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**FINANS
DANMARK**

Review of the role of the European Supervisory Authorities

Finance Denmark appreciates the opportunity to contribute to the Danish Government's reply to the Commission proposal on the review of the European Supervisory Authorities.

Høringssvar

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General comments

The ESAs play an important role in the European supervisory and regulatory landscape. Following the coming into place of an unprecedented reform program in recent years, the establishment of the Banking Union and UK's decision to leave the EU, it is timely to reflect upon earlier experiences and what framework will be needed going forward – in a changing political and market environment.

The ESAs in general, and the EBA in particular, have the immensely important and challenging tasks to ensure the functioning and development of the EU's internal market for financial services and capital – for all EU countries.

The current regime provides a good basis for a well-functioning internal market for capital and financial services.

While it is true that the ESAs will face new challenges in the years to come – both in terms of substance and in terms of the institutional framework – we think it is important to recognize that the ESAs have largely fulfilled their duties in a satisfactory way since the coming into place in 2011. Consequently, the current regulatory framework governing the ESAs is a good basis for a continued development of the ESAs' activities. That in turn speaks for a dig-where-we-stand kind of approach and that no radical changes should be introduced at this point of time. Initiatives to adjust the current setup and enhance the efficiency and co-ordination in the ESAs are however welcome.

We support the strengthening of the ESAs' role and power in the rule making processes. This will support the convergence within the EU and development of the single rulebook. However, we oppose a strong centralization of regulatory powers to the ESAs. There are important merits in applying the subsidiarity principles – also in this area. It is also of paramount importance to recognize differences when regarding business models, products, markets governance etc. in the financial sector. Principles of proportionality shall be recognized carefully at all levels. It is often at Level 3 administrative burdens are materialized.

The development of the single rulebook should not be achieved at the expense of well-functioning financial systems at member state level. It is therefore of paramount importance to maintain an appropriate balance between supporting the single rulebook and ensuring that specificities of the financial systems in individual member states are recognized.

Our comments can be summarized as follows:

- We welcome the initiative to strengthen the governance inside the ESAs, including adding external and independent expertise. Recruitment of members to the Executive Board must not become politicized.
- Non-euro-zone member states' interests must continue to be taken into account. Clear safeguards for non-euro-zone countries in the decision-making system of the ESAs, most importantly the EBA should continue to exist.
- One seat in the Executive Board should be dedicated to a member from a non-euro country.
- The far-reaching competences of the new Executive Board speak for introducing more checks and balances.
- The current funding system should be maintained.
- The total amount of resources spent on supervision in the EU should not increase.
- Any proposals for giving ESMA more direct supervisory powers should be preceded by careful consultations and impact assessments that show a clear benefit of such changes – a subsidiarity test.
- To pass the authority to approve prospectuses from the NCAs to ESMA does not add any value to the functioning of the EU DCM market. We are against handing over supervisory powers to ESMA.
- We are generally positive to initiatives strengthening the level playing field across Europe and work towards a more harmonized legal ecosystem in the area of collective investment funds – but we are concerned that it will raise barrier to entry if the application process is to be handled with ESMA instead of local NCAs.



- We welcome the general goal of improving stakeholder involvement and increase transparency, and we therefore welcome the Commission's proposals regarding enhancement of the level 3 procedures on guidelines and recommendations by e.g. requiring cost-benefit analysis.
- Improvements are also needed at level 2 to improve transparency and stakeholder involvement in both level 2 and 3 processes.
- In order to improve the stakeholder involvement and more generally to ensure satisfactory implementation processes, realistic implementation deadlines are key.
- The ESAs mandates, work plans etc. need to adapt to new developments and consequently, we welcome that new responsibilities in the areas of fintechs and sustainable finance are suggested.
- We believe and hope that the EBA could play a stronger role in ensuring that the EU punches its true weight in global foras such as the FSB and BCBS.

