



European Economic and Social Committee

ECO/379
Capital Markets Union

Brussels, 1 July 2015

OPINION

of the
European Economic and Social Committee
on the
Green Paper on Building a Capital Markets Union
COM(2015) 63 final

Rapporteur: **Mr Mendoza Castro**

Co-rapporteur: **Ms Angelova**

On 9 March 2015 the European Commission decided to consult the European Economic and Social Committee, under Article 304 of the Treaty on the Functioning of the European Union, on the

Green Paper on Building a Capital Markets Union
COM(2015) 63 final.

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 18 June 2015.

At its 509th plenary session, held on 1 and 2 July 2015 (meeting of 1 July 2015), the European Economic and Social Committee adopted the following opinion by 100 votes to 2 with 3 abstentions.

*

* *

1. Conclusions and recommendations

- 1.1 The Committee supports the Green Paper on a Capital Markets Union, awaits the Commission's proposals on what changes might be needed as to achieve the goals stated in the document and expresses its belief that the proposed measures will be based on a balanced consideration of the viewpoints expressed by all the stakeholders.
- 1.2 The aim of the Commission's initiative should be to create the conditions for an efficient, modern financial services sector with appropriate regulations, which grants access to capital providers by companies seeking investment, especially SMEs and high growth companies.
- 1.3 The EESC sees the capital markets as pools of liquidity, where companies can raise funds and trade in financial instruments, and strongly supports the ultimate goal of the CMU – to overcome the current fragmentation of the markets thus enabling the listing of all types of companies.
- 1.4 Since a Capital Markets Union (CMU) is to a significant extent a reality for large companies, the EESC stresses the need for measures that will also allow SMEs to benefit from it.
- 1.5 The CMU should improve the financing of the economy in the long term by tapping the potential for promoting the best practices of corporate governance and corporate social responsibility, focusing not only on economic but also environmental and social objectives.
- 1.6 SMEs' specific needs should be explicitly taken into account in any future decisions related to CMU. The EESC strongly recommends decisive and swift action to be taken in the following directions:

- Developing a secondary market;
- Devising a unified simplified standard for qualitative and quantitative requirements for listing SMEs on regulated markets for financial instruments;
- Introducing credit ratings according to a standardised transparent methodology;
- Accepting simplified standardised criteria (model) for registration on regulated markets, including a detailed mid-term business plan for investments and business development in addition to financial information;
- Creating more "tailor-made" investment products as these should more closely match companies' needs;
- Updating and amalgamating the definitions of micro, small and medium-sized enterprises in the different items of EU legislation so as to better reflect the variety of SMEs and differences between the Member States;
- Providing a definition of an emerging growth and high growth company and devoting special attention to the needs of such companies on the capital market;
- Creating a unified European stock-exchange segmentation model, which differentiates SMEs based on their type as issuers, or creating specialised segments on the respective national regulated markets.
- Encouraging the strengthening of the administrative capacity of national consumer protection bodies and financial regulation agencies.
- Providing investors with conditions which are at least comparable, if not better, than those on international markets.

1.7 The EESC concurs with the acknowledgement in the Green Paper that a very low proportion of household savings finds its way into more productive investments than government bonds or bank deposits, especially at this time of financial repression for savers.

1.8 The EESC highlights the importance of traditional banking for the stability of the financial system. The EESC acknowledges the importance of completing the European Banking Union.

1.9 Sustainable high quality securitisation calls for promoting basic structures with short intermediation chains.

1.10 The EESC considers that the Green Paper provides a comprehensive review of the current state of play in the capital markets in Europe, as well as the measures needed to achieve a CMU.

2. **The content of the Green Paper**

2.1 Compared with other jurisdictions, capital market based financing in Europe is relatively underdeveloped. European equity, debt and other markets play a smaller role in financing growth and European businesses remain heavily reliant on banks, making our economies vulnerable to a tightening of bank lending.

