 850	5 608 850		
Title 3	5 081 102	5 081 102		
<b>Total expenditure</b>	<b>25 967 360</b>	<b>25 967 360</b>	<b>28 259 478</b>	<b>28 259 478</b>

**Budget line** 12 03 03 — European Insurance and Occupational Pensions Authority (EIOPA)

## • Human Resources

Human Resources	2012		2013	2014
	Authorised under the EU Budget	Actually filled as of 31/12/2012	Authorised under the EU Budget	DB request
Establishment plan posts: AD	57	57	67	69
Establishment plan posts: AST	12	12	13	15
<b>Total Establishment plan posts</b>	<b>69</b>	<b>69</b>	<b>80</b>	<b>84</b>
Contract Agents	12	14	22	23
Seconded National Experts	8	8	12	13
<b>Total staff</b>	<b>89</b>	<b>91</b>	<b>114</b>	<b>120</b>

## • Financial Resources

Revenues	2013	2014
	Revenues estimated by the agency	Budget Forecast
EU contribution	7 506 988	7 513 976
Other revenue	11 260 482	11 270 964
<b>Total revenues</b>	<b>18 767 470</b>	<b>18 784 940</b>

Expenditure	2013		2014	
	CA	PA	CA	PA
Title 1	10 210 000	10 210 000		
Title 2	4 785 000	4 785 000		
Title 3	3 772 470	3 772 470		
<b>Total expenditure</b>	<b>18 767 470</b>	<b>18 767 470</b>	<b>18 784 940</b>	<b>18 784 940</b>

**Budget line** 12 03 04 — European Securities and Markets Authority (ESMA)

## • Human Resources

Human Resources	2012		2013	2014
	Authorised under the EU Budget	Actually filled as of 31/12/2012	Authorised under the EU Budget	DB request
Establishment plan posts: AD	63	65	106	113
Establishment plan posts: AST	12	10	15	15
Total Establishment plan posts	75	75	121	128
Contract Agents	10	12	25	26
Seconded National Experts	16	12	14	19
Total staff	101	99	160	173

## • Financial Resources

Revenues	2013	2014
	Revenues estimated by the agency	Budget Forecast
EU contribution	8 638 400	9 076 621
Other revenue	19 596 600	20 194 932
Total revenues	28 235 000	29 271 553

Expenditure	2013		2014	
	CA	PA	CA	PA
Title 1	17 464 000	17 464 000		
Title 2	5 825 000	5 825 000		
Title 3	4 946 000	4 946 000		
Total expenditure	28 235 000	28 235 000	29 271 553	29 271 553

In its opinions for the Committee on Budgetary Control on discharge in respect to the implementation of the budget of the ESAs,<sup>87</sup> the European Parliament's ECON Committee called on the European Commission to evaluate the possibility of a proposal entailing ESAs' budgets to be fully funded by the EU budget. It concludes that the current financing of the ESAs with a mixed-financing arrangement is inflexible, creates administrative burden and poses a threat to the Authorities' independence. This is also the view of the IMF.<sup>88</sup>

The proposal to have the ESAs' budget fully funded by the EU budget would have the merit of avoiding the complex relationship with the European Commission, favour a budgetary process and discussion exclusively based on the ESAs' priorities and alleviate NCAs' budgetary difficulties. But in itself this proposal will not bring additional funding.

Since 2012, CRAs (and soon trade repositories) have also contributed to the ESMA's funding but to a limited extent. In 2012, their budget contribution represented close to 15 % of an overall budget. Additional funding by market participants could be an attractive source of revenues for the ESAs without undermining their independence (most NCAs are partially or fully funded by contributions) and under the condition that it does not translate into or needing a duplication of regulatory fees for the industry. Such regulatory fees could be collected by NCAs on behalf of the ESAs.

<sup>87</sup> Opinions of the Committee on Economic and Monetary Affairs for the Committee on Budgetary Control on discharge in respect of the implementation of the budget of the European Securities and Markets Authority for the financial year 2011 (C7-0272/2012 - 2012/2209(DEC), for European Banking Authority for the financial year 2011 (C7-0270/2012 - 2012/2207(DEC) and for European Insurance and Occupational Pensions Authority for the financial year 2011 (C7-0271/2012 - 2012/2208(DEC).

<sup>88</sup> IMF Country Report No. 13/65, March 2013, p. 11.

## 2.4. Communication and Consultation

### 2.4.1. Language (Article 73 ESA Regulations)

Although the ESAs are located in different Member States<sup>89</sup> (and in two of them English is not the official language), all ESAs have adopted English as their working language. It has been generally accepted that English facilitates best the communication in Board of Supervisors and Management Board meetings, in stakeholder and working groups, and amongst the staff at meetings. There are no reported issues in respect of staff concern over the use of English as the working language.

Stakeholders agree that the use of English as the principle language of communication with the stakeholder community facilitates the work of the ESAs and recognises the significant cost and process efficiency impact of translating documents into more than 20 languages (see Annex, point 11). Furthermore, the use of a single language supports better supervisory convergence in the EU as it is the generally accepted language of the financial services industry as well as cross-NCA interaction. However, it is noted that this may put smaller, non-English speaking Member States and their stakeholders, especially consumers and small to mid-sized firms, at a certain disadvantage in terms of interpretation, understanding and ability to participate in consultations.

The ESAs have aimed to address any mis-interpretation by translating consumer warnings into all official EU languages, as was the case for the joint ESMA/EBA consumer warning on Contracts for difference (CFDs).<sup>90</sup> Guidelines and recommendations are also translated for ease of interpretation. There is currently no requirement on NCAs to translate consumer focused documentation into the national language, however if considered necessary, translation is carried out (for example, to contribute to important consultations and impact assessments). However, the time taken by NCAs to translate consultation papers detracts from the overall consultation time and as a consequence smaller firms may not be able to contribute as much as they would like, if at all.

### 2.4.2. Public Consultations

Open consultation and transparency are essential elements of ESA functioning. The ESAs are legally obliged to consult market participants, consumers and the public on draft RTS and draft ITS, guidelines and recommendations. The consultation process is defined in the ESAs Published Statements on Consultation Practices<sup>91</sup> and all ESAs have worked together to align processes where possible. As already mentioned, all consultations are carried out in English.

The ESAs apply the General Principles of consultation of the European Commission participation, openness and accountability, effectiveness, coherence, as well as the minimum standards for consultation.<sup>92</sup> Due to the vast number of draft RTS and draft ITS prepared by the ESAs in the last two years, the level of public consultation has been high, and has also brought to light a number of issues in terms of process, decision making and feedback.

<sup>89</sup> The EBA in London, the EIOPA in Frankfurt and the ESMA in Paris.

<sup>90</sup> <http://www.eba.europa.eu/documents/10180/16136/Investor-warning---CFDs.pdf>.

<sup>91</sup> EBA, Public Statement on Consultation Practices, EBA BS 2012 182 (II) (EBA DC 57- Annex 1), 25 August 2012. EIOPA, Public Statement of Consultation Practices, EIOPA BOS 11 016, June 2011. ESMA, Public Statement of Consultation Practices, ESMA/2011/11, 11 January 2011.

<sup>92</sup> Outlined in Communication from the Commission - Towards a reinforced culture of consultation and dialogue - General principles and minimum standards for consultation of interested parties by the Commission, COM(2002)704.



- Market participants across all sectors have outlined their frustration with the relatively short length of the consultation period and in certain cases, the three month timeline outlined in the General Principles of consultation has not been adhered to by the ESAs leaving participants unable to contribute as comprehensively as possible (sometimes only two to three weeks is provided to respond to an important piece of draft Level 2 legislation), (see Annex, point 12). However, it is appreciated that the ESAs are working against a tough deadline imposed by the European Commission or the legislation.
- There is not sufficient transparency over the number and timing of new consultations in the pipeline due for release over a given period. This inhibits stakeholder's ability to plan ahead for consultations and make resources available.
- After submissions are received, there is not enough transparency over how stakeholder input is taken into account. The ESAs publish high level, collective feedback but many stakeholders, even the ESA Stakeholder Groups themselves, are unsure of the value of their contribution and how their input has been assessed and used (see Annex, point 21). For the Stakeholder Groups in particular, more direct feedback would be beneficial and enhance the working relationships.
- For cross-industry bodies responding to consultations for all ESAs, the lack of a standard consultation template and the varying level of content and scale is different from one ESA to another. More alignment to ensure the same level of accuracy and explanation would be welcomed.
- The sole use of English, as highlighted above, inhibits participation amongst smaller Member States financial communities and small to mid-sized firms.

#### 2.4.3. Public Information

The ESAs are each required to publish and regularly update, information relating to its field of activities and areas of competence, and on registered financial institutions, in order to ensure information is easily accessible by the public.<sup>93</sup> They do so via their websites.<sup>94</sup>

The ESAs' **websites are the important communication tool** for their stakeholders. The level of internal (procedures, decisions, meeting minutes, annual reports, etc.) and external (warnings, consultation papers, reports, discussion papers, etc.) focused information published by ESAs ensures a high level of transparency over the ESAs' work and progress. In general the websites are seen as informative and up to date in terms of content - although they are **different and not aligned** as regards content (e.g. transparency on groups and committees) and structure. However the following issues have been noted (see Annex, point 13 - N.B. the EBA's website has been re-designed during 2013).

- The EIOPA's and in particular the ESMA's websites are **not as user friendly** as they could be. Technical issues (such as bugs and speed) are commonly experienced on the ESMA's website. This has impacted access to certain documents and caused frustration among users.
- Navigation around the EIOPA's website is hindered by the **lack of a document register** to easily locate information. Article 7.1 of the EIOPA's 'Decision of the Management Board concerning public access to documents'<sup>95</sup> of May 2011 states that a document register will be provided on the website to aid access to information. Both the EBA's new website and the ESMA's existing website include a document register.

<sup>93</sup> Article 8 (k) ESA Regulations.

<sup>94</sup> <http://www.eba.europa.eu/>, <https://eiopa.europa.eu/>, <http://www.esma.europa.eu/>.

<sup>95</sup> [https://eiopa.europa.eu/fileadmin/tx\\_dam/files/aboutceiops/Public-Access-\(EIOPA-MB-11-051\).pdf](https://eiopa.europa.eu/fileadmin/tx_dam/files/aboutceiops/Public-Access-(EIOPA-MB-11-051).pdf).

Unlike the ESAs, there is **no requirement for NCAs to re-publish ESA documents** such as recommendations, guidelines, warnings and opinions on their own websites. This raises the question of whether important information reaches the end user such as the consumer. In the case of the joint ESMA/EBA warning on CFDs, the ESAs published the warning on their respective websites as well as directly emailed the warning to hundreds of addresses selected from a large database of media outlets, trade associations, consumer associations and NCAs. The ESAs then monitored take-up in the media but are limited in what they can do to address this issue. Monitoring takes place primarily via web based alert system which informed the ESAs when a document was clicked on, forwarded or mentioned and by who.

Media coverage is also monitored. The EBA noted that two of the banking NCAs reproduced the warning in their own languages and did not deem this satisfactory. They subsequently approached all NCAs and requested them to state explicitly whether, and if so how, they intended to reproduce EBA output in general in their jurisdictions. Ten NCAs confirmed that they would publish EBA guidelines and recommendations on their websites, in the future and eight of them would do so for warnings. This will be monitored. The ESMA has stated that its Communications Team has begun work to further improve interaction between the Authority and the NCA press office network to improve the publication process.

### 3. THE EUROPEAN BANKING AUTHORITY (EBA)

#### KEY FINDINGS

- **The EBA has gained credibility in a highly challenging environment.** The Chairperson and senior members of staff are widely considered to have navigated a complex range of issues and, in doing so, displayed sound judgement. In particular, they have delivered a significant amount of technical regulatory output on the CRD IV package.
- **However, EBA's workload has been dominated by establishment tasks and post-crisis activities: the CRD IV package, the 2011 stress test and the subsequent recapitalisation exercise.**
- **This has had the greatest impact on its consistent supervisory mandate, notably the important areas of supervisory cooperation and peer assessment.** The EBA was given the key task of enhancing cross-border cooperation between supervisors. Although the college process is now improving the way supervisors work together, the EBA lacks the resources needed to develop this system. It has made limited progress in the area of peer reviews.
- **The EBA has been able to make more headway compared to other ESAs in the area of financial stability. However, the 2011 stress test proved challenging as a result of the EBA being granted significant responsibility by the Council without matching resources or powers.** It is broadly acknowledged that the EBA coordinated the stress test effectively in very difficult circumstances. Subsequently, its work on risk weighted assets is considered by NCAs and the industry to have been valuable, and it has also made a positive contribution in the area of recovery and resolution.
- **The EBA has made some progress in the area of consumer protection, but less than some stakeholders would like.** While the EBA's leadership is committed to developing its activities for this mandate, it has faced practical and cultural obstacles that will need to be addressed if progress is to be made in line with stakeholder expectations.
- **In future, the EBA will serve as a bridge between SSM participating and non-SSM participating members, and in this capacity it will be a guardian of coherence in banking regulation and consistent supervision for the EU as a whole.** It will have a key task in ensuring coherence in the common implementation of the **Single Rulebook** in the Single Market, as well as the preservation of common supervisory practices across the EU through the **Supervisory Handbook**. However, the respective roles and responsibilities of the EBA, NCAs and the ECB in the SSM - including in the area of stress tests - still has to be clearly identified.

#### 3.1. Overview

Structures have existed within the EU to promote coordination amongst national banking supervisors on individual financial institutions, and to share supervisory practices since the creation of the *Groupe de Contact* in 1972.<sup>96</sup> Since 1977, and starting with the First Banking Directive<sup>97</sup> on the coordination of the laws, regulations and administrative

<sup>96</sup> See Lannoo, K., 'Supervising the European Financial System', p. 11.

<sup>97</sup> Repealed Directive 77/780/EEC of 12 December 1977, OJ L 322, 17 December 1977, p. 30.

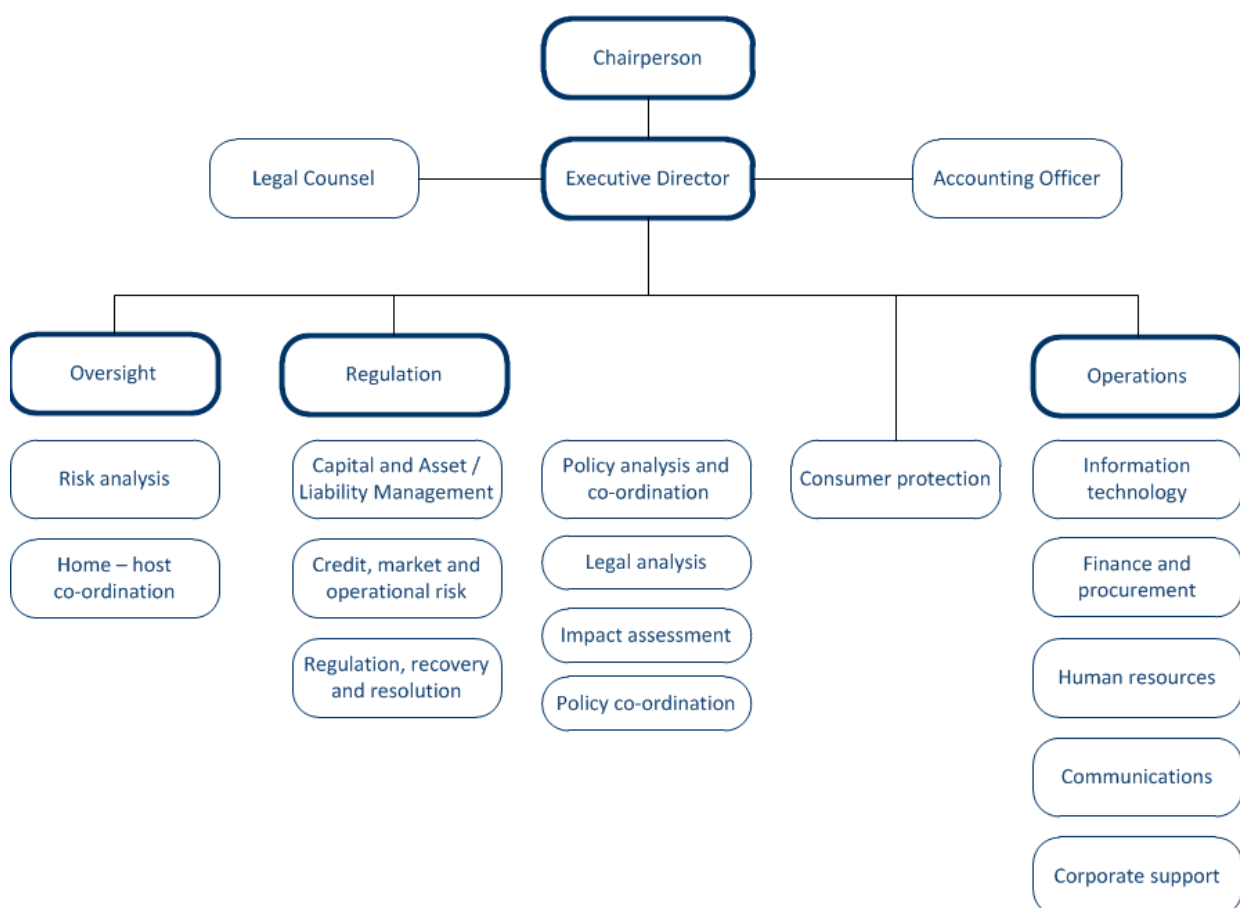
provisions, there has been a parallel legislative and regulatory process, through the Banking Advisory Committee (BAC) and then, from 2004, through CEBS, to harmonise the rules which govern banking and bank regulation in the EU, and achieve common implementation thereof. Finally, through the work of Banking Supervision Committee of the ECB, founded in 1998 and successor to the Banking Supervisory Sub-Committee of the European Monetary Institute, the EU's banking supervisors and central banks sought to identify risks to the stability of the financial system and individual institutions.<sup>98</sup>

The creation of the EBA brought together these three strands - cooperation amongst supervisors; rule-making and implementation; and financial stability as well as financial institution risk assessment – in one Authority. The EBA Regulation gave the EBA important new responsibilities in the area of consumer protection – responsibilities that had not been the focus of its predecessor bodies (or of all its members). In addition to the tasks set out in the EBA regulation, the EBA's responsibilities are derived from other relevant EU banking sector legislation.<sup>99</sup> We have assessed the EBA's performance against the EBA Regulation.

### 3.1.1. Organisation Chart

The EBA is organised according to the delivery of its key tasks:

**Figure 5: Organisation chart of the EBA** (August 2013)



**Source:** The EBA Website (August 2013), updated by Mazars for consistency across ESAs.

<sup>98</sup> See Lannoo, K., 'Supervising the European Financial System', p. 11.

<sup>99</sup> Predominantly the Capital Requirements Directive (CRD), the Capital Requirements Regulation (CRR), the Financial Conglomerates Directive (FICOD), the 3<sup>rd</sup> Anti-Money Laundering Directive (AMLD), the Deposit Guarantee Schemes Directive and the proposed Bank Recovery and Resolution Directive (BRRD), the forthcoming Single Supervisory Mechanism (SSM), and the proposed Single Resolution Mechanism (SRM).

The Chairperson, Andrea Enria, took office in March 2011 and the Executive Director, Adam Farkas, in April 2011 after being appointed by the Board of Supervisors and later confirmed by the European Parliament.

As at 31 December 2012, the EBA had 68 temporary agents, 14 SNEs and 12 contracted agents. It is planned that staff will increase to 123 by the end of 2013 (see also budget figures provided in section 2.3.4. Of the 29 former CEBS staff, 26 transferred to the EBA upon establishment. This includes the Director of the Oversight Department, Head of Policy Analysis and Co-ordination Unit and the Head of the Capital and Asset Liability Management Unit. Other Department Directors and Heads of Units were recruited externally.

In addition to the core organisation structure above, the main standing committees, subgroups, task forces and networks established by the EBA to assist, advise and support the EBA mandate and the execution of the work programmes are included below.

**Table 7: EBA standing committees, working groups, panels and task forces**

EBA Committee / Group	Mandate / Area of Work	Chairperson
<b>EBA Review Panel</b>	Discussed in section 3.3.4	Acting Chair A. Farkas, EBA
<b>Standing Committee on Regulation and Policy</b>	<p>Tasked with the development of binding and non-binding rules on banking, payments and e-money as well as early intervention and bank resolution.</p> <p><b>Subgroups:</b> Own Funds (includes as sub-group: Task force on Unrealised Gains - common with Accounting), Credit risk, Securitisation &amp; Covered Bonds, Liquidity, Operational risk, Governance and Remuneration, Crisis Management, Market risk</p> <p><b>Task Forces:</b> Leverage ratio, Model Validations, Market Infrastructures, Supervisory Disclosure</p> <p><b>Networks:</b> ECAIs</p>	<p>Co-Chairs:</p> <p>D. Rozumek, Czech National Bank (CZ); I. Vaillant, EBA</p>
<b>Standing Committee on Oversight and Practices</b>	<p>Tasked with contributing to supervisory cooperation, including functioning of colleges and joint assessment and decisions, on-going assessment of risks and vulnerabilities, and the establishment of high-quality common supervisory standards and practices.</p> <p><b>Subgroups:</b> Vulnerabilities, Analysis tools, Home-host and colleges, Risk assessment systems under Pillar 2, Implementation and supervisory practices</p>	F. Vargas Bahamonde, Banco de Espana (ES)
<b>Standing Committee on Accounting, Reporting and Auditing</b>	<p>Tasked with contributing to accounting, reporting, auditing and transparency.</p> <p><b>Subgroups:</b> Accounting (include as sub-group: Task force on Unrealised Gains - common with Own Funds), Reporting</p> <p><b>Networks under the Reporting subgroup:</b> COREP, FINREP, Auditing, Transparency</p>	F. Visnovsky, Prudential Supervisory Authority (FR)
<b>Standing Committee on Consumer Protection and Financial Innovation</b>	<p>Tasked with contributing to financial innovation and consumer protection.</p> <p><b>Subgroups:</b> Consumer protection, Innovative products</p>	Dr. A. Kruizinga, Dutch Central Bank (NL)
<b>Impact Study Group</b>	<p>Conducting quantitative impact studies regarding developments in the regulatory framework. The ISG is jointly established by the Financial Stability Committee (FSC) of the ECB and the EBA.</p>	Co-Chairs: E. Loeper, Deutsche Bundesbank (DE); C. Detken, ECB

EBA Committee / Group	Mandate / Area of Work	Chairperson
<b>a) IT Sounding Board* - b) XBRL subgroup</b>	Dealing with pan-EU related IT projects stemming from EU legislation and any other area where the EBA considers it necessary to develop coordinated or common IT solutions.	Co-Chairs: a) P. Mihalik, EBA; b) A. Weller, EBA
<b>Task Force on Consistency of Risk Weighted Assets</b>	Evaluating sources of material differences in RWAs across banks in the banking book and possibly the trading book in order to separate between intended and unintended drivers.	P. Bisio, EBA
<b>Stress-testing Task Force</b>	Developing the methodology for running the 2013/2014 EU Wide Stress Test exercise.	P. Haben, EBA
<b>Joint Committee Impact Assessment Adviser Network</b>	By working with the ESAs' dedicated Impact Assessment teams, the Network assists the ESAs to produce high quality impact assessments that contribute overall to better regulatory decision-making.	S. Dickinson, Prudential Regulation Authority (UK)
<b>ECB/EBA Joint Expert Group on the Reconciliation of Credit Institutions' Statistical and Supervisory Reporting Requirements (JEGRI III)</b>	The JEGRI has developed a classification system to bridge elements of the statistical and supervisory reporting frameworks relating to credit institutions (JEGRI II). In view of forthcoming changes to reporting guidelines, as a result of the CRD IV amendments, as well as potentially relevant changes to statistical or macro-prudential data requirements, JEGRI III will maintain and further enhance the classification system, with the aim to contribute to further reconciliation and the minimisation of reporting costs in the future.	D. Murn, Banka Slovenije (SL)

**Notes:** As of July 2013. The EBA's website does not contain specific sections or information on EBA Standing Committees. \*IT Sounding Board (ITSB) is the successor of the 'Committee on Operations and IT' since end 2011.

### 3.1.2. Specific Budget and Financial Transparency Matters

The EBA budget has more than doubled from EUR 12,683,000 (2011) to EUR 25,967,360 (2013).<sup>100</sup> Expenditure has not been in line with budget projections as highlighted below.

**Table 8: Expenditure of the EBA**

	2011		2012		2013
EUR	Budget	Actual	Budget	Actual	Budget
Staff	6,634,000	5,810,458	10,908,000	9,159,709	15,277,408
Infrastructure/administration	3,259,000	1,859,310	4,137,000	3,673,433	5,608,850
Operational	2,790,000	1,384,253	5,702,000	5,547,200	5,081,102
<b>Total</b>	<b>12,683,000</b>	<b>9,054,030</b>	<b>20,747,000</b>	<b>18,380,343</b>	<b>25,967,360</b>

**Source:** EBA published budget figures.

The European Parliament's ECON Committee has noted that the EBA 'spent only part of the appropriations entered in the 2011 budget and infers from this that there have been problems with budget planning and implementation, preventing some core goals from being

<sup>100</sup> The initial and amended budgets and the accounts of the EBA are published on the EBA website along with the Decision of the Management Board on the Financial Regulation of the European Banking Authority of March 2011 <http://www.eba.europa.eu/about-us/budget-and-accounts>.



achieved; any further repetition of such outcomes should be averted'.<sup>101</sup> It also voiced the widely held view that current financing arrangement of the EBA is '*inflexible, creates administrative burden, and poses a threat to the agencies' independence*'. This is discussed in more detail in section 2.3.4 above as it is a matter of concern for all ESAs.

### 3.2. Assessment of Regulatory Work

The EBA's main task has been to **progress the Single Rulebook for banking**. The Regulation Department is responsible for regulatory work.<sup>102</sup>

#### 3.2.1. Scope of Regulatory Work and Contribution to the Single Rulebook: the CRD IV package

The CRD IV package, which comprises the new Capital Requirements Directive 2013/36/EU (CRD IV) and the Capital Requirements Regulation (EU) No 575/2013 (CRR), implements Basel III in the EU. This new legislation is a key component of the Single Rulebook and an important post-crisis reform of the EU framework for banks. As a consequence, it has driven most of the EBA's regulatory work and placed significant demands on the EBA.

These demands have been practical: there has been limited time to respond to, and consult on, the mandates given by the European Commission. They have also been technical: the content of certain Level 1 legislative mandates has made it challenging for the EBA to prepare the resulting draft implementing measures. Specifically, EBA has received mandates which have been ambiguous or unclear which has led to the preparation of associated draft technical standards being more challenging than anticipated. The CRD IV package is complex. The EBA is a repository of technical knowledge but it is unclear how this knowledge has been utilised effectively during the legislative process to the benefit of all parties. Another challenge has been the development of advice on delegated acts and draft technical standards before the final adoption of the Level 1 legislation. Sometimes agreements reached by the EBA by qualified majority voting (QMV) were contradicted by a decision in the Council giving privilege to decision by unanimity. Table 9 illustrates the level of work for the Single Rulebook.

**Table 9: Regulatory measures of the EBA**

Category	CRD III	FICOD	EMIR	CRD IV	CRR	Prop. BRRD	Other	Total
Advice on delegated acts		1						<b>1</b>
RTS		2	1, <b>1</b>	<b>3</b>	16, <b>17</b>	<b>3</b>		<b>43</b>
ITS			<b>2</b>	<b>4</b>	7, <b>8</b>			<b>21</b>
Guidelines	8, <b>1</b>				<b>1</b>		<b>1</b>	<b>11</b>
Recommendations						1	4 (+1*)	<b>6</b>
<b>Total</b>	<b>9</b>	<b>3</b>	<b>4</b>	<b>7</b>	<b>49</b>	<b>4</b>	<b>6</b>	<b>82</b>

**Source:** EBA website (as of July 2013); **Notes:** **Black** - Measures finalised and adopted. **Red** - Measures currently under development (subjected to public consultation); \*Agreement on a Recommendation.

<sup>101</sup> Opinion of the ECON for the Committee on Budgetary Control on discharge in respect of the implementation of the budget of the EBA for the financial year 2011 (C7-0270/2012 – 2012/2207(DEC), p. 13.

<sup>102</sup> With 23 staff, approximately 30 % of the total staff, dedicated to this area.

### 3.2.2. Opinions: ten prepared to date

The EBA has contributed to Level 1 legislation to the wider policy debate on banking by means of letters and opinions to the European Parliament, the Council and the European Commission on key regulatory matters. These have included opinions in the area of shadow banking, central counterparties, consumer protection and technical regulatory capital matters.

The EBA has an important role by contributing to policy debates and providing opinions. It has been active in fulfilling this role with many non-public contributions, sometimes in the form of letters from the Chairperson, supplementing the public opinion. While it is difficult to measure the effects of these contributions, in general stakeholders attach importance to the EBA's outputs.

## 3.3. Assessment of Supervisory Work

The context for the EBA's supervisory role of ensuring consistent supervisory practices at a national level has been challenging. The crisis has caused cooperation and trust between banking supervisors to decrease because of inherent conflicts of interest between home and host stakeholders, and banks – sometimes under pressure from national supervisors and/or governments – have reduced cross-border activity in the EU.<sup>103</sup> Although the EBA was created to promote greater cooperation between supervisors, in practice it had to lean against a trend towards more national decision making, the reasons for which were identified in the early stage of Europe's financial crisis.<sup>104</sup>

### 3.3.1. College of Supervisors: a good start, but a lot is still to be achieved

Colleges of supervisors combine NCAs of cross-border banking groups (and, in some cases, third countries) to coordinate supervisory activities. Colleges have a role in fostering information exchange between home and host authorities to support planning and performance of key supervisory tasks and in the preparation for and the handling of crisis situations. The EBA's<sup>105</sup> role in the college environment is to develop best practices by knowledge transfer, challenging regulated firms' cross-border structures and identifying risks, mediating disagreements between NCAs and ensuring effective emergency plans are in place. It is both a full member of all colleges and a policy setter.

Of more than 80 supervisory colleges that are established in the EEA, the EBA has focused on 40 '**priority**' colleges established for the supervision of the largest EEA cross-border banking groups. While the college process has gradually become more effective, it is not yet as effective a mechanism for supervisory coordination as the EBA, NCAs nor the industry would like.

- While there is strong support among NCAs for the principles of the college process, as college practice requires NCAs to pool supervisory sovereignty there has been some hesitation to fully embrace the process.
- In 2011 this was particularly true in cases where an individual bank's financial strength was uncertain and public monies may have been required. In these cases, the perceived need of NCAs to protect national depositor and/or fiscal interests sometimes took precedence over supervisory cooperation. In at least one case, the EBA was not made aware of a major supervisory matter.

<sup>103</sup> See Milesi-Ferretti, G.-M. and Tille, C., p. 297-298.

<sup>104</sup> See Lord Turner Review, p. 100-102.

<sup>105</sup> The EBA's role is outlined in Article 21 EBA Regulation.

- Latterly, there has been increased acceptance amongst NCAs of the college process, and the EBA has been actively involved in colleges to resolve important cross-border supervisory issues.
- A key factor contributing to greater engagement with colleges has been the carrying out of the joint assessment cycle<sup>106</sup> (developed by CEBS via Guidelines to assist the consolidating supervisor and supervisors of subsidiaries involved in the supervision of an EEA cross-border banking group to reach a joint decision on the application of the Pillar 2 provisions related to the Internal Capital Adequacy Assessment Process (ICAAP) and to the Supervisory Review and Evaluation Process (SREP) under the CRD). This process increases contact between NCAs, and it involves them in meaningful discussions of risk and risk mitigation.
- From an industry perspective, there is some disappointment that the colleges are yet to deliver either a higher standard of coordinated supervisory activity, or to secure greater efficiency in the supervisory process by removing duplicative requests or activities by NCAs. In this respect, the college process is not yet analogous to a supervisory process in its own right. In time, though, the introduction of the SSM will likely lead to a further evolution of practice in this area, at least for colleges where the SSM is home supervisor.

The key issue today is the EBA's ability to support the extension of the college process to a larger number of banks, and to deepen the effectiveness of existing colleges. There is a widely held view that colleges are most effective when the EBA representative has supervisory experience: this allows the EBA to engage in discussion of supervisory issues, and gives it the credibility to influence college decisions or settle disagreements between NCAs. It is recognised, however, that the EBA does not have these resources in sufficient quantity. The college process will not evolve unless this issue is addressed.

The second key issue is the EBA's ability to use its binding mediation power to settle disagreements between NCAs. To date, the EBA has not used its formal mediation procedures<sup>107</sup> to bind the college participants. Instead, it has adopted a less formal approach by pursuing reconciliation initiatives outside the scope of the EBA Regulation. This happened, for example, when the proposed unilateral implementation of macro-prudential measures by one Member State was judged to have a negative impact on a cross-border bank from another Member State. While this approach has largely been successful, the EBA itself considers that there is ambiguity about when and how the formal binding mediation power can be used. As this weakens the EBA's position, and therefore its ability to supervise the college process, this issue needs to be addressed. The EBA has also used Non-Binding mediation procedures<sup>108</sup> for some NCAs too.

### 3.3.2. Delegation of Tasks

No tasks have been delegated to the EBA by NCAs as allowed by the EBA Regulation.<sup>109</sup> It is unlikely it will happen in the future as the SSM creates a powerful supervisory institution, representing the majority of Member States. It is unlikely to want to cede tasks to the EBA.

<sup>106</sup> For details on the process see CEBS Guidelines for the joint assessment of the elements covered by the supervisory review and evaluation process and joint decision regarding the capital adequacy of cross-border groups (GL 39), 22 December 2010.

<sup>107</sup> The EBA's binding mediation role is set out in Article 19 EBA Regulation.

<sup>108</sup> See section 2.3.5.

<sup>109</sup> Article 11 EBA Regulation.

### 3.3.3. Common Supervisory Culture

The EBA has a mandate to assist in the building of a common EU supervisory culture, developing consistent supervisory practices and ensuring uniform procedures and approaches.<sup>110</sup> This is important not only in ensuring supervisory practices promote adequate soundness but also because an uneven approach to supervision in the EU could facilitate regulatory arbitrage. In such a situation banks could choose to locate operations or conduct activities in Member States with a more accommodating supervisory regime, leading to a failure to control properly the resulting prudential or conduct risks. Equally, if one Member State considers that another is not operating the right standards, it could take measures designed to protect its national banking system and customers. This would, by definition, impact the operation of the Single Market.

The EBA has undertaken work to achieve this mandate, including the construction of a common supervisory reporting framework for NCAs designed to make it easier for banks to submit data and for supervisors to monitor individual banks and compare them with EU peers. It also provides training to NCAs to promote common practices and culture.

The next key step is the development of the common EU **Supervisory Handbook**, proposed when the SSM was announced on 12 September 2012.<sup>111</sup> This is important because although all NCAs maintain formal procedures for the supervision of financial institutions, typically informed by a common set of principles,<sup>112</sup> the procedures and practices vary between NCAs. This introduces a very practical obstacle to the harmonisation of common supervisory practices and culture and affects supervision in the ESFS. It also impacts banks operating across Member States. Evidence from the crisis also suggests that the strength or otherwise of supervisory practices had a significant bearing on the magnitude of financial sector stress and, in some cases, contributed to individual bank failures.<sup>113</sup> The Supervisory Handbook would, as a minimum, define a base level of common procedures to be adopted in all Member States. There is disagreement about the level of detail these procedures should contain, as well as the degree of harmonisation in the actions which supervisors take to implement these procedures. These issues will need to be addressed in the design of the Supervisory Handbook.

