Nordic Securities Association

MEMO

Position Paper

Capital Markets Union (CMU)

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The Nordic Securities Association (NSA) supports the Commission's plan to build a European Capital Markets Union (CMU). The Action Plan published in September 2015 reveals an ambitious plan with several important ideas; SMEs' access to capital markets financing is eased, and barriers hampering cross-border investments within EU will be removed. These actions are necessary in order to strengthen Europe's economy, stimulate growth, and create jobs.

Significant inefficiencies and barriers for cross-border investment
There is a need to identify and evaluate the main inefficiencies and barriers in contributing to the European Capital Markets, not only for growth and jobs, but also for long-term investments and financial stability. Despite earlier efforts, the development of single market for capital has been slow, and there are still many obstacles hampering cross-border investments. These obstacles arise from national law (e.g. insolvency, tax and securities laws), and from a fragmented market infrastructure.

Primary and secondary markets are interdependent
Stronger and more effective capital markets in Europe require recognition and handling of the critical dependency between primary markets (issuance) and secondary markets (market making and trading). A well-functioning secondary market is essential to gain investors' confidence to invest in the primary issue. Furthermore, it should be carefully investigated how to stimulate both the supply and demand side within the EU framework.

Deep and liquid markets are crucial
Liquid and efficient secondary markets are a prerequisite for the activities in the primary markets, as they enable investors to trade also large orders whenever they wish and with minimal market impact. Creating an investor appetite to invest in SMEs and other financing opportunities, which will help the economy to grow, requires confidence that the markets operate efficiently and are sufficiently liquid to protect their investment. When markets are less liquid and investors do not have the ability to trade at any point in time, it is likely that investors will decide not to invest in the first place, or will at least require a substantial compensation for illiquidity. This increases the cost of capital and implies that it will be more difficult for SMEs to mobilise the available capital and get it to where it can be most productive.

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Therefore, it is crucial that the increased use of fixed income and equity funding is not undermined by limiting secondary markets through regulation. We are confident that the Commission understands the benefit of liquidity provision as a key element of the CMU policy objectives[1]. However, we are concerned since we are having trouble understanding how these policy objectives are reflected in the regulation – in addition on the more technical level. In this respect we urge the Commission to adopt a balanced approach on the liquidity and transparency calibration in MiFID2/MiFIR, as also described in our attached CMU impact assessment paper. We are indeed concerned that the proposed liquidity calibrations in the available draft technical standards will work against the building of the CMU.

Simple and flexible regulation is needed

Rather than building the CMU through detailed and burdensome EU regulation, the CMU should emerge by tearing down unnecessary impediments that hinder cross-border investments and prevent efficient access to capital. Therefore, we encourage the European Commission to simplify the regulation and make it as flexible as possible in order to support economic growth without jeopardizing investor protection. In this respect, we welcome the Commission call for evidence on cumulative impact on recent (and upcoming) regulation. Furthermore, a uniform application of the rules throughout the EU is also necessary. Currently the Member States' national competent authorities have very divergent practices while the rules are the same. In this context it is very important to state that lack of supervision could not be taken care of by stricter rules/legislation.

Strong support for Call for evidence and Better Regulation agenda

The call for evidence is closely linked with the Commissions "Better Regulation" agenda. We fully support these initiatives and endorse that new regulation and revision of current legislation should in all possible instances seek to promote growth and jobs in Europe. In short:

- The EU needs to be big on the big things and smaller on smaller things.
- Lawmakers should focus on areas in which regulation can add the most value.
- We are concerned that an increasing part of the regulation is being pushed from level 1 to level 2 in order to achieve political agreements on level 1. This creates tensions in the level 2 process. In this context, MiFID2/MiFIR is a warning example.

Wanted: an overview and assessment before launching new regulation

Furthermore, a proposed legislative act cannot be viewed in isolation, but must be assessed in conjunction with existing regulation. The diverse and complex requirements that investment firms in the EU must comply with are scattered across a wide range of different legal acts, and often the different requirements

[1] European Commission: Green Paper on Long Term Financing of the European Economy (2013), page 23:*"providing liquidity is an important function of secondary markets. Liquid and well-functioning secondary markets encourage activity in primary markets too, as this enables investors to sell their investments quickly and at low cost when needed"*

are overlapping. Consequently, there is an overwhelming risk of inconsistencies, which in turn will make regulatory compliance highly complex.

