European Economic and Social Committee

ECO/298
Role of civil society in financial regulation

Brussels, 22 February 2012

OPINION

of the
European Economic and Social Committee
on
How to involve civil society in financial regulation
(own-initiative opinion)

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On 20 January 2011, the European Economic and Social Committee, acting under Rule 29(2) of its Rules of Procedure, decided to draw up an own-initiative opinion on

How to involve civil society in financial regulation.

The Section for Economic and Monetary Union and Economic and Social Cohesion, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 2 February 2012.

At its 478th plenary session, held on 22 and 23 February 2012 (meeting of 22 February 2012), the European Economic and Social Committee adopted the following opinion by 66 votes to 53 with 41 abstentions.

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1. Conclusions and recommendations

1.1 One of the reasons for the financial crisis was inadequate and ineffective regulation and supervision of the financial markets. One of the difficulties in financial regulation is how to ensure that differing and contradictory positions are given a balanced hearing. There is no effective counterweight to the legitimate representation of the financial sector's interests. Political debate primarily plays out between the legislator on one side and the financial sector concerned on the other.

1.2 With financial regulation in particular the European Economic and Social Committee (EESC) is well-placed to rectify the lack of civil society involvement, because the EESC includes representatives both of financial industry associations and of consumer organisations and trade unions. The EESC cannot, and has no desire to, be a substitute for the direct involvement of civil society organisations. Civil dialogue is a public, democratic opinion-forming process in which all relevant stakeholders should be effectively involved.

1.3 In the EESC's view, it goes without saying that the financial sector itself has a legitimate place in the opinion-forming process. It is the financial companies that are affected by regulation and have to meet the requirements and implement the statutory obligations. The EESC also recognises that the majority of sectors and companies within the financial industry operate honestly and with integrity and had no part in causing the financial crisis.

1.4 Given the complexity of the detailed legislation, it is crucially important for civil society organisations not just to set basic objectives and call for a general tightening-up of the rules, but to put forward knowledgeable and practical proposals and arguments. This will require considerable efforts to ensure that the organisations can enter discussions on an equal footing with the legislator and with other organisations.

1.5 The European Commission, European Parliament, Council and Member States must take initiatives themselves to achieve wider involvement of civil society in the regulation of financial markets.

1.6 The European Central Bank, the European Systemic Risk Board and the newly established European Supervisory Authorities should ensure that civil society organisations are adequately involved in their work. The procedures of the stakeholder groups that must by law be consulted by the supervisory authorities should allow for the specific characteristics of civil society organisations to be taken into account.

1.7 It may in certain cases be appropriate to provide civil society organisations with financial support from EU funds in order to rectify deficiencies in the representation of key interests. In such cases, it must be ensured that the financial contributions are fully transparent, that the independence of the organisations is guaranteed and that they are not given preferential treatment in their dealings with the Commission over organisations that have not received such support.

1.8 Alongside consumer organisations and trade unions there are a whole range of other groups that could make significant contributions to discussions on the financial markets, including charitable organisations, small and medium-sized enterprises, organisations of institutional investors, industrial and service undertakings with major financial operations and associations of such undertakings, financial intermediaries and even ratings agencies. Given the competitive environment in financial markets, representatives of sectors other than those directly affected by regulation could also make valuable contributions.

1.9 Not all subjects are equally amenable to contributions from civil society organisations. While consumer protection issues, the use of tax revenue to rescue financial institutions and taxation of the financial sector lend themselves particularly well to such contributions, detailed technical issues such as calculating solvency or financial reporting are of less interest.

1.10 It is not enough to make sweeping and indiscriminate calls for tighter regulation: that is of no help to the legislator. Not only must proposals be as specific as possible, but the advantages and disadvantages of stricter rules must also be weighed up.

1.11 The EESC encourages European and national civil society organisations to take a closer interest now in financial regulation. Many such organisations would do well to set themselves the discrete (and in some cases new) objective of promoting financial market stability and extend their fields of interest and activity accordingly.

1.12 In the EESC's view, it would be worthwhile for these organisations to take advantage of their role in financial regulation to broadcast a positive message about the EU's successful work in this field to their members and the general public.

1.13 Despite its evident specific mistakes, the European financial industry has also been one of the victims of the crisis, and it therefore needs to contribute to effective financial regulation. The individual sub-sectors of the financial industry should not hesitate to comment on the regulation of other sub-sectors in the interests of financial market stability.