There is also now a question as to whether there will be *one* EU-wide supervisory handbook. The ECB has indicated that it will develop its own **ECB supervision manual**.<sup>114</sup> Although the ECB has been keen to stress that this will be consistent with the **EBA handbook**,<sup>115</sup> there is a risk that differences could emerge between SSM and non-SSM supervisory practice (differences possibly compounded by the maintenance of equivalent sub-EBA handbooks or manuals in non-SSM Member States). If the EBA, ECB and non-SSM NCAs' handbooks are fully consistent, this should not in principle be a barrier to the harmonisation of supervisory practice and culture. However, it would seem more likely that the intended purposes of an EU-wide supervisory handbook will be achieved if there is a single EU handbook rather than multiple texts. Equally, there is good evidence to suggest that regulatory arbitrage is likely to be reduced if a truly common set of standards is

<sup>110</sup> Article 29 EBA Regulation.

<sup>111</sup> European Commission, Communication from the Commission to the European Parliament and the Council, 'A Roadmap towards a Banking Union', COM(2012)510, 12 September 2012.

<sup>112</sup> The Basel Committee on Banking Supervision, 'Core principles for effective banking supervision - revised version endorsed by global bank supervisors', September 2012.

<sup>113</sup> See example in Honohan, P., 'The Irish Banking Crisis, Regulatory and Financial Stability Policy, 2003-2008, A Report to the Minister for Finance by the Governor of the Central Bank' May 2010, p. 7.

<sup>114</sup> Constâncio, V., Vice President of the ECB, 'Establishment of the Single Supervisory Mechanism; the first pillar of the Banking Union', Speech 31 January 2013.

<sup>115</sup> Constâncio, V., Vice President of the ECB, 'Public Hearing on Financial Supervision in the EU', Speech, 24 May 2013.

agreed and enforced.<sup>116</sup> Failure to produce this result could also mean that subsidiaries located across 'handbook borders', and there will be a significant number of them, will not benefit from a single Supervisory Handbook.

### 3.3.4. Peer Reviews: two reviews currently in progress

The EBA is responsible for carrying out periodic peer reviews of the effectiveness of supervisory activities of NCAs<sup>117</sup> with those of their peers. The objective of the EBA peer review process is to achieve greater consistency in supervisory outcomes. In doing so, the EBA is required to assess the adequacy of competent authorities' resources, their governance arrangements, the degree of convergence in the application of European laws, and supervisory practice. The EBA established its Review Panel in May 2011. In June 2012 it adopted a methodology for conducting peer reviews.<sup>118</sup> The EBA's Board of Supervisors is currently undertaking two peer reviews on stress testing and concentration risk which are scheduled to finish over the course of 2013.

The value of this type of comparative work has long been recognised internationally, and is enshrined in such processes as the IMF Article IV and Financial Sector Assessment Programme (FSAP) processes.<sup>119</sup> The financial crisis has led to a broadening and deepening of peer review processes internationally.<sup>120</sup> Within the EU, a number of shortcomings in supervisory practice, structures and resources have been identified through these international processes. Although these issues pre-date the EBA's creation, the more intensive use of peer reviews, at an earlier stage, could have fostered improvements in supervisory practice. A more rigorous EU peer review process, in which NCAs worked together, might have encouraged EU's fledgling system of harmonised banking supervision to develop more quickly. More obliquely, a joint and public effort to raise standards could have worked to increase confidence in the EU's willingness to work together, but also to expose and possibly address a shared set of banking sector problems. This was tried in a small way in Ireland to re-build confidence.<sup>121</sup> However this was an exception. Instead, Member States have commissioned their own reviews of their own national banking supervision arrangements.<sup>122</sup> This is not the EBA's fault. However, the under-utilisation, as well as the late commencement, of the peer review process could be seen as a missed opportunity for the EU to set its own supervisory house in order in a coordinated way.

### 3.3.5. Mediation: progress but no binding mediation procedures to date

The EBA has received two formal requests for non-binding mediation, both started as investigations into alleged breach/non-application of Union law (as noted in section 3.3.6), and both related to home/host unilateral measures concerning ring fencing liquidity and/or capital. There was a further case stemming from an EBA investigation of alleged breach of Union law in 2012, and the involved parties opted to explore other reconciliation measures. One case was mediated successfully by the EBA, the other is currently on-going. The successful mediation resulted in the involved parties agreeing to a written agreement, and the second was closed after one party did not put forward any allegations towards the other

<sup>116</sup> Discussed in Quaglia, L., 'Financial regulation and supervision in the European Union after the crisis', 2013.

<sup>117</sup> The EBA's role is outlined in Article 30 EBA Regulation.

<sup>118</sup> Proposed EBA Review Panel Methodology for the Conduct of Peer Reviews, EBA BoS 2012 107, 24 May 2012.

<sup>119</sup> For an analysis of the lessons from the FSAP process see Eijffinger, S. and Masciandaro, D., *Handbook of Central Banking, Financial Regulation and Supervision*, 2011.

<sup>120</sup> FSB peer review documents, see for an overview [http://www.financialstabilityboard.org/list/fsb\\_publications/tid\\_176/index.htm](http://www.financialstabilityboard.org/list/fsb_publications/tid_176/index.htm).

<sup>121</sup> The Central Bank of Ireland, *The Financial Measures Programme Report*, Ireland, March 2011 p. 13.

<sup>122</sup> For example, *Independent Commission on the Future of the Cyprus Banking Sector, Interim Report*, Cyprus June 2013.

party and was in agreement with the measures taken by the latter. This non-binding mediation has been seen as a breakthrough in terms of EBA's mediation role. The EBA has since been contacted by a number of other NCAs regarding potential non-binding mediations. The EBA has also launched an own initiative mediation where progress is on-going.

In comparison, the EBA's role in the settlement of cross-border disagreements and mediation<sup>123</sup> appears limited due to the perceived imprecise nature of the EBA Regulation which makes the EBA's powers, as well as the triggers for binding mediation, uncertain both to the EBA itself as well as NCAs. For this reason, there have been no instances where binding mediation powers have been used.

### 3.3.6. Breach of Union law: two investigations launched on ring-fencing measures

The EBA launched two own-initiative EBA investigations on breach of Union law (Article 17 EBA Regulation) in October 2012. Both concerned the imposition of national bank ring-fencing measures. One of the cases was settled on the basis of a request for non-binding mediation. The other was closed following discussion with the NCAs concerned.

Although the EBA has identified further potential breaches, it considers that a lack of specificity in Article 17 EBA regulation makes it difficult to pursue investigations. In one particular instance, the EBA suggested that the application of a national law conflicted with EU law and departed from international standards. However, the EBA determined that the structure of this law negated the EBA's ability to challenge it under the founding regulation. This is an area where the EBA's founding regulation needs to be reviewed to establish the operability of its powers. However, the recent decision by the Joint Board of Appeal provides helpful clarifications (see section 6.2.2).

## 3.4. Assessment of Financial Stability Work

The EBA is required to monitor developments in financial markets and test the resilience of individual financial institutions and the EU financial system as a whole.<sup>124</sup> In this capacity, and working together with the ESRB and other ESAs, the EBA's function is to act, after NCAs, as a distinct and independent line of defence within the ESFS against financial sector risks. The work conducted by the EBA to date is summarised below.

### 3.4.1. Identification and response to systemic risk

The EBA uses a range of tools to fulfil its systemic risk identification responsibilities. These include:

- **Key Risk Indicators (KRIs).** The EBA collects items of information which, considered in their own right and together, could provide early warning of potential risk events. The KRIs are reported quarterly by NCAs and cover 57 banks from 20 EEA countries.
- **Risk dashboard.** Using the information gathered for the KRIs, the EBA produces a quarterly dashboard summarising the state of the EU banking sector. This is designed to inform discussion of risks, and, if judged necessary, lead to further research and/or supervisory or policy interventions.
- **Risk and Vulnerabilities Reports.** Article 32(3) EBA Regulation requires the EBA to produce annual reports on risks and vulnerabilities of the European banking sector which describes the main developments and trends that affected the EU banking sector in a given year and provides the EBA's outlook on the main micro-prudential risks and vulnerabilities in the future. Together with the other ESAs, it also contributes to the Joint

<sup>123</sup> Article 19 and 31 EBA Regulation.

<sup>124</sup> Specified in Article 23, 24 and 32 EBA Regulation.



Committee cross-sectoral risk and vulnerabilities reports, which are provided to the ESRB and the Economic and Financial Committee (EFC).<sup>125</sup>

The frequency and quality of individual NCAs' market oversight work varies significantly within the EU.<sup>126</sup> Although the EBA's work is not equal in quality to the best-in-class produced at a Member State level, it is considered of sufficient quality and frequency to add value to the risk assessment process within the ESFS. It serves two important purposes. It facilitates discussion of risk amongst NCAs, albeit the EBA Board of Supervisors has not been able to spend significant time doing so. Most important, it creates the opportunity for supervisory or policy responses where these would be merited.

### 3.4.2. Stress Testing the Banking Sector

The 2011 stress test has been the EBA's most significant and most public action. In 2010, the EBA's predecessor, CEBS, conducted a stress test of 91 EU banks.<sup>127</sup> Following the exercise, heightened market uncertainty about the worsening position of euro area banks and sovereigns, particularly for countries in an external support programme, created significant pressure for a test which might restore confidence in the EU banking sector. This led the EBA to commence preparations for its test in early 2011 which is mandated in the EBA Regulation.<sup>128</sup>

In the period leading to the test, expectations of what it might achieve were raised, largely because of the market pressures at that time. This pushed the issue of the publication of the results to the fore. There was significant discussion amongst EBA members of the pros and cons of different publication scenarios. It was finally decided that the test's ability to influence confidence in the EU banking sector was best served through disclosure and the announcement of higher capital requirements (and other adjustments) to meet, at least in part, the outcomes of the test.

From the start there was a gap between the expectations for the test and the EBA's powers and capabilities to address them:

- The EBA did not perform the test. This was done by NCAs, who also had direct contact with banks, which the EBA did not because it lacked the legal authority to perform the test itself.
- The EBA also faced significant logistical challenges in overseeing the test. There were approximately 5000 data points to manage for each bank in the sample. This was performed using an off-the-shelf spread sheet package (MS Excel). This created problems of data storage. It also left very little time for the EBA to interrogate the meaning of the data because a significant effort was required to construct and manage what proved an unwieldy, non-bespoke software tool.

<sup>125</sup> To access risk reports <http://www.eba.europa.eu/risk-analysis-and-data/risk-assessment-reports>.

<sup>126</sup> For a comparative analysis of international, including EU, financial stability reports, see Čihák et al., *Financial Stability Reports: What are they good for?*, IMF Working Paper No.12/1, Washington, 2012.

<sup>127</sup> See CEBS'S Press Release on the Results of the EU-wide Stress Testing Exercise, 1 October 2009, <http://www.eba.europa.eu/documents/10180/15977/CEBS-2009-180-Annex-2-%28Press-release-from-CEBS%29.pdf>; CEBS'S Press Release on the Results of the 2010 EU-wide Stress Testing Exercise, 23 July 2010, <http://www.eba.europa.eu/documents/10180/15938/CEBSPressReleasev2.pdf/4a5b185f-43bf-4e4d-b1de-c50c7e656b87>; EBA 2011 EU-wide Stress Test Results, <http://www.eba.europa.eu/risk-analysis-and-data/eu-wide-stress-testing/2011/results>.

<sup>128</sup> Article 23(1) EBA Regulation.

### 3.4.3. Outcomes of the Stress Test: recapitalisation exercise

The main outcome of the test, and consistent with its stated purpose, was to start a process through which the capital position of EU banks was strengthened. This objective was pursued iteratively during 2011.

- In July 2011, at the time the stress test results were published, the EBA issued a recommendation<sup>129</sup> to NCAs that certain banks be required to take steps to strengthen their capital position.
- In October 2011, the EBA announced that banks would be required to put in place a temporary capital buffer against sovereign debt exposures.<sup>130</sup>
- In December 2011, the EBA confirmed the October recommendation and additionally required banks to establish an exceptional and temporary buffer such that the Core Tier 1 capital ratio reached a level of 9 % by the end of June 2012.<sup>131</sup>

Based on its own calculations, the EBA exercise has led to an increase in capital of EU banks of EUR 200bn.<sup>132</sup> Some of the lessons of the 2011 stress test are included below.

- **Co-ordination ex-ante between the entity performing the test and those taking the decision on how to respond to the results is critical.** A consistent weakness in the EU crisis management framework has been the absence of any certainty about what backstop measures will be taken to address losses identified during a stress test or similar diagnostic evaluation, as well as the possible fiscal consequences of any measures. In 2011, the test occurred without there being a clearly identified set of actions to address the results. This was of particular significance at that time for NCAs with large banking sector problems. For these countries, the results of the test had the potential to affect sentiment towards their banks. It also had the potential to create additional fiscal pressures for Member State governments, and thus add to Sovereign financing challenges.
- **The scenarios which underpin a stress test need to be credible.** An observable problem of the 2011 test was that elements of the test were considered not to have taken full account the realities of the economic and fiscal situation then facing a number of Member States. The most notable problem was the decision – later reversed – not to reduce the value of the sovereign debt holdings of banks to reflect market judgments at that time.
- **Power, resources and expertise available for the test.** In 2011, the EBA was, in practice, only resourced and empowered to coordinate a test performed by NCAs, and even then only thinly resourced. It could not interrogate the results itself in any depth. In consequence, its ability to safeguard the integrity of the test, as well as its ability to assess NCA performance consistent with its wider objectives for supervisory convergence, was impaired.
- **The measures used to assess a bank's financial strength need to be credible.** A necessary condition for a credible stress test is that the benchmarks against which a bank will be assessed are robust. In 2011, the EBA made some progress in this area by establishing a definition of Core Tier One capital better aligned to Basel III and changed

<sup>129</sup> EBA 2011 EU-Stress Test, Aggregate Report, 15 July 2011.

<sup>130</sup> EBA Capital buffers for Addressing Market Concerns Over Sovereign Exposures Methodological Note, 26 October 2011.

<sup>131</sup> EBA Recommendation on the creation and supervisory oversight of temporary capital buffers to restore market confidence (EBA/REC/2011/1), 8 December 2011.

<sup>132</sup> EBA Risk Assessment of the European Banking System, January 2013, p. 6.

market expectations on bank capitalisation. Equally, the establishment of the pass/fail threshold of 5 %<sup>133</sup> provided a sounder basis for the test than that applied in 2010.

- **Information about the quality of assets and the quality of information about asset values.** On 16 May 2013, the EBA recommended that NCAs conduct asset quality reviews to address concerns about the impact of macroeconomic conditions on asset quality.<sup>134</sup> This work is important as information about assets is a basis for the capital calculations performed in a stress test. As such, confidence in a stress test can be enhanced if NCAs have first sought to establish, independent of a bank and its auditors, whether the basis for asset values is sound. In practice, this means understanding whether potential losses, and thus future capital needs, have been estimated with sufficient prudence. Such a process can also reveal whether a bank has gaps in its information about its assets which might cause a supervisor to make further adjustments to information used in a stress test. In 2011, only a handful of NCAs possessed this information, and the EBA had little, if any, line of sight on asset quality and the reliability of information on assets included in the test.
- **The form and quality of publication.**<sup>135</sup> The discussion about whether or not stress test results in 2011 should have been published obscured a more important set of questions which needed to be addressed in the design of the test: Why information might be disclosed publicly? What information should be disclosed? How it could be disclosed? When this should happen? While the test did lead to the publication of significant data on individual banks, the EBA was not given the time to consider issues of publication neither in depth, nor to prepare a set of more detailed accompanying disclosures which might have better informed analysis of the results.

#### 3.4.4. Study of the Consistency of Risk-Weighted Assets

After finalising the 2011 EU-wide stress test and the recapitalisation exercise, the EBA commenced work to understand apparent variations in risk-weighted asset calculations, and an interim report was published in February 2013.<sup>136</sup>

The majority of stakeholders consider this report to have been both timely and valuable. Recently, supervisors in the UK and Denmark requested banks to raise additional capital to address suggested shortcomings in risk-weighted asset calculations.<sup>137</sup>

#### 3.4.5. Action in Emergency Situations: voluntary code of conduct issued to NCAs

The EBA Regulation gives the EBA a role in dealing with the risk of, and an actual, emergency situation.<sup>138</sup> Specifically, the EBA must facilitate and, where deemed necessary, coordinate any actions undertaken by the relevant NCAs. The EBA's ability to perform such a role remains untested. The EBA's power in this area depends on the declaration of such an emergency by the Council. To date, the Council has neither considered nor declared an emergency.

<sup>133</sup> <http://www.eba.europa.eu/-/the-eba-announces-the-benchmark-to-be-used-in-the-2011-eu-wide-stress-test>.

<sup>134</sup> <http://www.eba.europa.eu/-/eba-recommends-supervisors-to-conduct-asset-quality-reviews-and-adjusts-the-next-eu-wide-stress-test-timeline>.

<sup>135</sup> For an academic study of the arguments for and against publication of stress tests, see Goldstein, I. and Sapra, H., *Should Banks' Stress Test Results be Disclosed? An Analysis of the Costs and Benefits*, The University of Chicago Booth School of Business, 2 April 2012.

<sup>136</sup> Interim Results of the EBA Review of the Consistency of Risk-Weighted Assets. Top-down Assessment of the Banking Book, 26 February 2013.

<sup>137</sup> PRA announcement: <http://www.bankofengland.co.uk/publications/pages/news/2013/013.aspx>; see also Bloomberg Article on Danske Bank <http://www.bloomberg.com/news/2013-06-17/danske-told-by-fsa-to-add-18-billion-to-risk-weighted-assets.html>

<sup>138</sup> Article 18 EBA Regulation.

The EBA issued a voluntary Code of Conduct to NCAs in July 2012 on how the emergency situation process should operate. This manual provides guidance on the procedures to be followed both prior to, and in the event of, an emergency situation arising in one or more cross-border banking groups.

### 3.4.6. Recovery and Resolution Planning: a valuable contribution so far

The implementation of effective recovery and resolution regimes has been a post-crisis priority for policymakers internationally.<sup>139</sup> The FSB has led this work<sup>140</sup> and in the EU, translating the FSB's work into institutional arrangements is now a key area for the development of the ESFS; the design of the Single Resolution Mechanism was announced on 10 July 2013.<sup>141</sup>

The EBA is responsible for the co-ordination of the development of effective and consistent recovery and resolution plans.<sup>142</sup> The EBA's work in the area is primarily driven by the development of Europe's crisis management framework<sup>143</sup> and the European Commission's Proposal for a Directive for the recovery and resolution of credit institutions and investment firms.<sup>144</sup> Outputs in this area have included the provision of advice to the European Commission, the publication of an Opinion in March 2011,<sup>145</sup> and the publication of Discussion<sup>146</sup> and Consultation<sup>147</sup> papers on the composition of recovery plans. In due course, the EBA will publish draft RTSs and other guidelines in this area.

## 3.5. Assessment of Consumer Protection Work

The EBA has pursued a number of consumer protection activities.

- In February 2013, it published a joint EBA / ESMA warning to retail investors about the dangers of investing in Contracts for Difference (CFDs).<sup>148</sup> This has been the only formal consumer warning issued.
- It completed an analysis of indebtedness and consumer detriment in the mortgage market. This included preparatory work on two guidelines – guidelines on responsible lending (using the Financial Stability Board Principles for Sound Residential Mortgage Underwriting Practices as a basis) and guidelines on the treatment of borrowers in payment difficulties – as well as publication of Opinions on best practices in these two areas in June 2013.

<sup>139</sup> Attinger, B., *Crisis Management and Bank Resolution, Quo Vadis Europe?*, Legal Working Paper Series No. 13, December 2011.

<sup>140</sup> FSB, Key Attributes of Effective Resolution Regimes for Financial Institutions, October 2011

<sup>141</sup> [http://europa.eu/rapid/press-release\\_IP-13-674\\_en.htm](http://europa.eu/rapid/press-release_IP-13-674_en.htm).

<sup>142</sup> Article 25 EBA Regulation.

<sup>143</sup> [http://ec.europa.eu/internal\\_market/bank/crisis\\_management/index\\_en.htm](http://ec.europa.eu/internal_market/bank/crisis_management/index_en.htm).

<sup>144</sup> COM(2012) 280 final.

<sup>145</sup> Opinion of the European Banking Authority on the Commission's Services consultation 'Technical Details of a Possible EU Framework for Bank Recovery and Resolution', 3 March 2011.

<sup>146</sup> EBA Discussion Paper on a template for recovery plans, EBA/DP/2012/2, 15 May 2012.

<sup>147</sup> EBA Consultation Paper Draft Regulatory Technical Standards On the content of recovery plans under the draft directive establishing a framework for the recovery and resolution of credit institutions and investment firms, EBA/CP/2013/01, 11 March 2013.

<sup>148</sup> <http://www.eba.europa.eu/documents/10180/16136/Investor-warning---CFDs.pdf>.

The founding regulation was intended to equip the EBA to be an influential consumer protection regulator. In practice, the EBA considers that it faces certain limitations:

- The power to prohibit or restrict certain financial activities is restricted to cases for which specific legislation has been issued, or in the case of an emergency situation (Article 18 EBA Regulation). Both these conditions are dependent on the European Commission's and Council's activities. Currently there are no legal provisions relating to the EBA scope of action which provides for the application of EBA competence to ban activities and no emergency situation has so far been declared. This is an area of uncertainty in the existing regulations which will need to be clarified if the EBA is to take on such a role.

Compared to its prudential responsibilities, the EBA's consumer mandate has comprised only a small part of its remit and comprises only three resources, one of which is a Contract Agent. It is possible that an increase in resources would allow the EBA to do more in this area. It should be noted, though, that the EBA's Board of Supervisors' membership is mainly drawn from NCAs whose main or sole focus is prudential supervision, and the individual members are themselves usually prudential supervisors. This arguably creates an inherent, and possibly unavoidable, prudential bias. In some cases, it also means that the NCAs who attend EBA meetings are not the representatives of the national consumer agencies responsible for implementing consumer protection measures. The situation will not change significantly with the SSM as consumer protection is not in the mandate of the ECB.

Some stakeholders, including some NCAs, conclude from this that the EBA is not the right body to hold consumer protection responsibilities; though it is not clear which other body would be better positioned. Other stakeholders wish to see the EBA develop and pursue a clearer strategy in this area, with performance indicators established to track its progress. If it is agreed by the Council and the European Commission that the EBA should be more effective in this area and the relevant powers are available, with sufficient clarity as to their purpose and role, the EBA will require more resources.

### 3.5.1. European System of Deposit Guarantee Schemes: work currently on hold

The legislative process for the approval of the European Commission's proposal for the review of the deposit guarantee scheme directive (DGS) is on hold.<sup>149</sup> The EBA is therefore waiting for legislation to progress.

## 3.6. The Evolution of the EU Banking Supervisory Framework

The SSM's creation has the potential to allow many long standing problems in the euro area system of banking supervision to be addressed. The main one is the possibility for the SSM to overcome any resistance or hesitation at the level of the Member State to address actual or prospective banking sector weaknesses, due to the fact that the SSM will be required to pursue the interests of the euro area as a whole. The second is the SSM's potential, because it will be a single structure, to secure more effective supervisory practice across the euro area as a whole. The third is its capacity to supervise cross-border banking groups and activity more effectively than the current home-host arrangements between Member States.

In realising these benefits, however, the SSM has the potential to affect the operation of the Single Market in financial services as it creates a powerful supervisor capable of exercising significant influence over the conduct of bank supervision and the development of EU banking policy. A number of stakeholders have expressed concern that supervisory

<sup>149</sup> [http://ec.europa.eu/internal\\_market/bank/guarantee/](http://ec.europa.eu/internal_market/bank/guarantee/).

practice and culture, but notably the application of existing legislation, could diverge within the Single Market following the SSM's creation. This is a particular worry for banks with significant SSM and non-SSM operations. Doubts have also been raised about whether the EBA will preserve its regulatory responsibilities in the face of the three powerful SSM and non-SSM supervisors, the ECB, Bank of England and Swedish central bank (Sveriges Riksbank). If this were to happen, many stakeholders consider that it would inevitably reverse the development of the Single Market with the possible economic consequences that this would bring with it.

For these reasons, the majority of stakeholders want to see the EBA properly resourced so that it can help to secure coherence between SSM and non-SSM members on EU banking matters. They also want to avoid it becoming the 'poor relative' of the EU's larger supervisors. In this scenario, it would not attract enough staff of the right quality, or have sufficient influence, to counterbalance the influence of the EU's powerful central banks on banking policy and supervisory practice. On its own, such influence would not be problematic, especially if it fostered the development of the Single Market. There is already a strong tradition of central banks working with each other in the Basel Committee and elsewhere on issues of common concern. However, the introduction of the SSM, and the consequent breaking of the original ESFS structures for banking supervision, could well lead to a layering of national and SSM specific requirements which undercut the Single Rulebook and Supervisory Handbook. It could also impact cross-border banking activity if the new supervisory structures facilitate a further weakening of the home and host supervisory processes originally designed to facilitate the Single Market. The structures, of themselves, would not cause this to happen. They do, though, make it easier to occur if there is a continued drift towards national - or its euro area equivalent - decision-making in banking supervision. Already some NCAs have 'ring-fenced' the capital and/or liquidity of a non-domestic bank in order to either protect domestic creditors or make it more difficult for banks to exit a certain market. A strong EBA, equipped with the powers and resources to monitor cross-border supervisory practice, is needed to lean against this trend.



## 4. THE EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS AUTHORITY (EIOPA)

### KEY FINDINGS

- **The construction of the EIOPA, achieved in a challenging context is commendable.** The Chairperson and Executive Director have managed to calibrate limited human and financial resources to a wide ranging work programme and succeeded in attracting high quality staff. The EIOPA became member of IAIS, and has contributed to the on-going discussions related to the proposed Omnibus II Directive and draft implementing measures for Solvency II.
- **Unlike the ESMA and the EBA, the EIOPA inherited responsibility for two sectors, insurance and occupational pension funds, where national markets, products and legislation vary markedly from one Member State to another.** The construction of new draft regulations and technical input to the legal framework discussions have therefore been complex, in both the areas of insurance and occupational pension funds, with a considerable amount of work which is not reflected by draft regulatory measures (draft RTSs, draft ITSs, guidelines and recommendations). The convergence of supervisory practice is at a very early stage.
- **The delay in the application of Solvency II, the Directive designed to address the patchwork of regulatory standards for insurance across the EU, means that any assessment of the EIOPA's performance can only be preliminary.** Only when Solvency II is implemented in Member States will there be an EU-wide framework for insurance regulation and supervision.
- **The implementation of Solvency II is necessary for a common, modern supervisory regime for the EU as a whole.** Most of EIOPA's work has been devoted to developing the Solvency II framework as well as the Institutions for Occupational Requirement Provision (IORP) Framework and Directive. The implementation of these regimes will allow EIOPA to exercise its mandate in full.
- **The EIOPA contributed to the development of this framework, including through a significant technical input at Level 1 legislation, but many stakeholders consider that the process was often hurried at the expense of a thorough consideration of sometimes difficult issues.** Although the EIOPA has produced a significant volume of technical material, including in complex areas such as long-term guarantees, the process had to involve compressed consultation processes. This is largely the result of the legislative process as discussed previously in section 2.4.2., and has affected the quality of discussion at the Board of Supervisors. It has also impacted stakeholders' ability to contribute to the development of legislation.
- **Some stakeholders consider that the extensive use of guidelines to develop Solvency II is not a sufficiently robust foundation for the new framework.** Considering the importance of the Solvency II framework, the legal status and scope of the binding and non-binding instruments needs to be clarified, albeit the EIOPA considers that the use of guidelines is both legitimate and necessary before the implementation of Solvency II.
- **The EIOPA has largely established its operations and infrastructure. More staff with technical expertise and supervisory experience will be needed to develop EIOPA's supervisory role.** The EIOPA has faced a significant shortage of

staff with adequate supervisory experience and technical knowledge for aspects of Solvency II, especially in the area of internal models.

- **The colleges of supervisors need to be enhanced to improve coordination for cross-border groups.** Although the EIOPA has sought to strengthen the college process, more progress should occur with the lead supervisor model to create a more straight forward decision making process within colleges.
- **The practice and quality of insurance supervision varies markedly between Member States.** The EIOPA has only started the process of moving supervisors to work to a common set of higher standards. Once the Solvency II framework is implemented, greater focus on developing a common supervisory culture, and more intensive use of the peer reviews will be required.
- **The EIOPA has made good progress on financial stability.** This is an important area given the fragile economic conditions in the EU, but also the comparatively much larger focus among EU policymakers on banking sector risks. The EIOPA is now well organised to contribute further in this area, but greater access to the data from individual insurance entities is needed from NCAs.
- **The EIOPA has actively pursued its Consumer Protection mandate compared to the other ESAs.** Its work on consumer protection and financial innovation are widely considered to have added value to the discussion of the risks which face the EU insurance industry and the EU's citizens.

#### 4.1. Overview

Unlike the other ESAs, the EIOPA's mandate covers **two different sectors, insurance and occupational pension funds**. The EIOPA was established while its key legislative framework was under development. The Level 1 **Solvency II Directive** 2009/138/EC was adopted by the European Parliament in 2009.<sup>150</sup> Following a debate and an impact assessment on some limited but important Pillar 1 issues (which have delayed the final decisions by the co-legislators), the Solvency II is adopted, published and in force, but its implementation and application has been postponed several times: beyond 1 January 2014 and potentially until 2016. The **proposed Omnibus II Directive**<sup>151</sup> should set the scope of draft RTSs and draft ITSs to be drafted by the EIOPA. Once applied and adopted, Solvency II and Omnibus II will give the EIOPA the full ability to act as an ESA.<sup>152</sup> In the meantime, the EIOPA is working on interim pillar 2 and 3 measures of the framework via guidelines<sup>153</sup> to open the door to a more consistent supervisory approach.

In addition to the tasks set out in the EIOPA regulation and work load created by the Solvency II Framework Directive, the EIOPA's responsibilities are derived from the **IORP Directive** 2003/41/EC<sup>154</sup> and the **Insurance Mediation Directive** 2002/92/EC (**IMD**) and the **proposed IMD 2** legislative proposal.<sup>155</sup>

<sup>150</sup> The Solvency II framework aims to review the prudential regime for insurance and reinsurance undertakings in the European Union and to harmonise the supervisory regime.  
[http://ec.europa.eu/internal\\_market/insurance/solvency/future/index\\_en.htm](http://ec.europa.eu/internal_market/insurance/solvency/future/index_en.htm).

<sup>151</sup> COM(2011)8.

<sup>152</sup> To see status and progress [http://ec.europa.eu/internal\\_market/insurance/solvency/future/](http://ec.europa.eu/internal_market/insurance/solvency/future/).

<sup>153</sup> See Opinion of the EIOPA of 20 December 2012 on interim measures regarding Solvency II, [https://eiopa.europa.eu/fileadmin/tx\\_dam/files/publications/opinions/EIOPA\\_Opinion-Interim-Measures-Solvency-II.pdf](https://eiopa.europa.eu/fileadmin/tx_dam/files/publications/opinions/EIOPA_Opinion-Interim-Measures-Solvency-II.pdf).

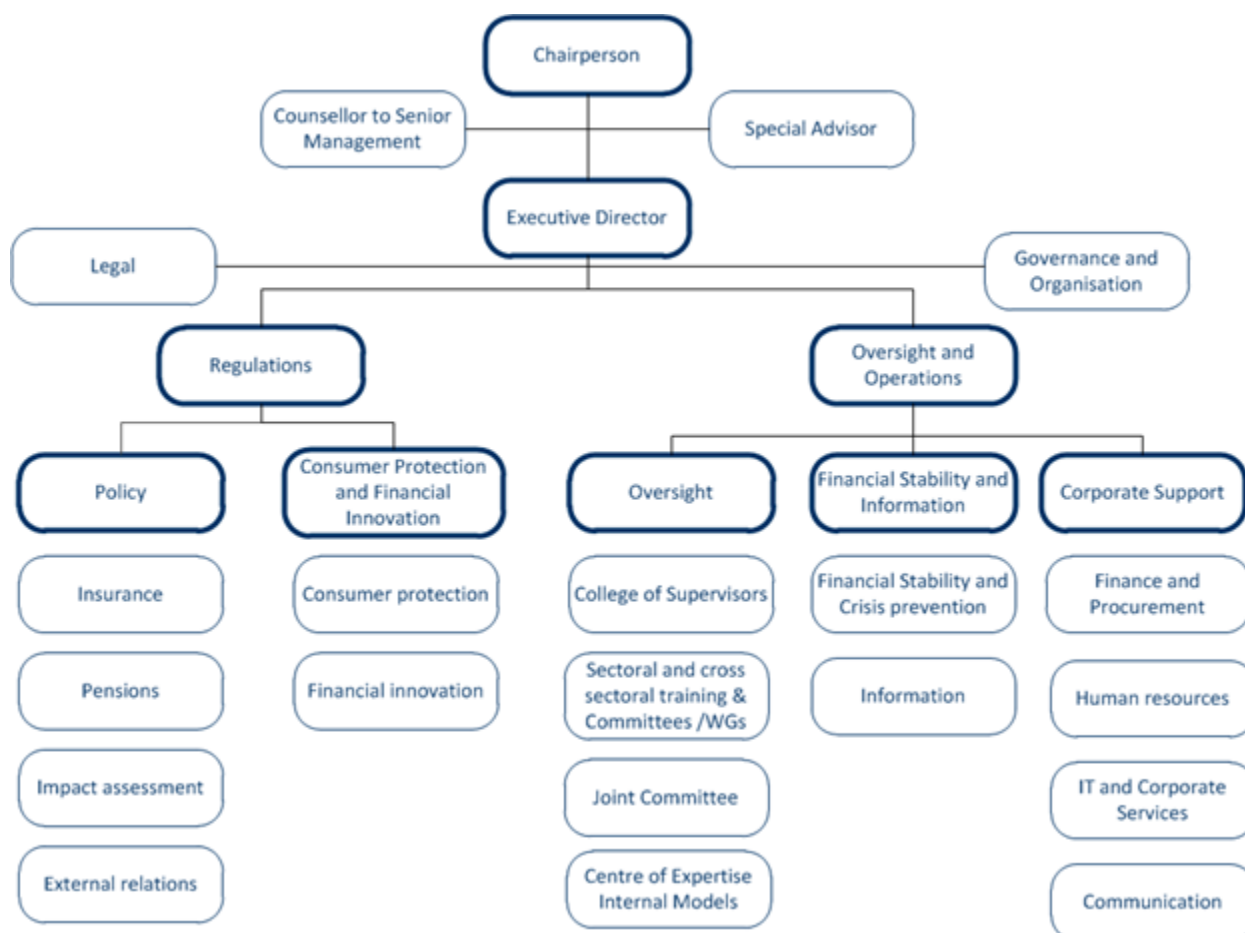
<sup>154</sup> OJ L 235, 23 September 2003, p. 10.

<sup>155</sup> COM(2012)360.

#### 4.1.1. Organisation Chart

The EIOPA is organised according to the delivery of its key tasks.