Governance inside the ESAs – non-euro-zone member states' interests must continue to be taken into account

We welcome the initiative to strengthen the governance inside the ESAs, including adding external and independent expertise. A more formal involvement of external and independent experts ought to strengthen the quality of the work as well as the legitimacy towards the external environment.

However, from a non-euro-zone country perspective, we have some important observations from the proposal that should be taken into account during the coming negotiations:

Euro-zone and non-euro-zone countries' interests must be balanced

EU's internal market consists of both euro-zone and non-euro-zone countries, and all interests must be considered in order to ensure the best outcome and not risk the legitimacy of the system. Consequently, there must continue to be clear safeguards for non-euro-zone countries in the decision-making system of the ESAs, most importantly the EBA. Appropriately designed, such safeguards should not risk the efficiency of the decision making process, merely ensure that non-euro-zone countries are not overrun and that unintended consequences are avoided.



It is welcome that the non-euro-zone country safeguard in the EBA's Board of Supervisors is maintained

In the current EBA regulation, Article 44, there is a non-euro-zone country safeguard for decisions according to specific mentioned articles (the "double majority"). Besides qualified majority in the Board of Supervisors, also separate simple majority amongst respectively participating Member States (euro-zone countries) and non-participating Member States (non-euro-zone countries) is required. The current voting rules in EBA should be maintained. We acknowledge that they in principle have been maintained in the proposal.

However, some of the below described proposed amendments seem to alter the double majority safeguard, even though it is in principle maintained. This is by narrowing down the safeguard by deleting the reference to Articles 17 and 19 (since the decision making power on those articles is suggested to be moved to the Executive Board), and by not having specific requirements to the composition of the Executive Board. New safeguards should be introduced to maintain the balance.

One seat in the Executive Board should be dedicated to a member from a non-euro country

In the current EBA regulation, Article 45, there is a non-euro-zone country provision requiring at least two representatives of the Management Board to come from non-participating Member States (non-euro-zone countries). This safeguard has not been maintained in the amended article 45(2) when appointing members to the new Executive Board. The sentence *"the Executive Board shall be balanced and proportionate and shall reflect the Union as a whole"* is no guarantee for a diversified board when it comes to having in-depth knowledge and understanding of local markets, actors etc. outside the euro-zone.

Consequently, we propose that one seat in the Executive Board is always dedicated to a member from a non-euro-zone country.

Recruitment of members to the Executive Board must not become politicized

The proposed new Executive Board shall replace the current Management Board and Chairperson. When hiring the members to the Executive Board, the Commission shall make up a shortlist of applicants, and based on the shortlist, the Council shall appoint the members (article 45 in the ESA-regulations).

We see some challenges in the proposed setup. It is essential that the members of the Executive Board have a solid knowledge of capital markets, financial regulation etc. We believe that the Board of Supervisors is best suited to make up a short-list of candidates that fulfils all the necessary criteria.



We also find that having the Council hire members to an Executive Board does not live up to usual governance standards and will introduce a more complex and less efficient governance structure. In a usual governance setup, members of an Executive Board are hired by the Board (of Supervisors), they refer to the Board (of Supervisors), and they can be fired by the Board (of Supervisors). To whom will the members of the Executive Board refer and be accountable to in the proposed setup where they are hired by the Council? Some clarifications and possibly accountability provisions would be welcome.

The far-reaching competences of the new Executive Board speak for introducing more checks and balances (new article 47 in the ESA-regulations)

With the proposed article 47, some decision powers are moved from the Board of Supervisors to the new Executive Board. The Executive Board will have power to take decisions “for the purposes of Articles 17, 19, 22, 29a, 30, 31a, 32 and 35b to 35h”.

It is very important to consider the effects of this balance between the Board of Supervisors and the Executive Board. We do not see a clear line in why the said articles have been chosen. It is worth noticing that especially articles 17 and 19 can have far-reaching consequences for institutions since decisions according to those have to be made public (according to article 39(6)).