- 2.2 There is also insufficient investor confidence, and European savings may not always be being put to the most productive use.
- 2.3 Building a CMU is a key initiative in the work programme of the Commission.
- 2.4 A CMU would ensure greater diversification in the funding of the economy and reduce the cost of raising capital, particularly for SMEs.
- 2.5 More integrated capital markets, especially for equity, would enhance the shock-absorption capacity of the European economy and allow for more investment without increasing levels of indebtedness.
- 2.6 A CMU should enhance the flow of capital - through efficient market infrastructure and intermediaries - from investors to European investment projects, improving allocation of risk and capital across the EU and, ultimately, making Europe more resilient to future shocks.
- 2.7 The key principles underpinning a CMU are: it should maximise the benefits of capital markets for the economy, jobs and growth; it should create a single market for capital for all 28 Member States; it should be built on firm foundations of financial stability; it should ensure an effective level of consumer and investor protection; and it should help to attract investment from all over the world and increase EU competitiveness.

3. **General comments**

- 3.1 The Committee fully supports the Commission's initiative. If all the Member States of Europe are to thrive in a vibrant, knowledge based economy, a Capital Markets Union is a necessary structural reform. The blockage to the EU-wide development of a range of innovative financial products has to be freed up, as this is holding back competitive financing for investment, particularly for small and medium sized companies, start-ups and for long term infrastructure products.
- 3.2 The aim of the Commission's initiative should be to create the conditions for an efficient, modern financial services sector with appropriate but not excessive regulations, allowing a much wider range of sources of investment finance and thereby addressing the worryingly low level of investment.
- 3.3 The EESC sees capital markets as pools of liquidity, where companies can raise funds and trade with financial instruments. Taking this as a starting point, the EESC believes that the CMU has already been achieved for large companies and, in reply to the Commission's questions in the Green Paper, will focus mostly on measures that will allow SMEs and high growth companies to also benefit from such a union.

- 3.4 The CMU should improve the financing of the economy in the long term by tapping the potential for promoting the best practices of corporate governance and corporate social responsibility, focusing not only on economic but also environmental and social objectives.
- 3.5 The Green Paper views SMEs as a targeted issuer. As such, SMEs' specific needs should be explicitly taken into account in any future decisions, as far as bonds or other fixed income financial instruments are concerned, as follows:
- proper choice of financing maturities;
 - structure of financing and pay-back;
 - cost of financing, including that related to entering the respective market;
 - content and structure of warranties and collateral for preparing the respective investment product.

In order to adequately address all these needs, it is vital to devise simplified and standardised products and procedures for the participation of SMEs on capital markets.

- 3.6 The EESC calls on the European Commission, European supervisory authorities and the member states to act with caution when producing and transposing future legislation aimed at achieving a functioning CMU to ensure that the European capital market provides investors and issuers with conditions which are at least comparable, if not better, than those on international markets.
- 3.7 An effective capital markets union is not possible without involving and attracting EU citizens as individual investors. The EESC concurs with the acknowledgement in the Green Paper that a very low proportion of household savings finds its way into more productive investments than government bonds or bank deposits, especially at this time of financial repression for savers.
- 3.8 The importance of traditional banking to the stability of the financial system should be underlined.
- 3.9 A sustainable high quality securitisation market – such as the Green Paper refers to – calls for promoting basic structures with short intermediation chains to link borrowers and savers directly.

4. **Answers to the questions posed in the Green Paper**

4.1 **Priorities for early action**

1) *Beyond the five priority areas identified for short term action, what other areas should be prioritised?*

A large part of the proposed measures are focused on primary markets. Bearing in mind the specific characteristics of SMEs, it is also necessary to explore possibilities for developing the secondary market.

In particular, it is vital to devise a unified simplified standard for qualitative and quantitative requirements for listing SMEs on regulated markets for financial instruments. A mechanism to make traded SMEs more attractive for investors should also be developed, bearing in mind SMEs' limited financial and administrative resources.