**Figure 6: Organisation chart of the EIOPA**



**Source:** EIOPA website (August 2013), updated by Mazars for consistency across ESAs.

The EIOPA established two committees, in addition to the Managing Board, to organise its work and establish controls.

- **The Internal Monitoring Group**, chaired by the Chairperson of the EIOPA, is composed of members of the Board of Supervisors. Its role is to take conclusions from the committees and translate them into proposed policy action.
- **The Quality Control Committee** composed of representatives from the Board of Supervisors, Management Board and Executive Director. Its role is to oversee the implementation of internal procedures and decisions.

The Chairperson, Gabriel Bernardino, and the Executive Director, Carlos Montalvo, took office in March and April 2011, respectively, after appointment by the Board of Supervisors and later confirmed by the European Parliament.

The EIOPA has structured its organisation along two key departments (Regulations and Oversight and Operations) working with five units devoted to policy issues (regulatory work), consumer protection, oversight (colleges of supervisors), Financial Stability and Information and Corporate Support. As at 31 December 2012, the EIOPA staff total was 91, with 22 of those being SNEs or contract staff. A large part of the resources have been devoted to regulatory work. The EIOPAs supervisory area is less well-resourced compared

to other areas. For example, there are seven staff member allocated to the colleges of Supervisors unit which is low in comparison to the 91 colleges that are active.

The implementation and application of the Solvency II Framework Directive will have two consequences: the need for additional staff to supervise the consistent implementation of the Directive; and the reallocation of existing staff from regulatory to supervisory roles.

This will represent both a quantitative and qualitative challenge for the EIOPA. To bring the added value that NCAs expect, and therefore strengthen its credibility as an Authority, the EIOPA will need expert and experienced staff with enough seniority to strengthen the consistent supervision role. So far, the EIOPA has attempted to recruit staff who meets this requirement. It has, though, proved difficult due to budget constraints and the limitations of the administrative processes which bind the ESAs. Some NCAs also consider that the criteria for the recruitment of more experienced staff from the NCAs are too restrictive (as discussed in section 0). In addition to the core organisation structure above, the main standing committees, sub-groups, task forces or networks established by the EIOPA to assist, advise and support the EIOPA mandate and execution of the work programmes are stated below.

**Table 10: EIOPA standing committees, working groups, panels and task forces**

<b>EIOPA Group/Committee</b>	<b>Mandate/Area of Work</b>	<b>Chairperson</b>
<b>Review Panel</b>	Discussed in section 4.3.4	J. Adams, FSA (UK)
<b>Equivalence Committee</b>	Undertakes full equivalence assessments and/or gap analysis of supervisory systems in relation to Articles 172, 227 and 260 of Solvency II Directive 2009/138. Furthermore, the Equivalence Committee contributes to enhancing European convergence in legislation and supervision in the field of insurance by establishing the methodologies needed for pursuit of equivalence assessment work, may it be undertaken by the Committee itself or the national supervisors.	E. Forshaw, PRA (UK)
<b>Insurance Group Supervision Committee</b>	Develops regulatory policy related to the supervision of insurance groups within the Solvency II framework, taking into account the principles of proportionality and subsidiarity. It also provides guidance regarding the operational functioning of colleges of supervisors (colleges) as well as EIOPA's role in colleges.	F. Parente, IVASS (IT)
<b>Internal Governance, Supervisory Review and Reporting Committee</b>	Develops advice, draft technical standards and guidelines to contribute to the convergent implementation of Solvency II in the areas of the system of governance, including Own Risk and Solvency Assessment sub-group of the NAIC transparency and accountability of supervisory authorities, supervisory review process, public disclosure and supervisory reporting, and valuation of assets and liabilities (other than technical provisions) on request to EIOPA or on EIOPA's own initiative.	V. Hiji, DNB (NL)
<b>Internal Models Committee</b>	Develops advice, draft technical standards and guidelines to contribute to the convergent implementation of Solvency II in the area of internal models on request to EIOPA or on EIOPA's own initiative and to ensure a consistent pre-application process for internal models across the EEA and a good cooperation among supervisory authorities in this field.	P. Cadoni, FSA (UK)

<b>EIOPA Group/ Committee</b>	<b>Mandate/Area of Work</b>	<b>Chairperson</b>
<b>Financial Requirements Committee</b>	Develops advice, draft technical standards and guidelines to contribute to the convergent implementation and supervision of Solvency II in the areas of standardised capital requirements, own funds and technical provisions as requested to EIOPA or based on EIOPA's own initiative.	O. Ermert, BaFin (DE)
<b>Occupational Pensions Committee</b>	Develops draft technical standards in areas specified in the IORP Directive, as amended by the Omnibus I Directive. Issues guidelines and recommendations, in order to help establish consistent, efficient and effective supervisory practices within the ESFS in the field of IORPs and ensure the common, uniform and consistent application of the IORP Directive.	B. Kennedy, Pensions Board (IE)
<b>Committee on Consumer Protection and Financial Innovation</b>	Contributes to EIOPA's work in the areas of Consumer protection and financial innovation, to issue guidelines, recommendations and best practices, in order to help establish consistent, efficient and effective practices across the EEA.	P. de Chatillon, ACP (FR)
<b>Financial Stability Committee</b>	Supports EIOPA's internal market and stability related issues for conducting supervisory tasks. The Committee cooperates closely with the other ESAs, the ECB and ESRB, for instance on stress testing.	P. Darlap, FMA (AT)
<b>IT and Data Committee</b>	Deals with any form of pan-EU related IT projects stemming from EU legislation (either current or future) and any other area where EIOPA Members or EIOPA consider it is necessary or useful to work together on IT issues.	P. Hoedjes, EIOPA
<b>Task Force on Insurance Guarantee Schemes</b>	Provides input into the European Commission's policy making with regards to Insurance Guarantee Schemes. In this regard, the Task Force analyses the existing cooperation mechanisms among European Insurance Guarantee Schemes and/or between IGS and NCAs with regard to cross-border activities. The Task Force looks into the role of IGSs in the winding up procedures in the Member States.	O. Joergen Karlsen, Finanstilsynet (FI)
<b>Task Force on Crisis Management</b>	Develops EIOPA's institutional framework to carry out its crisis prevention, management and resolution responsibilities under the EIOPA Regulation. Its specific role is to put in place the structures for EIOPA to deal with a crisis situation.	M. Andersson, Finansinspektionen (FI)
<b>Task Force on Personal Pensions</b>	Created to provide the European Commission with technical advice on the prudential regulation and consumer protection measures that would be required to develop an EU Single Market for personal pension schemes (both defined benefit and defined contribution schemes).	P. Pénzeš, National Bank of Slovakia (SK)
<b>Long-Term Investment Task Force</b>	The European Commission has asked EIOPA in a letter from 26/9/2012 to examine whether the calibration and design of capital requirements for investments in certain assets under the envisaged Solvency II regime necessitates any adjustment or reduction under the current economic conditions, without jeopardising the prudential nature of the regime. The Task Force will produce the draft for the final response to the request mentioned as well as any other necessary draft documents connected to it.	P. Hoedjes, EIOPA

**Notes:** As of July 2013. The EIOPA's 'Internal Monitoring Group' is an internal coordination group with a selected number of participants. It is covered in section 4.4.1 and 4.4.3.

#### 4.1.2. Specific Budget and Financial Transparency Matters

The EIOPA budget has increased from EUR 10,667,000 in 2011 to EUR 18,767,470 in 2013. The EIOPA considers that although the higher amount provides the ability to perform the tasks assigned in the EIOPA Regulation, it is not sufficient to complete the work it has been given since 2011.

**Table 11: Expenditure of the EIOPA**

	2011		2012		2013
EUR	Budget	Actual	Budget	Actual	Budget
Staff	4,810,000	4,462,998	9,080,000	7,661,224	10,210,000
Infrastructure/ administration	2,937,000	1,774,100	3,595,000	3,119,711	4,785,000
Operational	2,920,000	342,565	2,980,000	3,407,598	3,772,470
<b>Total</b>	<b>10,667,000</b>	<b>6,579,663</b>	<b>15,655,000</b>	<b>14,188,533</b>	<b>18,767,470</b>

**Source:** EIOPA published budget figures and Annual Report 2011/2012 (updated).

## 4.2. Assessment of Regulatory Work

#### 4.2.1. Scope of Work and Contribution to the Single Rulebook: Solvency II and IORP

The Solvency II and IORP regimes are the main components of the Single Rule Book for insurance and pensions. There has been extensive work to develop these two regimes, including the quantitative impact study exercises (the LTGA, the QIS 5 for Solvency II and the first QIS exercise for Pensions), the design of the new regimes and the impact assessments. As an illustration, 220 meetings have been held in 2012 by committees, subgroups, panels, and task forces (also reflecting a significant investment for NCAs involved in the working groups). This work is not, however, reflected in the number of draft implementing measures issued to date. As such, a direct comparison should not be made to the EBA and the ESMA outputs.

**Table 12: Regulatory measures of the EIOPA**

Regulatory Measure	Solvency II	IORP	Other	Total
RTS	-	-	0; 2	0; 2
ITS	0; 3	0; 1	-	0; 4
Technical advice request from the European Commission	2; 0	2; 0	4; 2	8; 2
Guidelines and recommendations	0; 6	-	1; 1	1; 7
Opinions	2; 0	-	2; 0	4; 0
<b>Total</b>	<b>13</b>	<b>3</b>	<b>12</b>	<b>28</b>

**Source:** EIOPA website (as of July 2013). **Note:** **Red** – Measures currently under development (subjected to public consultation). **Black** – Measures finalised and adopted.



## Analysis of work under both frameworks

The Solvency II Framework Directive and the IORP Directive are ambitious in purpose, broad in scope and complex in their technical detail. Their development would have posed a challenge to any regulatory authority. This was the particular and challenging case for the EIOPA which assembles 28 NCAs, and had to deal with the pre-existing combination of national legislation, standards and practices across the EU which are varied and, in some cases, contradictory. The industry has also challenged the level of requirements on the grounds that it would damage the global competitiveness of the EU insurance sector.

Stakeholders, including NCAs, recognise that the EIOPA has had some success progressing the Single Rulebook within this difficult context. In particular, a good, if not perfect, balance is thought to have been struck between the need to secure high quality outputs while dealing with a high volume of work. There are, though, two major concerns about the way in which the frameworks have been developed:

- **The time needed to achieve this work has been underestimated by the European Commission and legislators.** This has created a pressure to produce documents within a tight timeframe. This has impacted the EIOPA's consultation processes. It has also diverted its resources from other areas of its mandate.
- **The relationship between the objectives and the detailed drafting of implementing measures (draft RTS, draft ITS, guidelines and recommendations) is uncertain in some cases.** Some industry stakeholders are concerned that the EIOPA's outputs are too detailed, and consequently have added more layers of requirements than are necessary.

Both points argue for stronger central management of the overall organisation of regulatory work. It also suggests that the Board of Supervisors should discuss not only the content of the technical frameworks, but also how they will be implemented. Finally, it suggests that the EIOPA is much more involved in the technical design of the legislation but challenged more thoroughly on the regulatory objectives.

The EIOPA envisages the use of non-binding guidelines to ensure consistent preparation of parts of the Solvency II Framework Directive considering that the in-force status of Solvency II provides the basis for the use of guidelines even if it is not yet implemented. It also considers that the guidelines are related to part of the regime which should not be affected by the present re-discussion on the Directive and will not pre-empt this discussion. Nevertheless, industry stakeholders believe that there are interactions between each part of the regime and the implementation of guidelines should be carefully monitored.

## 4.3. Assessment of Supervisory Work

Similar to the other ESAs, the EIOPA Regulation has equipped the Authority with legal powers to ensure consistent application of EU law by NCAs.

### 4.3.1. College of supervisors

The EIOPA participates and contributes to the efficient, effective and consistent functioning of the colleges of supervisors of groups of insurance companies.<sup>156</sup> The EIOPA participates in almost all of the 91 colleges, monitoring agendas and annual action plans.<sup>157</sup> The priorities are set by the EIOPA based on the results of stress tests exercises, the outcomes of the QIS's and the pre-application for an internal model.

<sup>156</sup> Article 21 EIOPA Regulation.

<sup>157</sup> EIOPA's action plan 2013 for colleges, EIOPA-BoS-13/012, 29 January 2013.

Step by step, the roles of colleges have been progressively enhanced and became more focused on the most important issues. On-going decisions should also facilitate access to data issues. Nevertheless, only seven EIOPA staff members have been directly assigned to the unit to monitor and engage with the 91 colleges. The role of the EIOPA within the colleges is complex and time consuming. It requires particular knowledge, skills and experience, especially in the complex area of pre-application of internal models. The college process requires a significant amount of coordination work. The EIOPA is also required to favour convergence of supervisory practices. To date, facing a lack of staff and experienced people, the EIOPA has not been in a position to address these issues. Consequently, there is considerable scope for the EIOPA to step-up the intensity of its work in this area.

These concerns also highlight a lack of legal certainty about the group supervisor's ability to play a lead role in the supervision of an insurance group. No significant progress on group supervision and the functioning of colleges is likely to be achieved without more clarity and emphasis on the role of the group supervisor. The role of the EIOPA should be reviewed and reassessed accordingly.

There is an expectation amongst NCAs from Member States with less developed regulatory regimes that the EIOPA will provide leadership in colleges on internal models. There is also a particular industry demand for an efficient pre-application process. To date, work in this area has been mainly developed in the policy working groups on internal models or within NCAs.

It is hoped that the college process can be used to enhance understanding of internal model issues, improve the soundness of the pre-application process, and set appropriate standards for the post-implementation monitoring of internal models. Present experience illustrates the complexity and the diversity of possible approaches for the pre-application.

To assist this process, the EIOPA has established a **Centre of Expertise Development** to discuss with the NCAs the way to organise the acquisition of a common expertise based on the experience involved in the pre-application and to further develop consistency in supervisory approaches to internal models.

#### 4.3.2. Delegation of Tasks: no delegation to date

There has been no delegation of tasks or responsibilities<sup>158</sup> between NCAs or from an NCA to EIOPA. It is generally noted that the basis for delegation is uncertain and the NCAs' appetite for such delegations is low because of the continuing importance of national accountability mechanisms.

Some stakeholders consider, however, that there could be scope in future to use the delegation power in some specific areas, principally internal models and, separately, cross-border decision making in the college process. Another area could be non-bank financial institution resolution (see section 4.4.4 below). Equally, it has been suggested that the use of delegation during the development of the Solvency II framework could address some of the concerns raised about uneven implementation (see above, section 4.2.1). For this to work, though, not only would there have to be unanimous support among NCAs, but the EIOPA would need to be properly resourced to execute what would be a demanding task. It is not clear whether either condition could be achieved. It is clear that there would be very significant operational risks of changing the current approach to the development of Solvency II in the course of what is a very challenging process.

<sup>158</sup> Article 28 EIOPA Regulation.

#### 4.3.3. Common Supervisory Culture: hindered by the lack of implementation of the Level 1 legislation

The EIOPA has an important role to develop a common supervisory culture of EU insurance and occupational pensions markets.<sup>159</sup> However, the delay in the implementation of the Solvency II Framework Directive has inhibited convergence in supervisory culture. This is important because convergence amongst insurance supervisors is less than that of their counterparts at the EBA and the ESMA. The consequence of the lack of convergence is greatest for those Member States where insurance legislation and regulation are less developed and in some cases where the need for improvement is greatest.

To make progress in this area, each year the EIOPA develops sectoral and cross-sectoral training programs for national insurance and occupational pensions supervisors. The EIOPA has also initiated the constitution of a Steering Committee on the '**Supervisory Review Process**'. The Chairperson leads this and is in charge of overseeing the development of a supervisory handbook. This initiative could reinforce the convergence of supervisory practices. The fact that this Committee includes Board of Supervisors members is thought to give it extra legitimacy.

#### 4.3.4. Peer Reviews: four reviews conducted in 2012

The EIOPA is responsible for conducting thematic peer reviews<sup>160</sup> across all NCAs to enhance convergence in supervisory practices. The EIOPA's Review Panel carried out four reviews in 2012 on various topics such as the supervisory practices for the pre-application of internal models and the supervisory practices for branches of EEA undertakings. In 2013 and 2014, six peer reviews are planned. In 2012, teams of 20 experts prepared approximately 156 reports and conducted 14 visits to NCAs.

According to the EIOPA, the **success of the peer reviews** is a result of the process used involving senior and experienced supervisors from NCAs', onsite visits, and ex-post scrutiny of the results. Some peer reviews have been considered a useful benchmarking exercise. However, peer review results, as adopted by the Board of Supervisors, have not been seen to lead to changes in the supervisory practices. This poses the question if a broader change to the peer review process toward more independent assessments should be considered and become a higher priority for EIOPA.

#### 4.3.5. Mediation: no formal mediation procedures to date

In order to settle disagreements between NCAs, EIOPA established a Mediation Panel in 2012 as well as mediation procedures.<sup>161</sup> The panel comprises two members and four substitutes appointed by the Board of Supervisors.

To date, no mediation has been triggered. This can be explained by the fact that Solvency II is not yet implemented.

#### 4.3.6. Opinions: four prepared to date

The EIOPA issued two opinions in 2012, one on external models and data, and the other on interim measures regarding Solvency II. Two other opinions were published in 2013, an opinion on Payment Protection Insurance and an opinion on the Supervisory Response to a Prolonged Low Interest Rate Environment (submitted for consideration by the EIOPA Board

<sup>159</sup> Article 29 EIOPA Regulation.

<sup>160</sup> Article 30 EIOPA Regulation.

<sup>161</sup> Article 19 and 20 EIOPA Regulation.

of Supervisors at the end of 2012).<sup>162</sup> An unpublished, internal opinion on the supervisory response to the vulnerability of insurers to bank and sovereign risk was also prepared.

The Low Interest Rate Environment Opinion<sup>163</sup> of February 2013 is an example of the attempt the EIOPA has made to address risks to the insurance and pension sectors. The effectiveness of this opinion does, though, depend on actions NCAs take in response.

#### 4.3.7. Breaches of Union law: one investigation launched on the breach of the IMD

To date, one investigation of a breach of the IMD Directive has been launched (Article 17 EIOPA Regulation). In three other cases, the EIOPA decided not to open an investigation as the NCAs cooperated in a transparent way, providing the requested information within the required deadlines.

In the absence of the Solvency II regime, breach of Union law powers are limited. The implementation of the new regime may increase the need for the EIOPA to use more extensively the powers to enforce consistency in the implementation of EU law.

### 4.4. Assessment of Financial Stability Work

#### 4.4.1. Identification and Response to Systemic Risk

The EIOPA is required to monitor developments in financial markets and test the resilience of individual financial institutions and the EU financial system as a whole. In this capacity, and working together with the ESRB and other ESAs, the EIOPA's function is to act, after NCAs, as a line of defence within the ESFS against financial sector risks. An effective organisation has been developed to carry out the activities. It includes:

**The Task Force on Crisis Management** has developed the EIOPA's framework to carry out its crisis prevention, management and resolution responsibilities and put in place the structures for EIOPA to deal with a crisis situation. This framework was adopted by the Board of Supervisors in December 2011. **The Financial Stability Committee** develops a market surveillance framework to monitor and report on market trends and financial stability related issues. **The Internal Monitoring Group**, chaired by the Chairperson and composed of members of the Board of Supervisors, plays an important role in the decision making process. It draws together the work of other EIOPA Working Groups, along with other sources of analysis, and transposes analytical findings into practical policy measures for consideration by the Board of Supervisors.

The EIOPA contributes to financial stability in different ways, such as:

- the preparation of semi-annual surveys presenting the key issues of national market developments as part of the preparation of the Financial Stability Report;<sup>164</sup>
- an EIOPA opinion on the prolonged period of low interest rates was submitted for consideration by the EIOPA Board of Supervisors at the end of 2012;<sup>165</sup>
- following an ESRB Decision 2011/6,<sup>166</sup> EIOPA now shares key market data with the ESRB on an aggregated basis every quarter;

<sup>162</sup> All opinions are available on the EIOPA website <https://eiopa.europa.eu/en/fixed-width/publications/eiopa-opinions/index.html>.

<sup>163</sup> EIOPA, Opinion of the EIOPA of 28 February 2013 on Supervisory Response to a Prolonged Low Interest Rate Environment, BoS 12/110, 28 February 2013.

<sup>164</sup> Financial Stability Report 2012, Second half year report, EIOPA-FS-12-097, 10 December 2012.

<sup>165</sup> EIOPA, Opinion of the EIOPA on Supervisory Response to a Prolonged Low Interest Rate Environment, 28 February 2013.

- the EIOPA has regular meetings with the ECB (which services the ESRB) and participates in the Contact Group on Data; and
- the EIOPA Risk Dashboard (internal version) and the Financial Stability Review are presented at the ESRB General Board and are sent to the European Parliament.

### Quantitative Data and Common Supervisory Reporting

The EIOPA has access to several reports and data including.

- a quarterly report on the 30 largest EU insurance groups collected by the NCAs. Data is anonymous when reporting to the EIOPA;
- external data, mainly through a market data provider, on the same 30 groups and on a broader set of institutions and general financial and macro variables; and
- a yearly report from NCAs for the full set of EU insurers, on an aggregated basis.

Stress tests and related exercises, and specific trends and information collected via its participation in the colleges of supervisors, provides additional information to develop the EIOPA's own analysis. **Access to data is a key issue for each of the ESAs' work** on financial stability. In the EIOPA's case, it has been hampered by some specific restrictions.

- The quality and consistency of the data from one country to another varies significantly. This inhibits the EIOPAs ability to assess and challenge key indicators. Solvency II does not, of itself, resolve this issue. As such, progress in this area will need to occur before and following the new framework coming into force.
- At times, the flow of data from NCAs to EIOPA has been limited. The EIOPA considers that this has affected its ability to perform certain tasks. The main reason for this is a different reading by the EIOPA and NCAs, on the need for the EIOPA to have access to specific kinds of data. A second explanation is a concern by some NCAs, on the capacity of the EIOPA to preserve confidentiality of institution specific data when bound by the EU rules applicable to the access to documents held by the EIOPA. It is difficult to determine how much substance there is to this second point.

#### 4.4.2. Stress Testing the Insurance Sector

In 2011, the EIOPA performed a stress test covering 129 market participants.<sup>167</sup> In 2012, targeted stress tests were conducted in Member States where it was considered that vulnerability was higher. A further full stress test is currently being planned.

The EIOPA has encountered some obstacles during these stress tests. In certain aspects, these mirror the EBA's experience (see sections 3.4.2 and 3.4.3). The first category of challenges is practical; access to source information and the ability to challenge the quality of information in returns to NCAs, are both key issues. The second category is methodological. A stress-test configured as an aggregated micro stress test, being essentially static, does not take into account second round effects, so that it gives only a partial indication of the impact of the hypothetical stresses. More fundamentally, there is a question about whether any of the tests so far have been sufficiently challenging.

The EIOPA's ability to develop its stress testing capability, and to improve the quality of its methodology, will require further investment and therefore will also require additional resources to be able to perform further tests.

<sup>166</sup> ESRB, Decision of the ESRB on the provision and collection of information for the macro-prudential oversight of the financial system within the Union, (ESRB/2011/6).

<sup>167</sup> EIOPA insurance stress tests <https://eiopa.europa.eu/activities/insurance/insurance-stress-test/index.html>.

#### 4.4.3. Actions in Emergency Situations

To date the Council has not declared an emergency situation and therefore EIOPA's powers under such circumstances cannot be assessed. EIOPA has a role to coordinate actions undertaken by the NCAs in case of adverse market developments.<sup>168</sup> The EIOPA has developed a Crisis Management framework operated by the Internal Monitoring Group. This framework includes: regular meetings, feedback to NCAs in relation to assessments of risks arising in the insurance sector, information sharing and discussion of key risks.

#### 4.4.4. Recovery and Resolution Planning: substantial submission to the European Commission

The EIOPA has contributed to the European Commission consultation on the development of a recovery and resolution framework for non-bank financial institutions. This submission covers all aspects of recovery and resolution from the objectives of resolution to appropriate tools and funding.

It describes in particular a detailed set of processes to facilitate and coordinate supervisory actions by NCAs, including the identification of adverse developments, the development of EIOPA actions in response to a decision by the Council on the existence of an emergency situation taking decisions under Articles 18(3) and (4) EIOPA Regulation, and responding to ESRB recommendations and warnings and the processes to address recommendations made by the ESRB.

It also highlights issues specific to insurance, particularly the greater stability relative to banks<sup>169</sup> and the importance of the protection of policyholders as an objective of the prudential supervision of insurers.<sup>170</sup>

Non-bank financial institution resolution is an emerging area in international regulation. At present, it is not clear what future demands the European Commission process will create for EIOPA. Because it is a largely new area, in which many NCAs have limited knowledge and experience, there could be a case for EIOPA to take a lead role on behalf of EU supervisors, possibly through a formal delegation. The answer to this depends, though, on the content of the final legislation, and in particular the balance between national and EU responsibilities in a resolution situation.

Furthermore, EIOPA's focus is currently on international organisations' (IAIS and IOPS) work to contribute to the development of sound international regulatory and supervisory standards in the insurance and occupational pensions sector. Whereas the participation in IAIS' work has already started in 2011 and is focusing on systemic risk and ComFrame,<sup>171</sup> the process of IOPS' membership was initiated in 2012 and should be concluded in 2013.

<sup>168</sup> Article 18 EIOPA Regulation.

<sup>169</sup> The Geneva Association reminded that due to the specificities of insurance, *'the resolution of insurers can take place in a more orderly fashion, especially if compared to banks'*, *'Insurance and Resolution in Light of the Systemic Risk Debate, A contribution to the financial stability discussion on insurance'*, Geneva Association Report, February 2012, p. 2.

<sup>170</sup> In ICP 1 of the IAIS Insurance Core Principles (Objectives, Powers and Responsibilities of the Supervisors): *'The principal objectives of supervision promote the maintenance of a fair, safe and stable insurance sector for the benefit and protection of policyholders'*.

<sup>171</sup> Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame).



## 4.5. Assessment of Consumer Protection Work

The EIOPA has outlined a broad ranging strategy for consumer protection. The Authority believes that this goes beyond pure regulatory and supervisory tasks, and protects consumers by identifying and taking remedial actions in the field of its competences. It has sought to match its ambition with practical support: six staff members are currently dedicated to consumer protection, and this is envisaged to increase to 14 by 2016 (not including NCA staff dedicated to the EIOPA Committee on Consumer Protection).

The Committee on Consumer Protection and Financial Innovation brings together all relevant NCAs and other authorities responsible for supervision of insurance intermediaries at a national level. To reach common positions on cross-sectoral issues, this committee co-operates with the other ESAs, particularly through the Joint Committee's Subcommittee on Consumer Protection and Financial Innovation set up in May 2012. This is illustrated by the Consumer Strategy Day that took place in June 2013 and organised jointly with the ESMA and the EBA.

The insurance and pension funds markets are fragmented with significant differences in products, networks and intermediaries and even legal, social and tax frameworks. There is therefore presently within EIOPA a resistance to embrace all consumer protection matters equally across the three sectors. For insurance supervisors, there is also no clear evidence that one supervisory approach is more efficient than another.<sup>172</sup> This could evolve in the future with the adoption of more horizontal EU legislation compatible with a better capacity to differentiate the insurance specificities when necessary.

Some stakeholders consider that the EIOPA has addressed issues which have arisen at a national level which are irrelevant for the overall EU market (e.g. the opinion on Payment Protection Insurance). With the use of opinions, the EIOPA faces an inherent difficulty when communicating these vulnerabilities which differ in nature and intensity in each Member States or when these vulnerabilities are already addressed at national level or even when there is not enough evidence as to why these issues illustrate more generic vulnerabilities in the European market.

### 4.5.1. Consumer Trends, Education and Training Initiatives

The EIOPA has been active in mapping consumer protection practices by carrying out a survey of competencies of NCAs on consumer protection and sanctions provided by national laws for violations of the IMD provisions. Furthermore, the EIOPA has reported on good practices of information to members of Defined Contribution Pension Schemes and on the existing cross-border cooperation mechanisms between Insurance Guarantee Schemes in the EU. The EIOPA has also published reports on '*Good Practices for Disclosure and Selling of Variable Annuities*',<sup>173</sup> and '*Best Practices by Insurance Undertakings in handling complaints*'.<sup>174</sup> Guidelines on complaints-handling by insurance intermediaries are being prepared.

### 4.5.2. Consumer Warnings: none issued to date

Like the other ESAs, the EIOPA can issue warnings in case a financial activity poses a serious threat to its objective of protecting consumers or temporarily prohibit or restrict certain financial activities with the criteria and conditions of the Article 9 EIOPA Regulation.

<sup>172</sup> Alternatives to the present system, see Group of Thirty, *The Structure of Group Supervision, Approaches and Challenges in a Global Marketplace*, 2008, p. 23-38.

<sup>173</sup> EIOPA-CP-11/007, 4 April 2012.

<sup>174</sup> EIOPA BoS 12/070, 12 June 2012.

To date none of these powers have been used. The EIOPA considers that without the adoption of a sector specific legislation or a modification of Article 9(5) EIOPA Regulation, it has no power to prohibit or restrict financial activities.

#### 4.5.3. Insurance Guarantee Schemes

The EIOPA provided the European Commission with a '*Report on the Cross-Border Cooperation Mechanisms between Insurance Guarantee Schemes in the EU in 2011*'<sup>175</sup> and a '*Report on the Role of Insurance Guarantee Schemes in the Winding-Up Procedures of Insolvent Insurance Undertakings in the EU/EEA*'<sup>176</sup> in 2012. Currently, progress leading to the development of an initiative related to a directive on Insurance Guarantee Scheme is bound to the resolution of funding issues.

The EIOPA has contributed significantly to legislative initiatives on Consumer Protection. Examples of this work include the revision of the IMD advising the European Commission on disclosure requirements in the context of the review of the IORP, and reporting on the existing cross-border cooperation mechanisms between Insurance Guarantee Schemes in the EU.

#### 4.6. Assessment of Pensions Work

The EIOPA has organised its work on pensions under the Occupational Pensions Committee which is composed of internal EIOPA staff and NCAs' staff from working groups. This Committee, created by the EIOPA's predecessor, has been adapted to the new EIOPA regulation.

The importance of pension funds within the overall framework of savings, public sector benefits and retirement provision varies significantly from one Member State to another. This reflects the important political, social and cultural difference between Member States. This means that there are fewer cross-border issues for the EIOPA to consider. There are, furthermore, important differences between the insurance and pension sectors. For this reason, the EIOPA's work on insurance can inform only its work on pensions to a lesser extent. The breadth of its mandate thus creates practical challenges for the EIOPA which the other ESAs do not face.

Both sectors have some common issues and face similar risk factors such as the low interest rate environment. Moreover, some solutions to the social protection issues in Europe would progressively mitigate the links between insurance and pension funds. This suggests that the EIOPA develops common methodologies and supervisory practices enhancing the supervisory response to these issues on both sectors.

The EIOPA has sought to develop its knowledge of the differences between national pension regimes. It has developed a database of pension funds. The major action was to complete the first Quantitative Impact Study. The EIOPA has given high priority in the Work Programme for 2013<sup>177</sup> to the IORP Directive (standards, tasks following the results of the Quantitative Impact Study and an improved methodology for the calculation of sponsor support see Assessment of the Regulatory work).

<sup>175</sup> EIOPA-TFIGS-11/007, June 2011.

<sup>176</sup> EIOPA-TFIGS-12/007, 25 May 2012.

<sup>177</sup> EIOPA work programme 2013, EIOPA-12/103.

## 5. THE EUROPEAN SECURITIES AND MARKETS AUTHORITY (ESMA)

### KEY FINDINGS

- **The establishment of the ESMA, achieved in difficult circumstances is commendable.** The Chairperson and Executive Director have been successful in calibrating scarce human and financial resources to a wide ranging work programme and succeeded in attracting high quality staff. The ESMA implemented transparent processes in line with EU rules.
- **The ESMA has carried out intensive and innovative regulatory activity to produce implementing rules for revised legislation and for newly regulated activities.** On top of drafting implementing rules, the ESMA should be formally allowed to express its view on the design of the EU financial sector and its regulation and supervision. In particular, creating a financial system that favours the financing of the EU economy, growth and jobs (in particular SMEs and mid-caps companies) should become an explicit objective of the ESMA and the other ESAs. After some hesitation, an active Stakeholder Group has started to provide valuable input.
- **The ESMA's scope of action has expanded since its establishment to areas that were not regulated prior to the crisis.** This includes direct supervisory powers to supervise on an EU-wide basis CRAs and trade repositories. The supervision of CRAs by the ESMA is evidence of successful EU-wide regulation and supervision of financial activity. **This said, for both the regulatory work and direct regulation, several practical improvements can be proposed to enhance the ESMA's efficiency.**
- **The ESMA's supervisory consistency work has had less impact.** For legal reasons the ESMA has not developed consistent supervisory practices such as colleges of supervisors and EU-wide short selling restrictions. For practical reasons the ESMA has not conducted stress tests. Its oversight of consistent implementation of EU laws and implementing rules by NCAs has not been ambitiously developed; peer reviews, mediation and breach of Union law procedures have been either timid or non-existent. It appears to be more a structural inhibition than excessive caution. Interestingly, the ESMA has issued several opinions directed to NCAs to try to ensure consistent application of EU law.
- **The role of the ESMA in newly regulated activities has increased the role of securities' regulators in financial stability matters.** This is not yet fully reflected in the ESRB work. Despite limited legal tools, the ESMA has been active in crisis management during emergency situations.
- **Finally, investor and consumer protection has formed an intrinsic part of the regulatory work of the ESMA, but the understanding and identification of consumer trends is more difficult due to the challenge of obtaining uniform information on those matters across the Member States and the ESMA's lack of proximity to retail investors.** The ESMA has nevertheless made a significant effort to reach retail investors in their local market, in particular by translating the 'Investor Corner' and warnings into all EU official languages. Here again, the supervisory capacity to act in cases of a threat to the consumer is the less intensively used power. This is because the legal conditions for its use are almost impossible to fulfil.

## 5.1. Overview

Like the EBA and the EIOPA, the ESMA was born during the financial crisis and post-crisis environment characterised by a highly volatile market. This created a strong political will to restore confidence in the financial markets. Therefore, from the outset, EU institutions gave the ESMA the task to enhance the protection of investors and promote stable and well-functioning financial markets in the EU. To do so, the ESMA's main focus is on

- the development of the Single Rulebook,
- the enhancement of consistent supervisory practices, and
- the direct supervision of CRAs.

Securities markets activities are governed by a diverse range of EU laws. According to the ESMA Regulation, ESMA's scope of action covers the securities and markets activities regulated by key EU Directives and Regulations on i.a. investor compensation, the provision of investment services, trading venues, disclosure and content of financial information, collective and alternative investment management, market integrity and CRAs. The ESMA acts on corporate governance, audit and financial reporting matters to the extent necessary to ensure effective and consistent application of the relevant EU legislation. The ESMA is also able to take appropriate action in the context of takeover bids, clearing and settlements and derivatives. Since its establishment, the ESMA's scope of action has been expanded by sector specific legislation to short selling practices and post-trading market infrastructures (OTC derivatives, CCPs and direct supervision of trade repositories).

The ESMA is the only ESA entrusted with direct supervisory responsibilities. These powers cover entities or activities not regulated prior to the crisis and therefore these were not regulated by NCAs.<sup>178</sup> For the other legislative initiatives already covering regulated financial activities, the focus of any new competence given to ESMA has been on developing the Single Rulebook, with some expansion of its supervisory role but most often limited to the coordination of direct supervision by NCAs.

