



# **Financial Services User Group's (FSUG)**

## **Consultation on the review of the European System of financial supervision**



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FSUG c/o European Commission  
Internal Market and Services DG  
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# **CONSULTATION ON THE REVIEW OF THE EUROPEAN SYSTEM OF FINANCIAL SUPERVISION**

## **SUBMISSION BY THE FINANCIAL SERVICES USER GROUP (FSUG)**

### **INTRODUCTION**

The FSUG is a group of 20 expert individuals appointed by the European Commission to represent the interests of consumers, retail investors and micro-enterprises.

The group's role is to:

- advise the Commission in the preparation of legislation or policy initiatives which affect the users of financial services
- provide insight, opinion and advice concerning the practical implementation of such policies
- proactively seek to identify key financial services issues which affect users of financial services
- liaise with and provide information to financial services user representatives and representative bodies at the European Union and national level.

The FSUG is supported by Internal Market and Services DG and DG Health and Consumers.

FSUG is pleased to submit a response to such an important consultation. Our submission is in two parts. The Background and Summary of Views provides a reminder of why serious reform of EU financial markets is needed and summarises our views. The second part contains our response to the specific questions in the consultation. We have focused our response on those issues which most affect financial users within our remit.

### **BACKGROUND**

A modern economy and society needs an efficient, effective, accountable financial system and financial services industry. But following repeated market failures, it is self-evident that the financial sector must be radically reformed. The ongoing financial crisis is the most obvious, high profile example of large scale market failure. Far from managing risk more effectively, certain activities and 'innovations' actually magnified risk in the financial system.

Less obvious, but equally important for financial users, are the chronic market failures that have been overshadowed by the systemic financial crisis. These failures include: embedded inefficiencies and high costs; the growth in extractive business models; misallocation of capital and resources; value destruction of savings, pension and investment portfolios; weak or misdirected competition that benefits dominant providers, intermediaries and distributors not the end-user; the growth in financial innovations of little or no social utility (or toxicity); poor financial

advice, misselling and aggressive behaviours; reckless lending ; poor quality service; and chronic financial exclusion. These failings have seriously hindered the establishment of a truly effective single market in financial services. Market failure has been in evident across the board and not been limited to one particular sector – although the degree of market failure obviously varies with certain sectors responsible for disproportionate levels of financial detriment.

What is striking is how badly much of the financial services industry has performed even during comparatively 'good times' in the run up to the financial crisis. As the European Commission's own Consumer Markets Scoreboard shows, the financial sector is one of the consistently worst performing consumer sectors. But we face a new, even more difficult, financial and economic reality defined by a range of macro and micro socio-economic events which put sustained pressure on household budgets, expose poor value and inefficiencies in the financial services supply chain and threaten the commercial viability of dominant business models. This makes the challenge of making markets work all the more difficult and necessary. Dealing with this new economic reality requires a new economic paradigm to understand the role and efficiency of markets and a new regulatory model to make markets work in the interests of society.

#### **SUMMARY OF VIEWS**

Three clear regulatory challenges have emerged post financial crisis:

- i) creating financial stability;
- ii) safe financial institutions through enhanced prudential regulation; and
- iii) making markets work for financial users, the wider economy and society.

So far, systemic risk management and prudential regulation has dominated the policy agenda. Huge intellectual effort and regulatory resources have been devoted to promoting financial stability and improving prudential regulation. We fully appreciate the need to promote financial stability and resilience, and ensure that financial institutions are sound and prudently run. But the challenge of making markets work has not been given anywhere near the same priority. Policymakers must recognise that ensuring financial markets work in the interests of financial users is just as important to the citizens' welfare as financial stability and prudential regulation.

We attribute the failure of financial regulation to four main reasons: i) a flawed economic paradigm and regulatory philosophy that wrongly assumed a degree of market effectiveness not borne out by objective analysis; ii) a flawed, unrealistic regulatory model that failed to understand the root causes of market failure and, consequently, failed to apply effective policy interventions; iii) an approach to regulation that was too slow and unresponsive to emerging crises and market failure and inconsistent, weak implementation and enforcement of policy; and iv) ineffective regulatory structures and poor governance and accountability.

As we explain in our paper, ***Making financial services work for financial users: new model financial regulation***<sup>1</sup> market reform, in turn, requires a profound change in the philosophy, culture, and approach to regulation. We need a new regulatory philosophy and culture that puts financial users at the heart of market reform and establishes the primacy of financial users – that is, markets exist to serve the interests of users and society, not the other way around. This requires a more robust, sceptical, early interventionist, and precautionary approach to regulation. A more precautionary, early intervention approach is appropriate for complex, high risk markets such as financial services – this means a greater emphasis on ex-ante regulation. Good regulation does not stifle genuine innovation and choice – indeed, good regulation promotes socially useful innovation and choices.

Furthermore, making markets work requires a better understanding of the root causes of market failure. The activities and behaviours of the institutions and intermediaries at each part of the supply chain must be aligned to the interests of financial users.