While retaining the main principles for taking investors' interests into account, it is recommended to start with some specific issues in the Prospectus Directive in order to relieve the administrative and bureaucratic requirements wherever possible, and to explore the possibilities of liberalising some disclosure requirements for SMEs:

- Shortening the deadlines for consideration of the prospectus for issuers who already have securities admitted to trading on a regulated market and have made a public offering of securities, and are respectively public companies or registered as issuers. Deadlines may accordingly be reduced to 7 days. A special procedure should be provided for listing SMEs in a simplified way, especially if they are to be traded on the unofficial market of the stock exchanges. The Directive should allow greater national discretion for national regulators to regulate listing of SMEs.
- Pursuant to Article 14, paragraph 2 of Directive 2003/71/EC, the notification for public offering and the initial and final term of the subscription shall be published in one daily newspaper. Requirements for publication of announcements/notifications and the prospectus itself on paper and in daily newspapers should be increasingly limited. The disclosure of information on the Internet, especially through the websites of the respective regulated market or of the company, should become the main means of communication between the issuer and investors. On the other hand, there may be a certain uniformity of requirements for information disclosure via websites - through unification or a special page for investors; the latter could thereby acquire information more quickly and easily on the essential aspects of the publicly offered securities.

2) *What further steps around the availability and standardisation of SME credit information could support a deeper market in SME and start-up finance and a wider investor base?*

Useful measures in this context would be:

- introduction of credit ratings according to a standardised transparent methodology;
- acceptance of simplified standardised criteria (model) for registration on regulated markets, including, besides financial information, a detailed mid-term business plan for investments and business development.

3) *What support can be given to European Long Term Investment Funds (ELTIFs) to encourage their take up?*

The most pressing measure is to review the regulatory requirements for pension funds and insurance companies in the different Member States with a view to liberalising their portfolios where necessary with respect to the possibility of investing in ELTIFs. Pension funds and insurance companies will be interested in this form of asset and also have the funds to capitalise ELTIFs. To enhance this process, it will be useful to develop a unified profitability evaluation model covering the whole investment chain.

4) *Is any action by the EU needed to support the development of private placement markets other than supporting market-led efforts to agree common standards?*

No. Action by the EU might be needed if these market-led efforts do not succeed.

4.2 **Measures to develop and integrate capital markets**

5) *What further measures could help to increase access to funding and channelling of funds to those who need them?*

In general, access to finance would improve if more "tailor-made" investment products were created as these should better match companies' needs (for example as regards maturity, collateral and structure of payments).

Also, regulatory bodies should allow the possibility of debt-instrument issuance, which as a kind of contract with bondholders should be as similar as possible to project financing and corporate lending from banks.

6) *Should measures be taken to promote greater liquidity in corporate bond markets, such as standardisation? If so, which measures are needed and can these be achieved by the market, or is regulatory action required?*

Yes, standardisation will improve liquidity in corporate bond markets. In this case, taking regulatory measures discussed and agreed with all stakeholders makes sense.

7) *Is any action by the EU needed to facilitate the development of standardised, transparent and accountable ESG (Environment, Social and Governance) investment, including green bonds, other than supporting the development of guidelines by the market?*

Yes, standardisation criteria should include specific principles regarding environmental, social and governance investment. The EESC supports the promotion of "Green Bonds" as well as "green" mortgages, loans for energy efficiency projects and renewable energy, among others. All of these should be included in the investor's options. The EESC finds it necessary to disseminate information and launch campaigns to promote ESG investments widely and publicise best practices in this regard, including in close cooperation with and through networks of business and investors associations.

8) *Is there value in developing a common EU level accounting standard for small and medium-sized companies listed on multilateral trading facilities (MTFs)? Should such a standard become a feature of SME Growth Markets? If so, under which conditions?*

The current European definition of SMEs includes firms of vastly different sizes and does not allow for differentiation on the basis of industry. The EESC supports a standard European definition of micro, small and medium-sized enterprises and calls for the various definitions given in different items of EU legislation to be updated, so as to better reflect the variety of SMEs and differences between the Member States, and amalgamated¹. It suggests providing a definition of an emerging growth and high growth company and devoting special attention to the needs of such companies on the capital market. Without this, MTFs will only include a limited number of countries, and growth markets will not be able to attract many cross-border investors. The content of such a standard should be in conformity with SMEs' limited financial and administrative capacity.