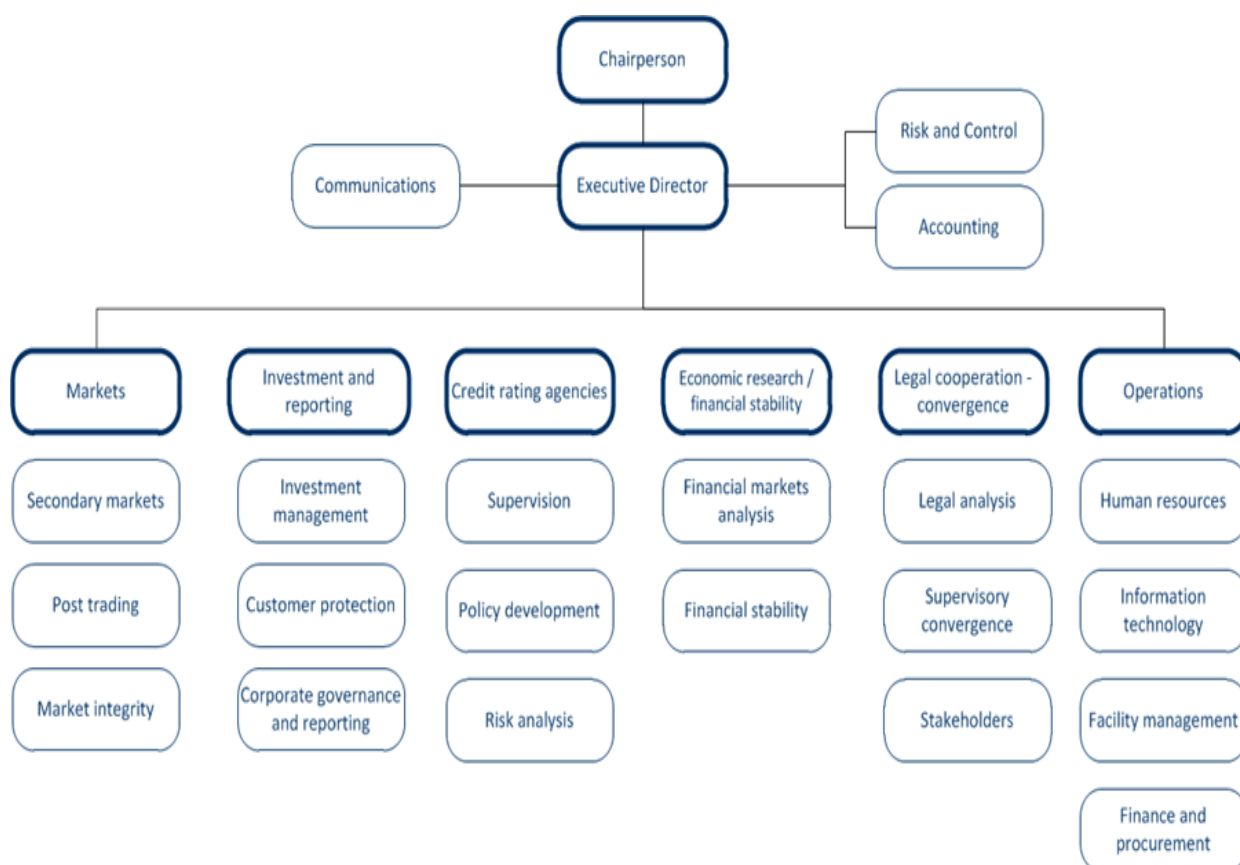
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<sup>178</sup> See Sasso, L., Kost de Sevres, p. 11 - 18.

### 5.1.1. Organisation Chart

The ESMA is organised to deliver its key tasks. The Organisation Chart is as follows:

**Figure 7: Organisation chart of the ESMA**



**Source:** The ESMA Annual Report 2012, updated by Mazars for consistency across ESAs.

The Chairperson, Steven Maijoor took office in April 2011 and the Executive Director, Verena Ross on June 2011 after being appointed by the Board of Supervisors and later confirmed by the European Parliament. The staff of the Authority was recruited via an open recruitment campaign and almost all key positions were newly filled (complete renewal of the existing CESR). The new organisation was redesigned to better reflect the scope of action and powers given to the ESMA.<sup>179</sup>

Three divisions were established, two dedicated to the scope of action of the ESMA (markets, investment and reporting) and the last one exclusively dedicated to the operation of the ESMA. In addition, three units devoted to Economic research and financial stability, legal cooperation and supervisory convergence, and for the direct supervision of CRAs were set up. Stakeholders consider the ESMAs staff to be high quality with strong technical ability and a pragmatic way of working. Staff members are respected by the financial sector, notably by the directly supervised CRAs.

In addition to the core organisation structure above, the main Standing Committees, Groups, Panels, Task Forces or Networks established by the ESMA to assist, advise and support the ESMA mandate and execution of the work programmes are displayed in the table below.

<sup>179</sup> For a comparison of powers of CESR and the ESMA see Möllers, T., p. 402.

**Table 13: ESMA Standing Committees, Working Groups, Panels and Task Forces**

<b>ESMA Committee /Group</b>	<b>Mandate/Area of Work</b>	<b>Chairperson</b>
<b>Review Panel</b>	Discussed in section 5.3.5	J. Guill, Luxembourg CSSF (LU)
<b>Market Integrity Committee</b>	Market surveillance, enforcement of securities laws, facilitation of cooperation between NCAs and exchange of information for market abuse investigations.	K. Botopoulos, Hellenic CMC (EL)
<b>Secondary Markets Committee*</b>	Issues related to the structure, transparency and efficiency of secondary markets, including trading venues and OTC markets. Consistent implementation of MiFID and implementation rules.	M. Wheatley, FCA (UK)
<b>Investor Protection and Intermediaries Committee*</b>	Issues related to the provision of investment services and activities by investment firms and credit institutions; consistent implementation of MiFID intermediaries with particular regard to investor protection (conduct of business rules, distribution of investment products, investment advice and suitability).	J. P. Servais, FSMA (BE)
<b>Investment Management Committee*</b>	Issues related to collective investment management, covering both harmonised and non-harmonised investment funds and consistent implementation of the UCITS Directive, the directive on AIFM and depositories.	G. Murphy, Central Bank of Ireland (IE)
<b>CRAs Technical Committee</b>	Providing advice on policy decisions regarding CRAs to ESMA staff, to the Board of Supervisors, or to any other relevant internal committees or panels	V. Ross, ESMA
<b>Corporate Finance Committee*</b>	Consistent implementation of the Prospectus Directive, including questions and answers, advice on implementing standards and equivalence with third countries, corporate governance and notification of major shareholdings under the Transparency Directive.	G. Rameix, AMF (FR)
<b>Corporate Reporting Committee*</b>	Accounting and enforcement of IFRS, audit, publication of periodic information and storage of regulated information.	H. Lausch, BaFin (DE)
<b>Post-trading Committee*</b>	All issues related to the provision of central counterparties, clearing and settlement services as well as operation of trade repositories. Advice to the European Commission and technical standards relating to the EMIR (European OTC derivatives, CCPs, trade repositories). Operational preparations for direct supervision of trade repositories.	G. Vegas, CONSOB (IT)
<b>Financial Innovation Committee*</b>	Achieving a coordinated approach to the regulatory and supervisory treatment of new or innovative financial activities.	A. Tuominen, FSA (FI)
<b>Economic Markets' Analysis Committee</b>	Financial markets monitoring and analysis: pro-active identification, monitoring, and assessment from a micro-financial level of trends, potential risks and vulnerabilities in financial markets across borders and sectors. Cost-benefit analysis and impact assessment of existing, planned or proposed regulation and supervisory practice (ex-ante/ex post).	R. Gerritse, AFM (NL)
<b>IT Management and Governance</b>	Development and maintenance of ESMA IT projects.	N. Vasse, ESMA
<b>Commodity Derivatives Task Force*</b>	Monitoring and analysis of all regulatory and industry developments relevant to financial commodity markets, such as energy markets, emission allowances, and agricultural commodities.	M. Wheatley, FCA (UK)

**Notes:** As of July 2013. \*A Consultative Working Group has been established.



Except for direct supervision of tasks conducted directly by the ESMA, all other tasks are prepared by groups led by the head of a NCA and composed of experts from the ESMA and the NCAs. The 'rapporteurship' of those groups is carried out by the relevant ESMA division or unit. Those Standing Committees, Groups, Panels or Task Forces dealing with intense regulatory activity have created consultative working groups. This provides valuable and rapid market participant expert opinion on possible options considered by the Standing Committee or working group during the course of their work. The added value of this practice is not questioned. Rather the way in which these consultative working groups are put together is not considered sufficiently transparent. A clarification would be welcomed and the final composition of these consultative working groups could be subject to an opinion of the SMSG.

#### 5.1.2. Specific Budget and Financial Transparency Matters

Since 2011, the ESMA budget has increased by 65 % from EUR 16,962,000 (2011) to EUR 28,325,000 (2013). This reflects the significant level of additional regulatory and operational tasks assigned to the ESMA. The initial and amended budgets, and the accounts of the ESMA, are published on the ESMA website.<sup>180</sup>

**Table 14: Expenditure of the ESMA**

	2011		2012		2013
EUR	Budget	Actual	Budget	Actual*	Budget
Staff	8,460,000	6,636,610	12,132,000	8,586,000	17,464,000
Infrastructure/ad-ministration	4,702,000	4,083,287	4,497,000	3,312,686	5,825,000
Operational	3,800,000	1,783,120	3,650,000	1,326,000	4,946,000
<b>Total EUR</b>	<b>16,962,000</b>	<b>12,503,023</b>	<b>20,279,000</b>	<b>13,224,686</b>	<b>28,235,000</b>

**Source:** The ESMA published budget and Annual Reports 2011 and 2012.

**Note:** \*2012 actual expenditure is based on that 'committed' at 31 December 2012.

The European Parliament's ECON Committee noted in its '*Opinion for the Committee on Budgetary Control on discharge in respect of the implementation of the budget of the European Securities and Markets Authority for the financial year 2011*', that current financing of the ESMA is '*inflexible, creates administrative burden, and poses a threat to the agencies' independence*'. This is discussed in more detail in section 2.3.4 above as it is a matter of concern for all ESAs.

## 5.2. Assessment of Regulatory Work

#### 5.2.1. Regulatory Work and Contribution to the Single Rulebook: a wide scope

Of the three ESAs, the ESMA is the authority that has been confronted with the most intensive regulatory workload due to wide-ranging legislative activity including the revision of existing legislation and a number of new Directives and Regulations. In both cases the new legislation (or upcoming legislation) calls for a very significant number of RTSs and ITSs to be drafted or delegated acts. The table below provides an overview of such prolific regulatory activity.

<sup>180</sup> <http://www.esma.europa.eu/page/Corporate-information>.

**Table 15: Regulatory measures of the ESMA in respect of new legislation**

Level 1	EMIR	Short-Selling Regulation and CDS	AIFMD	CRA CRA 2 CRA 3	Total
Advice on delegated acts	8	2	1	11+3	<b>25</b>
RTS	38		1	4	<b>43</b>
ITS	2	5			<b>7</b>
Guidelines/Recommendations	1	2	7		<b>10</b>
Q&A issued?	Yes	Yes	No	Yes	/
<b>Total</b>	<b>49</b>	<b>9</b>	<b>9</b>	<b>18</b>	<b>85</b>

**Table 16: ESMA's regulatory measures regarding the review of existing legislation**

Level 1	MiFID	MAD	Prospectus	Transparency	UCITS	Total
Proposed revised legislation	MiFID2 MiFIR	MAD2, MAR + Benchmarks	Adopted Prospectus 2	Transparency 2	Adopted Recast UCITS	Total
Advice on delegated Acts			1			1
RTS			2			2
ITS			1			1
Guidelines, Recommendations*	4*			2*	2	8
Q&A issued*	Yes	Yes	Yes	Yes	Yes	12

**Note:** \*Guidelines, recommendations or Q&A issued to ensure consistent implementation of existing or adopted revised legislation.

The procedure for developing and adopting draft technical standards and guidelines clarifies the responsibilities of the parties involved, the organisation of work, and is similar to that of both other ESAs. Broadly speaking, a regulatory work programme is prepared every year based on the regulatory agenda defined in Level 1 legislation and the deadlines attached as well as on the basis of the ESMA's objectives, tasks and resources. For each work-stream, a project leader (an NCA representative or an ESMA staff member) is nominated. In most cases this falls within established Standing Committees, if not, a specific Task Force is composed. The project may require a cost-benefit analysis and a public consultation, and will involve the opinion of MSG. Once approved by the Board of Supervisors, the draft standards are submitted to the European Commission for endorsement and sent to the European Parliament and the Council before adoption.

According to the ESMA, the workload impact is difficult to assess precisely, as not all technical standards have the same complexity or the same resource requirements. For example, one provision may be read initially as requiring a single technical standard, but in fact combines so many different dimensions that it ultimately requires several standards to be developed.

One of the reasons for this intense regulatory activity is that the Omnibus I Directive<sup>181</sup> gave explicit powers to the ESMA to draft RTS and ITS and adopt guidelines or recommendations to provide additional details to a number of securities and financial markets Directives and Regulations adopted within the context of the EU Financial Services Action Plan under the Lamfalussy approach<sup>182</sup>. More significantly, by way of transposing the G20 Roadmap adopted in by the Leaders' Summit in Pittsburgh in September 2009,<sup>183</sup> the EU has initiated and adopted several EU laws aimed at regulating a number of activities, entities or financial products that were not previously directly regulated but which played a significant role in the crisis.<sup>184</sup> This new set of EU legislation covers:

- the registration and supervision of CRAs (one Regulation and two amending Regulations) to enhance transparency of methodologies and avoid conflicts of interests;
- the regulation of post market infrastructure to reduce risks in the OTC markets;
- the limitation of volatility during severe market movements by restricting or banning short-selling practices or aspects of the CDS market;
- the creation of a supervisory framework for alternative investment managers.

The ESMA has to date acted as producer of the draft implementing rules of the framework agreed by EU institutions, but did not contribute to the design of Level 1 legislation. The opportunity for the ESMA to provide securities supervisors' input into the architecture of the EU legislative framework is requested by several NCAs and would have many significant benefits. This will allow using experience and insight to inform the legislative process on key structural issues at stake regarding the financing of the EU economy, the desired market structure or the key principles for the supervision of the financial system. In addition, it would contribute to a better definition of scope for delegated acts or technical standards which sometimes has created difficulties of interpretation or practical execution. An option to include EU securities regulators and supervisors view point in the key debates leading to Level 1 legislation may be to provide the ESMA, as well as the other ESAs, with a right to give a formal opinion on any legislative initiatives within its current or proposed scope of action.

Article 1(5) ESMA Regulation defines the key objectives that would guide such formal opinions on future legislation or the drafting of delegated acts. However, it should be noted that such objectives are focused on major post crisis remedies to restore stability and confidence.<sup>185</sup> There would be merit in adding a more specific objective regarding the creation of a financial system that favours proper financing of the EU economy, growth and job creation.

For example, most of the EU legislation and implementing measures are conceived to apply to major market players and there is no impact assessment of the cumulative effect of this legislation. This has created a significant difficulty and cost for small and mid-cap listed companies, for whom the requirements are disproportionate. This has had the effect of reducing the number of companies listed on EU regulated markets. Therefore, a general

<sup>181</sup> Directive 2010/78/EU, OJ L 331, 15 December 2010, p. 120.

<sup>182</sup> European Parliament Factsheet, Financial Services: the Lamfalussy Process and the Development of European Supervisory Authorities, [http://www.europarl.europa.eu/ftu/pdf/en/FTU\\_3.4.4.pdf](http://www.europarl.europa.eu/ftu/pdf/en/FTU_3.4.4.pdf).

<sup>183</sup> The European Union's Roadmap for Financial Reform under the political authority of Commissioner Michel Barnier, [http://ec.europa.eu/internal\\_market/finances/docs/roadmap/financial\\_reform\\_en.pdf](http://ec.europa.eu/internal_market/finances/docs/roadmap/financial_reform_en.pdf).

<sup>184</sup> Wymeersch, E., 'The Institutional Reforms of the European Financial Supervisory System, an Interim Report' Ghent Univ. *Financial Law Institute Working Paper No. 2010-01*, 25 January 2010, p. 3-5.

<sup>185</sup> See Ferran, E., Babis, V., 'The European Single Supervisory Mechanism', *University of Cambridge Faculty of Law Research*, Paper No. 10, March 2013, p.28 and 33.

principle of 'Think Small First' should be applied to any legislation and delegated act prepared. This would remove the need to redesign or amend adopted binding legislation or technical standards to take small businesses into account<sup>186</sup> (see Annex, point 20). It is also often noted that the European Commission and the co-legislators should give further clarity on the choice between direct delegated acts or RTSs and ITSs in order to achieve a better understanding of the Single Rulebook.

In terms of public consultations on draft implementing rules, in 2012 the ESMA gave early indication of the workload and timing of the intense regulatory activity by publishing a 'regulatory programme'<sup>187</sup> that anticipated the consultations for the year. Echoing the complaints by the industry due to short consultation periods, the ESMA has requested the European Commission to define the deadlines of its adoption of RTSs and ITSs in calendar months and not calendar dates. To allow sufficient time for consultation and in-depth consideration of arguments put forward by market participants as well as an informed consideration of issues at stake by the European Parliament and the Council, the ESMA considers that 12 months is a reasonable period to produce a quality draft RTS or draft ITS. So far, the process of adopting RTSs and ITSs by the European Commission following the opinion of the European Parliament and Council has not been tested extensively.

During the drafting process and consultations, the ESMA is considered to be open and professional when interacting with the market players. This been said, this is less true when experienced by national associations or more local market players that consider the ESMA too distant.

Finally, the ESMA has developed and expanded the practice of publishing sets of Questions and Answers on the practical application of the EU legal framework that provides harmonised practical details on the way in which the NCAs will respond to practical implementation issues raised by market participants on the day to day application of the EU laws and technical standards. These sets of Questions and Answers are supplemented and updated periodically.

### 5.3. Assessment of Supervisory Work

Similar to the other ESAs, the ESMA Regulations have equipped it with legal powers to ensure consistent application of EU law by NCAs, as well as direct supervision in certain areas.

#### 5.3.1. EU Wide Direct Supervision of CRAs and trade repositories: the ESMA acting as a 'national supervisor'

Unlike the other ESAs, sector specific legislation has entrusted the ESMA with direct supervisory powers over CRAs in 2011 followed by trade repositories in 2012.

#### Credit Rating Agencies (CRAs)

The ESMA very progressively assumed responsibility for supervising CRAs registered in the EU. In the first CRA Regulation adopted in September 2009, competences for the registration and supervision of CRAs in the EU were given to the NCAs. The CRA II Regulation, which became applicable July 2011, granted the responsibility to the ESMA. Its main activities are:

- In the course of 2011, the role of the ESMA progressively moved from ensuring consistency across the assessment of the CRAs applications for registration being

<sup>186</sup> See Demarigny, F., 'An EU-listing Small Business Act. Establishing a proportionate regulatory and financial environment for Small and Medium-sized Issuers Listed in Europe (SMILEs)', March 2010.

<sup>187</sup> ESMA 2012 Regulatory Work Programme, <http://www.esma.europa.eu/system/files/2012-275.pdf>.

undertaken by NCAs to its current policy and supervisory role. During the initial registration process, the ESMA facilitated the coordination of NCAs, among college members and across applications. The direct supervisory powers are exercised on a day to day basis by the Chairperson, the Executive Director and the dedicated unit of staff. The Executive Director chairs the CRA Technical Committee which acts as a forum for NCAs to exchange their views on the application of the Regulation but also to prepare any regulatory text and to assess non-EU countries CRA regimes that are requesting equivalence. The efficiency of the Technical Committee is of particular importance for NCAs that often request more information on the manner ESMA exercises its role and any likely impact on their national supervisory tasks.

- Of the 22 registered CRAs<sup>188</sup>, three operate under a group structure, totalling 16 legal entities in the EU, which means that the total number of CRA entities registered in the EU is now 35. In addition, two Japanese CRAs have been certified.
- After registration, the ESMA has regularly engaged with CRAs following an analysis of periodic information, notification changes in the initial conditions, complaints and other market intelligence. The ESMA has conducted two investigations of groups of registered CRAs and one investigation of an individual CRA. These investigations include on-site inspections directly carried out by the dedicated ESMA staff unit. It has been experienced that in the course of those investigations the border between the legitimate compliance check role of the ESMA and the need to preserve the independence of ratings was tested. The level of intrusion of ESMA regarding methodologies of rating is a delicate matter that requires careful monitoring both for the interest of ESMA and the added value of independent ratings for the functioning of financial markets.
- To support its supervisory activities the ESMA has developed several IT tools, such as 'SOCRAT' which aims to facilitate processing of ratings data in a standard and automatic manner and 'CEREP' which is a central repository to make historical information available to the public.
- In order for CRAs in the EU to be able to endorse ratings issued in third countries the ESMA has conducted several equivalence reviews of regulatory regimes outside the EU. The ESMA has endorsed regulatory regimes from Argentina, Brazil, Canada, Hong Kong, Mexico, Singapore and the United States to be as stringent as the EU. As required by the ESMA Regulation, the ESMA has entered into Memoranda of Understanding (MoUs) with the relevant NCAs of each country.
- The ESMA has prepared advice to the European Commission on delegated acts, drafted RTSs and published guidelines. The advice given to the European Commission was for the definition of the fees that CRAs should pay annually to the ESMA. The level of fees is proportioned to the turnover of each CRA.
- The ESMA has conducted its supervisory activities with a high level of transparency by publishing supervisory and policy work periodically, as well as an annual report outlining activities.

Although two years is a short period to comprehensively evaluate the direct supervisory function, the general view is that the ESMA has efficiently established the process and organisation to professionally execute this task (see Annex, point 15). For CRA groups no longer obliged to deal with their NCA, the establishment of one single supervisory function for the EU improves efficiency and simplifies the process. Furthermore, the ESMA considers that it carries out its supervision of the Single Market as an NCA would do in a national

<sup>188</sup> <http://www.esma.europa.eu/page/List-registered-and-certified-CRAs>.

market. This is also the impression of the market. But it has been highlighted that, going forward, for legal reasons the ESMA will have to separate internally its various roles regarding CRAs (regulatory, on-going supervision, investigatory (the investigating officer) and above all, sanctioning).

### Trade Repositories

Under the EMIR Regulation, the ESMA has direct EU-wide registration, supervision and recognition responsibilities for trade repositories that centrally collect and maintain the records of derivatives (to enhance derivative markets transparency and reduce financial stability risk). As for CRAs, trade repositories will contribute fees directly to the ESMA, for the performance of supervisory tasks that will be proportioned to their turnover.

The reporting start date if a trade repository is registered in the EU is likely to be towards the end of September 2013. It is therefore too early to draw any conclusion on this exclusive, direct supervisory role now. During the course of 2012, the ESMA advised the European Commission and prepared draft RTS and draft ITS on procedural rules and details for the registration of trade repositories.<sup>189</sup>

#### 5.3.2. College of Supervisors: starting in the course of 2013

The ESMA Regulation opens the possibility for the Authority to contribute only to the colleges established by a sector specific EU law. Unlike the banking and insurance sector, such sector specific legal basis has only been given to the ESMA very recently for CCPs (or clearing houses) under the EMIR Regulation. Work on this area is due to start in the course of 2013. This said, the ESMA has had a short and temporary experience of colleges in respect to CRAs. During the six month period when CRA registration power was in the hands of NCAs (before being transferred to ESMA), the ESMA did play a considerable role in ensuring as much consistency as possible between the various colleges analysing the applications, both between NCAs for group CRAs and between the various applications.

Under the EMIR Regulation, the ESMA will have a seat on all CCP colleges (but no voting right) and be tasked with ensuring consistent application of the EMIR Regulation, building consistent supervisory practices, validating CCP risk models and, if so required, settling disagreements between NCAs. As the only member on all CCP colleges, the ESMA will be in a strong position to identify emerging issues and monitor risks as well as prepare and coordinate EU-wide assessments of resilience of CCPs to adverse events.

In preparation for such a role, the ESMA has modelled the likely composition of 24 colleges and has made a head-start by drafting guidelines and recommendations regarding the functioning of the colleges, a risk assessment framework and a protocol for the exchange of information and crisis management procedures.

Building on the experience in the banking and insurance sectors, several stakeholders consider it relevant to expand the coordination role of the ESMA to colleges of securities supervisors that currently exist and function outside an explicit reference in the EU law. For example, securities supervisors of cross-border market operators running regulated markets in several Member States have established colleges that have different degrees of coordination intensity. So far the ESMA has refrained to request to participate in such adhoc colleges without a clear reference in the MiFID. One could wonder if a more consistent application of the MiFID (or its successor(s)) and of the supervision of regulated markets or other forms of trading venues across the EU would not be favoured by a legal

<sup>189</sup> Final Report: Draft technical standards under the Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC Derivatives, CCPs and trade repositories, ESMA/2012/600, 27 September 2012, [http://www.esma.europa.eu/system/files/2012-600\\_0.pdf](http://www.esma.europa.eu/system/files/2012-600_0.pdf).



coordination role given to the ESMA in colleges of market operators and other trading venues. Similar thought could be extended to asset management companies or CSDs.

### 5.3.3. Delegation of Tasks: an unused pragmatic supervisory tool

Since the establishment of the ESMA no delegation of tasks or responsibilities between NCAs facilitated by the ESMA has been reported. No delegation was given by the NCAs to the ESMA as a central, single, less costly and EU-wide supervisor. On one occasion the NCAs agreed to delegate to the ESMA their ability to negotiate with non-EU countries' supervisors. Within the framework of the AIFMD, the ESMA has been entrusted with the tasks of negotiating a framework administrative arrangement (or MoU) for the exchange of information with non-EU country supervisors regarding alternative investment managers.<sup>190</sup> This framework agreement led to the signature of numerous bilateral administrative arrangements between the NCAs and non-EU country supervisors.<sup>191</sup>

The possibility to delegate tasks or responsibilities between NCAs or to the ESMA has therefore not been used to the extent permitted by the ESMA Regulation. It is, however, considered by commentators as a pragmatic tool for a less costly integrated supervision of the Single Market.<sup>192</sup> The capacity to delegate tasks and responsibilities allows a progressive adaptation of the EU supervisory framework in accordance with the speed and intensity of integration of market players or activities without requiring a legislative change.

As an example, the fragmentation of the trading of securities between several trading venues of different nature created by the MiFID makes it more complicated for NCAs to collect the market data needed for market surveillance purposes and enforcement of market abuses. An initial step was made by the creation of a central IT tool for NCAs to exchange trade reports overnight. The revision of the MiFID provides an opportunity to enhance this initial IT platform, so as to further reduce IT costs between NCAs and create a common central real time market surveillance tool to compensate the fragmentation trading venues in the Single Market. It should be analysed by the ESMA whether this could be achieved through a pragmatic delegation of tasks given to the ESMA.

### 5.3.4. Common Supervisory Culture: pragmatic supervisory tools

The ESMA is required to play an active role in building a common EU supervisory culture and consistent supervisory practices<sup>193</sup> which can be achieved through different means set out in the ESMA Regulation including: the exchange of confidential information for enforcement purposes, the review of application of RTSs and ITSs, recommendations and guidelines, the organisation of training programs for NCAs' personnel or even the encouragement of secondments of staff between NCAs.

The ESMA has made progress towards this objective which is described below:

- Q&As: To complement the RTSs/ITSs, the recommendation and guidelines, the ESMA has developed sets of Questions and Answers on the practical application of the direction and regulations within its scope of action. This has been done in particular for Prospectuses, Short Selling, UCITS, CRAs, MAD, AIFMD and EMIR.

<sup>190</sup> ESMA Guidelines on the model MoU concerning consultation, cooperation and the exchange of information related to the supervision of AIFMD entities, ESMA/2013/998 of 18 July 2013.

<sup>191</sup> See ESMA press release ESMA/2013/992 of 18 July 2013; [http://www.esma.europa.eu/system/files/2013-992\\_press\\_release\\_on\\_aifmd\\_mous.pdf](http://www.esma.europa.eu/system/files/2013-992_press_release_on_aifmd_mous.pdf).

<sup>192</sup> Wymeersch, E., 'The Institutional Reforms of the European Financial Supervisory System, an Interim Report', *Ghent Univ. Financial Law Institute Working Paper No. 2010-01*, January 2010, p. 12.

<sup>193</sup> Article 29 ESMA Regulation.

- The Provision of opinions to NCAs: to ensure that a specific NCA or several NCAs apply EU law in a uniform manner the ESMA has developed Opinions as a pre-phase instrument to supervise the proper implementation of the EU law by the NCAs before using more coercive powers. This is analysed in section 5.3.7.
- The uniform application of International Financial Reporting Standards (IFRS) in accordance with the ESMA's scope of action. This consists of several activities: comments on exposure drafts sent to the international standard setter and its interpretation committee, the publication of accounting enforcement decisions taken by national enforcers and the publication of specific 'Statements' or even recent publication of 'Common Enforcement Priorities' for the Annual Financial Statements a few weeks before the end of the fiscal year. These statements or measures are adopted by the Board of Supervisors. This role regarding consistent enforcement of IFRS has proven useful to providing harmonised practices for those who prepare and audit IFRS Financial Statements. However, the supervisory framework in which it is developed in the EU is unclear and lacking predictability. Indeed, the only official body giving authoritative guidance on IFRS is the IFRS Interpretation Committee and such guidance is endorsed by the European Commission after the opinion of a dedicated group composed of professionals, the European Financial Reporting Advisory Group (EFRAG). But it is clear that when approving prospectuses or registration documents, securities regulators express a position on IFRS implementation and that an EU harmonised approach is to the benefit of a level playing field. But the legal basis of such common approaches is unclear. There would be merits in clarifying roles in the EU on IFRS harmonised approaches and ensuring more predictability of such decisions.
- Together with the other ESAs the ESMA organises the training of staff to strengthen a common supervisory culture. The number of seminars of this cross-sector training programme has significantly increased from 2011 to 2012 as well as the number of participants. To favour an equal level of participation by the NCAs, the ESAs have decided to provide financial support to participants where needed.

#### 5.3.5. Peer Reviews: from 'peer' to 'independent' reviews?

The ESMA Review Panel operates on the basis of the Review Panel Protocol<sup>194</sup> and the ESMA Review Panel Methodology.<sup>195</sup> The panel assesses the overall process of implementation, provides common understanding and expresses views on specific problems in the implementation process encountered by individual NCAs. The panel uses mappings and based on commonly agreed benchmarks, self-assessments to obtain a first picture of the practice of supervision in a given area. In certain circumstances, the Review Panel carries out 'selective peer reviews', i.e. it establishes a special group to address issues of a technical nature or focus on a limited group of countries.

The ESMA completed two peer reviews in 2011 which addressed the Prospectus Directive and the Mapping of the Transparency Directive. Four peer reviews were conducted in 2012 which addressed the actual use of sanctions under the Markets Abuse Directive and on supervisory practices issues, respectively on Money Market Fund Guidelines and on the conduct of business rules under MiFID.

Some stakeholders note that the manner in which the final reports of the Review Panel are drafted and adopted is heavily influenced by the interest of the NCAs. The fact that they review each other does not favour an independent assessment of compliance with EU laws

<sup>194</sup> Decision ESMA/2011/BS/229 establishing ESMA's Review Panel.

<sup>195</sup> ESMA Review Panel Methodology, ESMA/2012/33.

and rules. The peer reviews were conceived by the predecessors of the ESAs, which were Committees of supervisors working together on a voluntary basis and this process was introduced as such in the ESA Regulations. Common opinions coming out from interview consider that now that the ESAs are established by law with legitimate powers, that the time has come for the ESMA to conduct independent assessments of regulatory and supervisory frameworks in the Member States.

This could indeed be achieved by the ESMA using independent and experienced external experts. As a reference, a model could be the Financial Services Assessment Programme (FSAP) conducted by the IMF. It would also be important that the outcome of such independent reviews translates into concrete action plan leading to tangible and consistent application of EU laws and rules.

#### 5.3.6. Mediation: bad publicity for NCAs?

The ESMA also adopted common Mediation Panel Rules of Procedures, jointly developed within the Joint Committee, in June 2012. The Mediation Panel was subsequently formed in November 2012 from voting members of the Board of Supervisors after a call for candidates. As of today no formal mediation request has been publicly disclosed by the ESMA. Some stakeholders consider that although mediation requests were envisaged, mutual understanding between NCAs or the issuance of guidelines have prevented the need for formal procedures.

#### 5.3.7. Opinions and breaches of Union law: Opinions as a pre-phase of an investigation?

The ESMA adopted Rules<sup>196</sup> for breach on Union law investigations on 19 June 2012. In 2012, the ESMA reported that it had assessed approximately 30 requests which concerned the activities of NCAs or financial market participants. It was considered that the majority of these requests concerned the activities of financial market participants and did not demonstrate or suggest a breach of Union law by NCAs. However, approximately 12 of these requests led to further correspondence between the ESMA and the relevant NCAs or to obtain further information. But according to the ESMA none of these cases have led to open a breach of Union law investigation.

It should be noted that the ESMA links its ability to issue opinions to NCAs under Article 29(1)(a) ESMA Regulation to the breach of Union law investigations according to Article 17 ESMA Regulation, i.e. opinions are issued before a conclusion on opening breach of Union law investigation is reached. By doing so the ESMA has adopted a pragmatic and progressive approach to ensure uniform interpretation and consistent supervisory practices by the NCAs. The adoption of an opinion directed to one or more NCAs is used as a first phase that could eventually lead to a breach of Union law investigation if that opinion is not adhered to by the NCA or the NCAs. It should, however, be noted that such opinions are not binding.

The ESMA has issued several opinions under Article 29(1)(a) ESMA Regulation. Not all publicly disclosed opinions are related to a pre-phase breach of Union law procedure but the ESMA has reported that several informal and non-public cases may potentially lead to a breach of Union law procedure. The main opinions issued by the ESMA cover three main areas: Secondary markets, prospectuses, UCITS and short-selling.<sup>197</sup>

<sup>196</sup> Decision ESMA/2012/BS/87 on Rules for breach of Union law investigations.

<sup>197</sup> They could possibly be found on ESMA's 'Documents' website, <http://www.esma.europa.eu/documents/overview/10>.

Overall, it is difficult to assess whether the breach of EU law procedure has produced more consistent application of EU law. In particular, there is no real transparency on the requests for investigation, the justification for not opening an investigation or launching a procedure. A view generally expressed is that the NCA decision making powers within the Board of Supervisors and their common interest for not initiating and disclosing conflicting proceedings about compliance within EU law has inhibited action by the ESMA in this area.

More generally, opinions as developed by the ESMA could be a very effective tool to answer questions from market participants who consider that divergent application of EU law prevents the establishment of a level playing field. Several market participants have highlighted their frustration for not getting rapid and harmonised responses from the ESMA. A more straight forward ESMA capacity to reply to market needs for clarity would significantly favour consistent supervisory practices across the EU. The recent Decision by the Joint Board of Appeal will contribute to create more clarity on the duty to act of the ESAs (see section 6.2.2 below).