The effectiveness of the ESFS and ESAs therefore can only be judged against the challenges we describe above. Unfortunately, as we explain below, we take the view that, overall, the new European system of financial supervision (ESFS) and the new European Supervisory Authorities (ESAs) while undertaking some very critical work in relation to financial stability and micro-prudential regulation, has so far made very little difference to financial users. Of course, this may change for the better and we have made a number of recommendations which, if adopted, would put the interests of financial users at the heart of the ESFS and ESAs.

In particular, we would highlight that:

- the ESAs have not sufficiently prioritised the critical challenge of protecting consumers and making markets work concentrating most effort on financial stability and micro-prudential regulation. This requires a rebalancing of priorities and allocation of greater regulatory resources to consumer protection and making markets work;
- the ESAs have so far not made use of their new powers to prohibit or restrict certain financial activities that harm financial users, and to investigate breaches of EU Law. These powers should have been a very powerful intervention to protect financial users, promote genuine innovation, and make markets work. We urge the ESAs to proactively identify harmful, risky, or socially useless financial activities and products and utilise these powers;
- the ESAs have focused too much on regulatory processes rather than outcomes. We suggest that the ESAs should publish consumer and market outcomes against which to judge the effectiveness of EU financial markets and financial regulation. ESAs should publish a performance report on annual

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<sup>1</sup> [http://ec.europa.eu/internal\\_market/finservices-retail/docs/fsug/papers/new\\_model\\_fin\\_regulation-2012\\_09\\_en.pdf](http://ec.europa.eu/internal_market/finservices-retail/docs/fsug/papers/new_model_fin_regulation-2012_09_en.pdf)

basis setting out how well relevant financial markets have performed over the year and a forward looking risk outlook setting out the key risks to the relevant consumer and market outcomes. In addition, to aid informed debate, the ESAs should publish a comprehensive consumer trends report.

- we have serious concerns about the governance and accountability mechanisms relating to the regulatory system. The ESAs have been in contravention of provisions requiring a balance of industry and retail user representatives in the relevant "Stakeholder Groups" to the disadvantage of financial users. Furthermore, the sheer imbalance between the resources available to industry representatives and financial user representatives undermines the ability of user representatives to participate. The ESAs, as soon as is practicable, should take action to rectify this imbalance to ensure the interests of financial users is properly represented.
- the current structure of the ESAs, with the separation of banking, insurance and pensions, and securities markets and asset management supervision, encourages a silo effect and an inconsistent approach to regulation. FSUG argues that the time is now right for a move to the 'twin peaks' structure of regulation and the establishment of a dedicated, single Financial Consumer Protection and Markets Authority covering all financial products regardless of legal or corporate structure.

## **RESPONSE TO SPECIFIC QUESTIONS**

### **1. The European Supervisory Authorities (ESAs)**

#### **1.1. Effectiveness and efficiency of the ESAs in accomplishing their tasks**

**1.1.a.** How do you assess the impact of the creation of the ESAs on the financial system in general and on (i) financial stability, (ii) the functioning of the internal market, (iii) the quality and consistency of supervision, and (iv) consumer and investor protection in particular?

##### **Financial stability**

It is probably too early to say how effective the ESAs have been in promoting financial stability. This will only emerge over time. However, we do take the view that the recent work of the ESAs creates a much improved framework for financial stability and prudential regulation.

##### **Functioning of the internal market**

From a consumer perspective, the creation of the ESAs has had very little impact on the functioning of the single retail market. Genuine consumer led cross border transactions remain an unrealistic prospect due to business and commercial barriers, and consumer attitudes. The same is also true for the execution of voting rights of shareholders cross border. However, the ESAs do not seem to prioritise these issues.

##### **Quality and consistency of supervision**

The problem here is not the detailed supervisory approach rather the structure of the ESAs which encourages a silo approach to regulation. This undermines regulatory consistency.

##### **Consumer and investor protection**

The creation of the ESAs has not any significant impact on improving consumer and investor protection or making financial markets work in the EU. This can be partly explained by the limited mandate in this area and because most of the legislative proposals relating to consumer protection in the financial services area have not yet been finalized (mortgage credit, KID for PRIPs, MIFID, IMD2, Payment account, Payment Services). The ESAs have not yet been requested to work on implementing measures.

However, as we explain in the summary above, even within the constraints of this limited mandate, the ESAs have not in our view been effective with regards to consumer and investor protection and making markets work. Much of the problem can be explained by the inadequate governance of the ESAs.

Furthermore, the ESAs have not made use of potentially powerful new powers provided by the new ESFS Regulations including:

- Product intervention (article 9.5 of the Regulations): so far the ESAs have

not used this provision to ban or even temporarily prohibit the distribution of toxic or dangerous financial products. In addition, article 9 – although it is titled “tasks related to consumer protection...” - refers only to financial risks and stability motives for any product intervention, not to consumer protection motives. Article 9.5. should be amended to provide the ESAs with real power to ban or put on hold the selling of financial products that are toxic or not suited for retail clients in particular .

- Power to investigate potential breaches or cases of non implementation of EU Law (article 17 of the Regulations). We are not aware of any examples of the ESAs, so far, making any use of this new power, even though the Securities & Markets Stakeholder Group made a request to ESMA regarding retail investor protection.