If decision powers are moved to the Executive Board, it is in our opinion essential to ensure a better balance of the composition of the Executive Board in relation to non-euro country representation and to ensure a more transparent governance setup regarding who refers to whom etc., as well as a more optimal hiring setup, cf. comments above.

The current funding system should be maintained

We are skeptical to introduce grand changes to the current funding system.

To ensure effective, transparent and equal supervision in all Member States, the EU budget should remain the main source of ESA funding. This gives the European Parliament legitimacy to supervise the ESAs, thus rendering them democratically accountable. The financial industry is already contributing through National Supervisory Authorities, and this system should be maintained as it stands. We do not see that there is any need to increase the total costs relating to supervision as such at the EU level.

The ESAs were formed mainly to assist the European Commission in strengthening the financial sector by developing draft technical standards and issuing guide-



lines and recommendations. In working on regulatory technical standards or implementing technical standards the ESAs are, in fact, performing tasks that should normally be performed by the European Commission pursuant to Articles 290 and 291 of the TFEU. This supports the argument that a significant part of the costs of the ESAs should be covered by the EU budget.

More clarity at level 1 is needed to avoid unpredictability

If the co-legislators nevertheless choose to move forward along the lines of the Commission proposal (according to which maximum 40 percent of the ESAs' budget should come from the EU budget and the remaining part via direct contributions from the sector) there must, as an absolute minimum, be more clarity in the level 1 text as to how much each financial institution should contribute. We consider it excessively unpredictable for the institutions to decide the methodology for collecting each institution's contribution via a level 2 Commission delegated act.

Clear checks and balances must be introduced

Further, it creates unpredictability that the ESAs themselves (the Executive Boards) decide on their own budget, including the size of the budget, together with the fact that the EU budget funding is formulated as maximum 40 pct. ("shall not exceed 40 pct.") which gives no guarantees on the actual size of EU funding. Institutions could end up paying very large contributions.

The total amount of resources spent on supervision in the EU should not increase

In order to be able to deliver on an ambitious agenda, the resources of the ESAs could be increased appropriately. However, the total supervisory costs for each institution should not increase – so if it is deemed necessary to increase the budget of the ESAs, national FSAs' budgets should decrease by the same size. We would also expect the ESAs to optimize their efficiency in a way to minimize the need for additional funding. Therefore, it is important to have some checks and balances on the budgets set by the ESAs to ensure that increases in ESA budgets correspond supervisory powers taken over from national FSAs – so that national FSAs do not end up as losers in the game.

ESMA powers on direct supervision

Any proposals for giving ESMA more direct supervisory powers should be preceded by careful consultations and impact assessments that show a clear benefit of such changes – a subsidiarity test. According to our view, the rationale for centralizing powers must be that a central body – in this case the ESMA – can solve



what the national FSAs cannot, or can solve it more effectively or in a more coordinated and consistent manner than national FSAs.

In that regard, it is warranted to underline the importance of having knowledge and an in-depth understanding of local market conditions, actors etc. when exercising supervisory powers. Supervision that requires understanding of local markets ought to stay local. The development of the internal market for financial services shall however, also support the increased cross-border trade and infrastructure, and in such areas centralization by giving ESMA direct supervision could be necessary following appropriate impact assessments etc.

The Commission proposes several new areas for direct supervision by ESMA. If the ESMA powers are to be extended, please see below our specific comments on each area:

Prospectuses:

We are against handing over supervisory powers to ESMA and have the following concerns:

To pass the authority to approve such prospectuses from the NCAs to ESMA does not add any value to the functioning of the EU DCM market, as the current system works efficiently and without problems, thus the suggested change will not add value to either issuers nor investors. Further, it should be noted that this notion was rejected following strong advocacy efforts during the PD III legislative process, which itself was only concluded in June this year.