## 5.4. Assessment of Financial Stability Work

At first glance, financial stability is not one of the core priorities of securities regulators, which focus more often on transparency and investor protection matters. However, the financial crisis and the extension of the scope of action of securities regulators, including the ESMA, to newly regulated markets, activities and products, has demonstrated that they have an increasingly significant role to ensure the stability of the financial system as a whole. The ESMA Regulation has therefore empowered the ESMA with crucial tasks to identify and provide a response of systemic risks emerging from markets, to carry EU-wide stress tests of market participants in their scope of action and on a real-time basis take action on emerging situations as well as contribute to recovery and resolution in case of the failure of a market participants or infrastructure.

### 5.4.1. Identification and Response to Systemic Risk: making securities regulators concerns heard

The ESMA should monitor and assess market developments as well as potential risks and vulnerabilities in the area of its competence. The ESMA carries out this activity in close co-ordination with the EBA, the EIOPA and the ESRB and where necessary, informs the European Parliament, the Council and the European Commission. To do so, the ESMA has developed five core tools for the identification and monitoring of systemic risks:

- the ESMA's Weekly Financial Monitor, which provides for continuous market monitoring (this is an internal document);
- the ESMA's Risk Dashboard, which is produced on a quarterly basis for the ESRB and traces several categories of risks (liquidity risk, market risk, contagion risk and rollover risk);
- ESMA's Reports on Trend, Risk and Vulnerabilities,<sup>198</sup> produced twice a year, which deliver a review of markets, risks and policy implications on a longer time period that describes trends in securities markets (among investors and market infrastructures), risks in financial markets and vulnerabilities;
- based on the above, contributions to the Joint Committee Risk Subcommittee Risk Report; and
- occasional in-depth studies on specific topics.

<sup>198</sup> ESMA Report on Trends, Risks and Vulnerabilities, No 1 and 2, 2013.

The result of all this financial stability work is to notably identify and provide appropriate responses to systemic risk directly, or through the Joint Committee, to the ESRB.

In addition to the institutional link between the ESMA and the ESRB, the ESMA contributes to the various ESRB permanent groups (General Board, Advisory Technical Committee, Analysis Working Group and Instruments Working Group) and expert groups (Retailisation, CDS, Bank Funding, Money Market Funds and shadow banking) as well as to the dedicated working group (securities financing transactions team, the ESRB group on stress tests). In return, the ESRB and the European Commission participate in the ESMA's Committee for Economic and Market Analysis. A number of stakeholders interviewed note that to date banking matters have been the ESRB priority. But the expansion of the ESMA's scope of action to OTC markets and market infrastructures are progressively making securities regulators concerns more pivotal for the financial stability as a whole.

#### 5.4.2. Stress Testing: to come on trading venues and CCPs

Contrary to the EBA and the EIOPA, the ESMA has not conducted stress tests since its establishment. There is no legal obstacle to do so, but the ESMA's stress-testing activity will start only in 2013. A stress test framework will be gradually developed for trading venues CCPs and alternative fund managers. This will require the design of risk scenarios, the coordination of implementation, the proper collection of information from NCAs, the evaluation of stress testing results, a possible publication of warnings or guidelines following evaluations, and the monitoring and coordination of the application of incoming regulatory requirements for stress testing. No assessment can therefore be made at this juncture.

#### 5.4.3. Action in Emergency Situations and Recovery and Resolution Planning: a real capacity to act?

To date the Council has not declared an emergency situation and therefore the formal ESMA powers under Article 18 ESMA Regulation cannot be assessed as such. This being said, to anticipate adverse market developments and determine whether a pan-European coordinated action might be required, the ESMA has developed several crisis scenarios (the relevance of which are in constant monitoring). These crisis scenarios include, in particular: an EU-wide trading suspension, the ban on short selling (general or for a specific sector or financial instrument), the suspension of redemption of units of UCITS, the impact of settlement fails and the impact of the failure of a clearing member or a CCP.

The ESMA has also elaborated a number of processes that would enhance the capacity of the ESMA and the NCAs to react promptly in cases of a market crisis, in particular: a co-ordination framework in case of restriction of short positions by one or more NCAs, a capacity to exchange information with the ECB on CCPs, a fluid operational exchange of information in case of suspensions or removals of financial instruments from trading, and an inventory of examples and practices regarding NCAs contingency planning.

Operationally, the ESMA has reported several occasions, during which an emergency conference call of the Board of Supervisors was necessary to discuss adverse market developments, for instance, on sovereign debt disclosure in July 2011 and to co-ordinate short selling bans in August 2011 and July 2012.

**Box 4: The short selling chaos**

Short selling restrictions or bans illustrate the need for an EU-wide approach, but also the limitations on what the ESMA can achieve in emergency situations. Before the entry into force of the Short Selling Regulation (EU) No 236/2012, the ESMA did not have capacity to monitor the consistency of decisions taken by NCAs that were covering very different categories of financial instruments and with poor assessment of their cross-border consequences. An effort to make those national measures compatible and transparent was the maximum that the ESMA was able to achieve. The ESMA has not been able to co-ordinate the timing of effective lifting of these measures in February 2012, nor to align their content in July 2012.

The Short Selling Regulation entered into force in November 2012 and provides the ESMA with an enhanced capacity to act on short-selling restrictions or bans. The legislation has increased the ESMA's capacity to coordinate the introduction of emergency measures by one or more NCAs. It has even empowered the ESMA with a capacity to directly restrict or ban short selling in the EU but subject to a number of complex conditions. This direct ability to act is currently challenged in front of the EU Court of Justice.

All in all, the willingness to cope with market volatility during crisis periods has led to a very confusing intervention by some individual NCAs on an EU basis, despite a tentative coordination action by the ESMA. This has created uncertainty and disruptions for intermediaries and has not significantly reduced volatility.<sup>199</sup> The Short Selling Regulation offers the possibility to better handle these risks on an EU-wide basis, in particular if it is not contradicted by the EU Court of Justice.

Finally, so far the ESMA has not tested its capacity to contribute and participate actively in consistent recovery and resolution plans to minimise the systemic impact of the failure of a market player or infrastructure.

**5.5. Assessment of Consumer Protection Work**

Consumer and investor protection is one of the general statutory tasks attributed to the ESMA and its Regulation specifies certain roles and powers to achieve consumer protection.<sup>200</sup> It is a horizontal objective that is achieved through various aspects of ESMA work, if not all. For example, on the regulatory side, general sets of guidelines have been published with the clear objective to enhance the level of information and the fair treatment of investors, in particular:

- two guidelines related to the MiFID provisions relating to suitability of advice to clients<sup>201</sup> and the compliance function<sup>202</sup> of investment services providers;
- guidelines on exchange-traded funds and other UCITS issues;<sup>203</sup> and

<sup>199</sup> Cinquegrana, P., 'Short Selling: A known unknown, Financial Markets,' *ECMI Commentary No. 23/29*, May 2009.

<sup>200</sup> Article 9 ESMA Regulation.

<sup>201</sup> MiFID Supervisory Briefing Suitability, ESMA/2012/860, 19 December 2012, <http://www.esma.europa.eu/system/files/2012-850.pdf>.

<sup>202</sup> Guidelines on certain aspects of the MiFID compliance function requirements, ESMA/2012/388, 6 July 2012, <http://www.esma.europa.eu/system/files/2012-388.pdf>.

<sup>203</sup> Guidelines for competent authorities and UCITS management companies: Guidelines on ETFs and other UCITS issues, ESMA/2012/832EN, 18 December 2012, [http://www.esma.europa.eu/system/files/2012-832en\\_guidelines\\_on\\_etfs\\_and\\_other\\_ucits\\_issues.pdf](http://www.esma.europa.eu/system/files/2012-832en_guidelines_on_etfs_and_other_ucits_issues.pdf).



- guidelines on remuneration of AIFMs.<sup>204</sup>

Nonetheless, there are focused work streams explicitly dedicated to investor or consumer protection.

#### 5.5.1. Consumer Trends, Education and Training Initiatives: an Investor Corner in 20 languages

The Financial Innovation Standing Committee was formally established in September 2011.<sup>205</sup> So far, the Committee led a project to develop data reporting templates in order to fulfil its responsibilities under Article 9(1) and Article 9(2) ESMA Regulation to collect, analyse and report on consumer trends, and to monitor new and existing financial activities. The collection of this information has been more challenging than expected and has not yet permitted significant achievement from the Committee so far.

Providing information to investors is also a priority for the ESMA. The ESMA website contains a subsection dedicated to retail investor issues and in particular an Investor Corner in the form of a 'Guide to investing'<sup>206</sup> which includes tips and useful information for investment decisions (key question to ask before investing, transparency on charges) as well as a link to the websites of the NCAs. The Investor Corner is translated into 19 languages.

Finally, the ESMA organised an Investor Day in December 2012, focusing on regulatory intervention, the next potential threats for investors, the changes in the face of financial product distribution and what regulators can learn from behavioural finance. From 2013, the three ESAs are organising their Consumer/Investor Days jointly as previously mentioned in sections above.

#### 5.5.2. Consumer Warnings: Three Warnings Issued to Date

The ESMA has issued three EU-wide consumer warnings translated in all official languages of the EU.

- First, in December 2011, regarding unauthorised firms offering foreign exchange investment and on the main risks involved in foreign exchange (forex) trading;
- Second, in September 2012, regarding the internet distribution of financial products generally in order to alert retail investors on tangible risks related to aggressive selling/marketing techniques used by firms on the internet; and
- Third, in February 2013, published a joint EBA/ESMA warning to retail investors about the dangers of investing in **Contracts for Difference (CFDs)**.

#### 5.5.3. Banning of Financial Activities: Almost an Empty Box

As with other ESAs, the ESMA may temporarily prohibit or restrict certain financial activities.<sup>207</sup> However, the ESMA Regulation sets out a number of conditions for this banning or restriction to become operational. These conditions include the fact that such activities should threaten the orderly functioning and integrity of financial markets or the stability of the whole financial system in cases specified and under the condition lay down by the EU legislation included in the ESMA's scope of action. So far the only legislation that envisages such a restriction is the Short Selling Regulation which has become applicable in

<sup>204</sup> Guidelines on sound remuneration policies under AIFMD, ESMA/2013/201, 11 February 2013, <http://www.esma.europa.eu/system/files/2013-201.pdf>.

<sup>205</sup> In line with Article 9(4) ESMA Regulation.

<sup>206</sup> Guide to investing, 19 October 2012, <http://www.esma.europa.eu/system/files/2012-682.pdf>.

<sup>207</sup> Article 9(5) ESMA Regulation.

November 2012 only under specific circumstances and in accordance with various conditions (see Box 3). It is therefore not surprising that the ESMA has not yet prohibited or restricted any financial activity and it is not likely to do so in the very near future.

#### 5.5.4. European System of Investor Compensation Schemes

The ESMA is waiting for progress in the legislative process for the approval of the European Commission's proposal on the Investor Compensation Scheme Directive<sup>208</sup> before conducting work in this area. No analysis can be carried out.

Stakeholders consider that, more than for the EBA or the EIOPA, investor and consumer protection forms an intrinsic part of the regulatory work of the ESMA, as it is included directly or indirectly in almost all the key EU Acts or implementing rules, and on that front the ESMA has been extremely active. The understanding and identification of consumer trends is perceived to be more difficult not only because of the challenge of obtaining uniform information on those matters across the Member States, but also due to the ESMA's lack of proximity to retail investors. Stakeholders stress the fact that more resources devoted to this task and to assist consumer associations contributing in the consultative working group of the Financial Innovation and Consumer Protection (or even in the SMSG) would help the gathering knowledge on consumer trends. The ESMA has made a significant effort to reach the retail investor in their local market both by using the network of NCAs and translating the 'Investor Corner' and warnings into EU official languages. It would be interesting to measure the impact of such publications. As regards the supervisory capacity to act in cases of threat to consumer, the fact is that this is the less intensively used power, and a widely shared view is that this is because the conditions set to make it operational are almost impossible to fulfil.

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<sup>208</sup> COM(2010)371 final.

## 6. THE JOINT COMMITTEE AND JOINT BOARD OF APPEAL

### KEY FINDINGS

- **The Joint Committee is seen by the ESAs as a useful mechanism to carry out cross-sector projects and has provided a valuable contribution in establishing common procedures and rules across the ESAs.** However, the value of the Joint Committee is not well understood outside the ESA executives themselves, even at Board of Supervisors level.
- **There is no compelling evidence that supervision in the EU would be more efficient if the three ESAs were under the same roof.** However, the EU regulatory framework is progressively favouring a supervisory structure articulated along two key objectives: consumer protection and prudential supervision.
- **The Joint Board of Appeal has so far published only one decision.** Such a decision creates a precedent in favour of a more active stand of the ESAs on supervisory matters (in particular breach of Union law) and clarifies the legal status of guidelines and recommendations for the interpretation of the scope of EU law provisions.

The ESA regulations provide for the establishment of two joint bodies, the Joint Committee and the Joint Board of Appeal.<sup>209</sup> The following chapter outlines the purpose of each body and assessment of activities to date.

### 6.1. The Joint Committee

#### 6.1.1. Overview

The purpose of the Joint Committee of the ESAs is to facilitate cross-sectoral ESA cooperation. It has both an internal facing remit and an external one. Externally, its main objective is to address cross-sectoral supervisory issues and ensure consistency in policy making amongst ESAs. From an internal, operational perspective, the Joint Committee is responsible for developing internal rules of procedures as well as a consistent interpretation of the respective ESA internal by-laws, budgetary processes and IT solutions.

The Joint Committee is composed of the Chairpersons of the three ESAs and the Chairpersons of the Sub-Committees. A small staff complement (between two and four per ESA) supports the Joint Committee. The Executive Directors, a representative for the European Commission, the ESRB are invited to attend meetings as observers. The ESA Regulations<sup>210</sup> specify that the focus of Joint Committee should be:

- financial conglomerates,
- accounting and auditing,
- micro prudential analyses of cross-sectoral developments,
- risks and vulnerabilities for financial stability,
- retail investment products,
- measures combating money laundering, and

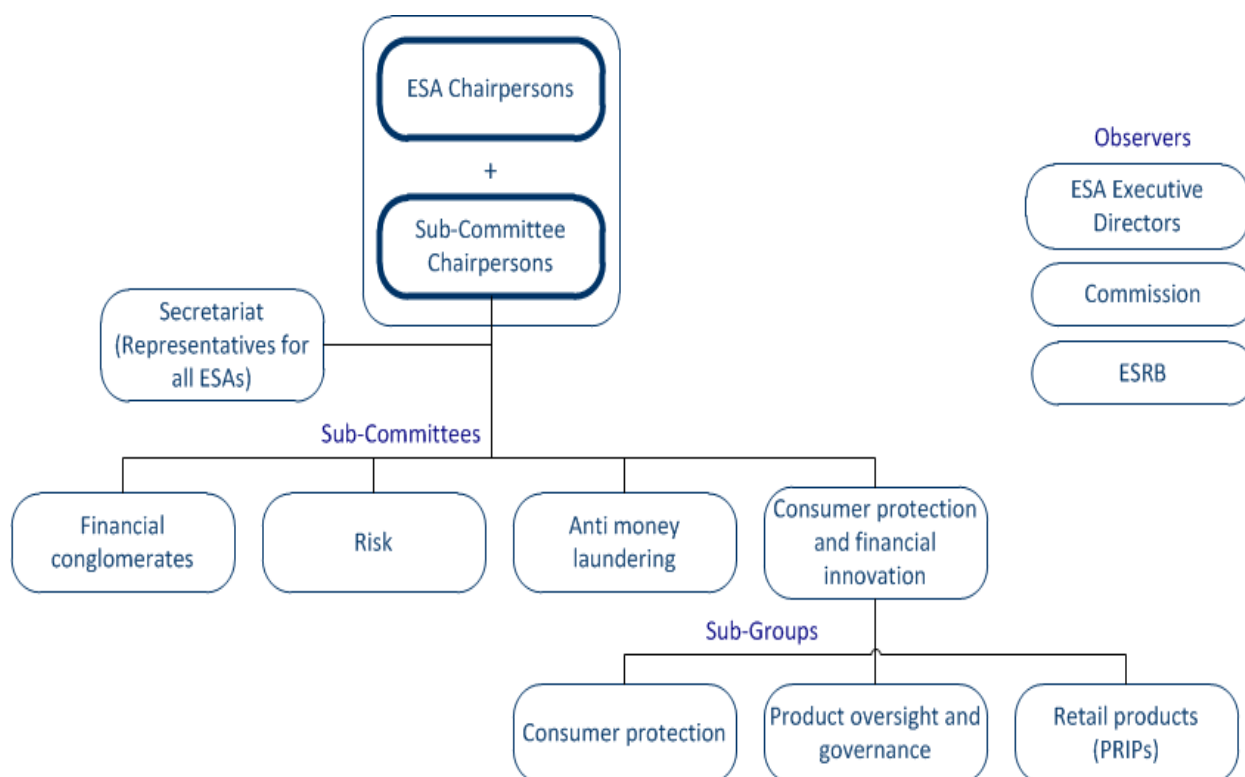
<sup>209</sup> Article 58 and 59 ESA Regulations establish the Joint Board of Appeal, its composition, operation and independence.

<sup>210</sup> Articles 54(2) ESA Regulations.

- information exchange with the ESRB and developing the relationship between the ESRB and the ESAs.

Under the lead of the Chairs, and through the support of the Secretariat staff, the Joint Committee carries out its work through four sub-committees responsible for cross-sectoral matters. These sub-committees are comprised primarily of NCA staff, approximately 30 per group. The organisation of the Joint Committee is outlined below:

**Figure 8: Organisation of the Joint Committee**



**Source:** Mazars representation based on information gathered.

The Rules of Procedure<sup>211</sup> prepared and adopted by the ESAs in 2011 outline the workings of the Joint Committee including composition, tasks, sub-committees, joint work programme, budget and reporting amongst other areas. Meetings of the Joint Committee take place at least every two months, in addition to sub-committee meetings. The role of Chairperson of the Joint Committee is rotated on an annual basis amongst the Chairpersons of the ESAs.

#### 6.1.2. Assessment of Work

Similar to the ESAs, the Joint Committee prepares and publishes an annual work programme<sup>212</sup> highlighting priority actions over the coming 12 months, which is derived from the ESA regulations as well as other key EMIR and anti-money laundering regulations. In practice, the ESAs collaborate through the Joint Committee on a number of initiatives, and also directly with each other outside of the formal Joint Committee arrangement. A summary of key actions to date include:

<sup>211</sup> Decision JC DOC 2011 001.

<sup>212</sup> Outlined at <https://eiopa.europa.eu/joint-committee/index.html>.

**Table 17: Sub-committees and -groups, and key actions of the Joint Committee**

Area	Work to date
<b>Financial conglomerates sub-committee</b>	<p>A large part of the work of the sub-committee to date has been responding to the ESAs' response to the call for advice from the European Commission on the review of the Financial Conglomerates Directive (FICOD),<sup>213</sup> specifically on scope of application, internal governance and supervisory empowerment and sanctions issues. After a three month consultation period, final advice was provided to the European Commission in October 2012.<sup>214</sup></p> <p>In parallel, the sub-committee prepared a proposal for draft RTS on the uniform conditions of application of the calculation methods of own funds, Article 6(2) FICOD.<sup>215</sup> The consultation was launched in August 2012. The work on the joint RTS is in a very advanced stage and almost ready to be submitted to the European Commission. However due to the delay encountered with regard to CRR/CRD IV and Solvency II, EIOPA (currently chairing the Joint Committee) has not been in a position to finalise the proposal.</p> <p>In addition, the ESAs have hosted a training session for NCAs on the supervision of Financial Conglomerates to enhance supervisory convergence. Each year, the Joint Committee publishes a list of identified Financial Conglomerates in accordance with FICOD.</p>
<b>Cross-sector developments, risks and vulnerabilities sub-committee</b>	<p>The main work of the sub-committee on Risk relates to the production of a bi-annual 'Report on Risks and Vulnerabilities in the EU Financial System'.<sup>216</sup> This report aims to contribute to a cross-sectoral approach to risk analysis and financial stability, and is shared with the ESRB and the Council's Economic and Financial Committee (EFC). It is in addition to the sector specific risk reports produced by the ESAs themselves.</p>
<b>Consumer protection and financial innovation sub-committee (three sub-groups)</b>	<p><b>Consumer protection.</b> The sub-group has been working on how principles developed for complaints handling in the insurance sector can be applied to securities and banking. There is also a plan to improve ESA templates for collecting, analysing and reporting on consumer trends based on lessons learned from ESMA's initial collection round.</p> <p><b>Product oversight and governance.</b> The sub-group carried out a survey of NCAs to map current practices in financial institutions in relation to product approval and governance. The mapping was conducted in September 2012 and will inform the development of a set of high level principles for product approval.</p> <p><b>Retail products (PRIPs/KID).</b> The sub-group started work on developing proposals for the European Commission regarding delegated acts, and development of draft RTS on areas outlined in the Packaged Retail Investment Products legislative proposal.<sup>217</sup></p> <p>In addition, the Sub-Committee organised the first joint ESA Consumer Strategy Day which was held in Paris on 25 June 2013. The aim of the event was to provide a forum for exchange and discussion on important and current cross-sectoral consumer issues.</p>
<b>Anti-money laundering</b>	<p>The sub-committee's work on assessing the situation across EU Member States of the legal and regulatory provisions, as well as supervisory standards in relation to the application of the Third Money Laundering Directive (AMLD)<sup>218</sup> has resulted in</p>

<sup>213</sup> OJ L 35, 11.2.2003, p. 1.

<sup>214</sup> EBA, EIOPA and ESMA's Response JC/2012/88 to the European Commission's Call for Advice on the Fundamental Review of the Financial Conglomerates Directive of 2 October 2012, <http://www.eba.europa.eu/cebs/media/Publications/Other%20Publications/Opinions/JC-2012-88-FINAL--ESAs-Joint-response-to-the-COM-call-for-advice-on-fund.pdf>.

<sup>215</sup> EBA, EIOPA and ESMA Joint Consultation Paper JC/CP/2012/02 of 31 August 2012, <http://www.eba.europa.eu/cebs/media/Publications/Consultation%20Papers/2012/JC%2002/JC-CP-2012-02-on-RTS-on-Article-6-2-FICOD.pdf>.

<sup>216</sup> Joint Committee Report JC RSC 2013-001 of 13 March 2013, [http://www.esma.europa.eu/system/files/jc-2013-010\\_jc\\_rsc\\_joint\\_risk\\_report\\_2.pdf](http://www.esma.europa.eu/system/files/jc-2013-010_jc_rsc_joint_risk_report_2.pdf).

<sup>217</sup> COM(2012) 352 final.

<sup>218</sup> OJ L 309, 25.11.2005, p. 15.

<b>sub-committee</b>	two reports, both published in April 2012. <sup>219</sup> In addition, in August 2012, a Protocol on cooperation between home and host supervisors <sup>220</sup> was published to support effective anti-money laundering supervision of agents and branches of payment institutions in host Member States in accordance with the Payment Services Directive ( <b>PSD</b> ). <sup>221</sup> In December 2012, another report was published on the application of anti-money laundering and counter terror financing obligations <sup>222</sup> to, and the supervision of, e-money issuers, agents and distributors in Europe.
<b>European Market Infrastructure Regulation (EMIR) sub-committee</b>	Outside of the sub-committee structure, the Joint Committee has been tasked with drafting a RTS on EMIR. In March 2012, a <i>Joint Discussion Paper on Draft Regulatory Technical Standards on Risk Mitigation Techniques for OTC Derivatives not cleared by a CCP under the EMIR</i> <sup>223</sup> was published. In June 2012, the Joint Committee wrote to the European Commission suggesting a postponement of the deadline for the submission of the RTS, in order to take account of on-going European and global developments in OTC derivatives regulation
<b>Working with the ESRB</b>	The Joint Committee is continuing to develop the relationship between the ESAs and ESRB. The ESRB is a participant at Joint Committee meetings thereby facilitating information exchange, and also receives a copy of the Risk and Vulnerabilities Report prepared by the Risk Sub-Committee bi-annually. A risk outlined in the early 2012 report on Credit Default Swaps was further followed up the ESRB. A project was initiated last year to improve data collection from financial market participants but has lagged.
<b>Cross-Sector Training Programme</b>	The Joint Committee is also responsible for co-ordinating the development and maintenance of an NCA cross-sector training manual and programme. The objective of the programme is to provide training courses and practical guidance to the NCAs for the organisation and hosting of training events. During 2011 and 2012, 23 training courses were rolled out. In 2012, the ESAs co-operated in the development of a common questionnaire aimed at assessing the demand for training needs in 2012 and to identify volunteers to host and organise seminars. 12 more sessions are planned to take place in 2013.
<b>EBA/ESMA cooperation</b>	<p>In September 2012, the Joint Committee and Board of Supervisors of EBA and ESMA agreed to work more closely on certain areas:</p> <ul style="list-style-type: none"> <li>• Established a network of experts in October 2012 to exchange information on investigations and enforcement activities of NCAs;</li> <li>• Completed the Euribor-EBF review process, and published their findings and recommendations in January 2013,<sup>224</sup> and</li> <li>• Set up an EBA-ESMA Task Force in October 2012 to develop Principles focused on benchmark process in Europe (interest rate and other). A consultation paper<sup>225</sup> was published in January 2013.</li> </ul> <p>This work is being led by EBA and ESMA but under the umbrella of the Joint Committee, to which the ESAs provide regular updates.</p>

<sup>219</sup> Report JC/2011/096 AMLTF/2011/05 on the legal, regulatory and supervisory implementation across EU Member States in relation to the Beneficial Owners Customer Due Diligence requirements under the Third Money Laundering Directive [2005/60/EC], April 2012, and Report JC/2011/097 AMLTF/2011/07 on the legal and regulatory provisions and supervisory expectations across EU Member States of Simplified Due Diligence requirements where the customers are credit and financial institutions under the Third Money Laundering Directive [2005/60/EC], April 2012.

<sup>220</sup> Supervisory Cooperation Protocol between 'Home Supervisor' and 'Host Supervisor(s)' of July 2012.

<sup>221</sup> OJ L 319, 5 December 2007, p. 1.

<sup>222</sup> Report JC 2012 086 on the application of AML/CTF obligations to, and the AML/CTF supervision of e-money issuers, agents and distributors in Europe of December 2012.

<sup>223</sup> Joint Discussion Paper JC/DP/2012/1, Draft RTSs on risk mitigation techniques for OTC derivatives not cleared by a CCP under the Regulation on OTC derivatives, CCPs and trade repositories, 6 March 2012.

<sup>224</sup> EBA and ESMA Euribor Recommendations to EBF of 11 January 2013, [http://www.esma.europa.eu/system/files/eba\\_bs\\_2013\\_001\\_euribor\\_-\\_recommendations\\_to\\_ebf.pdf](http://www.esma.europa.eu/system/files/eba_bs_2013_001_euribor_-_recommendations_to_ebf.pdf).

<sup>225</sup> EBA and ESMA Consultation Paper ESMA/2013/12 of 11 January 2013, <http://www.esma.europa.eu/system/files/2013-12.pdf>.



The Joint Committee appears to fulfil its role, which is to ensure proper coordination between the ESAs and consistency on regulatory and supervisory matters going across two or three sectors. Overall, the ESAs agree that the Joint Committee serves as a useful mechanism to enhance coordination within a supervisory system articulated along three financial sectors regulated at EU level by three separate authorities. However, its work is largely unknown to stakeholders.

The areas of work identified by Joint Committee in its work programme are those defined in the ESAs Regulations or result from an agreed practical view that a common approach is beneficial. The scope of action of the Joint Committee is therefore relatively limited. One important step was taken with the creation of the sub-committee on Consumer Protection and Financial Innovation to enhance consumer protection and help the ESAs fulfil their mandates in this area as well as to prepare the implementation of the PRIPS. For the first time, the Joint Committee has structured its work according to a key supervisory objective and not according to a specific legislation. A further step could be for the Joint Committee to organise its work around two major supervisory objectives and therefore only two standing sub-committees: one devoted to prudential matters (including financial conglomerates) and the other consumer protection and financial innovation. Other tasks of the Joint Committee could then be carried out on an ad hoc basis through informal working groups. To give weight to the work of such standing committee, the ESAs could delegate some tasks for which each individually has limited resources or difficulties in establishing as a priority within its own work programme. As an example, the EBA could pool together its resources to support the work of the standing sub-committee on consumer issues and take a more cross-sector approach to its consumer protection tasks.

One of the key matters for review on the functioning of the ESAs is to assess whether separate supervision at EU level of banking, insurance and occupational pensions, securities and financial markets is still appropriate. The creation of the SSM in particular prompts this question as it creates a single prudential supervisor for a group of Member States but leaves consumer protection/conduct of business supervision at the national level. Possible options would be to create a single authority for the three sectors or two separate authorities respectively in charge of prudential supervision and consumer protection/conduct of business respectively ('twin peaks'). This is neither an original theoretical model nor a perfect approach to supervision of financial activities. The pros and cons of the various possible supervisory architectures have been extensively studied.<sup>226</sup>

Currently the architecture of EU law is heavily organised by sector as evidenced by the different directives and regulations defining the scope of action of each ESA. With the exception of the FICOD and PRIPs Directives, there is very little legislation generally applicable to the three sectors. In addition the technicality and specifications of the three sectors have increased over the past decade and this calls therefore for a specific regulatory and supervisory approach rather than a holistic one leading to the creation of the single authority.

In consideration of the fact that the recruitment of quality staff is one of the key challenges of the ESAs, it would not be appropriate to create uncertainty by envisaging a single authority at this juncture. However, there is progressively a regulatory move towards a supervisory system articulated along two key objectives of financial supervision: consumer protection and prudential stability. As an example, EU legislation excludes any prudential

<sup>226</sup> Wymeersch, E., 'Europe's New Financial Regulatory Bodies', *Journal Of Corporate Law Studies*. 11(2), 11 April 2011, p. 443-462.

regulatory or supervisory matter from the scope of action of ESMA, and excludes any conduct rules from the scope of the EBA.

## 6.2. The Joint Board of Appeal

### 6.2.1. Overview

The Joint Board of Appeal was appointed by the ESAs in 2011 following a call of interest by the European Commission and held its first meeting in December of 2012. Its objective is to protect independently and impartially the rights of those affected by decisions adopted by the Authorities. It is the first time that such a body has been established at EU level in the financial services area.<sup>227</sup> It is comprised of 12 professionals (six members and six alternates) in the fields of banking, insurance, occupational pensions and securities markets or other financial services, and with the necessary legal expertise to provide expert legal advice in relation to the activities of the Authorities. The members are appointed by the Management Board of the three ESAs from a short list proposed by the European Commission and after consultation of the three Boards of Supervisors. The Board of Appeal is supported through the ESAs' Joint Committee in terms of administrative matters. Even though its Secretariat is provided by the Authorities, the Board is fully independent and current staff of NCAs, or other national or EU institutions, involved in the activities of those authorities are excluded from the Board.

### 6.2.2. Assessment of the Work

The Board of Appeal held two meetings in 2012 and adopted its rules of procedure, guidelines for parties who want to appeal proceedings and an indicative form for a 'notice of appeal'. The scope of access is still a matter of legal uncertainty both in terms of ESA decisions covered and whether the Joint Board of Appeal is a necessary step before the Court of Justice of the EU.<sup>228</sup>

The only appeal publicly known to date was from an Estonian company against a decision by the EBA relating to suitability of members of the management body of the Estonian branch of a Finnish Bank. The Board of Appeal reviewed and interpreted CRD 2006/48/EC against the EBA Guidelines on the assessment of the suitability of members of the management body and key function holders. It concluded in its Decision<sup>229</sup> that the matter was within the EBA's powers of investigation. The case was remitted to the EBA to adopt the appropriate decision in accordance with the Board of Appeal's findings.

In other words, the Joint Board of Appeal has not taken a decision on the substance of the matter raised in its first decision. But, importantly, it has created two precedents:

- It has overruled the decision of the EBA that declared itself unable to legally intervene to investigate the matter based on a too restrictive reading of its powers under the EBA Regulation and the applicable EU law.
- It has clarified the legal status of Recommendations and Guidelines by recognising that they do not constitute a binding Act, but that *'they address the matter from a practical perspective and assist in the interpretation of the scope of the provisions of Directive 2006/48/EC'* (paragraph 56, p. 16).

<sup>227</sup> Blair, W., 'Board of Appeal of the European Supervisory Authorities', *European Business Law Review*, Forthcoming University of Oslo Faculty of Law Research Paper No. 2012-30, October 2012.

<sup>228</sup> See Van Cleynebreugel, P., Judicial Protection Against EU Financial Supervisory Authorities in the Wake of Regulatory Reform, *ELSA Malta Law Review*, Vol. 2, 2012, October 2012.

<sup>229</sup> Decision of the Joint Board of Appeal of the ESAs given under Article 60, Regulation (EU) 1093/2012 and the Board of Appeal's Rule of Procedure (BOA 2012 02), BOA 2013-008, 24 June 2013.

By deciding so, the Joint Board of Appeal gave a first indication of the scope of appeals that are admissible and in relation to which the ESAs have a duty to act regarding matters of consistent supervision.

This first decision of the Joint Board of Appeal also showed the important role played by the Joint Board of Appeal within the whole ESFS. By deciding rapidly on an appeal (two months) it creates a more fluid functioning of the Single Market and is a real added value compared to a case directly brought before the Court of Justice of the EU (which is eventually the sole interpreter of EU law). In order to keep this expeditious way of responding to decisions by the ESA, and in particular breach of Union law, the Joint Board of Appeal should resist taking a too procedural approach when examining appeals. There are, nevertheless, certain procedural issues that have been highlighted, for which a legal or practical clarification would be beneficial, in particular, a clarification of the parties' right to refer suspensive decisions to the Court of Justice of the EU. For example, to ensure further transparency and predictability, hearings could be made public and the Joint Board of Appeal could have the explicit power to review the amount of fines (currently it can only confirm or annul an ESA decision) and the power to award costs.

As the Joint Board of Appeal is likely to examine several appeals in the future, it would be wise to appoint the members of the Joint Board of Appeal at different points of time, so as to create more continuity and avoid situations, where it would not be possible to assign a rapporteur for an appeal when all members of the Appeal Board would be reaching the end of their mandate.