We also have concerns about the enforcement of regulation. There appears to be no meaningful progress in limiting cases of misselling (such as misleading information, conflicts of interests in the distribution of financial products, etc.). In particular, article 27 (fair, clear and not misleading information) and 26 (prevention of “inducements”) of the MiFID implementation Directive are not properly enforced.

As mentioned in the Summary, we have concerns about the lack of meaningful reporting by the ESAs including reporting on consumer trends.

To be fair, in February 2013, ESMA published its first “Trends on risks and vulnerabilities” report but this has significant flaws:

- It is not focused on consumer trends: only one page is related to retail investors (p 21) in the whole report;
- Some of the measures included do not properly reflect retail investor experience. For example, the information on p21 of the report relating to portfolio returns is based on a composite portfolio constructed from various market indices. This could be a useful benchmark but does not allow stakeholders (and regulators) to judge how well the asset management sector is performing from the perspective of retail investors. To provide a meaningful reflection of investor experience ESMA should include the performance of actual packaged products including all charges, fees and expenses – this should be shown in nominal and real terms adjusted for inflation. ESMA should also use longer time periods which would be more relevant for long term investors.

With regards to EIOPA, a Methodology Report was released in November 2012, but the first actual report on consumer trends is scheduled only for November 2013, three years after the establishment of the ESAs. Only EBA has released two consumer trends reports in February 2012 and in March 2013.

However, we have more general concerns about the reporting framework for the ESAs. If the ESAs are to become truly user-focused rather than producer-focused, they must first understand what a successful financial market looks like from a financial user perspective.

To be fair, this is not just a criticism of the ESAs. While policymakers and regulators publish many reports on financial market ‘conditions’ such as market activities, size of markets, numbers of providers and products, trends in markets and so on, FSUG

is not aware of any comprehensive reports which actually evaluate the performance of financial markets from the user perspective - or indeed from the perspective of the wider economy and society.

The EU Consumer Market Scoreboard makes an attempt to measure performance from the user perspective. But even this is limited as it does not measure important outcomes such as fair treatment, effective competition, efficiency and value for money.

The absence of effective analysis and reporting can be explained in our view by the dominant approach to regulation which has hitherto assumed that if the theoretical conditions for competition exist, then the right market outcomes must follow. However, we know this is not necessarily the case and there is a world of difference between the illusion of competition and effective competition and innovation that benefits producers and innovation that delivers real benefits for financial users.

FSUG has developed a set of consumer and market outcomes<sup>2</sup> which allows policymakers and regulators to judge how well markets are meeting user needs. We have also developed a set of performance metrics to which allow analysts to evaluate performance against these outcomes. We urge the ESAs to prioritise the creation of a proper market and analysis reporting framework built around these outcomes and metrics. This reporting framework would allow the ESAs to:

- report on consumer trends in a more transparent, relevant way;
- analyse how well relevant financial markets have performed over the year;
- publish a forward looking risk outlook setting out the key risks to the relevant consumer and market outcomes;
- prioritise and allocate resources more effectively in consultation with stakeholders; and
- demonstrate real transparency and accountability.

Finally, we would argue that, in addition to the culture, approach and philosophy of regulation followed by policymakers and regulators, the current **structure** of the ESFS is a barrier to effective consumer protection and market regulation. The current structure of the ESAs, with the separation of banking, insurance and pensions, and securities markets and asset management supervision, encourages a silo effect and an inconsistent approach to regulation. FSUG argues that the time is now right for a move to the 'twin peaks' structure of regulation and the establishment of a dedicated, single Financial Consumer Protection and Market Authority covering all financial products regardless of legal or corporate structure. This Financial Consumer Protection and Markets Authority should be responsible for consumer and investor protection, conduct of business standards, ensuring financial users are treated fairly, and market efficiency.

**1.1.b.** Do the ESAs' mandates cover all necessary tasks and powers to contribute to the stability and effectiveness of the financial system? Are there elements which should be added or removed from the mandate? Please explain?

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<sup>2</sup> These can be found in our paper *Making financial services work for financial users: new model financial regulation*



As mentioned above, the effectiveness of the ESAs mandates with regards to financial stability will emerge over time. However, we do think that the ESAs are laying the groundwork for effective financial stability and micro-prudential regulation.

With regards to the effectiveness of the financial system, we would make two main comments.

As discussed above, ESAs have not made a significant contribution to consumer and investor protection and making markets work. This can be explained by the comparatively low priority given to consumer and investor protection compared to financial stability and micro-prudential regulation.

We argue that the solution in this case is to:

- revise and reinforce the ESAs mandate with regards to consumer and investor protection and making markets work;
- provide the ESAs with the necessary powers, duties and resources to carry out this mandate;
- adopt a new user-focused regulatory approach and philosophy which puts financial users, rather than producers, at the heart of the regulatory system;
- improve the performance and reporting framework to allow stakeholders to judge how well markets are actually performing from the user perspective; and
- as outlined above, move towards a twin peaks structure with the establishment of a single Financial Consumer Protection and Markets Authority. We also argue that each Member State should have its own properly resourced authority coordinated by the EU authority to ensure that legislation is enforced properly across the EU. An effective EU single market can only be built on the foundation of fair, efficient, transparent and safe individual markets.