1.14 The financial industry itself should also initiate dialogue with civil society organisations. Given the level public attention the financial sector has attracted in the wake of the financial crisis, it would be beneficial for it to open a dialogue with civil society organisations, exchange arguments and hear their suggestions.

1.15 The media obviously play a prominent role in the opinion-forming process in Europe, and it would be valuable for the position of civil society organisations to also be represented in the media to a greater extent.

1.16 The EESC will continue to pay close attention to proposals for financial regulation, and to hold broad-based discussions and issue substantive opinions on them, placing particular emphasis on incorporating the position of civil society representatives. The sections and study groups will hold hearings as part of the consultation process in order to get civil society organisations more closely and directly involved in its opinion-forming process.

1.17 When planning its work programme, plenary sessions, and section and study group meetings, the EESC will ensure that there is sufficient opportunity for in-depth discussion of financial regulation. It will manage its financial and human resources in such a way that members have access to qualified expert advice on financial regulation issues.

2. Objective of the opinion and background

2.1 The crisis in the financial markets[1] since 2008 has had a serious negative impact on ordinary people worldwide, particularly in the European Union, and the EESC has already examined the issue closely on a number of occasions. One reason for the market collapse, the speculation that preceded it and the trade in high-risk financial products was inadequate and ineffective regulation and supervision of financial markets.

2.2 One of the difficulties in adopting rules in this field has been, and still is, how to ensure that differing and contradictory positions are given a balanced hearing within a pluralistic and democratic opinion-forming process. There is currently no effective counterweight from civil

[1] The crisis caused by excessive public deficits is not discussed in this opinion, though the question could also be raised here of why civil society did not press more strongly, and at an earlier stage, for a reduction in borrowing.

society organisations to the legitimate representation of the financial sector's interests, and this asymmetry should be rectified in the new financial legislation.

2.3 As the European institution representing civil society, the EESC considers it a duty, alongside issuing its own opinions, to facilitate broad and comprehensive involvement of all relevant parties in the European legislative process. The EESC is therefore concerned when it regularly proves impossible to hold balanced debates in certain political domains.

2.4 The aim of this own-initiative opinion, therefore, is to analyse civil society's role in the regulation of financial markets and to make recommendations to enhance that role.

3. **Civil society involvement: shortcomings and obstacles**

3.1 To date financial regulation has been primarily monitored by those concerned within the financial sector, as was amply confirmed at the hearing held by the EESC on 28 November 2011. This cannot be attributed to a lack of openness on the part of the EU institutions; there has so far been little interest in the issue among organisations outside the financial industry, as evidenced for example by the low levels of participation in European Commission consultations, European Parliament hearings and public discussions.

3.2 Even now, political debate on directives or regulations relating to the financial sector primarily plays out between the legislator on one side and the financial sector concerned on the other. In other spheres, by contrast, the policy debate - in particular the debate between civil society organisations in Brussels - is also at the heart of pluralistic debate: for example, between employers and trade unions regarding social policy, between industry and environmental organisations on environmental policy, or between business and consumer organisations on consumer policy.

3.3 In the EESC's view, there are a number of reasons for these deficiencies in financial regulation.

3.3.1 The aim of financial regulation is to guarantee the security and stability of the financial markets, thus a rather abstract and intangible public good, which for a long time also appeared not to be under any threat. It was not easy to discern any substantial citizens' interests to protect, and so nobody outside the financial markets had much incentive, reason or motivation to consider these issues.

3.3.2 Financial markets are highly complex and difficult for non-experts to understand. The diversity of players, complexity of products and many-layered interactions make it difficult for organisations outside the sector to participate knowledgeably in the debates.

3.3.3 It is often difficult to determine the direct – and more especially the indirect – impact of regulation on the interests of the members of civil society organisations, particularly if it involves complex implementing provisions and technical standards rather than directives and regulations.

3.3.4 The process of regulating the financial markets is relatively difficult to understand. The Lamfalussy process used previously, and the current system of delegated acts, implementing acts and binding technical standards with many procedural steps and a large number of institutions and authorities involved to varying degrees, make it hard to issue focused opinions at the right moment. The substance of the regulation is also increasingly prescribed by global institutions such as the G20, the Basel Committee and the IASB (International Accounting Standards Board), whose activities are not very transparent.