Currently, issuers are able to choose their competent authority/home member state across the EU. If the proposal is implemented, this flexibility will no longer be available, as ESMA will be the only authority, which will effectively create a monopoly. We think it is efficient for an issuer to choose (if the issuer so desires) to have the regulator in the same country as the stock exchange where the issuer most frequently lists his bonds/notes. We find this minimizes the number of comments on the submitted documents and provides for a more efficient and streamlined process and we are of the opinion that this aspect is part of the issuers' decision-making process when deciding on home member state. It is our experience that the two entities coordinate their timing so that issuers have certainty as to when they will receive comments and thus an issuer can better plan and estimate time to market. This is very important to issuers and provides huge efficiency benefits to issuers. An issuer would lose this with a regulator in one jurisdiction and a stock exchange in another.



We are concerned that knowledge of local market conditions etc. built up in the experienced and competent teams in each of the NCAs throughout many years will be lost. Knowledge that today secures flexibility and the ability to respond quickly to market needs. It is not sure how ESMA will fill this loss of knowledge and ensure market effectiveness for the future.

We are against the proposal, as it will give both legislative and supervisory powers to one entity (ESMA), powers that are normally separated according to fundamental principles of constitutional law.

It should also be noted that property and shipping companies are using the issuance of bonds to a larger extent. It is therefore possible that it may have a negative impact on this segment of issuers in respect of timing, local knowledge of markets etc., cf. as stated above.

The proposal might add to the tendency of foreign issuers bypassing the EU listing process. Many exchanges believe that US issuers are choosing to bypass the European listing process, something that has become even more pronounced in the last 12 months since the introduction of the MAR regulation. Moreover, Latin American issuers are also now choosing Singapore over Europe. And more European issuers may do the same as the current Commission proposal will be seen as a step towards an inflexible, formal regime which will increase time to market.

Harmonized collective investment funds (EuVECA, EuSEF and ELTIF)

We are generally positive to initiatives strengthening the level playing field across Europe and work towards a more harmonized legal ecosystem in the area.

According to proposal managers of ELTIFs, EuVECAs and EuSEFs would be required to apply for authorization to ESMA, rather than the NCAs. ESMA would also be responsible for ensuring that the rules laid down in those Regulations are consistently applied throughout the EU.

We are concerned that this will raise barrier to entry as application process is to be handled with ESMA in Paris instead of local NCAs. There are very few such fund structures in the whole of EU so far and it is unlikely that it would help to launch new such products, if the authorization is moved to EU level. ESMA's role as an authorizing entity in financial markets makes sense when there are a small number of large entities operating in the whole of EU or large part of it, such as credit rating agencies. However, managers of ELTIFs, EuVECAs and EuSEFs should also be able to be smaller firms and not EU-wide operators only.



Coordination powers of ESMA on delegation/outourcing/risk transfers

Article 31a requires ESMA to coordinate supervisory actions of NCAs with a view to promoting supervisory convergence in the fields of delegation and outsourcing of activities and risk transfers. The NCAs would need to notify ESMA when they intend to authorize a plan by a financial market participant involving outsourcing or delegation or a risk transfer of a material part of its activities into third countries "to benefit from the EU passport while essentially performing substantial activities or functions outside the Union". ESMA may issue an opinion to NCAs regarding non-compliance of an authorization or registration.

This would give ESMA legal powers to enforce its July opinions on delegation regarding Brexit. However, more broadly speaking, these changes will affect all countries that utilize delegation to manage funds that are offered in the EU. While it is difficult to get accurate numbers, industry sources estimate that in excess of EUR 1.5 trillion of US and Asia Pacific equities and fixed income securities are offered via UCITS, not including assets managed in AIFs. These assets are largely managed by local portfolio managers to whom European asset managers have delegated the portfolio management, to get the best local investment expertise to the benefit of the investors of the UCITS/AIFs.

UCITS and AIFMD allow management companies to delegate functions such as custody and portfolio management subject to strict control, oversight and accountability. Being able to access best of breed portfolio managers and service providers is a cornerstone of the global success of the European UCITS regime. In our experience delegation works, it is properly supervised by the NCAs and there is no market failure that needs addressing.