Secondly, it is not actually possible to say with any degree of authority whether the EU financial system is operating effectively. The financial system consists of capital, wholesale, institutional and retail financial markets linked by a complex supply chain.

We described above how policymakers and regulators do not currently use appropriate analytical and performance frameworks to judge whether 'retail' financial markets are actually working for financial users.

But, the same applies to other parts of the financial system. It is important to remember that the financial system (including capital markets, wholesale and institutional market actors) exist to serve the interests and meet the needs of the real economy and financial users. However, we are not aware of any comprehensive studies produced by policymakers and regulators which objectively evaluate how well the financial system supply chain is meeting the needs of financial users and the real economy.

Therefore, in absence of such robust studies, we are unable to comment on how effective the ESAs are in promoting an effective financial system.

**1.1.c.** In your view, do the ESAs face any obstacles in meeting their mandates? If yes, what do you consider to be the main obstacles? Please explain.

The ESA's are generally very short-staffed which means that they are limited as to how much research they can carry out themselves. They are therefore reliant on stakeholders to provide them with analysis and information which in turn provides an advantage for industry representatives who are in a much better position to provide this input. The staffing shortages also mean that the ESAs struggle to assess how their own output might affect consumer protection.

As mentioned above, the ESAs have to work with different types of national supervisory authorities, and many national authorities competent for consumer protection cannot participate in the voting of consumer protection issues and are not even present during the discussions in the ESAs' Boards of Supervisors. This negatively impacts the decision making process.

In addition, the ESAs do not have the human resources to work on consumer affairs. For example, the consumer unit at EBA consists of two staff members appointed recently. This is clearly not sufficient. The ESAs should be appropriately staffed and have the resources to effectively discharge their duties.

Moreover, as we explain above, one of the main barriers to the effective functioning of the ESAs is the current governance structures. In addition to concerns about the structure of the relevant stakeholder groups, we have fundamental concerns about the governance of board of supervisors of the ESAs. These boards are made up of national Member State supervisors which can create conflicts of interest. For example, this could make it difficult for ESAs to ban dangerous products if national supervisors failed to ban these products, or investigate a potential breach of EU law by individual board members.

Furthermore, certain supervisory board members do not even have customer protection as part of their own mandates at Member State level. This must make it difficult for them to recognise the importance of and supervise the consumer protection mandate at EU level.

We urge that the governance structures of the ESAs be reviewed and a sufficient number of independent public interest members introduced to the supervisory board to ensure ESAs are able to operate effectively in the interests of financial users.

#### **1.1.1. Work towards achieving a single rulebook - regulatory activities**

**1.1.1.a.** Do you consider that the technical standards and guidelines/recommendations developed by the ESAs have contributed to further harmonise a core set of standards in the area of supervision (the single rulebook)? If you have identified shortcomings, please specify how these could be addressed.

**1.1.1.b.** What is your assessment of the work undertaken by the ESAs as regards providing opinions (e.g.technical advice) to the EU institutions?

We have no comment on the actual standards. However, we are concerned that the non-binding nature of the recommendations, guidelines and opinions issued by the ESAs with regards to consumer and investor protection seriously undermines their effectiveness. It is important to remember that many national supervisory authorities do not even have a consumer protection objective and can choose to ignore important standards, guidelines, and recommendations.

**1.1.2. Common supervisory culture/convergence of supervisory practices**

**1.1.2.a.** In your view, did the ESAs contribute to promoting a supervisory culture and convergence of supervisory practices? If you have identified shortcomings how could these be addressed?

For the reasons explained above, this is not happened in the area of consumer and investor protection.

**1.1.3. Consistent application of EU law**

**1.1.3.a.** In your view, do the procedures on breaches of EU law (Article 17 ESAs Regulations) and binding mediation (Article 19 ESAs Regulations) ensure the consistent application of EU law? If you have identified shortcomings how could these be addressed?

As we outline above, the ESAs seem not to have made good use of powers to ensure consistent application of EU law.

There is no single solution to this problem. Rather, this requires a more fundamental change in governance, approach and philosophy adopted by the ESAs.

**1.1.4. Emergency situations**

**1.1.4.a.** Do you consider the ESAs' role in emergency situations appropriate? Please explain.

We have no comment on this.

**1.1.5. Coordination function (Art 31 ESAs Regulations)**

**1.1.5.a.** Do you think that the coordination role of the ESAs is appropriate? If you have identified shortcomings, please specify how these could be addressed.

**1.1.5.b.** In your experience, to what extent have coordination activities carried out by the ESAs contributed to promoting a coordinated EU response to adverse market conditions? Please explain.

As we explain above, the silo approach to regulation undermines effective consumer and investor protection and efforts to make markets work. However, this silo approach is embedded in the regulatory system due to the structure of the ESAs. We argue for the establishment of a twin peaks system.