3.3.5 The large number of regulatory proposals, the speed of the legislative processes and the large number of stakeholders have stretched to the limit the capacity of decision-makers in the institutions to hold discussions, draft position papers and participate in conferences.

3.3.6 The high degree of global integration of financial markets, the global mobility of capital and sensitivity of trade have in the past always been hard to counter as arguments against intervening in European markets. Competition for volatile capital to promote growth and jobs made a "light touch" regulatory approach seem sensible, and for a long time this appeared to be adequate.

3.4 These difficulties are also the reason for the establishment of Finance Watch, an initiative by MEPs that brings together various European and national organisations to keep a critical eye on legislation relating to the financial sector.

3.5 There appears to be a similar issue in the Member States, where there is no evidence that civil society has significantly influenced financial regulation.

3.6 Problems seem to arise with taking account of the interests of small and medium-sized businesses in the financial sector, and with getting civil society involved. Many smaller financial institutions complain that the complexity of the rules and the high administrative costs involved make them difficult to implement.

4. General comments

4.1 Participatory democracy is a key component of the European social model and of European governance. Representative and participatory democracy are anchored in the Lisbon treaty, but all this requires is that the institutions give "citizens and representative associations" the opportunity to make their views known (Article 11 of the EU Treaty). It is therefore down to European bodies themselves to take the initiative where proposals prompt a one-sided reaction, or no reaction at all, from civil society.

4.2 It goes without saying that it is the democratically mandated institutions that adopt the decisions, and that civil dialogue has a purely preparatory and monitoring role.

4.3 The EESC is organised civil society's pre-eminent forum for representation, debate and expression of opinions, and serves as a vital bridge between Europe and its citizens; the EESC plays this role especially in relation to legislation.

4.4 With financial regulation in particular the EESC is well-placed to play a prominent role in rectifying the lack of civil society involvement, because it includes representatives both of financial industry associations and of consumer organisations and trade unions. The EESC's obligation to issue opinions on Commission proposals means that members systematically engage with the legal texts, and need no additional encouragement or motivation.

4.5 Since the start of the financial crisis the EESC has repeatedly expressed the views of civil society organisations, issuing around 30 opinions on the financial crisis in general and legislative initiatives in particular since mid-2008.

4.6 The lack of other civil society involvement makes it all the more important for the European institutions to pay attention to the EESC's opinions in this area.

4.7 The EESC cannot, and has no desire to, be an alternative to direct involvement of civil society organisations. Civil dialogue is a public, democratic opinion-forming process in which as many stakeholders as possible should be involved in various ways.

4.8 In the EESC's view, it is quite clear that the financial sector's involvement in the opinion-forming process is just as legitimate as other organisations'. It is the financial companies themselves that are affected by regulation and have to meet the requirements and implement the statutory obligations. Another reason why financial industry associations need to be involved is that the sector itself obviously has the greatest interest in financial stability. Its expertise is also required in order to make reliable impact assessments.

4.9 The EESC also recognises that the majority of sectors and companies within the financial industry operate honestly and with integrity and had no part in causing the financial crisis. In the EESC's opinion, the blanket condemnation of the financial sector that is sometimes heard is not justified. Most businesses in the sector have not profited from the excesses of the financial markets, but have themselves been negatively affected by the crisis and its impact, and the number of customers of financial institutions who have suffered losses has been limited, thanks partly to government assistance.

4.10 Nonetheless, the main victims of the financial and economic crisis have been individual citizens, as taxpayers, employees and consumers. They need, through their civil society organisations, to get more closely involved in drafting new rules for the financial sector, in order to ensure that a crisis of this magnitude does not occur again.

4.11 Given the complexity of the detailed legislation, it is crucially important for civil society organisations not just to set basic objectives and call for a general tightening-up of the rules, but to put forward knowledgeable and practical proposals and arguments. This will require a considerable effort to ensure that organisations can enter discussions on an equal footing with the legislator and other civil society organisations.

5. Detailed recommendations

5.1 The European Commission, European Parliament, Council and Member States must take initiatives themselves to achieve wider involvement of civil society in the regulation of financial markets.

5.1.1 It is absolutely crucial for the direct and immediate impact on civil society of proposed regulation to be set out simply, openly and precisely in the proposals, to enable organisations to better understand how the public will be affected.

