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European Commission,

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European Parliament - Hon Irene Tinagli – Chair of the ECON committee
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Dear Sirs, Dear Madam,

Proposals by the EFMLG regarding priorities of the Capital Markets Union going forward

The European Financial Markets Lawyers Group (EFMLG)¹ fully supports the Capital Markets Union (CMU), which in the medium to long-term will strengthen Europe's economy. Among others, a stronger and more integrated capital market in the EU, with barriers to cross-border investment being removed, will be more attractive to non EU capital and will ultimately reinforce the role of the euro in the world. The EFMLG also welcomes the creation of the High-Level Forum on CMU, which started its work on 26 November 2019, focusing on (1) the creation of an ecosystem enabling greater capital raising with special focus on innovative SMEs, (2) the development of the European capital market architecture with special focus on how new financial technologies can support this process, and (3) investment choice and accessibility to capital markets services to promote greater retail investors' participation.

In the Communication of the Commission on CMU of 15 March 2019, the Commission indicated, among others, that while the Commission action in respect of CMU has already started to have an effect [...] more work is clearly needed for a vibrant Capital Markets Union to be in place in the EU.

In the Mission Letter to Vice-President Dombrovskis of 10 September 2019,² President von der Leyen highlighted the importance i) to speed up the work towards a CMU to diversify sources of finance for companies, ii) to tackle the barriers to the flow of capital, iii) to explore ways to make cross-border

¹ The EFMLG is a group of senior legal experts from the EU banking sector dedicated to making analysis and undertaking initiatives intended to foster the harmonization of laws and market practices and facilitate the integration of financial markets in Europe. The members of the Group are selected on the basis of their personal experience amongst lawyers of major credit institutions based in the EU active in the European financial markets. The Group is hosted by the European Central Bank.

² The Mission Letter is available at https://ec.europa.eu/commission/sites/beta-political/files/mission-letter-valdis-dombrovskis-2019_en.pdf.

investments easier, iv) to improve the supervisory system, and v) to better harmonise insolvency and tax proceedings. Moreover, in the Call for Application for the above-mentioned High-Level Forum issued in October 2019,³ the Commission noted that i) the need to complete the Economic and Monetary Union and ii) the possible departure of the United Kingdom from the EU make CMU even more important to deliver a more stable, innovation-based and sustainable economic growth. Lastly, in its Conclusions on the Deepening of the CMU adopted on 5 December 2019,⁴ the ECOFIN Council declared that, despite the measures taken so far, the rationale for developing CMU further is still valid and this need is amplified by geo-political, social and economic developments that have taken place since 2015.

The EFMLG agrees with these reflections of the Commission and the ECOFIN Council and would like to take it as an opportunity to suggest a series of areas or directions which could be covered by the future work of the Commission, and of the EU in general, in respect of CMU.

Therefore, the EFMLG has prepared the below list of points for the consideration of the Commission. The EFMLG is aware of other initiatives which also make suggestions towards the deepening or the completion of the CMU.⁵ Certainly, some of the EFMLG points below may coincide with points made in any such other initiatives.

a) Harmonized legal and regulatory frameworks to support a fully integrated and unified Capital Market Union

With the growing digitalization of financial and banking services, competition between diverse service providers should be monitored and regulated in order to ensure a level- playing field for all market players.

Removing or at least substantially reducing legal, regulatory, tax and operational barriers to trading activities and, more in general, to cross border flows of capital and liquidity, working towards the further convergence, consistency and harmonization of national frameworks and further improving the transparency of capital markets transactions as well as the quality and the availability of market data

³ The document is available at https://ec.europa.eu/info/sites/info/files/business_economy_euro/growth_and_investment/documents/191010-cmu-high-level-forum-call-interest_en.pdf.

⁴ The ECOFIN Council Conclusions on the Deepening of the Capital Markets Union are available at <http://data.consilium.europa.eu/doc/document/ST-14815-2019-INIT/en/pdf>.

⁵ See, for instance, among others, the CEPS report “Rebranding Capital Markets Union” of 24 June 2019, available at <https://www.ceps.eu/ceps-publications/rebranding-capital-markets-union/>, the AFME report “Finance for Europe – Building competitive, resilient and integrated financial markets” of 10 July 2019, available at <https://www.afme.eu/reports/publications/detail/finance-for-europe--building-competitive-resilient-and-integrated-financial-markets>, the AFME report “Capital Markets Union – Key Performance Indicators” of 16 October 2019, available at <https://www.afme.eu/reports/publications/details/Capital-Markets-Union--Key-Performance-Indicators-Second-Edition>, and the JRC Technical Report “Monitoring the development and integration of EU countries’ capital markets”, available at https://publications.jrc.ec.europa.eu/repository/bitstream/JRC118408/2019_technical_report_cm_final.pdf. See also the Next CMU High-Level Group “Savings and Sustainable Investment Union” of 9 October 2019 available at <https://www.nextcmu.eu/publications/>.

at reasonable costs, which are largely the case under the empire of MiFID 2 but that, at least so far, have not materialized in all its potential, as well as the efficiency of securities record-keeping and settlement systems across the Union remain keys to stronger capital markets.

Also in light of the peculiar composition of the liabilities' structure of most European non-financial corporations characterized by strong reliance on the banking source of funding, it may be put forward that without an effective Banking Union, a truly and fully functional and integrated Capital Markets Union may seem to be out of reach. The CMU project, as a necessary complement to the Banking Union intrinsically linked to and mutually reinforcing this latter, is to be further developed in combination with a more effective, coherent and fully integrated Banking Union.

b) Pension funds across the European Union

The Pan-European Pension Product, established with the EU Regulation 2019/1238, is a step in the right direction towards the creation of a multi-pillar retirement savings system having a true European dimension, but it targets a minor proportion of EU inhabitants (workers moving from one country to the other).