Should the proposal go ahead, European investors need to be confident that ESMA has the expertise, market experience and knowledge of local markets to ensure their interests are being served at least as well as they are under existing practices. Similarly, the Member States, European Parliament, industry and taxpayers will need to be assured that this undertaking is an appropriate use of ESMA's resources and that the needs of the Capital Markets Union are best served by ESMA focusing so much of its resource on this major administrative task.

There is a concern that ESMA's role in approving third country delegation leads to a more costly and slower process weakening the time to market of European fund products, which could damage the competitiveness of European asset managers. There is also a concern whether this change could lead to less access to third country portfolio managers/service providers. This could damage the



UCITS regime the global success that is indeed largely based on the ability to delegate portfolio management globally.

Central Counterparties (CCPs)

To some extent we find it reasonable to extend ESMA supervisory powers of CCPs. However, regarding third country CCPs, London Clearing House is commonly used by Danish Banks, and with Brexit it will become a third country CCP. It is important not to risk such well-functioning CCPs by introducing new third country supervision.

Data reporting services (ARM, APA, CTP)

We see some merit in the proposal to centralize the authorization and supervision of data reporting service providers, cf. MiFID II, however, as regards ESMA access to MiFID II data, it must be ensured that no double reporting exists if firms are required to report data directly to ESMA.

Benchmarks

Regarding critical benchmarks, we find that the assessment of whether a given benchmark is "critical" requires local market understanding and should be assessed by the local FSAs. For international benchmarks and for third country benchmarks, centralization with ESMA supervision could make sense in order to enhance convergence and level playing field.

Level 2 and 3 processes – improve the involvement of stakeholders, increase transparency and ensure realistic implementation deadlines

We welcome the general goal of improving stakeholder involvement and increase transparency, and we therefore welcome the Commission's proposals regarding enhancement of the level 3 procedures on guidelines and recommendations by e.g. requiring cost-benefit analysis. However, improvements are also needed at level 2 to improve transparency and stakeholder involvement in both level 2 and 3 processes – see our suggestions below. All parties would gain from an improved system for stakeholder engagement.

Improve stakeholder involvement

This could for example entail more formal and informal opportunities for contributions from market participants in the level 2 and 3 processes and a strengthened role of the stakeholder groups. External consultations should be initiated earlier in the process than currently, with realistic response deadlines. The stakeholder groups should get involved earlier in the process and members should be al-



lowed to discuss upcoming issues with relevant stakeholders. Moreover, national FSAs should be allowed to consult national stakeholders on relevant topics.

Realistic implementation deadlines

In order to improve the stakeholder involvement and more generally to ensure satisfactory implementation processes, realistic implementation deadlines are key. The EU's legislative chambers must at all times ensure that there is sufficient time to prepare the level 2 and 3 texts, as well as sufficient time between the finalization of level 2 and 3 texts and their entry into force is needed for implementation. It should be considered whether dynamic implementation dates can be used that would be subject to the timing of finalizing level 2 and 3 measures and their implementation. Too short implementation deadlines lead to unsatisfactory implementation processes and entail heavy and expensive administrative burdens.

New responsibilities – fintechs and sustainable finance

The ESAs mandates, work plans etc. need to adapt to new developments and consequently, we welcome that new responsibilities in the areas of fintechs and sustainable finance are suggested. However, we will have to study this in more detail before making detailed suggestions for what should be the focus of these tasks.

The EBA could play a stronger role in international negotiations

It has been clear in recent years that the EU member states are sometimes rather uncoordinated in international fora, in particular the Basel Committee for Banking Supervision. We believe and hope that the EBA could play a stronger role here – ensuring that the EU punches its true weight in global fora such as the FSB and BCBS.

In line with the above, EBA also has a key role to play when it comes to re-creating trust in the IRB approach. The main aspect of this would be to improve the comparability of IRB models across institutions and member states and we would strongly encourage the EBA to continue this work with unchanged frenzy.

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