However, in the interim, there appears to be significant room for closer cooperation between the ESAs on consumer protection issues. Many issues affecting consumers fall between the ESAs e.g. the emerging product of peer-to-peer lending is an investment, savings and credit product which falls between ESMA and the EBA. Therefore, there should be an ongoing exchange on consumer risk issues not only at senior level between the ESAs but also between the stakeholder groups and in the case of ESMA the consultative group to the standing committee on financial innovation.

#### **1.1.6. Tasks related to consumer protection and financial activities**

**1.1.6.a.** How do you assess the role and achievements by the ESAs in the field of consumer protection? Please specify the main achievements by each ESA.

FSUG recognises the genuine attempts by the ESAs to communicate and reach out to financial users. There have been some positive developments. For example, in 2013, the three ESAs organized a joint Consumer Day which was very much welcomed, as consumer issues are similar whoever the financial services providers. EBA has organized two informal meetings with the main European user organizations, and EIOPA has at times provided "plain English" information and analysis of more technical issues to the user-side representatives of its Stakeholder Groups.

However, as we explain above, overall the ESAs have not had any significant impact on improving consumer and investor protection or making financial markets work in the EU. The reasons for this are also explained above (structure, limited mandate, powers, resources, priorities given to financial stability, governance and accountability, regulatory approach, culture and philosophy).

**1.1.6.b.** Are you aware of the warnings that were issued by the ESAs so far? If yes, please specify which ones and whether they have contributed to improve consumer protection or any other objective of the ESAs.

We have been aware of the few warnings issued by the ESAs. However, these have not been readily accessible for consumers, so they are unlikely to have any significant impact on protecting consumers. Information solutions such as warnings have limited impact in changing consumer and producer behavior, especially if they are only available on the ESAs website and only in English. If these are to have even a degree of impact, the way the ESAs communicate to general public should be improved.

#### **1.1.7. Direct supervisory powers**

**1.1.7.a.** How do you assess ESMA's direct supervisory powers? If you have

identified shortcomings, please specify how these could be addressed.

**1.1.7.b.** How do you assess ESMA's performance for the registration and supervision of credit rating agencies (CRAs)?

**1.1.7.c.** Do you consider that further responsibilities of direct supervision should be entrusted on one or more of the ESAs, particularly with regard to institutions or infrastructures of pan-European reach? Please explain.

As mentioned above, the key problem here is the silo approach which undermines effective regulation, supervision and enforcement. Minor reforms to the current structure and approach are unlikely to result in any significant improvement in effectiveness. We argue that a twin peaks approach would be much more efficient way of operating an effective, coordinated system of regulation, supervision, and enforcement.

## **1.2. Governance of the ESAs**

### **1.2.1. General governance issues**

**1.2.1.a.** Are the governance requirements sufficient to ensure impartiality, objectivity and autonomy of the ESAs?

**1.2.1.b.** How do you assess the accountability requirements? If you have identified shortcomings, please specify how these could be addressed.

As we explain above, we have serious concerns about the governance and accountability structures relating to the ESAs. Indeed, we view this as being one of the main barriers to the effective operation of the ESAs.

In addition to concerns about the structure of the relevant stakeholder groups, we have fundamental concerns about the governance of board of supervisors of the ESAs. These boards are made up of national Member State supervisors which can create conflicts of interest. For example, this could make it difficult for ESAs to ban dangerous products if national supervisors failed to ban these products, or investigate a potential breach of EU law by individual board members.

Moreover, certain supervisory board members do not even have customer protection as part of their own mandates at Member State level. This must make it difficult for them to recognise the importance of and supervise the consumer protection mandate at EU level.

We urge that the governance of ESAs be reviewed to introduce a sufficient number of public interest representatives onto the supervisory boards of ESAs.

Furthermore, as we also explain above, the reporting framework undermines accountability in the regulatory system. The ESAs do not employ performance and analytical models that objectively evaluate how well markets function from a financial user perspective. Without a proper market reporting and analysis framework it is not possible hold the ESAs to account for their own performance.

## **1.2.2. Decision-making bodies and voting modalities**

**1.2.2.a.** Does the current composition of the Board of Supervisors (BoS) ensure that it acts efficiently? If you have identified shortcomings, please specify how these could be addressed.

**1.2.2.b.** Does the composition of the Management Board ensure that the ESAs are run effectively and perform the tasks conferred on them? If you have identified shortcomings, please specify how these could be addressed.

**1.2.2.c.** Does the mandate of the Management Board ensure that the ESAs are run effectively and perform the tasks conferred on them? If you have identified shortcomings, please specify how these could be addressed.

See above for our explanation of how the structure of boards of supervisors may compromise the ability of the ESAs to operate effectively in the public interest.

## **1.2.3. Financing and resources**

**1.2.3.a.** How do you assess the arrangements on financing and resources? If you have identified shortcomings, please specify how these could be addressed.

No comment.

## **1.2.4. Involvement and role of relevant stakeholders**

**1.2.4.a.** How would you assess the impact of the relevant stakeholder groups within the ESAs on the overall work and achievements of the ESAs?

There is limited contact between the stakeholder groups and the board of supervisors with regard to consumer protection issues. Again, this links back to the fact that a large number of national supervisors are not responsible for consumer protection issues and there is no direct contact between the stakeholder groups and those other national authorities that are responsible for consumer protection.