5.1.2 If ultimately consultations on financial market matters produce little response from civil society, as has often been the case in the past, individual organisations should be specifically invited to take part. If necessary, the consultation time frames should be extended, as already provided for in the Commission's "smart regulation" initiative. Consultations should not just focus on technical matters, but specifically ask for the views of civil society. The particular perspective of civil society organisations should be taken into account.

5.1.3 Relevant organisations should be involved right from the start in public hearings of the European Commission or European Parliament. Despite their busy schedules, the institutions should be open to discussion with civil society organisations and take part in their events.

5.1.4 Groups of experts in the European Commission and the European Parliament should include representatives not only of the financial industry but also of other groups, though it must be ensured that the people nominated have the necessary expertise in the subject area in question: nothing will be gained if there is an imbalance in specialist knowledge.

5.1.5 It may in certain cases be appropriate to provide civil society organisations with EU financial support in order to correct deficits in the representation of key interests. However, this runs counter to the principle of autonomy and self-financing in defending civil society's interests, and may harm the independence of these organisations and lead to conflicts of loyalty on both sides. It must at any rate be ensured that the financial contributions are fully transparent, that the independence of the organisations is guaranteed and that they do not get preferential treatment in their dealings with the Commission over organisations that have not received such support.

5.2 Other EU bodies involved in financial regulation, such as the European Central Bank, the European Systemic Risk Board and the three European Supervisory Authorities (for banking, securities and insurance) should take account of the positions of civil society organisations in their work.

5.3 The procedures of the stakeholder groups that must by law be consulted by the supervisory authorities should permit the views of civil society organisations to be taken into account, allow for feedback to the relevant organisations, and thus become an additional route for involving civil society. This is not always the case at the moment, not least due to confidentiality requirements for documents and consultations that are excessive from the perspective of transparency.

5.4 Civil society involvement in financial regulation cannot be increased simply by making abstract political demands. We need a more specific concept of who should comment on which financial issues, and when they should do so.

5.4.1 Alongside consumer organisations and trade unions there are a whole range of other groups that could make significant contributions to discussions on the financial markets, including charitable organisations, small and medium-sized enterprises, organisations of institutional investors, industrial and service undertakings with major financial operations and associations of such undertakings, financial intermediaries and even ratings agencies. Representatives of financial sectors that are not directly affected by regulation could also make valuable contributions.

5.4.2 Not all subjects are equally amenable to contributions from civil society organisations.

5.4.2.1 While consumer protection issues, use of tax revenues to rescue financial institutions and taxation of the financial sector lend themselves particularly well to such contributions, detailed technical issues such as calculation of solvency or financial reporting are of less interest.

5.4.2.2 Organisations should not, however, focus solely on regulations at the point when they are adopted, but look at the whole gamut of regulation, including implementing provisions and technical standards, even if this may seem laborious.

5.4.2.3 The EESC does of course acknowledge that long-term stability and sustainability in financial markets result from the interplay between a large number of specific provisions that will each be discussed separately. Even if its organisations cannot look at all the documents presented, civil society must at least examine those topics that are key to the success of regulation as a whole, which means not only consumer law, but also for example regulatory oversight, capital requirements or corporate governance.

5.4.2.4 The issue is also that supposedly technical problems often conceal highly political issues that directly affect the general public. For example, the interest rate used for calculating reserves for pension funds has a significant impact on the ability of insurers to give long-term guarantees of pension levels.

5.4.2.5 It is not enough to make sweeping and indiscriminate calls for tighter regulation: that is of no help to the legislator. Not only must proposals be as specific as possible, but the advantages and disadvantages of stricter rules must also be weighed up, taking account of factors such as the burden on businesses (particularly small and medium-sized financial institutions), access to credit for individuals and businesses, and the functioning of the market.

5.4.3 Civil society should if possible make its voice heard at all stages of the decision-making process. In many cases, fundamental decisions are taken at an early stage, for example following initial consultation by the Commission or when the supervisory authorities are drawing up blueprints. Civil society organisations therefore need to be familiar with, and follow, the complex procedures referred to above, which are different from standard procedures.

5.5 The European Economic and Social Committee encourages European and national civil society organisations to take a closer interest now in financial regulation.

5.5.1 Many such organisations would do well, in the EESC's opinion, to set themselves the discrete (and in some cases new) objective of promoting financial market stability and to extend their fields of interest and activity accordingly.