## 7. CONCLUSIONS AND RECOMMENDATIONS

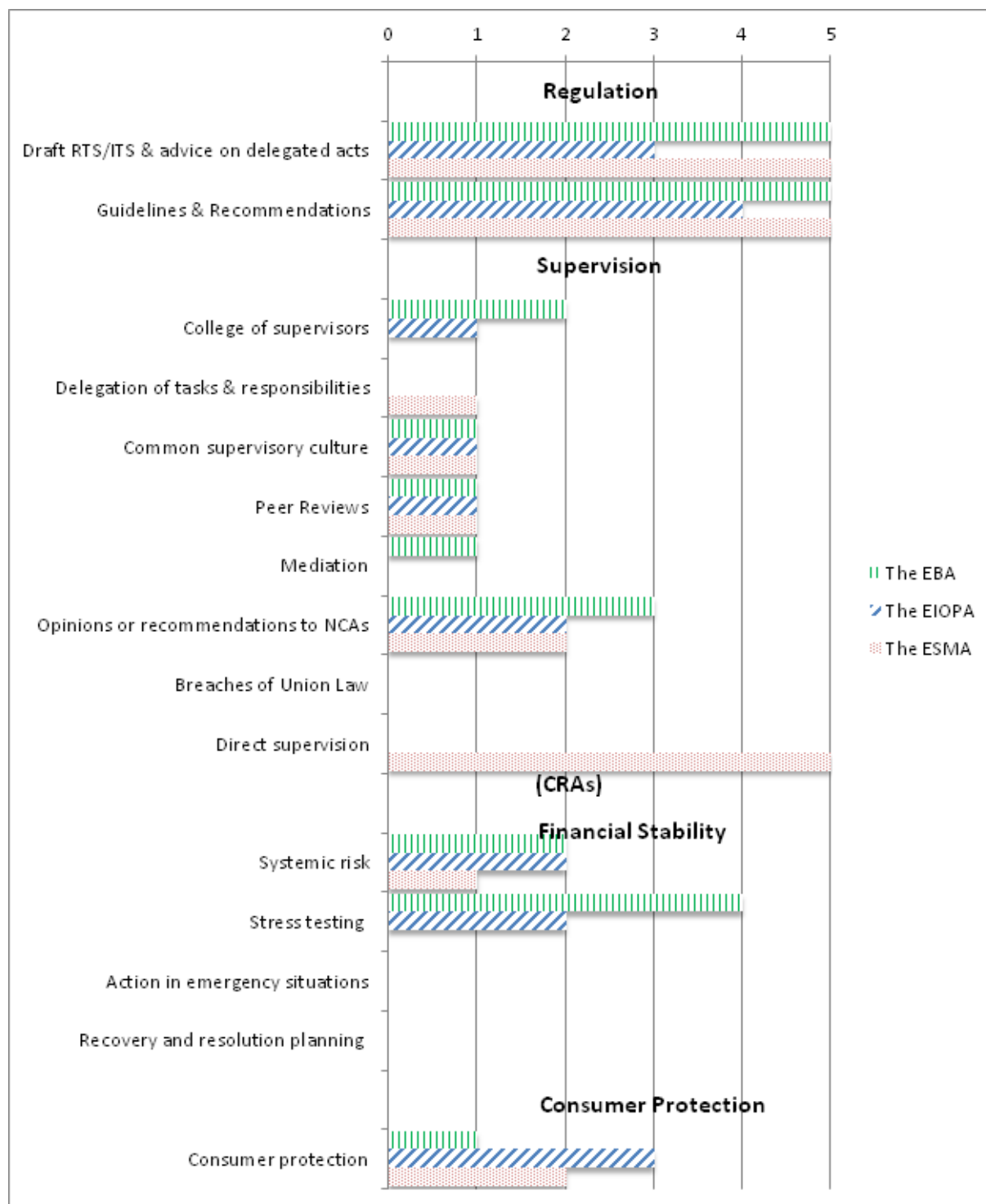
### 7.1. Conclusions

This review of the ESAs' performance confirms that, despite being established during a prolonged and severe crisis in Europe's financial and banking system, and when rapid and far-reaching change was occurring to legislative acts and regulatory standards in the EU and internationally, the ESAs have made significant progress towards being recognised Authorities in their own right. The ESAs have gained influence within the financial services industry and with national regulators in a relatively short period (see Annex, points 1, 2 and 3). From an operational perspective, the ESAs have been successfully established and have built well-functioning organisations while facing very material demands on limited resources. They have been successful in attracting quality staff with sufficient diversity. The Chairpersons, Executive Directors and senior members of staff have navigated a complex range of issues and, in doing so, displayed sound judgement when taking decision with objectivity and impartiality. This establishment of the ESAs, achieved in difficult circumstances, is commendable.

A key conclusion, valid for the EBA, the EIOPA and the ESMA, is that although the ESAs have contributed efficiently to the Single Rulebook, they have not used their powers to ensure consistent supervision across the EU to the extent anticipated by stakeholders. The ESAs have not played a comprehensive role in identifying (peer reviews), tracking (mediation), policing (opinions or recommendations), and enforcing divergent applications of EU law (breach of Union law) by the NCAs or providing rapid and consistent answers to market participants on divergent applications of EU law. The unanimous view of stakeholders is that the benefits of legal and regulatory harmonisation will be lost without consistent implementation and application across the EU. Consistent supervision should therefore be the ESA's priority going forward. ESAs' timid supervisory role to date might be explained by a lack of time and resources, initially concentrated on establishment, intense regulatory work, or even by an instinct to proceed cautiously. Such caution could be explained by a more acute national interest pressure on NCAs during the financial crisis undermining their normal cooperative stand. But the analysis shows that the governance arrangements and the legal conditions attached to the use of such powers are the key inhibiting factors of ESAs' supervisory role. This report recommends that there is more focus on consistent supervision in the Board of Supervisors.

The following chart on the intensity of use of the various roles executed by the ESAs<sup>230</sup> illustrates this key conclusion across a scale '0' to '5' ('0' means that the ESA has not used a power at all, '1' means the power has been used very little and so on, with '5' meaning the power has been used regularly and without constraints).

<sup>230</sup> This chart is for illustrative purposes only and is largely synthetic and judgement based. Judgements are based on matters previously analysed throughout the chapters above, the number and nature of decisions made, the allocation of resources to an area and the matters reflected in the publications and external communications reviewed discussed throughout this report.

**Figure 9: Intensity of use of ESA powers**

**Source:** Mazars.

Another significant conclusion is that the ESAs' independence and role within the ESFS, and relationship with other institutions, needs a stronger foundation. A number of steps are required to achieve that, in particular: an ability to contribute to the design of the EU financial system (and not only produce technical standards as requested), a higher administrative rank for the Chairperson, more senior staff, stakeholder groups composed of higher ranking practitioners and more consumers, additional resources, and flexibility to allocate budgets. Several recommendations thus suggest solutions to increase the ESAs' institutional profile and performance.

Less than three years is a short observation period. This being said, even based on almost identical Regulations, the ESAs' scope have evolved differently during their short lives. The EBA has been immediately confronted with the crisis and its role has already been modified to take account of the future SSM. The EIOPA has been active but is missing the implementation of the fundamental legal act to create a modern integrated Single Market for insurance undertakings. The scope of action of ESMA has been significantly expanded to newly regulated areas, including direct EU-wide supervision.

This raises several questions: Should the recommendations of this report be equally applicable to all ESAs? Should the recommendations be different and focus on making each ESAs more efficient within its own environment? What is the impact of the creation of the SSM on the ESAs? Is it the right time to consider regrouping the ESAs? What is then the ideal EU supervisory architecture?

Even if it is not echoed by the stakeholders interviewed, some may argue that the ESAs' structuring in three separate authorities might create inconsistencies of approach, favour regulatory arbitrage and a lack of cross-sector and holistic treatment of risks and supervisory responses. Two possible responses to these criticisms could be to merge the three ESAs into a single EU authority competent for the three sectors or to create two authorities: one in charge of prudential matters and the other one of consumer/investor protection matters ('Twin Peaks'). In itself, the creation of the SSM results in a more integrated prudential supervision of a significant number of credit institutions, but does not fundamentally change the debate on the pros and cons of more cross-sector structures within a single authority or spread between two authorities in charge of two distinct supervisory objectives (prudential and consumer/investor protection).

The conclusion of this review is that it would be premature to consider further redesigning the ESAs' structure per sector at this point. The merger of two or all three ESAs would create a number of uncertainties (legal framework, hesitation in the recently recruited staff, etc.) and additional costs. This is not what the ESAs need after three years of functioning. Equally, the location of the ESAs in London, Frankfurt and Paris has not been an obstacle to their successful establishment (see Annex, point 4) nor to close cooperation between ESAs.

There are also no failures justifying or compelling evidence for the creation of a single EU authority covering the three sectors. There are, however, factors pointing towards a trend to structure EU legislation and the ESA's supervisory roles according to two fundamental supervisory objectives: prudential supervision and consumer/investor protection supervision.

## **7.2. Recommendations**

The recommendations in this report seek to reinforce the ability of the EBA, the EIOPA and the ESMA to exercise the powers they have been granted already, in particular their powers in relation to supervisory consistency. Most recommendations suggest practical and operational improvements. Others require clearer interpretations of the ESA Regulations, and only a few recommendations would require a legislative change to the ESA Regulations (notably recommendations 3 to 7, 14, 20, 22, 35, 40, 43, 44, 45, 56, 64, 71 to 73).

### **7.2.1. Governance and Profile**

A key recommendation to enhance the performance of the ESAs is to introduce operational improvements in the governance structure, to raise the institutional profile of the Chairpersons, to strengthen the composition of the stakeholders groups and to base their funding on a separate line in the EU budget. Such enhancement of the ESAs' profile would increase the EU's influence vis-à-vis third country supervisors or within international supervisory organisations. As regards the ability to exercise powers to ensure supervisory



consistency more deeply, because the EBA will be the link and will create supervisory consistency between the euro area/SSM participating Member States' banks and the non-participating Member States' banks, such improvements are necessary for the EBA. Having in mind that the ESMA's extended scope of action and its direct supervisory tasks both require an ability to provide rapid responses to market players request for level playing field, the ESMA has also reached the point where a revised governance structure would be beneficial. The EIOPA's governance should also be reviewed as the creation and consistent implementation of the Solvency II and IORP regimes are challenges that require solid EIOPA governance.

### **Introduce operational improvements to the governance structure**

**1 - A strategic and policy oriented Board of Supervisors.** The ESAs' Board of Supervisors should devote more of its agenda to key policy and supervisory issues. It should define and express an ESA view on the key issues for the development of the ESFS. It should also consider the risks facing the ESFS and determine the appropriate regulatory and supervisory responses and approaches for the EU financial sector.

**2 - A sub-committee of the Board of Supervisors to address technical discussions.** To have more flexibility to set its own agenda the Board of Supervisors should create a sub-committee of the Board of Supervisors to filter remaining open issues and prepare technical decisions on regulatory matters that would become items for formal decision by the Board of Supervisors.

**3 – An Executive Board.** The ESAs should have a governance structure that includes an Executive Board composed of the Chairperson and some full-time members sitting in the Board of Supervisors. Executive Board members would vote in the Board of Supervisors on all issues except those requiring QMV (in particular regulatory work leading to binding implementing rules). Executive Board members would be selected according to their prior experience, be of senior role and reinforce the Chairperson's and the ESAs' decisions on matters relating to supervisory consistency. The members of the Executive Board would be appointed for a period of four years (renewable once) and not necessarily selected among active national regulators/supervisors. Areas of work or tasks performed by the ESAs could be allocated to individual members of the Executive Board.

**4 – Replacement of the Management Board.** The Executive Board should replace and takeover the tasks of the Management Board, perform direct supervisory functions (where applicable) as well as all other functions delegated by the Board of Supervisors.

**5 – Voting right of the Chairperson.** The Chairperson should have a casting vote on all issues decided by the Board of Supervisors except on matters requiring QMV (in particular regulatory work leading to binding implementing rules).

**6 – Appointment of the Chairperson.** Within such governance arrangements the Chairperson should be selected and proposed by the Board of Supervisors, appointed by the Council and confirmed by the European Parliament.

**7 – Appointment of the members of the Executive Board.** The members of the Executive Board should be selected and appointed by the Board of Supervisors and thereafter confirmed by the European Parliament.

**8 – Timing of governance improvements.** Such evolution in the ESAs' governance would require an initiative by the European Commission and an agreement by the two colegislators and should ideally be in place following the current review.

## **Increase the profile of the positions of Chairperson and Executive Director**

**9 – Appointment by the Board of Supervisors and confirmation by the European Parliament.** Under the current ESA Regulations, the appointment of the Chairperson and the executive director should be made in accordance with Article 48 and 51 ESA Regulations. The role played by the European Commission in the appointment of the first Chairpersons and executive directors should not be repeated.

**10 – Enhanced administrative profile.** The administrative ranking of the Chairperson should be at least as high as that of a Director General of the European Commission. The administrative ranking of the executive director should be at least as high as that of a deputy Director General of the European Commission.

**11- No additional conditions.** The age limit introduced for the appointment of the first Chairpersons should be abolished.

## **Enhance the Accountability, Transparency and Independence of the ESAs**

**12 – Accountability vis-à-vis the Council.** Chairpersons should be formally invited at least twice a year to ECOFIN meetings to report on their activities and present their work programme.

**13 - Authorities in their own right.** To the extent possible under the EU agencies framework, the independence and profile of the ESAs should be enhanced and translated in particular into a more flexible application of certain administrative rules duly justified by the specificities of their tasks (for example, for the recruitment of qualified staff in some, particularly technical, areas).

**14 - Funding** - ESA funding should form an independent line in the EU budget and in addition and, where possible without creating two layers of regulatory fees, contributions from regulated entities or activities (collected by the NCAs on behalf of the ESAs).

## **Strengthen the Stakeholders Groups**

**15 - Enhancing the contribution of the stakeholders groups.** The stakeholders groups should have a greater role in informing the ESAs' work. In particular, they should take a more strategic approach to identifying priorities for reform to Europe's financial sector, risk identification, and their oversight of the ESAs' regulatory and supervisory activities. The stakeholders groups should also use their powers to submit opinions and advice on supervisory consistency issues, the need for peer reviews or independent assessments (the list of matters to be reviewed should be submitted to the stakeholders groups), requests to investigate alleged breaches of Union law and alerting regulators on market developments more intensively. The ESAs should be obliged to provide reasoned responses to those opinions or advice.

**16 - Resourcing the stakeholder groups properly.** The ESAs should devote more resources to the activities of the stakeholder groups. Members of the groups should also be given a higher level of administrative support. The Chairpersons should have dedicated administrative and research support.

**17 - Appointing higher ranking practitioners and enhanced consumer representation.** Senior practitioners with global experience and a focus on access to capital and the financing of innovation and job creation (i.e. corporate CEOs or entrepreneurs) should be encouraged to be stakeholder group members. A higher representation of consumers is necessary and could be facilitated by a proper funding of their participation and contribution.

## **Contribute to cooperation with Third Country counterparts and International Organisations**

**18 - ESA participation in international regulatory discussions.** The ESAs have gradually increased their participation in international organisations in their respective sectors. This should be pursued to reinforce the representation of the EU within international organisations where ESAs should participate alongside the NCAs with the same membership status (for the EBA and the ESMA). The participation of the EU in the G8 or the G20 should be the model.

**19 - Mutual recognition agreements.** Building on the experience of the ESMA within defined mandates and with timely reporting, the NCAs should consider delegating to the ESAs the negotiation of mutual recognition framework agreements necessary for the application of EU law to third countries' market players.

### **7.2.2. Regulatory Work (The Single Rulebook)**

The ESAs have demonstrated an efficient capacity to develop draft technical standards, recommendations and guidelines (see Annex, point 18). They have conducted their regulatory activity which is consistent with global evolutions in their sectors and in line with the G-20 priorities. From the outset, they have been active producers of draft technical standards. After almost three years of intense regulatory activity, lessons can be learned and improvements put forward. The recommendations relate to the construction of the Rulebook itself or to practical aspects of the ESAs' regulatory work (content of mandates to draft technical standards, deadlines, etc.).

The first one relates to the fundamental objective of the regulatory activity. The objectives in the ESA Regulations are heavily driven by the post-crisis environment and focus mainly on restoring confidence and stability. A widely shared view is that creating a financial system favouring economic growth and job creation should be an additional explicit objective of the ESAs. In particular the ESAs should be obliged to propose proportionate regulatory measures in order not to damage small and medium size market players and therefore apply a 'Think Small First' principle. ESAs should also measure the impact of their proposals beyond the impact on their regulated entities and assess any unintended consequences on the EU economy.

The ESAs and the pan-European market players consider that the Level 1 legislation leaves too many options and discretions for Member States when transposing or implementing such new EU laws. This creates an expectation gap. Stakeholders expect the ESAs to reduce such diversity themselves by using their consistent supervision powers. But the ability to do so is almost nil in the absence of substantive harmonisation at Level 1. The ESAs should give an opinion on new proposed legislation within their scope of competence.

An unclear use of the hierarchy of norms at EU level is a common feature arising from the first years of adoption of delegated and implementing acts, RTSs and ITSs. The legislation is considered to be too detailed, and this affects the flexibility needed for very technical matters that should be easily and rapidly adaptable to market changes. The basic principle is that such acts should complement and refer to each other starting from key principles and ending in technical and practical details. In addition, there is no predictable reason that explains why co-legislators chose delegated acts (where the ESAs may act as advisors of the European Commission), implementing acts or technical standards (where the ESAs prepared a draft to be endorsed and adopted through a specific process). So far they are often used in parallel. Furthermore, the status of guidelines and recommendations lacks predictability, in particular in the absence of EU legislation. The recent decision of the Joint Board of Appeal contributes to specifying how such non-binding measures contribute to more consistent supervision across the EU.

The exercise of delegation to adopt technical standards is conferred for a period of four years. It would seem appropriate to evaluate the use of such delegation as a whole but also for each specific EU law in order to measure if the combination of the legislation and the implementing measures has produced the desired effects in each regulated area.

Finally, cross-sectoral conflicting definitions and inconsistencies between groups of binding Acts is a matter of concern for market players. Structuring the legislative and regulatory activity of the EU would increase the coherence of the Single Rulebook. For example, a codification of adopted Acts would significantly ease implementation. Preferably this should be done in two codes, already 'pre-designed' in the EU legislative and regulatory framework: a Prudential Code and a Consumer/Investor Protection Code.

## A Structured Rulebook

**20 – Financial markets favouring economic growth and job creation as an additional explicit objective of the ESAs' impact assessments.** In order to ensure that the ESAs regulatory activity takes due account of the need to create financial markets that favour long-term investment, economic growth and job creation, impact assessments should measure and explain the impact of proposed measures on such key objectives. ESAs should apply a **'Think Small First' principle** when developing new implementing measures and apply proportioned rules to small and mid-sized businesses. This recommendation echoes the concerns raised by the European Commission's Green Paper 'Long term Financing of the European Economy'<sup>231</sup>.

**21 - Contribution to the designing of the Single Market for financial services.** The legislative process could benefit from the regulator's and supervisor's knowledge on key structural choices and supervisory approaches to create integrated EU financial markets. For that purpose, the ESAs should give **formal opinions on proposed legislation within their respective scope of action**. This should be made explicit in Article 34(1) ESA Regulations.

**22 - Codification to ensure cross-sector and cross-legislation consistency.** To avoid conflicting definitions and legislations, a codification would significantly increase the coherence of the Single Rulebook. Considering the evolution of the structure of the EU legislation and the scope of action of the ESAs this codification could be composed of a **Prudential Code and a Consumer/Investor Protection Code**.

**23 - Full use of the EU hierarchy of norms.** Level 1 Legislation should focus on the key harmonised provisions leaving detailed and practical to delegated acts, implementing acts, RTSs and ITSs or non-binding measures, and allowing national discretions only in very specific circumstances (where it can be demonstrated that they do not impinge the concept and the stability of the Single Market).

**24 - Clarification on the use of direct delegated or implementing acts or delegated or implementing acts laying down RTSs or ITSs.** The need for flexibility should guide the co-legislators when choosing between the development of technical standards or specific delegated Acts. The use of RTSs or ITSs should be privileged as they imply a higher sense of ownership by the NCAs.

**25 - Evaluation of the power to adopt technical standards.** In addition to the European Commission report on the delegated powers themselves, each EU law and its implementing measures should be evaluated to assess the proper functioning of the hierarchy of norms and whether the combination of such acts has produced the desired effects.

<sup>231</sup> COM(2013) 150 final.

**26 - Relevance of non-binding measures.** The legitimacy of the ESAs when adopting Recommendation and Guidelines should be unquestionable. A clarification of the latitude resulting from Article 1(3) ESA Regulations would be welcomed. Expansion of the ESAs' scope of action by way of sector specific legislation should be added to Article 1(2) ESA Regulations.

**27 – Accuracy of Mandates.** As a matter of good practice, the ESAs should be consulted during the co-decision legislative process on the drafting of clauses referring to the scope of technical standards or delegated acts. The European Commission should also liaise with the ESAs, before sending formal requests for advice.

**28 - Deadlines leading to quality rules.** The reasonable timing for the full transparent and reasoned process for adopting RTSs and ITSs should be 12 months computed from the day of the adoption of the Level 1 legislation. Unless there is a justified emergency, this timing should be the norm.

**29 - Lobbying transparency.** Building on the transparency of meetings of Chairpersons or executive directors, when preparing draft technical standards, advice on delegated Acts or non-binding measures, the Chairpersons of standing committees or working groups should publish the names of market participants, consumer representatives or other relevant individuals or groups they have met each year. ESAs should also publish letters received by external parties in the course of their regulatory activity.

### Fluid Consultations

**30 –Predictability of regulatory work.** To the maximum extent possible, the ESAs should publish a calendar of consultations several months in advance. This would allow stakeholders to prioritise and prepare for consultations.

**31 - The use of 'concept papers'.** The existing consultation process can be improved by publishing concept papers on possible technical standards or delegated acts on Level 1 legislation not yet fully adopted.

**32 - Impact assessment for smaller market participants.** The ESAs should explain in each consultative paper the impact of the proposed measures on small businesses, financial sector innovation and barriers to entry to the financial sector.

**33 - Taking account of consumers.** The ESAs should include in all consultative documents a summary of the proposal in plain language and an explanation of why the proposed measures matter for consumers/users of financial services.

**34 - Composition of consultative working groups.** When consultative working groups composed of market participants are created to assist an ESA's standing committee or working group, they should reflect the balance of composition of the stakeholder group itself. The stakeholder groups should have the right to comment on the composition of such consultative working groups.

### 7.2.3. Supervisory Work - Need for a more intensive use of powers

The limited use of supervisory powers by the ESAs to ensure consistent supervision across the EU or to monitor the implementation of the Single Rulebook might be mitigated in part by enhancing the ESAs' governance structures. But the use such powers requires a number of legal conditions that are difficult to fulfil. These conditions include, for example, a declaration of emergency by the Council, no impact on fiscal responsibilities of Member States, a double legal basis (ESA Regulation and sector specific law), no NCA's competing decision or a demonstration that there is a threat to both the integrity of financial markets and the whole or part of the financial system. These conditions can be explicitly mentioned but sometimes result from interpretations.

The recommendations regarding the role of the ESAs to ensure consistent supervision result from the analysis of the work done so far by the ESAs and from a more ambitious approach often requested by stakeholders to ensure a level playing field (see Annex, point 17). They consist of suggestions for a more intensive use of these powers.

Direct supervision of CRAs is considered a success and shows the benefits of EU-wide approaches to supervision of highly integrated entities or activities.

**35 - Legal conditions to act.** When powers to ensure more consistent supervision across the EU are not used as a result of restrictive interpretations of the provisions of the ESA Regulations, the European Commission should bring more certainty about the conditions to fulfil to use such powers. This includes in particular the ability to prohibit certain activities. When this results from restrictive legal conditions, the EU legislators should consider making this powers more operational for the benefit of the stability of the EU financial system. This covers in particular action in emergency situations, safeguards and powers requiring an enabling sector specific legislation to be activated (double legal basis).

### Consistent Supervision

**36 - Supervisory level playing field.** To help secure a level playing field, the ESAs should be able to provide timely and definitive answers to market participants on issues relating to the application of EU law and rules (i.e. common definitions, regulatory treatment of product innovation). For that purpose, the ESAs should issue more opinions, or develop supervisory standards, under Article 29 of the ESA Regulations. They should also explore the possibility of publishing no action letters committing all NCAs.

**37 – More general and in depth use of colleges of supervisors.** The participation of ESA representatives in colleges of supervisors has improved the functioning of colleges, but the colleges have only made limited progress in enhancing supervisory convergence. Colleges practice should be legally significantly expanded in the area of securities markets. A more straight forward lead supervisor model should be legally extended to the colleges of insurance groups. To create more interaction and provide more harmonised operational supervisory responses, issues identified within colleges should be reported more systematically to the Board of Supervisors for action.

**38 – More resources, people and systems required to conduct stress tests.** The 2011 EBA stress test highlighted the need for significant resources, people and systems, to be devoted to a stress test exercise. In future, an independent (of the ESA, NCAs and the European Commission) analysis of the resources required to complete a stress test should be completed prior to the test taking place. The ESA performing the test should be granted any resources additional to its budget which might be identified through this analysis.

**39 - Delegation of tasks and responsibilities to reduce costs and enhance supervisory efficiency.** Following a cost benefit analysis, the NCAs should consider pragmatic delegations of tasks and responsibilities to the ESAs under Article 28 ESA Regulations where this would enhance the overall supervisory efficiency of the Single Market and mutualise costs (for example: the centralisation of IT systems to compensate for excessive fragmentation undermining proper supervision).

### Supervision of Implementation

**40 - From peer review to independent assessments.** Peer reviews were conceived before the creation of the ESAs, and with a model of voluntary cooperation envisaged. In the few cases where they have been carried out, they have not translated into meaningful list of implementation weaknesses and concrete action plans. The ESAs should now be able to conduct, in accordance with clear processes, independent assessments (including on-site visits), similar to an IMF FSAP, in order to strengthen supervisory consistency. The result of



these independent assessments, and associated plans to correct identified gaps, should be made public.

**41 – More intense use of mediation.** No case has been mediated by an ESA since establishment, even if some requests have been put forward. The ESAs have promoted mutual understanding between NCAs or the drafting of guidelines which have produced the desired effect. This said, the Board of Supervisors should be systematically informed of the decision to open or not to open mediation. After gaining some experience, the ESAs should review their mediation practice in order to assess if there are disincentives to trigger the mediation process.

**42 – Individual opinions and breaches of Union law:** No breach of Union law case has been reported. However, in some cases, the ESMA has issued opinions to individual NCAs as a preamble to a breach of Union law procedure. This practice could be extended to the other ESAs. In order to create more predictability of the application of EU laws, there should be more transparency on the decisions to open or not an investigation. The recent decision by the Joint Board of Appeal might force this to happen. After gaining some experience, the ESAs should review their breaches of Union law practice in order to assess if there are disincentives to trigger a breach of Union law procedure.

### Direct Supervision

**43 – Direct EU-wide supervision for highly integrated entities, activities or financial instruments.** EU-wide supervisory responsibilities have been successfully implemented by the ESMA. Where a cost benefit analysis demonstrated this would be beneficial for the overall supervision of the Single Market, the ESAs should be entrusted with additional direct EU-wide supervisory powers. Sector or product specific legislative initiative should demonstrate why it is more efficient that supervisory powers stay at Member States level. Candidates for such subsidiarity test could include: CCPs, CSD or index providers.

**44 – A Financial Markets Union? An Insurance Union?** Depending of the degree of integration of financial markets and the insurance market within the Single Market and the success of the ESMA and the EIOPA going forward, policy makers should consider at some point in time creating a Financial Markets Union and/or an Insurance Union.

#### 7.2.4. Consumer Protection

Consumer protection work has not been the highest priority of the ESAs, and each ESA has followed a different approach to fulfil their mandates. They have been active jointly and separately and made some progress in the area of consumer protection, but less than some stakeholders would like. The understanding and identification of consumer trends is more difficult due to the challenge of obtaining uniform information on those matters across the Member States and the ESA's lack of proximity to retail investors. Here again, the ESAs capacity to act in cases of a threat to the consumer is the less intensively used power. This is because the legal interpretation or conditions for its use are almost impossible to fulfil.

**45 – Clarity on the use of Article 9.5 of the ESA Regulation:** The European Commission or the co-legislators should create less restrictive conditions for the use of Article 9(5) ESA Regulations powers for the EU-wide banning of activities that threaten consumers. In situations where the ESAs decide not to take action, the European Commission should be duly informed.

**46 – Consumer protection policy and strategy:** Article 9 ESA Regulation confers a wide range of consumer protection tasks to each ESA. Together within the Joint Committee, and subsequently individually, the ESAs should elaborate a structured policy and strategy that would list priorities, define their respective roles, the articulation with the NCAs that

possess the best proximity with consumers of financial services and the necessary resources. The sub-committee on Consumer Protection and Financial Innovation of the Joint Committee should play here a pivotal role after close consultation of the relevant stakeholders.

In addition to the recommendations applicable to the three ESAs, the review shows that the EBA, the EIOPA and the ESMA have specific needs to carry out efficiently their tasks in their respective scope of action. Some recommendations are also put forward for the improvement of the functioning of the Joint Committee and the Joint Board of Appeal.

#### 7.2.5. The EBA

The EBA has gained credibility in a highly challenging environment. In future, it will serve as a bridge between SSM and non-SSM members, and in this capacity as a guardian of coherence in banking regulation and supervisory consistency for the EU as a whole. It will have a key task in ensuring coherence in the common implementation of the Single Rulebook in the Single Market, as well as the preservation of common supervisory practices across the EU through the Supervisory Handbook.

#### Colleges of supervisors

**47 - EU-wide colleges of supervisors.** The EBA needs to identify the number and nature of resources required for it to deliver a successful college process in particular for banks active beyond the SSM area. The Board of Supervisors and the European Parliament should consider this information as part of an overall review of the ESAs' resources.

**48 - Binding mediation within the colleges.** The operability of binding mediation powers should be reviewed with a view to eliminating any ambiguity which would inhibit the development of the college process.

#### Common supervisory culture

**49 - Consistency of the supervisory handbook.** The EBA should establish jointly with the ECB protocols for the development of the EU-wide and SSM-specific supervisory handbook to ensure that they are complementary and do not create breaches in the level playing field.

#### Consumer protection

**50 - Risk for banking services users.** The EBA should develop measures to allow it assess the progress of its strategy and indicators to allow it to identify new risks for consumers in the banking sector.

#### 7.2.6. The EIOPA

The main component of EIOPA's work has been on regulatory matters related to the delayed Solvency II Framework Directive as well as the Institutions for Occupational Retirement Provision (IORP) Directive. The delay on Solvency II has created hesitations and a lack of focussed project planning. The implementation of these regimes should help the EIOPA to exercise the full scope of its mandate and in particular should significantly ease the use of powers to ensure consistent supervision across the EU. A more straightforward functioning and decision making capacity of colleges of supervisors for insurance groups would contribute to more efficient supervision. The EIOPA has developed some significant initiatives in this direction but a reinforcement of the EIOPA's role based on a stronger expertise and legitimacy should be set up in parallel with a strengthening of the group supervisor's legal role.

## Regulatory work

**51 - Implementation of Solvency II.** Based on the outcome of the LTGA and the IORP assessment, co-legislators should promptly reach a balanced agreement on the implementation of the Solvency II framework.

**52 - Status of Interim Guidelines.** The status of EIOPA's work to prepare for the implementation of Solvency II should be clarified with the European Commission given the impact on the industry before the end of the discussions on the re-design of Solvency II and the deadline to implement of the framework.

**53 - Solvency II project planning.** To ensure efficient decisions by the Board of Supervisors and NCAs adherence, the EIOPA should set more clearly the key objectives, consequences, deliverables, means, and steps leading to the smooth implementation and application of the framework.

**54 - Sharing of experience on insurance and pension supervision.** To favour a more efficient regulation and implementation of the Solvency II and the IORP regimes, experience sharing on common issues should be further encouraged between insurance and pension working groups.

## Supervisory work

**55 - Common insurance supervisory culture.** The implementation of the Solvency II framework will significantly increase the opportunities to develop consistency of supervisory practices in the insurance sector. A supervisory handbook to implement the Solvency II framework will contribute to more harmonised approaches across the EU.

**56 - An enhanced group supervisor role.** Efficiency of colleges of insurance supervisors would benefit from a reinforced role given to the group supervisor and an increased ability to take final decisions. A more straightforward functioning of colleges should be developed building on experience gained in the banking sector with the lead supervisor model. It should be developed alongside the draft recovery and resolution mechanism.

**57 - Foster EIOPA expertise on internal models.** To ensure more consistency for internal model validation under Solvency II, the EIOPA should have full support to further develop a centre of expertise building on the successful experience of NCAs and in close cooperation with NCAs experts.

## Financial stability work

**58 - Better coordination to identify systemic risks and adverse market developments.** The EIOPA should better organise flows of information with NCAs to identify risks and measure their impact on both Members States and in the EU. This would enhance stress tests efficiency.

**59 - Access to relevant data.** The EIOPA should get more legal certainty to obtain and use formatted data without breaching data protection rules. This could be specified in a framework clarifying the ability to use such data.

### 7.2.7. The ESMA

The ESMA has carried out intensive and innovative regulatory activity to produce technical standards for revised legislation and for newly regulated activities and areas that were not regulated prior to the crisis. This has required and will require significant resources. This includes a successful EU wide direct supervision of CRAs (and soon trade repositories) for which some improvements can be suggested. The ESMA's work on consistent supervision has had less impact - notably the absence of stress testing of market infrastructures and work within colleges of supervisors. In addition, as with any securities regulator, the ESMA

should develop a capacity to promptly answer requests for clarification on the application of EU law by market players operating in a fluid market.

**60 - Additional resources.** The ESMA's budget should be increased to the extent necessary to fulfil it increasing its tasks and responsibilities. In addition to the general review of the funding of the ESAs, the ESMA should consider more industry financing.

**61 - Market trends knowledge from stakeholders.** The ESMA's Committee for Economics and Market Analysis could include a consultative working group to gain information from stakeholders.

### **CRA**s

**62 - Separation of CRA supervisory functions.** For legal reasons, the ESMA should clearly separate internally its various CRA direct supervisory roles: regulatory, on-going supervision, investigation (the investigative officer) and above all, sanctions.

**63 - Transparency vis-à-vis NCAs.** The ESMA should make supervisory actions regarding CRA that may impact the markets they are responsible for fully transparent to NCAs.

### **Colleges of supervisors**

**64 - More active participation in colleges of supervisors.** The ESMA should be legally allowed to expand the scope for participation in colleges of supervisors to include market operators of regulated markets and other trading venues as well as for cross-border asset management companies and central securities depositories.

### **IFRS**

**65 - Harmonised approaches to IFRS implementation.** The EU should clarify the role of the ESMA and other bodies for the definition of IFRS harmonised approaches in the EU. This will ensure more predictability and a level playing field.

### **Provide rapid responses to market players**

**66 - Level playing field and market responsiveness.** The ESMA should develop a capacity to promptly respond to market participants' questions about divergent implementation of EU law or rules by the NCAs to ensure a level playing field.

### **Stress testing, recovery and resolution planning**

**67 - Market infrastructures stability.** The ESMA should put in place stress testing and recovery and resolution planning for trading venues and market infrastructures (in particular CCPs).

#### **7.2.8. The Joint Committee**

The Joint Committee has proven a useful mechanism to conduct cross-sector projects. It has also provided a valuable contribution in establishing common procedures and rules of the ESAs. The Joint Committee enhances coordination within a supervisory system articulated along three financial sectors regulated at EU level by three separate authorities. However, the scope of action of the Joint Committee is relatively limited and largely invisible to stakeholders. One important step was taken with the creation of the Sub-Committee on Consumer Protection and Financial Innovation to enhance consumer protection and help the ESAs fulfil their mandates in this area. Further steps to organised work according to key supervisory objectives would increase the relevance of the Joint Committee.

**68 - Structuring the work according to key supervisory objectives.** To enhance its efficiency, and support the work of the ESAs, the Joint Committee should structure its work around two major supervisory objectives and be composed of two major standing sub-

committees: one devoted to prudential matters (including financial conglomerates) and the other consumer protection and financial innovation. The ESAs could delegate to such standing sub-committees some tasks for which they have limited resources or difficulties in establishing them as a priority.

**69 - Joint Committee and ESAs newsletter.** Stakeholders and the general public would benefit having an overall vision of ESFS achievements. Currently numerous publications on the ESAs' work are published separately and are difficult to track. The ESAs, the Joint Committee, (including the Joint Board of Appeal), should consider publishing a periodic newsletter announcing imminent consultations and reporting decisions taken jointly or in each sector.