9) *Are there barriers to the development of appropriately regulated crowdfunding or peer to peer platforms including on a cross border basis? If so, how should they be addressed?*

Differences between national legislations are a major reason for the weak development of prospective forms of investment such as crowdfunding. It is therefore advisable for the Commission to promote legislative harmonisation.

¹

In general terms, the common definition of SMEs is set out in EU Recommendation 2003/361, which is rather out of date and reflects neither EU enlargement, nor the economic realities following the crisis. For the purposes of the Green Paper, the definition of SMEs is given in Directive 2014/65/EU of 15 May 2014 on markets in financial instruments. There is another definition of SMEs in Directive 2013/34/EU of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings.

4.3 Developing and diversifying the supply of funding

10) What policy measures could incentivise institutional investors to raise and invest larger amounts and in a broader range of assets, in particular long-term projects, SMEs and innovative and high growth start-ups?

Before anything else, changes in the regulations for institutional investors' portfolios are needed, because in many Member States such investments are not allowed for them at all.

11) What steps could be taken to reduce the costs to fund managers of setting up and marketing funds across the EU? What barriers are there to funds benefiting from economies of scale?

The costs are not excessively high even now, and depend above all on marketing channels. Those funds which are marketed through branches of banks or other financial institutions do not usually have significant costs and do not face barriers for benefitting from economies of scale. Funds which are marketed separately would have higher costs.

Fund-raising prospectuses should be simplified and unified, as well as all the registration documents for entering the respective regulated market.

A unified European stock-exchange segmentation model is needed, which differentiates SMEs based on their type as issuers. The same result can be achieved by creating specialised segments on the respective national regulated markets.

12) Should work on the tailored treatment of infrastructure investments target certain clearly identifiable sub-classes of assets? If so, which of these should the Commission prioritise in future reviews of the prudential rules such as CRDIV/CRR and Solvency II?

To finance infrastructure projects, the EESC suggests:

- establishing a more comprehensive public review process for infrastructure to ensure planning is more strategically coordinated;
- increasing the focus of government and Europe-wide funding to financially unviable but socially important projects (potentially through (partial) guarantees in order to make them viable);
- producing an easy-to-understand guide to infrastructure finance through banks and capital markets;
- amending the accounting and regulatory treatment of infrastructure projects to make them more attractive for investors;
- defining certain clearly identifiable sub-classes of infrastructure projects and tailoring the treatment of infrastructure investments to them. This involves different risk evaluation for each sub-class and will improve predictability, in such a way as to make investments more attractive for institutional investors;

- increasing the use of structures which enable retail investors to participate better in illiquid financing;
- as the current Solvency II capital charges fail to distinguish between long-term corporate debt and infrastructure debt, the case should be considered for modifying this;
- improving the transparency and democratic accountability of public private partnerships by requiring public access to the full contracts and regular public reporting on their value for money.

13) Would the introduction of a standardised product, or removing the existing obstacles to cross-border access, strengthen the single market in pension provision?

Yes. Taking into consideration the fact that pension provision and philosophy is very different across the Member States and the goal stated by the EC in the Green Paper to achieve a pan-European retirement scheme.

14) Would changes to the EuVECA and EuSEF Regulations make it easier for larger EU fund managers to run these types of funds? What other changes if any should be made to increase the number of these types of fund?

It is possible that such changes would make large fund managers more interested in running such funds. However, this could also lead to excessive concentration and conflicts of interests. Therefore, before taking such a measure it is advisable to carefully research whether this is the main obstacle preventing large fund managers from running such funds.

15) How can the EU further develop private equity and venture capital as an alternative source of finance for the economy? In particular, what measures could boost the scale of venture capital funds and enhance the exit opportunities for venture capital investors?

The scale of private equity and venture capital funds could be increased by an appropriate relaxation of restrictions on the portfolios of institutional investors such as pension funds, insurance companies and Undertakings for Collective Investment in Transferable Securities (UCITSs).

