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EBF Contribution to the High-Level Forum on the CMU

The European Banking Federation fully supports the European Commission's efforts to relaunch the Capital Markets Union (CMU) and, specifically, the work of the High-Level Forum (HLF). The EBF sees the need for further integrated capital markets. Not least in view of the enormous challenges and strains posed and imposed by the Corona pandemic, a top priority must now be to eliminate all obstacles to economic growth.

Despite progress in the previous legislative cycle, further reforms are needed to remove regulatory obstacles so that EU financial markets can develop and integrate. A fully functioning CMU is vital to meet corporates' funding and investors' investment needs. Moreover, greater diversity of financing will make our financial systems more resilient and our economies more capable of confronting challenges such as climate change and digitalisation.

In particular, a more developed and more integrated CMU is a fundamental prerequisite for achieving the objectives of the EU's Sustainable Finance Action Plan. Only with a fully developed and integrated European CMU can capital flows be reoriented towards sustainable investment in the service of sustainable and inclusive growth.

Conversely, CMU will also be more successful with greater development of sustainable finance products. In that respect, ensuring access to and availability of digital, standardised and reliable environmental and sustainability data is critical to ensure a transparent identification of sustainable investments across borders. A transparent sustainable financial ecosystem will be a key driver for boosting the capital available for financing the sustainable transition.

The EBF has a long-standing engagement in capital markets policy, having contributed to the regulatory policies from the perspective of the universal, private banks which are both providers of capital markets services and products to investors and companies and users of capital markets themselves. On behalf of the banking sector, the EBF has consistently supported the development and integration of capital markets, and promoted the principles of transparency, efficiency, investor protection and investor choice and the issuers' interests.

In line with this engagement, in 2019, the EBF initiated **the Markets4Europe campaign**[1] to promote the **structural reforms,** required to develop and integrate the EU's financial markets, through regional conferences, technical workshops and advocacy. The campaign brings together **market infrastructures, banks, companies and investors;** it is guided by a group of former EU/national **Leaders** and supported by the **16 CEOs** of diverse users and providers of financial market services in the EU (some of which are represented in the HLF).

The **six principal recommendations of the Markets4Europe campaign**, published in its Roadmap[2], are:

- **Channel long-term savings into financing entrepreneurship**
- **Make cross-border investment as easy and reliable as domestic investment**
- **Remove tax obstacles faced by investors and companies**
- **Improve the companies' direct and indirect access to capital markets**

[1] https://markets4europe.eu/

[2] Available on Markets4Europe website

- Embark on an EU-wide campaign of financial literacy to educate the current and future generations of investors and entrepreneurs
- Strengthen the EU's international role in the financial sector

As the initiator and coordinator of the Markets4Europe campaign, the EBF is fully committed to these objectives and to the recommendations made for EU, Member State and industry action.

In addition, since the Markets4Europe's scope is broader than the banking sector, the EBF has also decided to identify the banking sector-specific priorities, with a focus on concrete and most immediate challenges ahead:

- ✓ **More efficient EU securities market processes**
- ✓ **Proportionate investor protection and fostering retail long-term investment**
- ✓ **Strengthening the securitisation market**

1. More efficient EU securities market processes

It should be just as convenient and inexpensive for investors to invest in securities throughout the EU as it is to invest in domestic securities. The servicing of their assets should not give rise to any new, complex processes with associated additional costs. Currently, diverging civil law measures, tax rules and regulatory requirements at national level are not only limiting investors access to capital market products but also affecting the consistency of the processes for settling trades, holding assets in custody and asset servicing across the EU.

- **Harmonised legal requirements and processes to reduce the obstacles to cross-border investments**

Operational, legal and tax barriers, known as the Giovannini Barriers, have been identified as critical obstacles to cross-border capital market activities[3]. While some of the main barriers have been overcome, others remain, and some new ones have appeared. Considering the nature of such barriers, a solution based on the combination of self-regulation by market participants (such as standard-setting and the establishment of market practices) and regulatory changes to current EU legislation should be pursued. To achieve such harmonisation and to help investors make cross-border investments in securities as smoothly as it is possible to invest in domestic securities, the EBF recommends in particular targeted changes in the following areas, as identified by the EPTF: complexity of post-trade reporting structures; fragmented corporate actions and general meeting processes; inconsistent application of asset segregation rules for securities accounts.

- **Common framework to facilitate direct market access for SMEs**

Concerning the development of the equity markets, the challenge is not only one of facilitating the listing of European businesses but also one of broadening the investor base. In this respect, the different initiatives adopted to promote the development of European capital markets, specifically that of growth markets for SMEs, must be supported and developed further.

- **Harmonisation of tax procedures**

The EBF advocates for simplifying withholding tax collection refund and relief at source procedures. Today tax procedures discourage investors from making cross-border investments because of the complexities in applying double taxation treaties (by both home and host tax authorities) and

[3] Report of the European Post Trade Forum (EPTF), established by the European Commission in 2016. The EPTF carried out in-depth analysis of the current structures governing all post-trading activities relating to capital market products, reviewed the current status of the Giovannini barriers and identified new barriers. In May 2017, it submitted an extensive report on the existing obstacles to the European Commission, together with proposals for overcoming them.

because of the administrative burden to be refunded. We acknowledge the European Commission's efforts to promote best practices.