#### 7.2.9. The Joint Board of Appeal

Following its first decision, the Joint Board of Appeal has given a first indication of the scope of appeals that are admissible and for which the ESAs have a duty to act regarding the matters of consistent supervision (in particular breach of Union law). It has clarified the legal status of guidelines and recommendations. By deciding rapidly on an appeal (two months) the Joint Board of Appeal creates a more fluid functioning of the Single Market and is a real added value compared to a case directly brought before the Court of Justice of the EU (which is eventually the sole interpreter of Union law). The Joint Board of Appeal is likely to examine an increasing number of appeals in the future and to maintain its efficiency some procedural aspects would benefit from a clarification.

**70 - Flexible and transparent procedural approach.** In order to keep this expeditious way of responding to decisions by the ESA, the Joint Board of Appeal should resist taking a heavily juridical or procedural approach when examining appeals. More transparency could be achieved by making hearings public.

**71 - Referral of suspensive decisions to the Court of Justice of the EU.** The provisions of the ESA Regulations should make it clear that a suspensive order of the Board of Appeal (or a refusal to make such an order) can be subject by the parties to an immediate proceeding before the Court of Justice of the EU.

**72 - Power to review fines.** For meaningful appeals, the Joint Board of Appeal should have the explicit power to review the amount of fines decided by an ESA (currently it can only confirm or annul a decision). It should also have the power to award costs.

**73 - Continuity.** To ensure continuity and avoid situations where it would not be possible to assign a rapporteur for an appeal, it would be wise to appoint the members of the Joint Board of Appeal at different points of time.

## REFERENCES

**Notes:** i) Links are as accessed in October 2013.

ii) Links to consolidated versions of legislation (which have no legal bearing) are for convenience only.

iii) ESAs own documents are to be found under EBA, EIOPA, ESMA, respectively; joint documents by EBA, EIOPA and ESMA are to be found under 'European Supervisory Authorities'.

iv) Otherwise, documents are sorted by date (ascending).

- Alford, D., *The Lamfalussy Process and EU Bank Regulation: Another Step on the road to Pan-European Regulation?*, Annual Review of Banking & Financial Law, Vol. 25, p. 389 (2006); [http://www.wiwi.uni-muenster.de/iw/downloads/web/ss09/WEB-11%20Alford\\_LamfalussyProcessandEUBanking\\_Final.pdf](http://www.wiwi.uni-muenster.de/iw/downloads/web/ss09/WEB-11%20Alford_LamfalussyProcessandEUBanking_Final.pdf).
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## ANNEX: SUMMARY AND OVERVIEW OF CONSULTATION AND INTERVIEWS HELD

This Annex provides a brief summary and a statistical graphic overview of the number of stakeholders consulted with over the course of this study to gather views and opinions on the ESAs' performance. The consultation was carried out by online questionnaires as well as face to face or telephone interviews with a wide range of stakeholders.

### The questionnaires

One online questionnaire per ESA was prepared covering the work and performance of the ESAs since their establishment in January 2011. The questionnaires comprised approximately 70 questions each covering the main responsibilities and tasks of the ESAs set out in the ESA Regulations, and sought ratings, opinions and comments. The deadline for completing the questionnaires was 21 June 2013 allowing for a five week response period. The questionnaires were accessible on the website of the ECON<sup>232</sup> and of the EBA, the EIOPA and the ESMA. Some market participants/associations indicated that they would recommend completing the questionnaires to their members. 105 informative responses to the questionnaires were received from stakeholders:

- 24 replies to the EBA consultation;
- 38 replies to the EIOPA consultation; and
- 43 replies to the ESMA consultation.

Most respondents provided very comprehensive answers to the questionnaires. Some respondents only answered questions applicable to their industry or type of organisation. The summary below is based on respondents that completed the questionnaire fully or partially (some stopped before the end of the questionnaire, others only responded to a selected number of questions). This has been taken into account when consolidating data: for each question the number of respondents that answered or skipped questions has been identified. Percentage figures are therefore based on a number of responses which differs from one question to the other. In addition, the respondents were given an opportunity to respond anonymously, which a number opted to do.

### Summary of responses to ESA questionnaires

In most cases respondents were offered the possibility to provide

- answers ranking from (1) worst to (5) best or '*not applicable*'; e.g. on the question '*how do you rate the ESA's performance against its mandate?*', respondents could answer: 'poor (1)', 'not good (2)', 'average (3)', 'good (4)' or 'very good (5)'.
- For some other questions the possible answers were 'yes' or 'no' or '*not applicable*'.

This summary reflects the majority of opinions of the stakeholders' responses to the key questions. For that purpose, categories of possible answers are regrouped to reflect such majority view and, when necessary, some significant opinions are highlighted.

- 1. ESAs purpose** – An clear majority of respondents (90 %) consider that they have 'good' or 'very good' understanding of each ESA as set in their founding regulations.
- 2. ESAs current role** – Generally speaking, respondents consider that they are 'well aware' or 'very well aware' of ESA's activities and achievements to date but with some nuances: 89 % for EBA (68 % being 'very well aware'), 75 % for EIOPA (43 % being 'very well aware') and 82 % for ESMA (37 % being 'very well aware').

<sup>232</sup> <http://www.europarl.europa.eu/committees/en/econ/subject-files.html?id=20130523CDT66527#menuzone>.

- 3. ESAS performance to date** – 50 % of respondents consider that the performance of the ESAs against their mandate has been 'good'.
- 4. Impact of location on recruitments** – Most of the respondent believes that the location of EBA (London), EIOPA (Frankfurt) and ESMA (Paris) has 'no obvious impact' or a 'positive impact' on recruitment: 85 % for EBA, 92 % for EIOPA, 75 % for ESMA.
- 5. Independence from Member States** – Respondents had different opinions for each ESA. On average, more than 50 % consider that the ESAs are 'independent' or 'very independent' from Member States but with significant difference. The EIOPA is considered the most independent (69 %), with ESMA (51 %, but 48 % believing that ESMA is only 'relatively independent' or has a 'limited independence'), and EBA (55 %, but 35 % believing that it is 'not independent' or has 'limited independence').
- 6. Independence from the European Parliament and Council** – Regarding the EU institutions, the ESAs are considered 'independent' or 'very independent' from the European Parliament: 78 % for the EBA, 61 % for the ESMA, but 48 % for the EIOPA. The opinion on the independence vis-à-vis the Council is more nuanced: 77 % for the EBA (but 11 % consider that EBA is only 'relatively independent'), 56 % for the EIOPA (but 32 % believing that EIOPA is only 'relatively independent') and 51 % for the ESMA (but 33 % believing that is only 'relatively independent').
- 7. Independence vis-à-vis the European Commission** – There is a clear difference of opinion regarding the independence of the ESAs vis-à-vis the Commission. Most consider that the ESAs are 'not independent', have a 'limited independence' or a 'relative independence': 72 % for the EBA (33 % consider that EBA has 'limited independence'), 80 % for the EIOPA (52 % consider that EIOPA has 'limited independence'), 83 % for the ESMA (36 % consider that ESMA has 'limited independence').
- 8. Accountability** – A clear majority of respondents (more than 65 %) consider that the accountability regime of the ESAs is 'relatively effective' or 'effective' but for EBA (47 %) and ESMA (38 %), the rate 'relatively effective' is the rate most often given.
- 9. Greater cooperation between NCAs** – A very clear majority of respondents believe that cooperation between NCAs has improved with the creation of the ESAs with some nuances per sector: Insurance (80 %), Banks (78 %), Pension (70 %) and, a little less for Security Markets (62 %).
- 10. Working relationship with the ESRB** – Respondents are clearly aware of the ESRB relation with the EBA (90 %) and with the EIOPA (76 %) but less with the ESMA (50 %).
- 11. Language of consultations** – A clear majority of respondents (more than 70 % on average) do not believe that a translation of ESAs work in the 23 official languages of the EU would lead to more participation and transparency in consultations.
- 12. Quality and timelines of publications** – There is a majority (more than 50 %) of respondents considering that the documentation produced by the ESAs (Advice on delegated Acts, drafts RTSs or ITSs, guidelines and recommendations, opinions, consumer warnings, ...) are of 'good' or 'very good' quality. But a visible lack of satisfaction on the timelines of these publications, in particular when it regards consultative documents with 'regular' being the most often rate given.
- 13. ESAs website** – The website of the EIOPA and the EBA are considered to be the most informative (78 % and 72 % 'good' and 'very good') by respondents but not the ESMA (41 % 'good' and 'very good' - 47 % stated only 'relatively good'). Respondents

consider that the EBA website is the most user friendly (58 % 'good' or 'very good' - however, this applies to the previous EBA website which has subsequently been re-designed in mid-2013), followed by the EIOPA website (50 % 'good' and 'very good') and the ESMA website not being considered user friendly (63 % 'poor' or 'not good'). A majority (more than 60 %) of respondents consider that the ESAs websites are up to date.

- 14. Consumer protection** - Consumer protection work is more known by respondents done by the EIOPA (79 %) than by the ESMA (66 %) and the EBA (66 %) and more than 50 % consider that it is effective. It should be noted that, when responding to questions about specific consumer protection work, some respondents responded 'not applicable' in the case of the EBA. They also consider that the three ESAs should play a more active role in reviewing and coordinating financial literacy and education initiatives by NCAs (on average more than 65 % considering this role not sufficiently developed). Expectations are clearly stronger on the ESMA in particular the collection, analysis and reporting on consumer investor trends (69 % considering that it should be further developed). As regards the contribution to the development of common disclosure rules, the expectation is higher on the EIOPA (68 % considering that it should be further developed) and on EBA (52 %). The issuance of warnings to consumers (only few have been issued by EBA and ESMA) is considered to be positive first action – more than 60 % of respondent considered it 'regular', 'positive' or 'very positive'.
- 15. Direct supervision of CRAs by the ESMA** - The direct supervision of CRAs by the ESMA is considered to be 'good' or 'very good' by 58 % of the respondents. A clear majority (66 %) of those who responded believe that CRAs play a more efficient role within the financial market since they were regulated and supervised at the EU level.
- 16. Colleges of supervisors** - A majority (55 %) of the respondents that have a direct experience in colleges of Supervisors in the banking and insurance sector believe that the college process is an effective addition to supervisory process.
- 17. Supervisory convergence** - A vast majority of respondents consider that the creation of the ESAs facilitates supervisory convergence (80 %) but when they rate the performance of each ESA to contributing to a consistent application of legal acts, opinions are more divided and diverse: Comparatively, the EBA is considered the best contributor (58 % of 'good' or 'very good') followed by the ESMA (51 %) and the EIOPA (46 %), which in contrast means that 42 % (EBA), 49 % (ESMA) and 54 % (EIOPA) of respondents believe that further progress is needed.
- 18. Regulatory work** - Generally, the regulatory work (advice on delegated acts, draft RTSs and ITS, issuance of guidelines and recommendations or opinions) of the ESAs is considered to be 'good' or 'very good' by 60 % of the respondents (on average). It should be noted that numerous respondents ticked the box 'not applicable' in the case of EIOPA due to the fact that the Solvency II directive is not yet applicable. Views are more divided regarding issuance of guidelines, recommendations and opinions by the ESMA (with 'average' and negative rates - (1) or (2) - reaching almost 50 %).
- 19. Measurement and monitoring of systemic risk** - Respondents consider that the EBA (52 % of 'good' or 'very good') and the EIOPA (50 %) have been the most active in monitoring systemic risk, less for the ESMA (52 % of 'average' rate).
- 20. Assessment of SMEs and MidCap market developments** - The majority of respondents do not consider that the ESAs have sufficiently assessed these market developments (60 % for EBA and 74 % for ESMA including 31 % rate of 'poor').

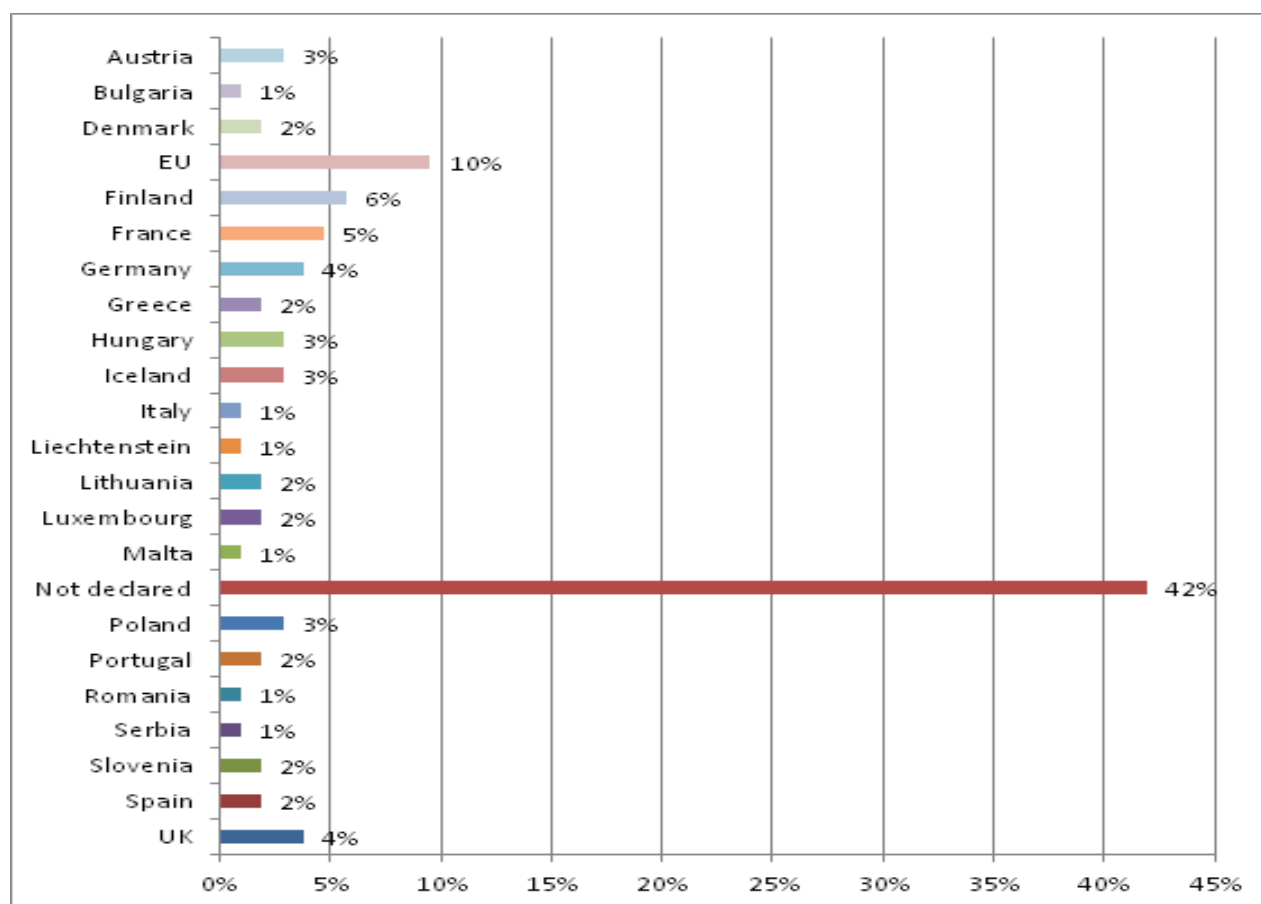
**21. Stakeholders Groups** – Respondents are well aware of the existence and functioning of the ESAs Stakeholders Groups but less of their contribution to the ESAs' work: 62 % are 'not aware', 'aware to a limited extent' or 'relatively aware' of the contribution of the SMSG (ESMA), 50 % for the IRSG and OPSG (EIOPA) and 48 % for the BSG (EBA).

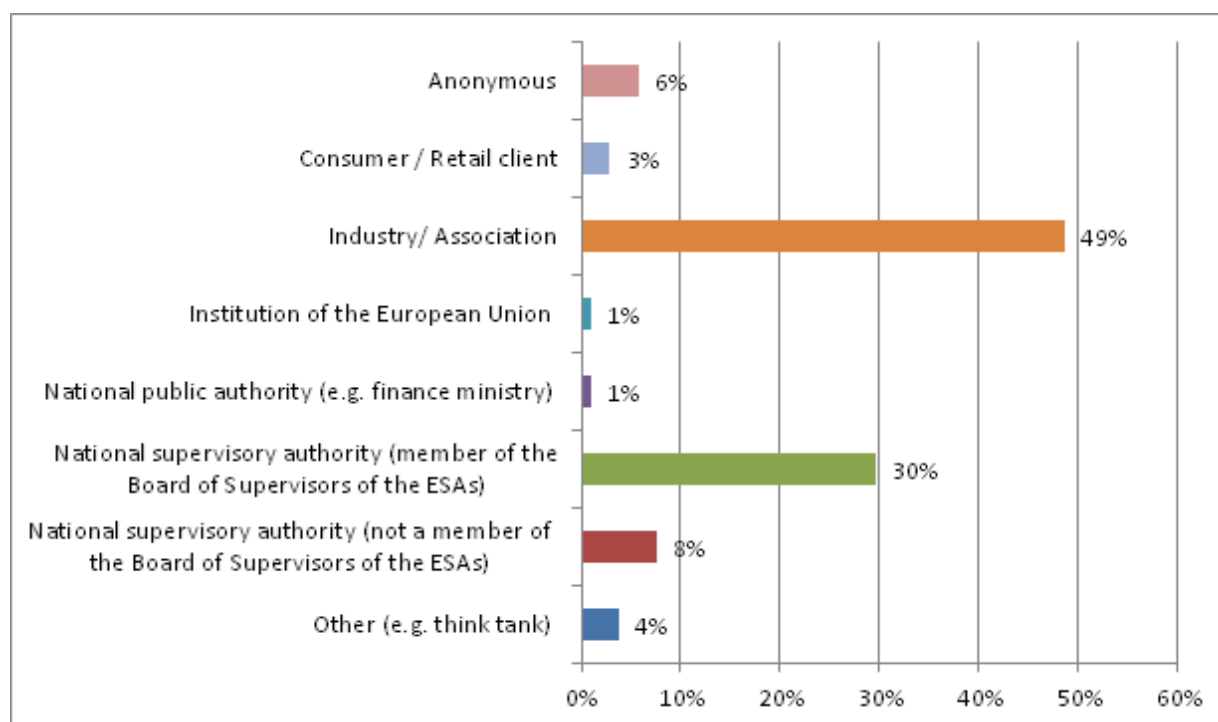
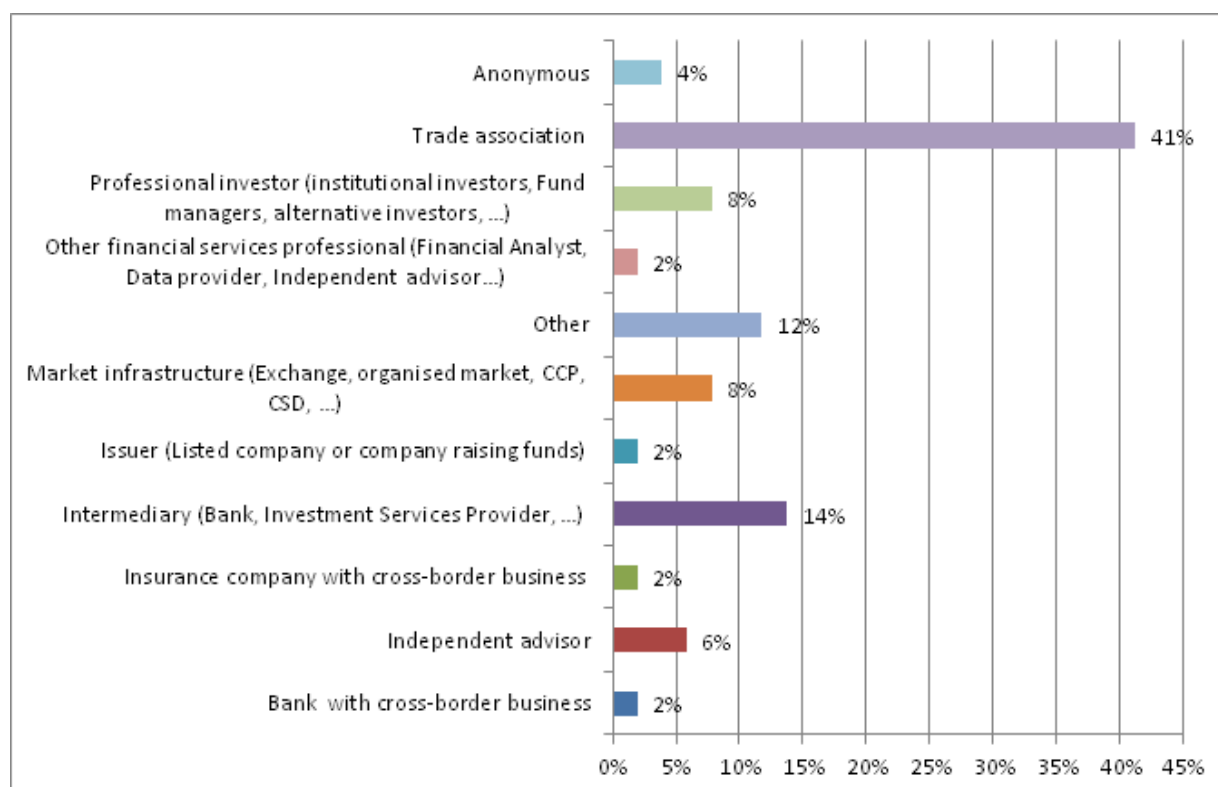
### Overview of questionnaire respondents

The following charts provide an overview of the percentage of responses received, by geographical region (EU means where the stakeholders' focus is cross-border such as industry/consumer associations or a cross-border banking or insurance organisation) and by category of stakeholder (where it is known), for all ESAs and by individual ESA.

### All ESAs (the EBA, the EIOPA and the ESMA)

**Figure 10: All ESA questionnaires respondents by geography**

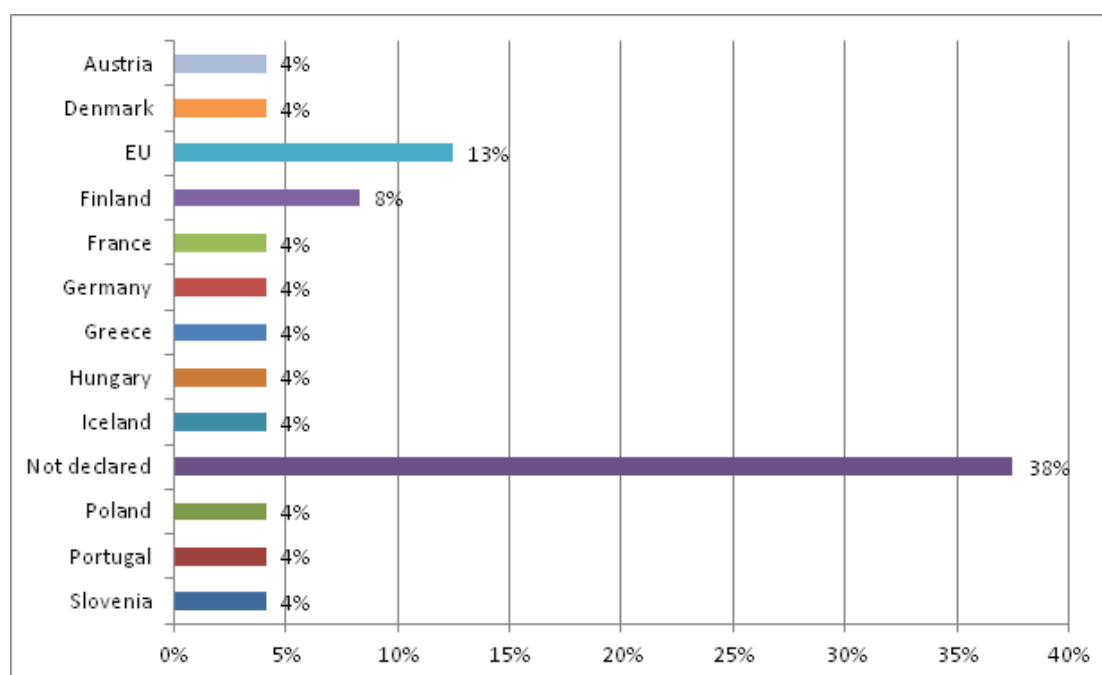


**Figure 11: ESA questionnaire respondents by institution category****Figure 12: ESA questionnaire: Industry/Association respondents by category**

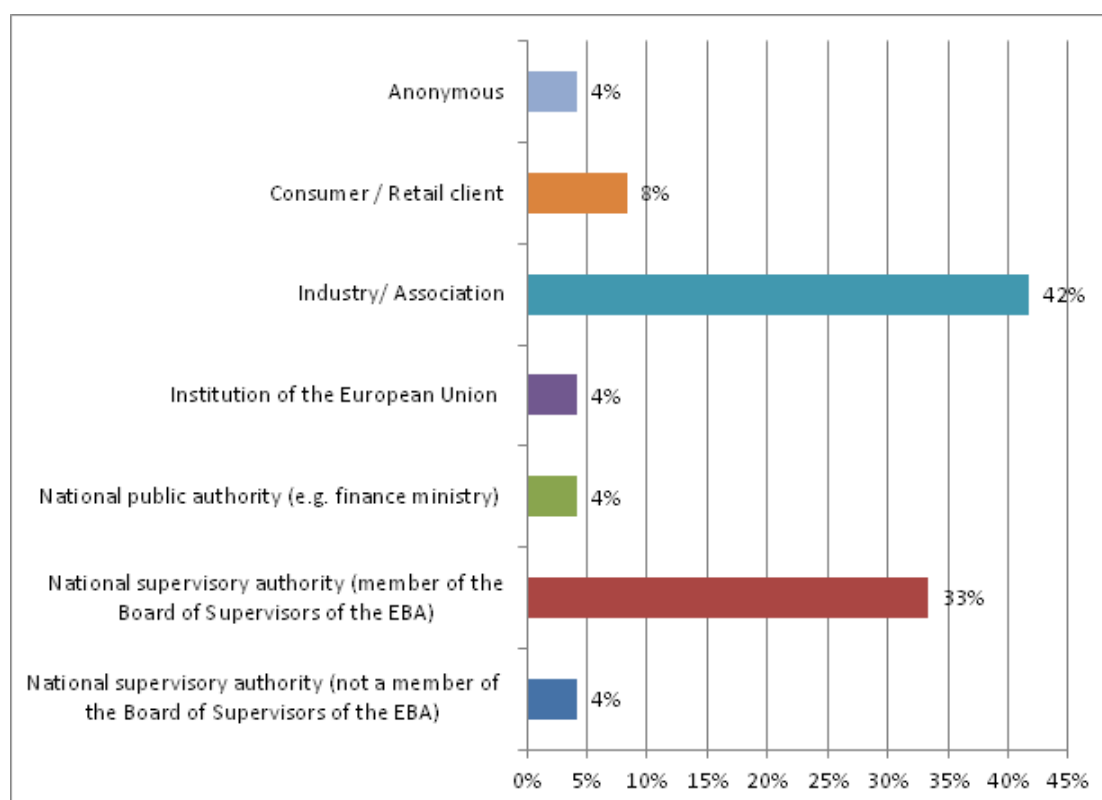


## The EBA

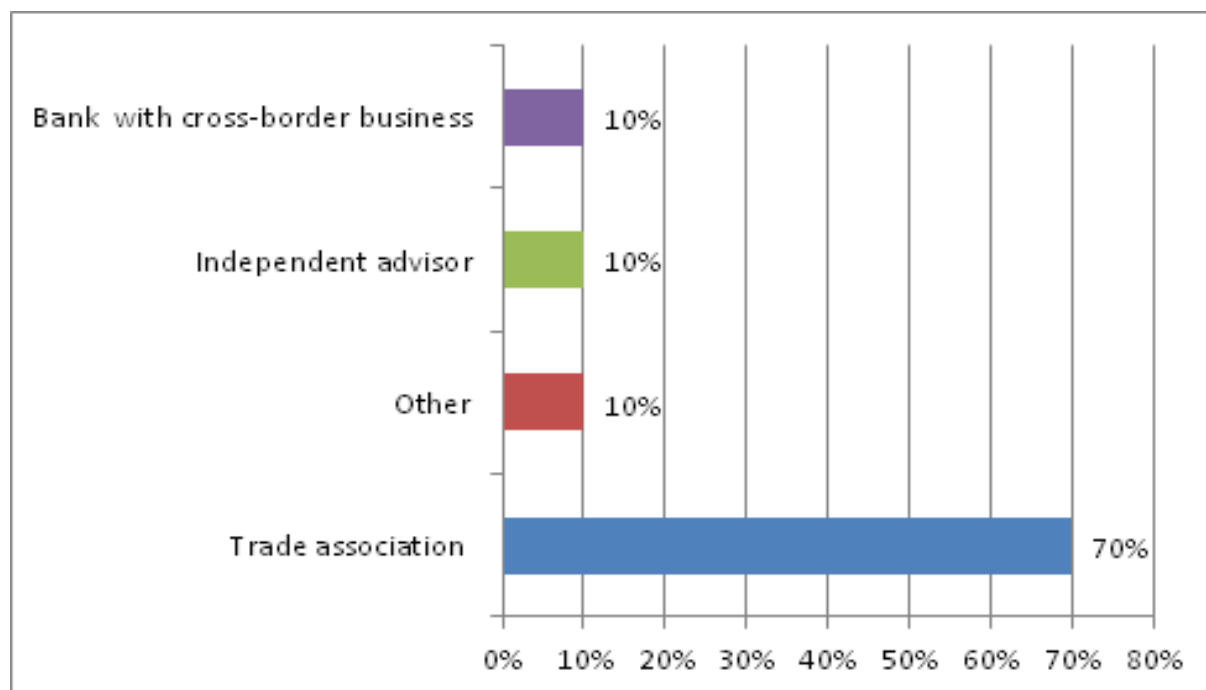
**Figure 13: EBA questionnaire respondents by geography**



**Figure 14: EBA questionnaire respondents by institution category**

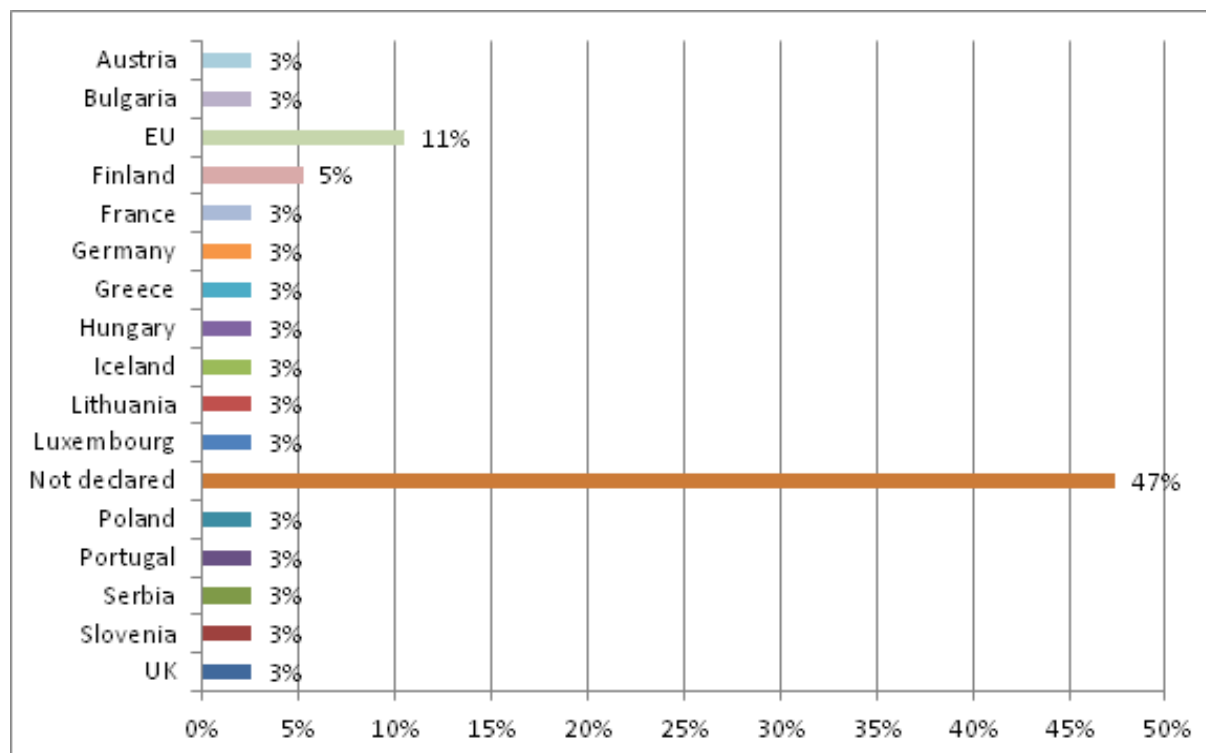


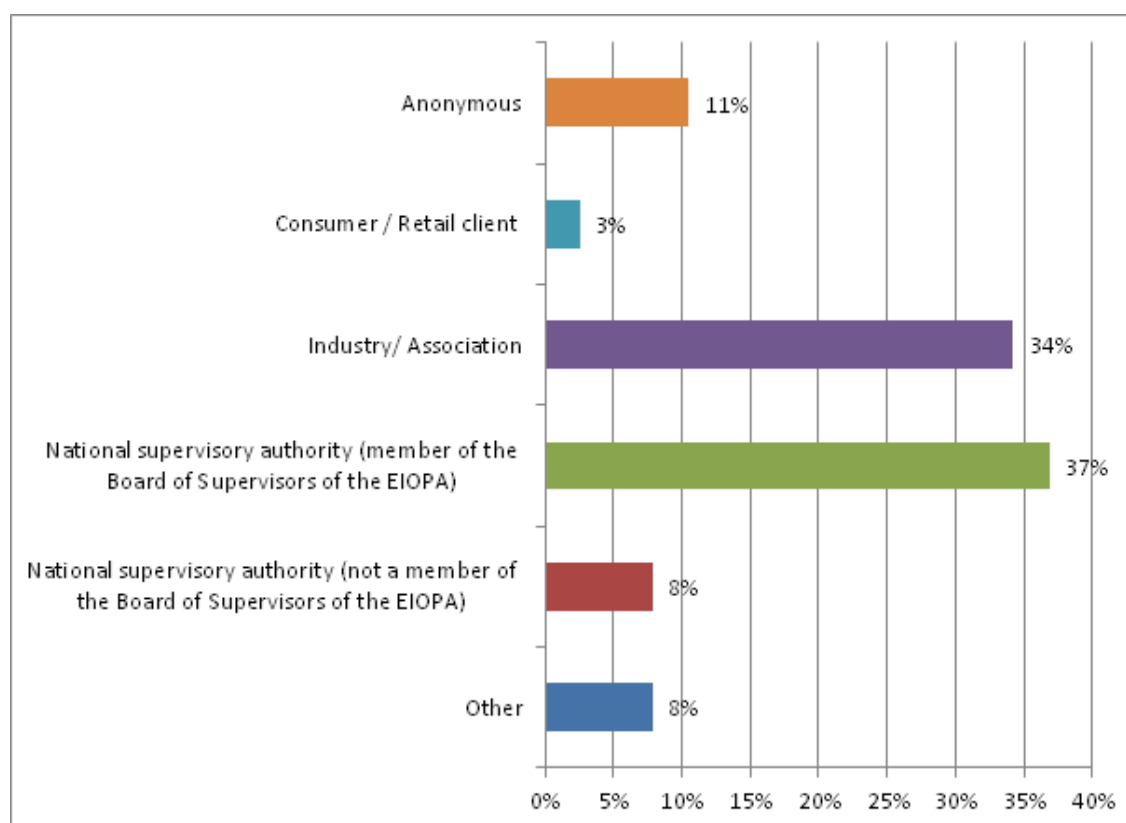
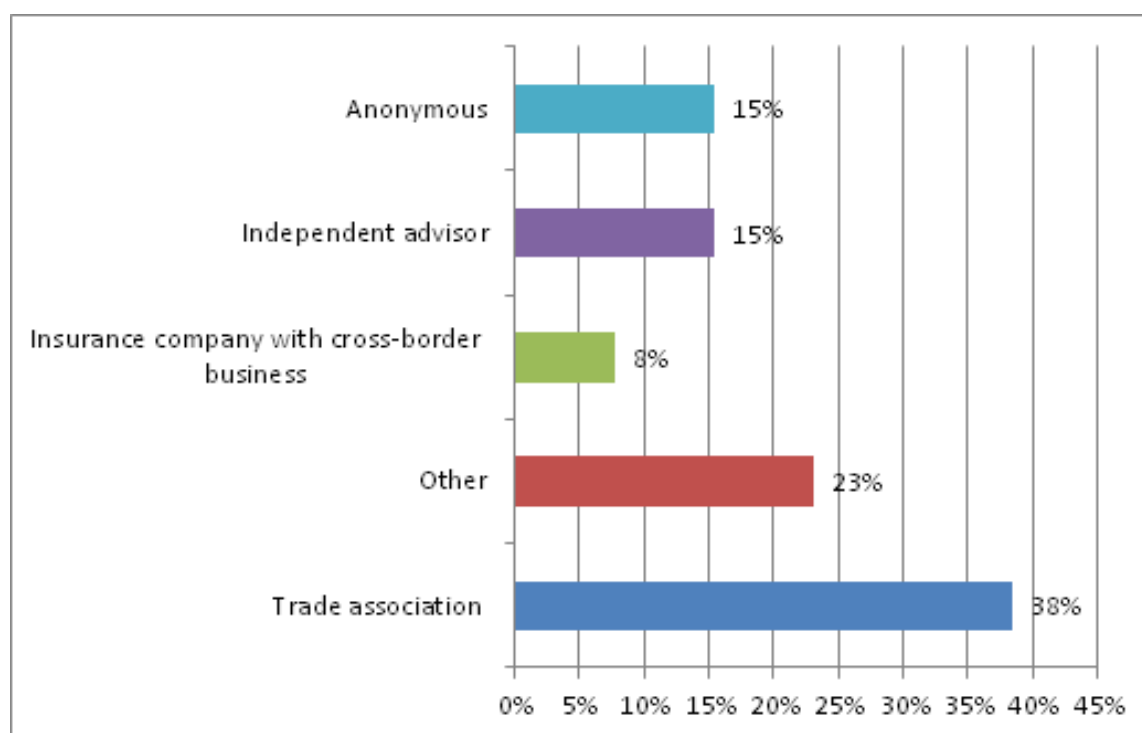
**Figure 15: EBA questionnaire: Industry/Association respondents by category**