16) Are there impediments to increasing both bank and non-bank direct lending safely to companies that need finance?

In the aftermath of the financial crisis, bank lending has suffered increased constraints as a result of tighter capital-adequacy requirements and the need to decrease risk exposure. Non-bank direct lending is not allowed by the legislation in many Member States; in many cases, insurance companies, pension funds and other financial institutions cannot lend directly to nonfinancial companies.

17) How can cross border retail participation in UCITS be increased?

Cross-border investments require a well-developed investment culture, relevant knowledge and foreign-language proficiency. So an increase in cross-border retail participation could only be

achieved by promoting the use of personal financial planners (consultants), who could help retail investors to make informed decisions in an international context.

18) How can the European Supervisory Authorities (ESAs) further contribute to ensuring consumer and investor protection?

In most Member States, national consumer protection bodies usually have relatively limited capacity in the financial services area. In some cases it is not even clear whether they have legal rights in this area and what these rights are. Therefore it might be useful for the European supervisory authorities to encourage strengthening the administrative capacity of national consumer protection bodies and financial regulation agencies in that regard.

19) What policy measures could increase retail investment? What else could be done to empower and protect EU citizens accessing capital markets?

Encourage Member States to establish favourable conditions for stock brokers and investment companies to establish funds for new ventures which permit tax incentives (such as a write-off of the investment against income tax for household savings). Together with improving institutional consumer protection (as suggested in the reply to the previous question), an increase in retail investment could also be stimulated by introducing different forms of financial education targeted at non-professional investors and savers, and very well regulated financial planning consultancy services for individuals.

20) Are there national best practices in the development of simple and transparent investment products for consumers which can be shared?

Best practices are not yet well established, they are still taking shape. Among the few examples is the process of accreditation of investment products by professional associations in the UK². In general the development of such products is not an easy task, because investment products may be complex by their very nature and also because issuers try to meet a variety of needs and try to differentiate their products from other similar products. Another problem might be the consideration that if the government tries to force the development of such products, this might be considered as intervention in the market and restricting competition. This is why, instead of making efforts in this respect, it would be more productive if the development of financial education and financial advisory services for individuals were encouraged.

²

The Association of British Insurers, British Bankers Association and the Building Societies Association in negotiations with the British Standards Institute decided to develop simple financial products which comply with an agreed set of principles, which are presented in the Sergeant Report (March, 2013).

21) *Are there additional actions in the field of financial services regulation that could be taken to ensure that the EU is internationally competitive and an attractive place in which to invest?*

Competitiveness should be viewed in a comparative perspective. Therefore the EU capital markets should provide investors with conditions which are at least comparable, if not better, than those on international markets. This would require measures to improve investor protection and adapt tax structures (with more careful scrutiny of the benefits and costs of the proposed tax on financial transactions).

22) *What measures can be taken to facilitate the access of EU firms to investors and capital markets in third countries?*

The best way is to stimulate cooperation with banks that have a well-developed network of branches in third countries.

4.4 **Improving market effectiveness – intermediaries, infrastructure and broader legal framework**

23) *Are there mechanisms to improve the functioning and efficiency of markets not covered in this paper, particularly in the areas of equity and bond market functioning and liquidity?*

Such mechanisms could include:

- a long-term minimal liquidity of the market for financial instruments issued by SMEs should be assured. This could be achieved by stimulating liquidity providers or market-makers that quote financial instruments issued by SMEs;
- increasing investors' trust in SMEs by introducing corporate-governance best practices, and involving key financial investors in their management;
- increasing SMEs' attractiveness – e.g. through possibilities for corporate guarantees (or guarantees from specialised institutions) for issues by SMEs, meeting certain criteria;
- introducing stimuli for SMEs listed on regulated markets;
- introducing stimuli for investors in issues by listed SMEs.