Supporting the development of a wider set of pension funds and retail products, alongside traditional national retirement schemes, able to mobilise and channel the European households savings (accumulated at an average rate than is well higher than US or Japan) towards return-generating productive investments may require, inter alia, fiscal incentives, while it would contribute to i) ensuring the sustainability of European pension systems in the context of ageing populations, ii) deepening the pool of long-term investors, and iii) due to the duration of related liabilities, fostering the investment in equity across Europe thereby contributing to unlocking the true potential of CMU and creating value to citizens.

c) Securities Regulator of CMU

CMU raised the expectation that a single European Capital Market Supervisor would be created, likewise the Banking Union. The ESAs review proposed to strengthen the role of ESMA, but no sufficient measure addresses this issue substantially.⁶ At this stage, the supervision of capital markets remains national, with ESMA as a coordinator. The powers of ESMA will be extended, inter alia, to benchmarks, data reporting service providers, and Market Abuse.

While the EFMLG is aware of the divergences across capital markets within the EU and their relatively multi-layered structure, the ECB would encourage the EU authorities not to abandon the reflexion on the need to centralise supervisory and regulatory powers under a single EU entity.

For instance, currently, the conduction of an IPO or a secondary offer is under the competence of national authorities and one can wonder whether the CMU would not benefit of a centralised securities authority, specifically regarding listing, prospectus approval and surveillance of disclosure obligations together with (a degree of) common capital market supervision.

⁶ See https://ec.europa.eu/commission/presscorner/detail/en/MEMO_19_1928.



Ultimately, the establishment of a European Union Securities Market Supervisor could be seen as a consequence of the implementation of CMU and as completion of its framework.

d) Safe asset for the euro area

Currently, a critical missing element of a fully integrated CMU is the absence –at least for the euro area- of a safe asset, i.e. a high quality asset in which market participants could invest.

A safe asset i) could provide a liquid source of high quality collateral ii) would greatly enhance portfolio diversification as well as the depths of liquidity in the capital markets iii) would improve the overall functioning of the banking system and the stability of the financial system as such, in particular, through its potential to break the negative feedback loops between sovereigns and domestic banks, and iv) would also represent a key step towards enhanced private risk sharing.

Such an euro-denominated asset could also serve the objective of i) deepening the integration and advance the Economic and Monetary union ii) facilitating the development of capital markets by introducing a genuine euro area yield-curve serving as pricing reference, and iii) fostering the international role of the Euro.

The EFMLG notes that the Commission's proposal for a safe asset in the form of sovereign bond-backed securities has not been progressed in the European Council. Therefore, also relying on the longstanding debate in this field and the various proposals put forward in the past years,⁷ different possible approaches to safe assets should be considered in close contact with all relevant actors and market participants. Also, the EFMLG notes that the issue of the sovereign-banking nexus remains an impediment to the progress in completion of CMU.

e) Crypto-assets

In January 2019, the EBA⁸ and the ESMA⁹ published two reports suggesting a common European legislation on crypto-assets and Initial Coin Offering (ICO) to ensure investor protection. The ESMA, in its report, states that where crypto-assets qualify as transferable securities, the legal framework for the regulation and supervision of financial instruments applies, but where a specific crypto-asset does not qualify as a financial instrument, no financial regulation or supervisory rules will apply, leaving investors exposed to substantial risks.

⁷ Among which, for instance, most recently, that of the French Banking Association (FBF) came up with three proposal in a memo dated May 2019 which basically proposes as follows :

- creation of private low risk reference asset classes, through the securitization of real estate loans that meet very high quality standards. A European agency (similarly to Freddy Mac and Fannie Mae in the US) could define and monitor compliance with the quality standard of underlying real estate loans;
- implementation of a European mechanism for the securitization of credits with a positive climate impact with a European label and the guarantee of a recognized public body, such as the European Investment or the "Climate Bank" proposed by the President of the French Republic;
- development of private reference asset classes through the securitization of consumer or corporate loans.

⁸ See <https://eba.europa.eu/eba-reports-on-crypto-assets>.

⁹ See <https://www.esma.europa.eu/press-news/esma-news/crypto-assets-need-common-eu-wide-approach-ensure-investor-protection>.



In addition to the laws relating to the regulation of transferable securities, other aspects are to be considered in connection with an ICO, including anti-money laundering and financial crime requirements, privacy and data protection issues, and taxation and accounting.

Specifically, the urgency regards the need to have in place appropriate risk disclosure requirements in relation to the issuer, the projects, and the rights attached to the ICO in order to ensure the adequate level of consumers' protection. As pointed out by ESMA, the quality, transparency, and disclosure of risks in the so-called ICO 'white papers' varies greatly and often emphasise the likelihood of financial returns to encourage speculative investments behaviours by consumers.¹⁰

For these reasons, a common EU regulatory framework on crypto-assets and ICO is necessary to complete the CMU, also taking into account that from 2015 to 2017, 40% of all the ICOs were based in EU.¹¹

Yours faithfully,

Otto Heinz

Chair of the European Financial Market Lawyers Group

¹⁰ See *Ibid*, p. 40. In the ICO context, 'white paper' is a document presented by the issuer, which contains technical and financial information to inform and encourage investors to participate in the offer of the cryptocurrency.

¹¹ See <https://www.coindesk.com/report-european-startups-take-in-half-of-all-ico-funding>.