## The EIOPA

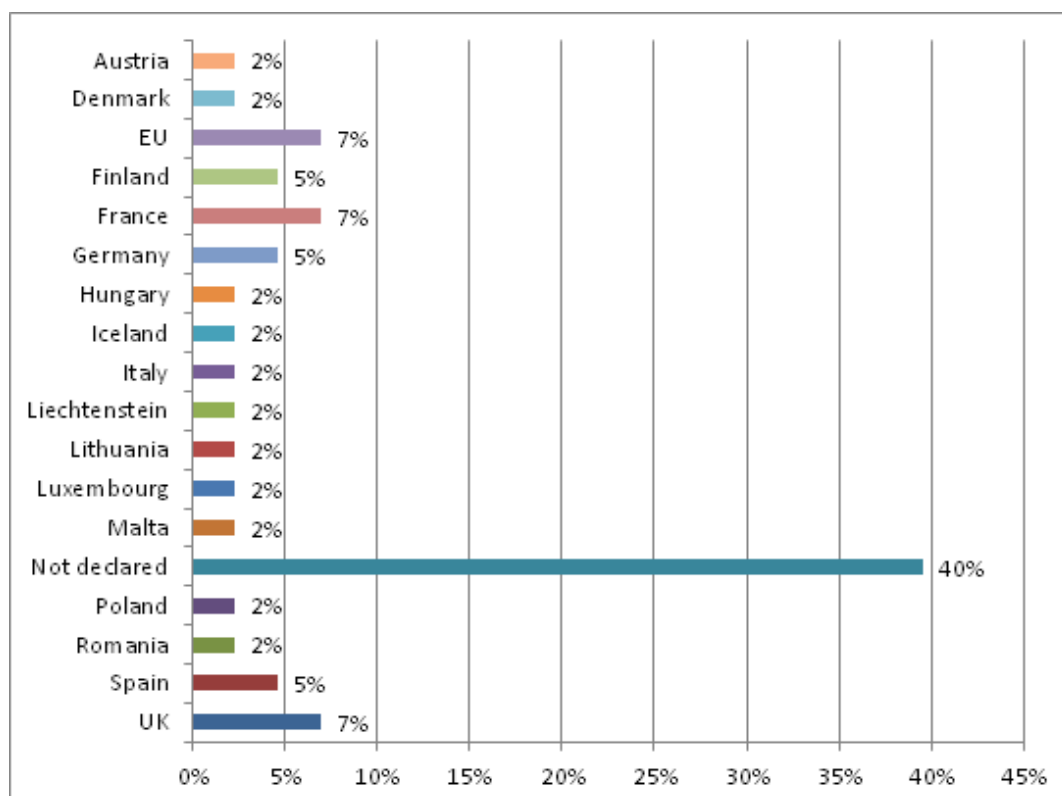
**Figure 16: EIOPA questionnaire respondents by geography**



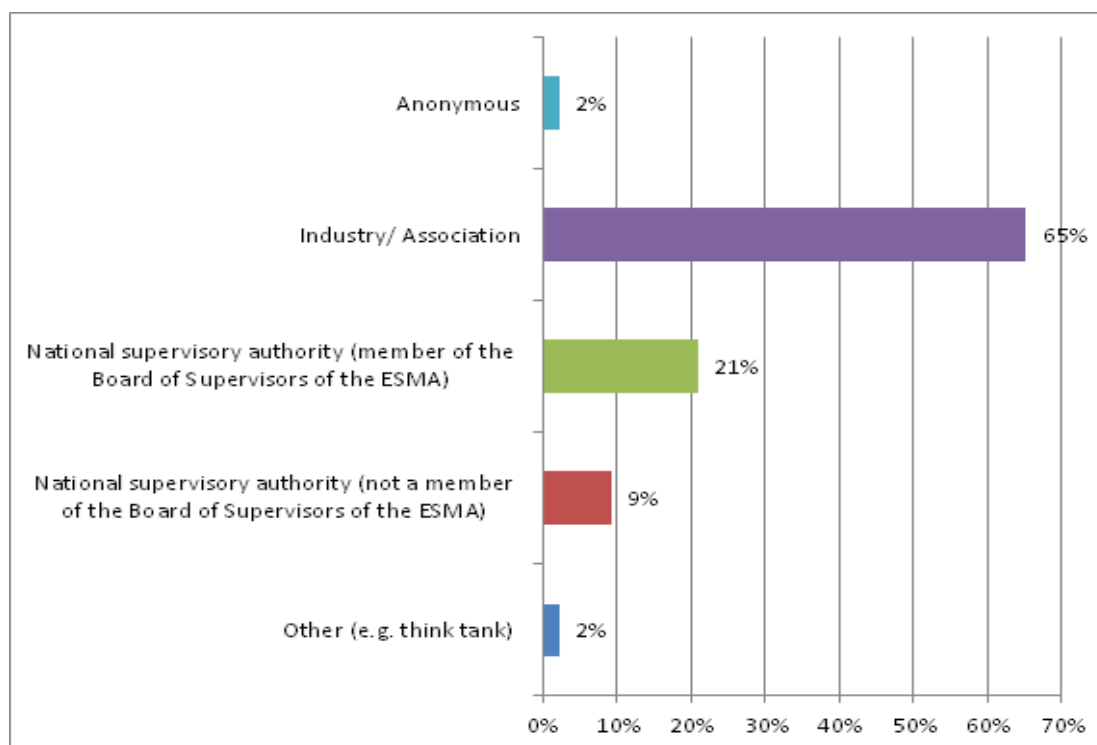
**Figure 17: EIOPA questionnaire respondents by respondents' institution category****Figure 18: EIOPA questionnaire: Industry/Association respondents by category**

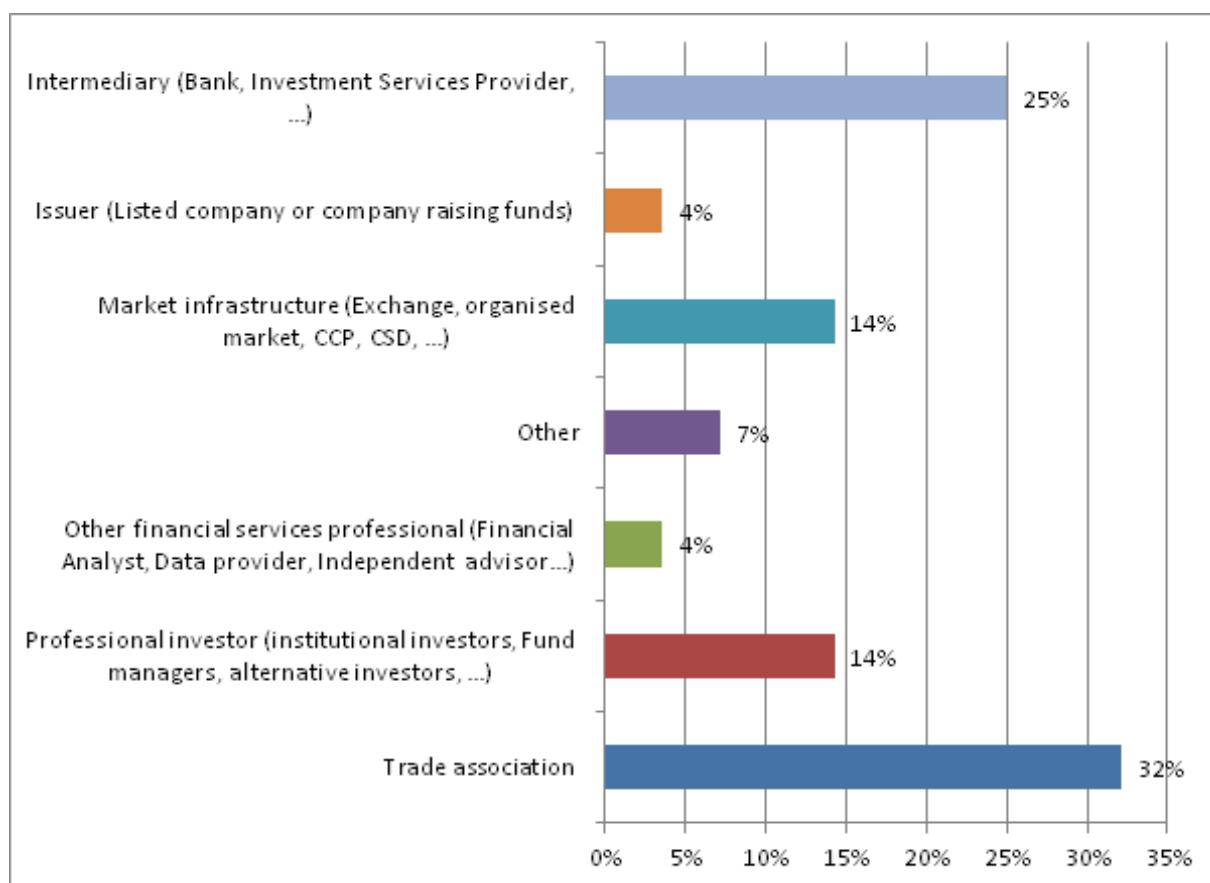
## The ESMA

**Figure 19: ESMA questionnaire respondents by geography**



**Figure 20: ESMA questionnaire respondents by institution category**



**Figure 21: ESMA questionnaire: Industry/Association respondents by category**

Statistical overview of interviews

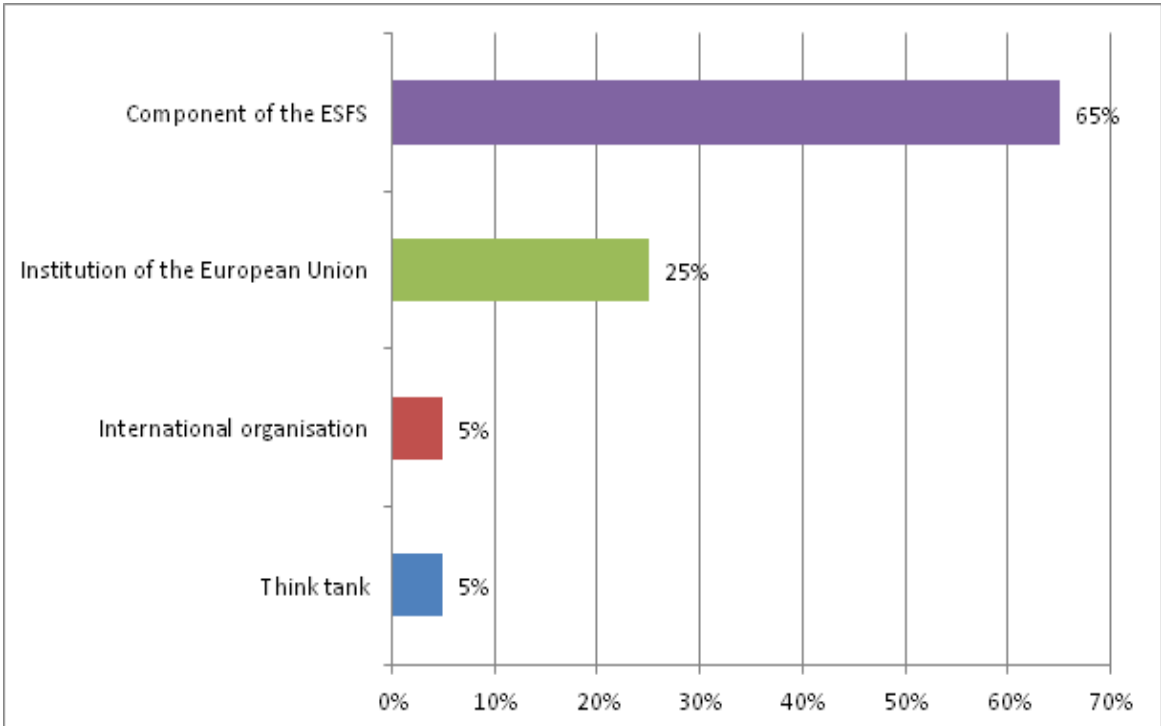
In addition to the questionnaire, a wide range of face to face or telephone interviews<sup>233</sup> with stakeholders and target groups took place to gather opinions and views. Approximately 120 requests for meetings were sent and some requests for meetings were received. The statistical overview of interviews reflects the interviews held.

Overall, 99 interviews were held with institutions, organisations, firms and experts as follows: the EBA (21), the EIOPA (26), the ESMA (32) as well as some covering the whole ESFS (20). The views collected have considerably enriched the understanding of the role and functioning of the ESAs. \*

The following charts provide a statistical overview of the percentage of interviews held, by geographical region (EU means where the stakeholders focus is cross-border such as industry and consumer associations or a cross-border banking or insurance organisations) of the stakeholder and by category of stakeholder, for the ESAs as a whole and by individual ESA.

The general ESFS interviews held were with institutions and representatives from the following categories:

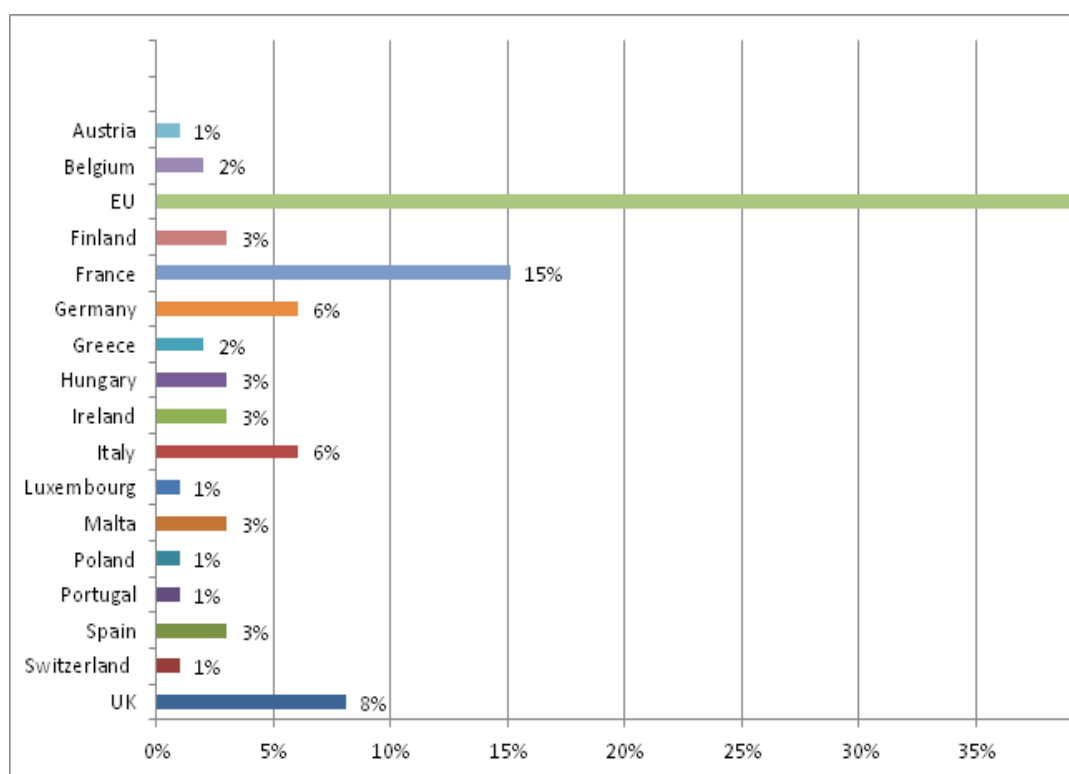
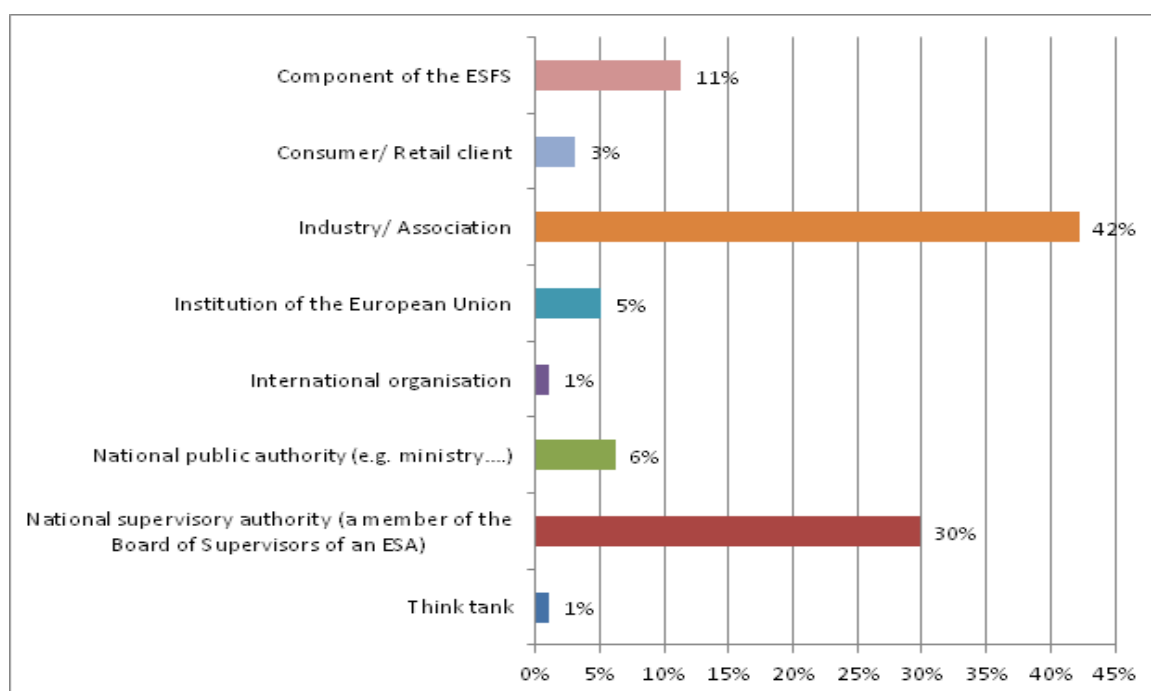
Figure 22: General ESFS/ESA interviews held



**Note:** Components of the ESFS include the ESRB, the ESAs themselves, ESA Stakeholder Group Chairs and representatives and a member of the High Level Group on Financial Supervision in the EU.

<sup>233</sup> In a very few cases, comments were provided via email rather than through direct engagement.

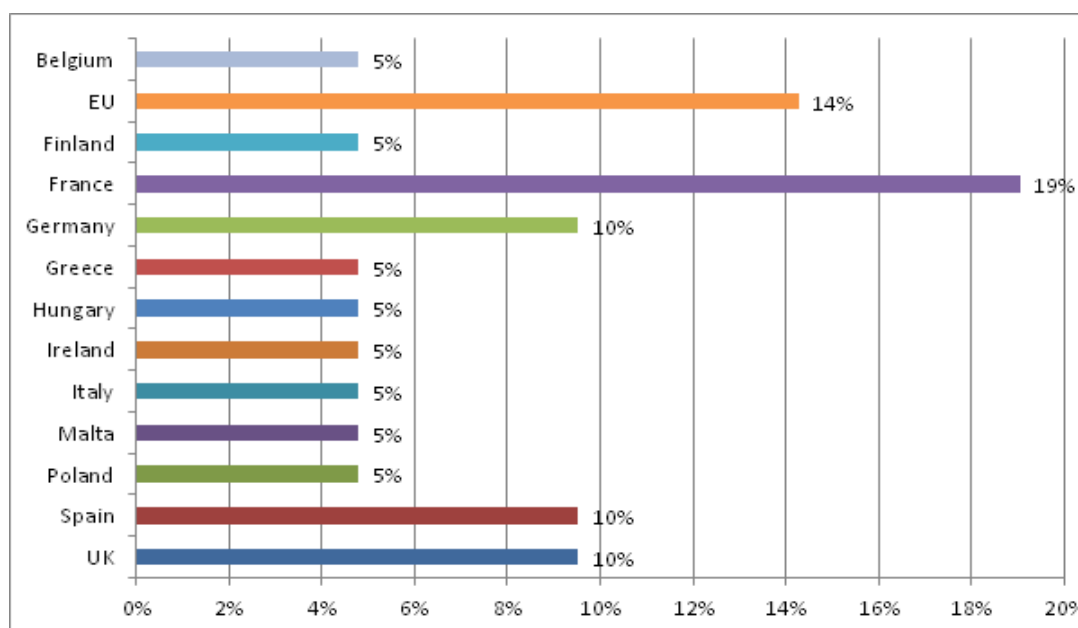


**All ESAs (the EBA, the EIOPA and the ESMA)****Figure 23: ESA interviews by geography****Figure 24: ESA interviews by institution category**

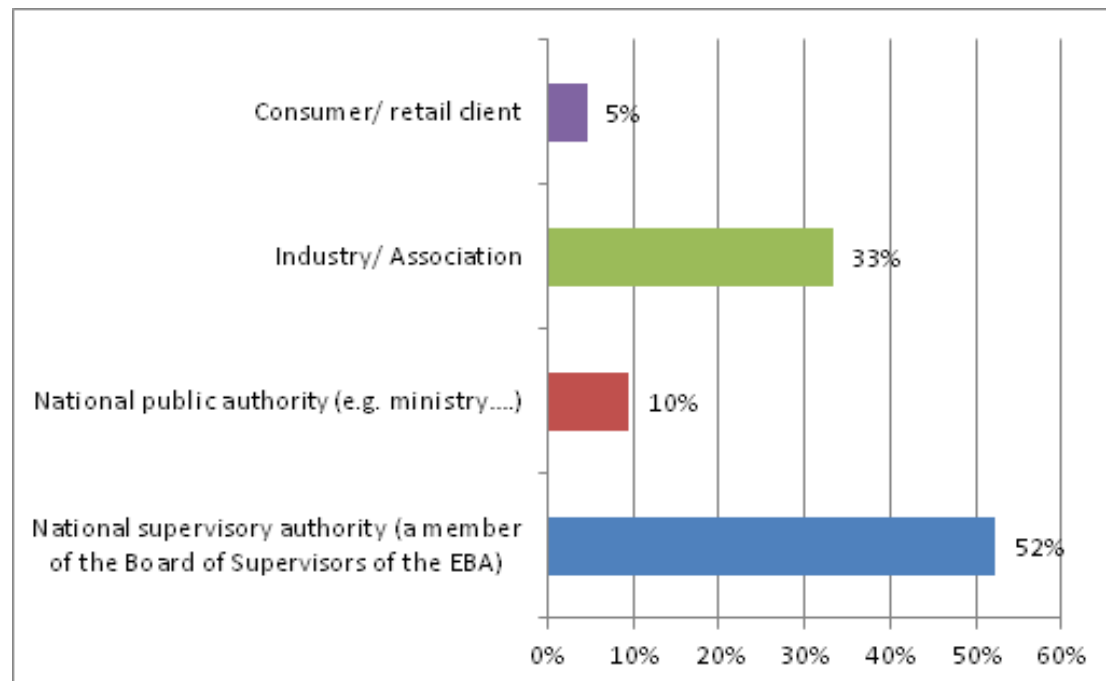
**Note:** Components of the ESFS include the ESRB, the ESAs themselves, ESA Stakeholder Group Chairs and representatives and a member of the High Level Group on Financial Supervision in the EU.

## The EBA

**Figure 25: EBA interviews by geography**

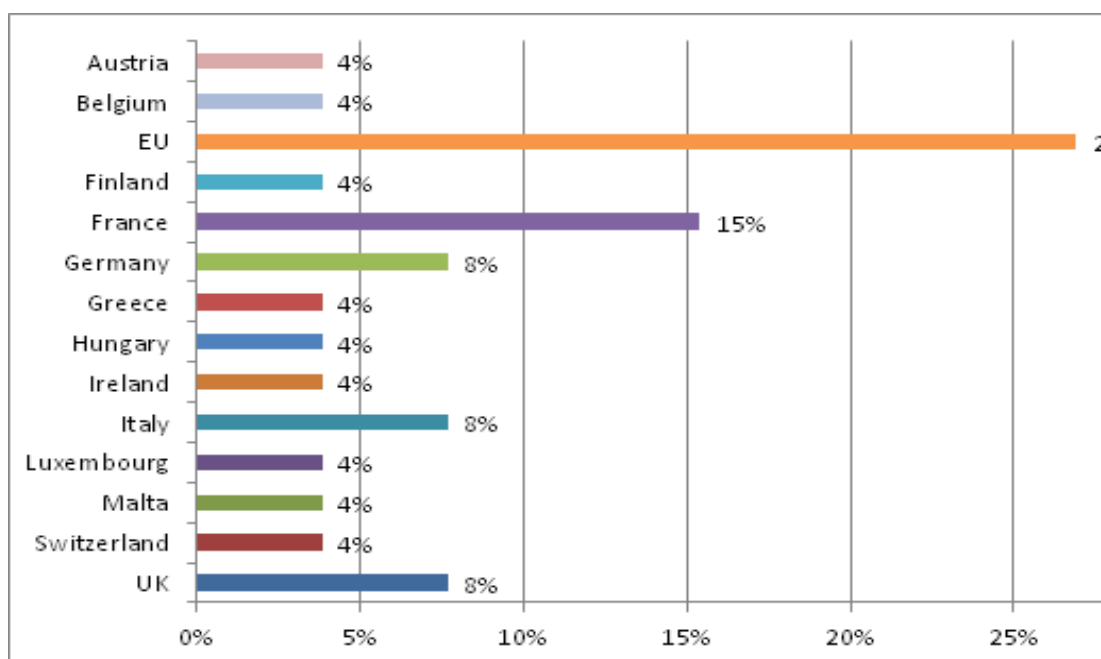


**Figure 26: EBA interviews by institution category**

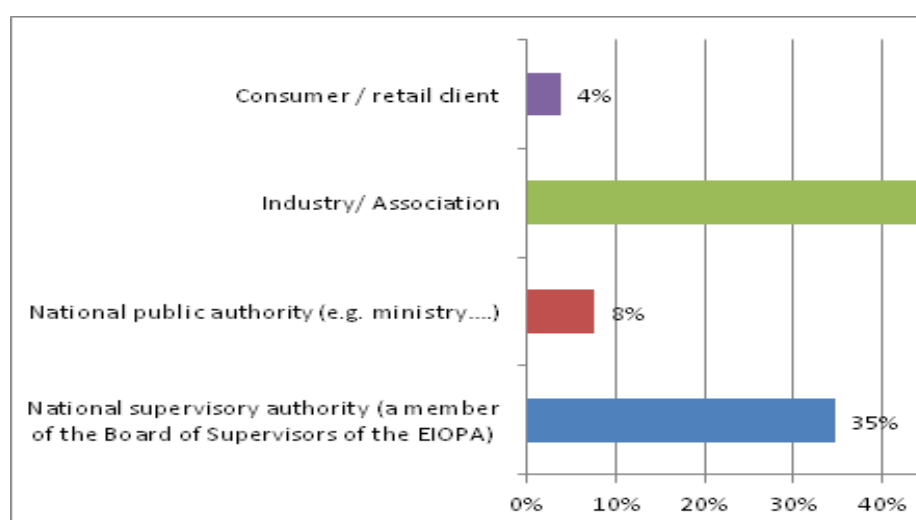


## The EIOPA

**Figure 27: EIOPA interviews by geography**

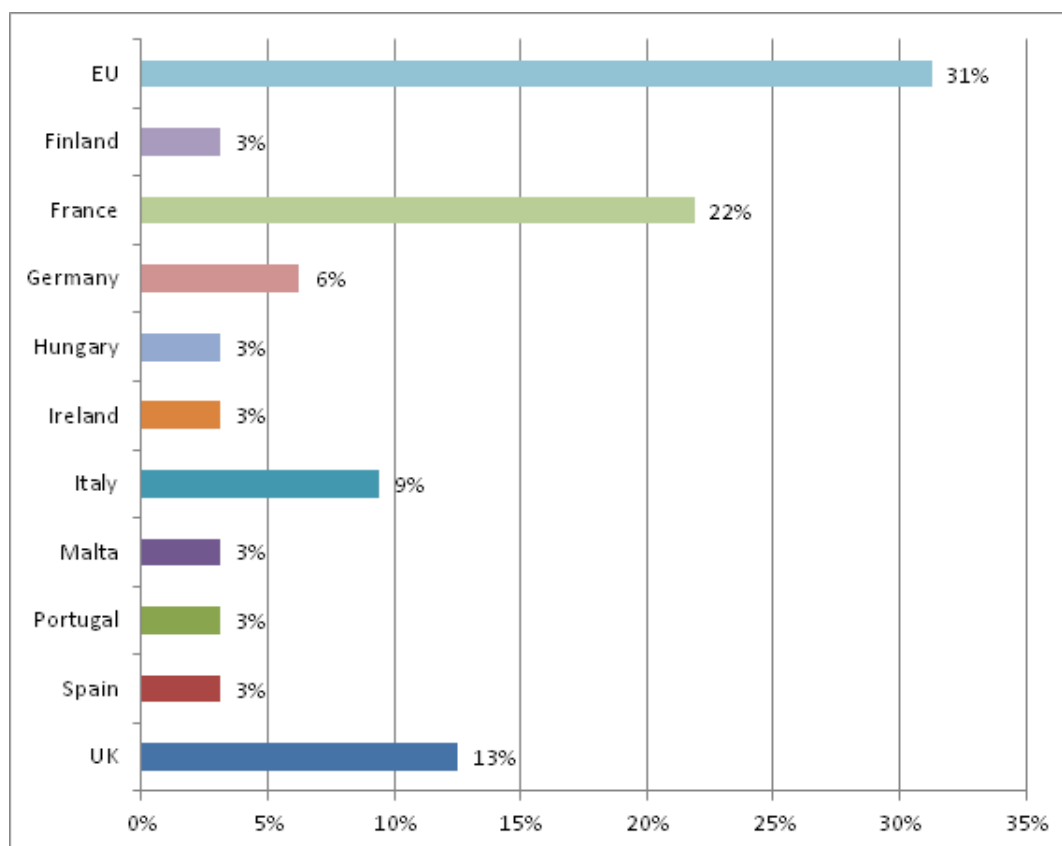


**Figure 28: EIOPA interviews by institution category**

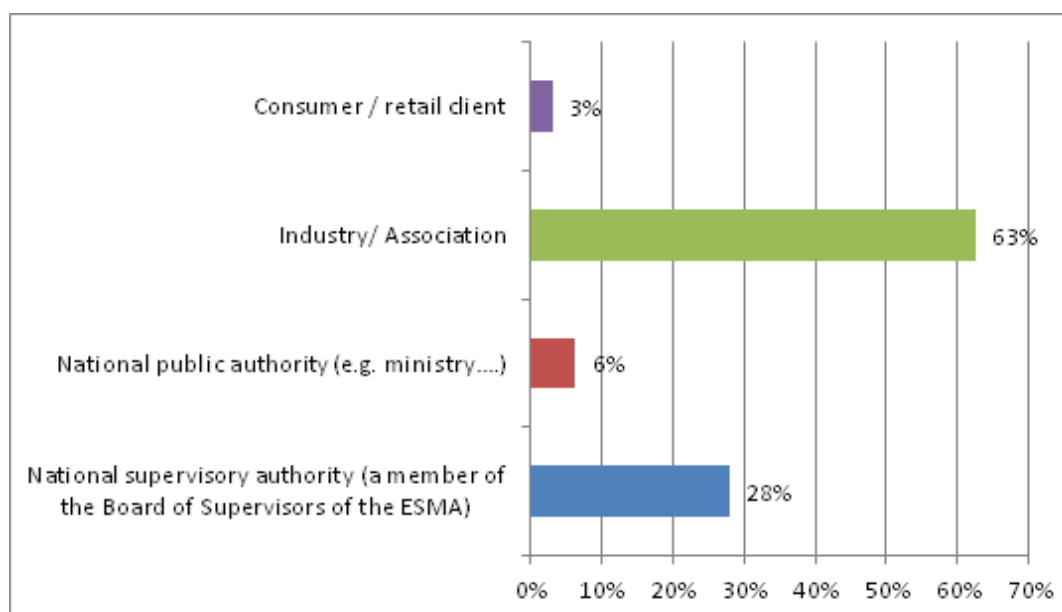


## The ESMA

**Figure 29: ESMA interviews by geography**



**Figure 30: ESMA interviews by institution category**





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