Moreover, there is the perennial problem of stakeholders from consumer and investor organisations not having sufficient independent resources to represent the public interest effectively. They are at a distinct disadvantage compared to the well resourced representatives from the industry.

**1.2.4.b.** Are you satisfied with the quality and timeliness of consultations carried out by the ESAs?

It would be helpful if the ESAs made direct contact with stakeholders if they considered that their input is of particular value and interest. Consumer groups have limited resources and it can be very helpful if they can provide input in the consultation process in a less formal and resource-intensive way or if they are made aware in what specific way their input is required rather than having to focus on the whole consultation.

Access to consultations is not a problem (available on the ESAs websites + via mailing list) and we do not question their quality and timeliness. However, we responded to few consultations in so far as the impact of these consultations is limited (in comparison with the consultations launched by the European Commission).

**1.2.4.c.** Are you satisfied with the appointment procedures for the stakeholder groups?

**1.2.4.d.** In your experience, does the composition of stakeholder groups ensure a sufficiently balanced representation of stakeholders in the relevant sectors? If not, which areas appear to be insufficiently/overly represented?

We have a number of serious concerns about the functioning of the stakeholder groups.

Unfortunately, the representation on the stakeholder groups is far from balanced. We think this contravenes article 37.2 and recital 48 of the regulations.

Retail user representatives number a small minority in each of the 30 member strong stakeholder groups. In contrast, industry representatives and their providers (auditors, lawyers, etc.) can represent at least half of the representation. One reason is that ESAs categorised industry service providers (such as accountants, lawyers, auditors etc.) as 'users'. thus violating the Regulations (the recitals clearly specify "retail" "users" exclusively – see above).

In September 2011, BEUC and EuroFinUse submitted a complaint to the EU Ombudsman in relation to the composition of EBA and EIOPA Stakeholder Groups established by Art 37 of the respective Regulations. These organisations complained about the selection procedure and unbalanced representation of stakeholders within the Groups. We are still awaiting the EU Ombudsman's final decision with regards to the complaints.

To be fair, we have observed some improvements with regard to the selection criteria, in particular on the definition of different stakeholder categories. However, the ESAs need to adopt much stricter definitions of user representative. For example, representatives that earn a significant proportion of their incomes/revenues from the industry cannot be said to be independently representing the interests of retail users. The same should apply to academics who earn income and fees from the financial services industry. Moreover, care must be taken when categorising representatives from 'trade bodies'.

However, ensuring an appropriate balance of representation on its own will not be enough. As mentioned above, industry representatives have a major resource advantage over user representatives. This undermines the ability of user representatives to play a full part in public debates and represent the public interest properly. This in turn risks a return to the 'group think' that played a major part in the failure of regulatory policy pre-financial crisis.

If ESAs are to ensure that the public interest is represented, adequate compensation and support must be made available to retail user representatives.

Furthermore, the input of the user representatives on the stakeholder groups is severely restricted by the lack of research resources available to them. The ESAs should consider making a research budget available to the stakeholder groups, especially on issues related to consumer and investor protection. Additionally, user representatives would benefit from technical support when it comes to the discussion of the more technical files. The ESAs should also look at ways of increasing the amount of time the stakeholder groups can commit to consumer protection issues for example by allowing the groups to split into sub-groups during part of the meeting to discuss different issues.

**1.2.4.e.** Is the work undertaken by the stakeholder groups sufficiently transparent? Do you see areas where the approach towards transparency needs to be revisited?

The rules of procedure do not allow members to share documents with other parties. Only the minutes of the meetings are available online. This is quite an important issue for consumer representatives where a wider sharing of information could allow them to tap into additional resources from fellow consumer organisations.

**1.2.4.f.** In your experience, are the ESAs, and in particular the ESAs stakeholder groups, sufficiently accessible for stakeholders not directly represented in these stakeholder groups?

ESAs contact with user representatives appears to be quite limited. We recommend that the ESAs undertake to meet formally on a regular basis with European organisations representing consumers and retail investors.

### **1.2.5. Joint bodies of the ESAs**

**1.2.5.a.** How do you assess the functioning of the Board of Appeal (BoA)? If you have identified shortcomings, please specify how these could be addressed.

**1.2.5.b.** What is your assessment of having one joined BoA for all ESAs as compared to a dedicated BoA for each ESA respectively?

**1.2.5.c.** How do you assess the functioning of the Joint Committee (JC)? If you have identified shortcomings, please specify how these could be addressed.

**1.2.5.d.** Does the JC ensure cross-sectoral cooperation and consistent approaches between the three ESAs? If you have identified shortcomings, please specify how these could be addressed.

We have no comments on the above questions.



## **2. ESRB**

### **2.1. ESRB's mandate and experience**

#### **2.1.1. Risk identification and prioritisation**

**2.1.1.a.** What are your views on the ESRB mandate? If you think it should be amended please specify how.

**2.1.1.b.** What are your views on the definition of systemic risk, as provided by the ESRB Regulation? If you think it should be amended, please specify how.