24) *In your view, are there areas where the single rulebook remains insufficiently developed?*

The single rulebook approach, developed for the banking sector through CRD IV, DGS and BRRD, creates a level playing field and furthers the single market. Extending this approach to the non-banking financial sector could therefore be very useful. An approach similar to that of the BRRD should also be introduced for central counterparties.

25) *Do you think that the powers of the ESAs to ensure consistent supervision are sufficient? What additional measures relating to EU level supervision would materially contribute to developing a capital markets union?*

On the question of supervisory convergence, the EESC:

- agrees on the need for corrective action to improve the operation of the European System of Financial Supervision (ESFS);
- calls for the promotion of measures to facilitate coordination between the ESFS, the new Single Supervisory Mechanism (SSM) arrangement and the Single Resolution Mechanism (SRM);
- calls for the regulatory functions of the ESFS institutions to be rationalised with a view to simplifying the regulatory framework and making procedures more transparent and effective;
- asks for a medium-term strategy designed to bring about organisational and functional consolidation on the part of the supervisors (by considering the possibility of a single seat and the adoption of a "twin peaks" model);
- calls on the European Commission to assess the feasibility of more structural measures regarding the organisation of the ESFS and the authorities' funding mechanisms.

26) *Taking into account past experience, are there targeted changes to securities ownership rules that could contribute to more integrated capital markets within the EU?*

The inter-relations between the depositary institutions should be improved, as should the security of cross-border clearing and settlement.

27) *What measures could be taken to improve the cross-border flow of collateral? Should work be undertaken to improve the legal enforceability of collateral and close-out netting arrangements cross-border?*

Measures are to be welcomed to create a unified European registry of cross-border collateral, or to interconnect the respective departments of the national registers. Without such measures being implemented, cross-border investment will remain limited.

28) *What are the main obstacles to integrated capital markets arising from company law, including corporate governance? Are there targeted measures which could contribute to overcoming them?*

The differences between commercial law, business practices and corporate governance models across the Member States are the most serious impediments for a Capital Markets Union. To overcome this will take a long time and will not be easy, but is a must. It will require careful study of Member States' jurisdictions.

29) *What specific aspects of insolvency laws would need to be harmonised in order to support the emergence of a pan-European capital market?*

Insolvency laws are vital for the capital markets and as in the case of commercial law and corporate governance should be harmonised after thorough research, because otherwise there is a risk that investment will move to countries where investors' rights are better protected. In particular, the fresh start option should be carefully considered.

30) *What barriers are there around taxation that should be looked at as a matter of priority to contribute to more integrated capital markets within the EU and a more robust funding structure at company level and through which instruments?*

The structure of taxation systems varies greatly across the Member States and is very sensitive to any changes. At the current stage, taxation harmonisation will be very difficult to achieve and should be viewed as an end-stage of the process.

31) *How can the EU best support the development by the market of new technologies and business models, to the benefit of integrated and efficient capital markets?*

The EU should concentrate on building a single digital network infrastructure, which should provide for swift, efficient and safe communications between markets, companies and investors³, as well as an opportunity for remote and cross-border participation in shareholders' general meetings and for voting. Efforts should also focus on finding ways to decrease the relatively high clearing and settlement costs when trading across borders.

32) *Are there other issues, not identified in this Green Paper, which in your view require action to achieve a Capital Markets Union? If so, what are they and what form could such action take?*

The Green Paper provides a comprehensive review of the current state of play in the capital markets in Europe, as well as the measures needed to achieve a CMU. At this stage it is better not to open more issues, but rather to better plan the timing for implementing the measures which have already been decided, and to select some important tactical reforms to start with: these should be tangible and have a direct and measurable impact. This will create a momentum which will facilitate the implementation of more difficult reforms in the future.

³

As an example of best practice, see the independent electronic marketplace for corporate lending FINPOINT <https://www.finpoint.co.uk/>

Notwithstanding, the EESC notes that the Green Paper does not address:

- The credit rating of financial instruments
- Measures related to the problem of the procyclicality of financial products.

Brussels, 1 July 2015.

The President
of the
European Economic and Social Committee

Henri Malosse