5.5.2 Given the complexity of the financial markets and rules governing them, as set out above, civil society organisations need to develop and expand human resources as needed with the appropriate specialist skills. It may also prove necessary to create new bodies, strengthen cooperation with national organisations and bring in external experts.

5.5.3 In this connection, the EESC welcomes the establishment of Finance Watch, a new European-level body that aims to promote financial market stability. This alone will not, however, be enough to allow broad civil society involvement.

5.5.4 Civil society organisations should also take part in public debates at European level and in the Member States, thus making a policy contribution to financial regulation.

5.5.5 In the EESC's view, it would be worthwhile for these organisations to take advantage of their role in financial regulation to broadcast a positive message about the EU's successful work in this field to their members and the general public.

5.5.6 Cooperation between national and European civil society organisations is particularly important in this field, firstly because the activities of European and national regulatory levels are especially complementary when it comes to financial regulation, and secondly because national organisations often have greater resources than the European umbrella organisations – resources that should be used, particularly in this domain, for efforts at European level.

5.5.7 Given the ease with which capital can be moved around the world, financial regulation needs to be brought up to a comparable level worldwide. Organisations that have an international focus or international connections could make a particular contribution in this regard. They can call for effective financial regulation to a comparable level worldwide, so as to curb competition between business locations based on minimal standards. The interests of global financial market stability must be defended with equal vigour in all financial centres worldwide.

5.6 Despite its evident specific mistakes, the European financial market has also been one of the victims of the crisis, and it therefore needs to contribute to effective financial regulation.

5.6.1 The individual sub-sectors of the financial industry should not hesitate to comment on the regulation of other sectors in the interests of financial market stability.

5.6.2 In the EESC's view, it is self-evident that the interests of the financial industry must be represented to decision-makers transparently and with integrity and respect. Associations representing industry regularly meet these expectations; the occasional activities of individual businesses and their business representatives did not always do so in the past.

5.6.3 The financial industry itself also needs to initiate dialogue with civil society organisations. Given the level of public attention the financial sector has attracted in the wake of the financial crisis, it would be beneficial for the financial sector to open a dialogue with civil society organisations, exchange arguments and hear their suggestions. This would be a significant step towards forming closer ties with society as a whole. Should the financial sector wish to use self-regulation to impose a particular conduct, it would be appropriate for civil society also to be involved in developing those rules.

5.6.4 In the interests of fair and transparent civil dialogue, the EESC welcomes the establishment of a joint register of lobbyists by the European Parliament and the European Commission and appreciates the findings of the European Parliament working group chaired by Mr Buzek. However, it would stress that tightening up the rules must not prejudice or hinder the participation of civil society organisations. This applies in particular to practical issues such as easy access to EU departments and attending public meetings.

5.7 Academia, social foundations and think tanks are urged to bring their judgment, expertise and experience to bear in discussions on the financial markets. Although such organisations do not generally focus on involvement in specific legislative work, they should take the opportunity to deploy their resources in the interests of avoiding future crises.

5.8 The media obviously play a prominent role in the European opinion-forming process, and it would be valuable for the position of civil society organisations to also be represented in the media to a greater extent. To this end, it may be necessary to persuade the relevant organisations to adopt positions on a specific issue, as at the moment few representatives take part in the public debate on their own initiative.

5.9 The European Economic and Social Committee itself intends to increase its involvement in discussions on plans for financial regulation.

5.9.1 The EESC will continue to pay close attention to proposals for financial regulation, hold broad-based discussions on them and issue substantive opinions, placing particular emphasis on incorporating the position of civil society representatives.

5.9.2 It will ensure that representatives of all three of its Groups are equally involved in the debate and take part in all stages of the process.

5.9.3 The sections and study groups will hold hearings during discussions in order to get civil society organisations more closely and directly involved in the Committee's opinion-forming process.

5.9.4 The EESC will ensure, when planning its work programme, plenary sessions, section meetings and study group meetings, that there is sufficient opportunity for in-depth discussion of financial regulation.

5.9.5 The EESC will also work to ensure that its members from the relevant civil society organisations look closely at issues surrounding financial regulation and influence their organisations accordingly.

Brussels, 22 February 2012

The President
of the
European Economic and Social Committee

Staffan Nilsson