However, we would also support simplifying and standardising withholding tax procedures at Member State level by implementing TRACE as a standardised system for claiming withholding tax relief at source of portfolio investments and by applying the proposed electronic format for the information to be reported by financial institutions to tax administrations and for the exchange of information between tax administrations. We also believe that such a new system would improve the security of transactions and would help to prevent fraud.

- **Review of the prudential treatment of investments by financial institutions**

Financial institutions play an important role in the capital market also as investors. Prudential treatment of their exposure should be revised to remove unnecessary constraints.

Private equity exposures for banks under Basel IV/CRR 3 are unduly penalized. In short, a high-risk weighting factor associated with all equity exposures by banks may reduce their investments in private equity and venture capital (in particular start-ups), an important mean of financing of the real economy. This may also prevent banks to invest in fintech start-ups to go through their digitalisation/innovation process.

Solvency II reform on the treatment for insurance companies of unrated bonds with third party assessment would also enhance the European private placement market, where insurance companies play an important role as investors.

2. Proportionate investor protection and fostering retail long-term investment

We would like to support a proportionate and appropriate level of investor protection rules which would not disincentivise them from investing in financial markets.

- **Long-term investment and financial education**

A major constraint in the development of EU Capital Market is the inability of pension funds to invest in capital markets. There is a range of factors that can explain this but the excessive constraints on the investment policies of pension funds is a critical obstacle. Furthermore, in some EU countries, pension funds do not have the necessary skills and assets-undermanagement to invest in real economy. Thus, the European regulatory framework regarding pension funds' investments should be reviewed in order to remove undue constraints on the capital available for investing in public and private equity markets and facilitate cooperation among pension funds that make it easier for them to invest in the real economy. Moreover, transnational European investments/programmes should be identified with the aim of channelling savings coming from EU citizens' retirement plans to infrastructures, utilities, research programmes, etc. by the intermediary of financial markets.

The financial literacy of the public, particularly regarding the capital markets, would allow European citizens to familiarise themselves with market products. The goal would be to develop a long-term investor base with a risk appetite that would allow investment in innovative initiatives, projects and businesses.

- **Tailoring PRIIPS and MIFID requirements to find the appropriate level of investor protection**

Investor protection rules should protect investors against risks. However, the most recent changes under MiFID II and the PRIIPs Regulation have led to investors being no longer able to buy capital market products designed and suitable for them because the rules governing distribution are inconsistent, incomprehensible or excessive and provide for no differentiation between investors in terms of their knowledge and experience. This needs to be remedied.

The easing of the conditions for marketing certain financial products (specifically in the MiFID 2, PRIIPs and IDD regulations) might encourage the reallocation of savings to corporate financing. In fact, regulation has had a negative impact on the amount of information provided to customers with no real benefit for their understanding.

3. Strengthening the securitisations market

High-quality securitisation tranches, which proved secure even during the financial crisis, should not be discriminated against compared to other financial products, especially as they provide an urgently needed bridge between bank lending and the capital market funding.

- **High quality asset classes**

The creation of high-quality asset classes for securitizations in the eurozone could help the CMU by providing the market with depth and liquidity. The introduction of private low risk reference securitizations might be considered in the form of:

- Securitisations that have performed very well and that meet the STS quality standards. Historic/empirical data should be used to identify such types of securitisation that have proven to be safe even during the financial crisis. To identify the types of low risk reference securitisations the segments listed in Art. 325 am (1) table 7 CRR II (among others Prime-RMBS and Auto-ABS) could be used as starting point,
- Securitisation of debt issues that have a significant sustainability impact, promoting development of market financing and support for sustainable finance

- **Relaunching securitisation**

The EU proposed in 2015 a framework for Simple, Transparent and Standardized securitisations ("STS") with an aim to revitalise the securitisation market in Europe which was drastically hit by the financial crisis. However due to, among others, unfavourable regulatory treatment (too high capital buffer requirement), very burdensome disclosure and due diligence requirements, the STS Regulation did not obtain the expected results. We deem that steps should be taken to review the STS Regulation, i.e. by simplifying and streamlining the disclosure requirements and by realigning the regulatory capital and liquidity treatment with those of similar products, like covered bonds.

More broadly, an efficient securitisation market should be further developed as it is an essential tool to allow banks to continue to finance their clients while controlling their balance sheet and capital requirements. Thus we support the idea to strengthen the securitisation market proposed in the latest reports of the "Markets4Europe" campaign (September 2019), of the IMF (September 2019), and of the "NextCMU" initiative (October 2019) launched by the ministries of finance of the Netherlands, France and Germany. Especially, synthetic securitisation shall be implemented in the framework of STS-securitisation.

As a conclusion, we believe that **some key performance indicators should be usefully introduced in order to assess the integration of capital markets across EU Member States**: i.e. how many investments are made by any Member State on instruments issued by private corporates of any other Member State. We also suggest making the support of any European programme or fund in the development of a company more effective, by increasing the available information on which European programmes/funds are suitable to finance the company's round of growth.