**2.1.1.d.** What aspects of EU financial stability should be addressed by the ESRB as a priority?

**2.1.1.e.** What is your assessment of the ESRB's coordination with other economic or financial policy areas or economic governance procedures, for example on macroeconomic imbalances?

**2.1.1.f.** Please outline and comment on the areas in which the ESRB has been most effective.

**2.1.1.g.** Should the ESRB specific mandate be adapted in light of the Single Supervisory Mechanism? If yes, how?

We have no comments on the above questions.

#### **2.1.2. Timeliness and appropriateness of warnings and recommendations**

**2.1.2.a.** What are your views on the powers conferred to the ESRB by the ESRB Regulation (i.e. the power to issue warnings and recommendations)? Are they sufficient? Please explain. What are your views on the use the ESRB has made of these powers in practice?

**2.1.2.b.** What is your assessment of the ESRB's public recommendations in terms of content and timeliness? What is their impact on the direct addressees, and indirectly on the relevant market/market participants? If you identify any potential improvements, please specify how these could be delivered.

**2.1.2.c.** Did the recommendations adequately address the relevant policy makers in alerting them to, and advising them on, the necessary measures for risk mitigation?

**2.1.2.d.** Were the recommendations specific enough and did they address the main specific risks that could be identified in the period under review? If not, where would you identify the shortcomings and how could these be improved?

We have no comments on the above questions.

### **2.1.3. Implementation of warnings and recommendations**

**2.1.3.a.** How do you assess the non-binding character of warnings and recommendations? Could such tools be strengthened? If yes, please specify how.

**2.1.3.b.** What is your assessment of the 'act or explain' mechanism chosen by the Regulation? If you identify any room for improvement please specify how this could be addressed.

**2.1.3.c.** What impact did public recommendations have on the market or public in general? Please outline your experience.

We have no comments on the above questions.

## **2.2. Institutional framework and governance of ESRB**

### **2.2.1. General governance issues**

#### **2.2.1.1. Key principles for good governance**

**2.2.1.1.a.** Do the regulations provide ESRB with the right structures to follow the good governance model in terms of openness, participation, accountability, effectiveness and coherence and to promote a common supervisory culture? Please explain our answer.

**2.2.1.1.b.** Has ESRB contributed to establishing a common macro-prudential policy framework and convergence of macro-prudential supervisory practices within EU? Please explain your answer.

**2.2.1.1.c.** Has the ESRB acted as an impartial body in the interests of EU as a whole? Please explain your answer.

#### **2.2.1.2. Accountability and transparency**

**2.2.1.2.a.** Are the ESRB's accountability and reporting obligations, (including the frequency), to the European Parliament and the Council sufficient and transparent enough? If not, please explain how they should be improved.

**2.2.1.2.b.** What is your assessment of the nature of these public hearings?

We have no comments on the above questions.

### **2.2.2. Decision-making bodies and voting arrangements**

#### **2.2.2.1. Voting arrangements for the designation or election of the Chair of the ESRB**

**2.2.2.1.a.** What are your views on the fact that the President of the ECB is by rule the Chair of the ESRB? If you think this rule should be amended, please specify how the ESRB Chair should be appointed. For example, should it be defined in the Regulation or should she/he be appointed by an EU institution or the ESRB itself? If by an EU institution, by which one and how?

**2.2.2.1.b.** Do the governance arrangements ensure that the Chair carries out his tasks with sufficient independence? If not, please specify where there is room for improvement and how this could be addressed.

We have no comments on the above questions.

### **2.2.2.2. Composition, mandate and functioning of the General Board**

**2.2.2.2.a.** What is your assessment of the composition, size and mandate of the General Board? If you identify any shortcomings please specify how these could be addressed.

**2.2.2.2.b.** What is your assessment of the relative representation of central banks on the General Board?

**2.2.2.2.c.** What is your assessment of the participation of the European Supervisory Authorities (EBA, EIOPA, ESMA)?

**2.2.2.2.d.** What is your assessment of the presence of non-voting members at General Board meetings?

We have no comments on the above questions.

### **2.2.2.3. Internal organisation**

**2.2.2.3.a.** What is your assessment of the supporting activities of the ECB to the ESRB, according to the relevant regulation (Council Regulation 1096/2010)? What are the key advantages and disadvantages of this set-up? If you identify any room for improvement, please specify how this could be addressed.

We have no comments on the above questions.

## **2.3. Access to data**

**2.3.a.** In your view, has the ESRB had adequate access to relevant data and financial information for the fulfillment of its mandate?

**2.3.b.** For the analysis of systemic risk, what is the balance needed between, on the one hand, data in summary or aggregate form and, on the other hand, firm-specific data?

**2.3.c.** How do you assess the data access procedures foreseen in the ESRB Regulation? If you identify any room for improvement, please specify

how this could be addressed.

We have no comments on the above questions.

## **2.4. ESRB external relations and communication**

### **2.4.1. Positioning of ESRB as an authoritative policy institution focused on monitoring and preventing systemic risks**

**2.4.1.a.** What is your assessment of ESRB communications?

**2.4.1.b.** What is your assessment of the ESRB's reputation as the body responsible for identifying and helping to mitigate systemic risk?