The CMU should apply a more holistic approach to regulating financial services. In particular, we would like to highlight the importance of a closer coordination between prudential and market regulation, such as CRDIV/CRR and MiFIR2/MiFIR impact on market making. This would create a more unified and consistent regulatory framework for the EU financial sector, which would be in sync with broader political objectives and easy to comply with. We believe that the CMU and the EU agenda on better regulation can contribute to ensuring this in the future.

What are the next steps in the Call for Evidence?
Inconsistencies and overlaps in regulation need to be ironed out. For instance, investor protection regulations such as MiFID2/MiFIR, PRIIPs, IDD, UCITS and the Prospectus regulation have several overlaps and inconsistencies. Therefore, we strongly support the Commission's initiative to assess the cumulative impact of previous (and forthcoming) regulatory reforms on the investment environment to ensure coherence and consistency.

We are especially interested to understand **how** the Commission will use the information gained from the consultation as we expect that the Call for Evidence will reveal a number of existing and upcoming legislative acts which could benefit from a revision[2]. We recommend the Commission to inform us of areas that require quick modifications, as soon as possible. This is important, as implementation work is on-going. Furthermore, the Commission should give a longer-term communication on more comprehensive work which will be undertaken as a result of the Call for Evidence and which will have wider implications to the EU financial rulebook.

Incentives to promote investments in SMEs
Another important task is to stimulate the **demand side** for investments by ensuring an encouraging framework and increased choices. Tax issues are not an EU matter as they are handled nationally. It is, however, important to stress that simple tax structures and tax incentives are useful tools to stimulate the demand side, which was also recognized in the Action Paper, in which the Commission will launch a package to promote best practice on tax incentives, among other things.

For institutional investors, their choices are further limited due to Solvency II. The high capital requirements especially for equities (except equity-like assets which qualify as infrastructure as these already face a rebate) should be revisited in order to enable the institutional segment properly.

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[2] http://ec.europa.eu/finance/consultations/2015/financial-regulatory-framework-review/docs/consultation-document_en.pdf page 4 and 5, where it appears that: "*It will help inform the individual reviews and provide a basis for concrete and coherent action where required…*" and "…*This call for evidence, alongside other work, will serve as a basis for identifying the main issues that require further attention from the Commission.*"

Furthermore, we believe that the Commission should continue the work with harmonization of **securities law** to ease cross-border investments. Questions related to conflict of law should be included. Legal certainty regarding conflict of laws, and predictable and reliable legislation that gives all parties involved the benefit of legal certainty in cross-border transactions, is essential to promote cross-border investment. Such legislation will form a base for appropriate investor protection, which is an absolute necessity before encouraging retail clients to invest on a cross-border level.

In this context, it is very important to clarify ownership of securities when trading across borders. The certainty provided by EU-wide legislation would provide reassurance to investors who may be trading outside their usual legal jurisdiction, and in the event of adverse market conditions, they may find themselves unable to determine e.g. which law is applicable to a transaction with a defaulting counterparty.

Encourage SMEs to use the capital market as funding source
Stimulating **the supply side** of capital by ensuring an encouraging framework is also very important. In this context it is very important that the infrastructure is smooth, and the process for accessing capital market becomes easier and cheaper, especially for SMEs.

Therefore, we welcome the Commission's **prospectus review** which is aimed to reduce the costs and administrative burden of the issuance of securities. However, the proposal should be formed in a way that does not harm the European wholesale bond markets. In addition, the categorisation of risk factors may prove to be counterproductive. Our position and proposals are described in more depth in our position paper on prospectuses.

Finally, we support the initiative to develop a **framework for STS securitisation,** which could help to increase growth and create jobs in the EU. The STS framework will incentivize banks in the EU to increase lending to SMEs, especially in a future business environment where funding could become less prevalent. The STS designation will also ensure a broader investor base and encourage cross-border investments. The NSA position and proposals are developed in our position paper on securitisation.