We have no comments on the above questions.

### **2.4.2. Interaction with other international bodies (e.g. G20/FSB)**

**2.4.2.a.** What is your assessment of the ESRB interactions with the International Monetary Fund (IMF); the Financial Stability Board (FSB); the G20 Group; macro-prudential authorities in any other relevant non-EU countries? If you identify any room for improvement, please specify how this could be addressed.

We have no comments on the above questions.

## **3. Cooperation and interaction between the ESAs (micro level) and ESRB (macro level)**

### **3.1. Assessment of market developments**

**3.1.a.** What is your assessment of the past stress test exercises that were initiated and coordinated by EIOPA and EBA? If you have identified any shortcomings, please specify how these could be addressed.

**3.1.b.** Did the stress tests and EBA's recapitalization exercise contribute to increase confidence in the stability of the financial system and increase the resilience of financial institutions? Please explain.

The EBA and ESRB were set up to avoid repeating the bank crises of 2008-2009, but we take the view that there is still room for improvement.

In particular, we have concerns that the EBA stress tests carried out in July 2011 were not effective. For example:

- Dexia was ranked number 9 European bank out of 92 banks by the EBA - about one month before collapsing with devastating effects on ordinary shareholders.
- The two biggest Cyprus banks (BoC and Laiki) also passed the test with the

EBA concluding that they required no additional capital – just about one and a half years before the EU was required to provide more than €11 billion in support and confiscate funds from bank depositors who bear no responsibility for this failure of bank supervision.

We can understand that the EBA was performing these stress tests in a very difficult, challenging environment. But the efficacy of the EBA and ESRB with regards to prudential regulation must be closely monitored and checked to ensure proper accountability.

### **3.2. Aspects of macro-micro interaction**

**3.2.a.** What is your assessment of the cooperation between ESRB and the ESAs? In which areas has cooperation been successful? If you identify room for improvement, please specify how this could be addressed.

**3.2.b.** What is your assessment of the ESAs' follow-up actions on the ESRB recommendations? Please explain.

**3.2.c.** Has ESRB contributed to the work of the ESAs by bringing a macro-prudential perspective into micro-prudential activities? If so, please comment on key successes and/or shortcomings.

We have no comments on the above questions.

### **4. Structure of the ESFS**

**4.a.** What is your assessment of the structure of the ESFS?

**4.b.** Does the structure of the ESFS facilitate the identification, monitoring and mitigation of systemic risk in the EU financial sector? Please explain.

**4.c.** Do you consider that the ESFS can be further simplified in order to tangibly enhance coherence between the ESAs and the ESRB? Please explain and add concrete suggestions, where possible.

**4.d.** Do you consider that the structure of the ESFS, in particular the roles of EBA and ESRB, will need to be revisited in light of the establishment of the Single Supervisory Mechanism (SSM) and the new role of the ECB within the ESFS? Please explain and add concrete suggestions, where possible. How should synergies in terms of supervision within ESFS including ECB be exploited? Please explain.

Our main comments on the structure of the ESFS relate to the efficacy of consumer and investor protection and making markets work.

We have no particular comments with regards to financial stability and prudential regulation. However, we would say that the ESRB and ESAs have so far not been able to demonstrate that they understand how the interaction between various actors in the financial services supply chain can impact on efforts to:

- i. maintain financial stability;

- ii. ensure financial institutions are soundly managed;
- iii. consumers are protected; and
- iv. markets are efficient.

Behaviours and activities in the wholesale and institutional markets are transmitted along the supply chain to impact on the behaviours of firms which in turn impacts on behaviours at the end of the supply in retail financial markets - and vice versa. Consumer behaviour in retail markets can also be transmitted back up the supply chain to impact on firm behaviour and wholesale and institutional market behaviour.

Similarly, the same effects can be observed with regards to regulatory decisions. Poor financial stability and prudential regulation can have adverse consequences for consumer protection, competition, market efficiency, and access to financial services.

This can be partly explained by the fact that policymakers and regulators do not employ a proper analytical framework to evaluate how well markets are actually working for financial users and undertake transparent impact assessments and cost-benefit analyses to understand the impact of regulatory initiatives.

**4.e.** From your experience, do you think that the ESAs and ESRB attract a sufficient number of diverse and excellent staff? If not, why not? If you identify room for improvement, please specify how this could be addressed.

We have no comments on the above questions.

## **5. Miscellanea**

**5.a.** Do you have any other comment on the effectiveness and efficiency of the ESAs and ESRB within ESFS and on ESFS in general? Please indicate whether the Commission may contact you for further details on the information submitted, if required.

To reiterate, the main comments we have relate to concerns about the overall structure, governance and accountability, regulatory culture, approach and philosophy, powers and duties of EU financial regulation. We argue for a fundamental reform of the regulatory system. 'Tinkering' with the system is unlikely to create the regulatory system we need to promote safe, resilient, fair, competitive, efficient, inclusive, transparent and accountable financial markets in the EU.

We would be very happy for the Commission to contact us for further details.

This marks the end of FSUG submission.