BNP Paribas Response to Green Paper on Building Capital Markets Union
Executive Summary

The Capital Markets Union (CMU) is a welcome initiative that, after a five-year period of regulatory emphasis on financial stability, shall turn the European focus towards the financing of growth. CMU will also play a key role in the financing disintermediation movement which is needed to compensate for the pressure to decrease bank lending due to the very demanding prudential capital and liquidity requirements that have been adopted in the aftermath of the crisis.

For BNPP, the top priority actions should be the following:

- The CMU's first step should be to preserve the capital markets capacities of European banks by reorienting current initiatives proving to be contradictory to the objective of well-functioning financial markets. In particular, capital markets financing cannot work without market making capacities, which are needed for liquid and efficient markets serving the real economy. As a consequence, European regulators should fundamentally reconsider, recalibrate or redraft pending hazardous regulations that would severely hamper market financing, such as the Bank Structural Reform which would increase the capital markets' price of funding, the Net Stable Funding Ratio which in its Basel form treats market making activities in a punitive manner, and the Financial Transactions Tax which would accentuate the fragmentation of the internal market, reduce market liquidity and increase the cost of financing.

- The securitization market needs to be revived. Its current low level (only a third of what it was before the crisis) unfairly harms Europe, although default rates of securitizations have been in reality very low in Europe. A correction of the calibration of securitization capital requirements is required in the various legislations which prevent banks from originating, arranging and sponsoring securitizations (mainly CRR-CRD IV) and prevent institutional investors from buying these instruments (mainly Solvency 2). This rebound of the securitization market is strategic for the SME segment but also for the mortgage segment. In particular, considering that mortgages represent one of the main volumes in banks' balance sheets, securitizing housing loans would free up an important capacity to lend that banks will be able to use to finance corporates, notably SMEs. In addition, considering the experience of the United States' government sponsored enterprises, the opportunity of a European backstop for mortgage securitization should be duly studied as it could be a critical catalyst to develop a deep, simple and safe securitization market.

- Rules impeding investments (in particular equity and long term investments) should be reconsidered. Solvency II's current calibration, which in particular constrains institutional investors' capacity to buy equities, is one example. More generally, an unfitting regulation of insurers is all the more penalizing for the good financing of the economy, as insurers can be considered to be the European equivalent of the US pension funds which play a key role in the US markets financing.

- It should also be noted that "classical" bank lending will remain a major source of financing in Europe and therefore should not be constrained by excessively restrictive calibrations for the Total Loss Absorbing Capacity, the Leverage Ratio, the Liquidity Coverage Ratio and the Net Stable Funding Ratio.

- Considering the precedent of the Banking Union, a more integrated supervision, with more powers given to the EU level consistently with the expanded needs of a genuine CMU, would in the medium to long term favour a better functioning and less fragmented EU financial market. In the short term, ESMA should fully use its existing powers to make sure the single rulebook is applied consistently within the EU.

As per the general approach, 2019 is too far a timeline considering the need to revive urgently European growth. We would then recommend a step by step approach with some building blocks to be achieved as soon as 2016 or 2017.

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Green Paper on Building a Capital Markets Union

BNP Paribas Response

BNP Paribas Group (www.bnpparibas.com) is a European leader in banking and financial services, with a significant and growing presence in the United States and leading positions in Asia. The Group has one of the largest international banking networks, with a presence in over 75 countries and nearly 190,000 employees including 147,000 in Europe - among whom 18,000 in Italy, 16,500 in Belgium, 58,000 in France and 3,700 in Luxembourg. BNP Paribas enjoys key positions in Corporate and Investment Banking, Private Banking & Asset Management, Insurance, Securities Services and Retail Banking.

Introduction

BNP Paribas welcomes the Capital Markets Union Green Paper as a clarion call for growth after a five-year period when the cursor was firmly on the side of financial stability and less on the financing of the economy by banks, which is their main role in Europe. Beyond boosting much needed economic growth by rebalancing and diversifying the sources of, and the access to, non-bank funding, the CMU represents a singular opportunity to further develop the single market in the entire EU by enabling the free movement of capital and the integration of its capital markets. Moreover, adopting the right CMU agenda can help meet long-standing major policy objectives such as creating an enabling environment for the financing of long-term projects in Europe, of the energy transition (infrastructure and green bonds), and of businesses --not only large companies which are already largely financed by the markets, but also SMEs, which are the engines of future employment growth.

As major actors in the capital markets and in the broader economy, European banks have a key role to play in building CMU and welcome the project’s ambition and the opportunity that it represents. CMU also provides timely momentum to take stock and make adjustments to existing or pending legislative and regulatory initiatives that would unduly hamper their capacity to finance the economy and play their essential market making and liquidity provision roles to the capital markets. To that end, it is important to note that bank lending will remain the main source of financing and therefore should not be constrained further. In addition, obstacles to market making should be avoided to allow for stronger and more liquid capital markets.

BNP Paribas fully supports the five priorities for short term action outlined in the Green Paper, in particular the priority of reviving securitisation in Europe. In our response we provide contributions on possible specific measures to meet the objectives of CMU. In more general terms, we would also like to emphasize below three key areas that, in our view, will greatly contribute to making CMU a success for the benefit of Europe and its citizens.

Reviving the Securitisation Market in Europe

We fully support the Commission's views on the need to revive the securitisation market and the specific consultation on a framework for STS securitisation as a way to repair the unjustified penalization of the EU market. As the Commission rightly points out, securitisation issuances in Europe are only a third of what they were before the crisis[1]. The stigma attached to this financial process is unfairly harming Europe although default rates of EU securitisations have been incomparably lower than those in the US, and CRD4 already prevents any form of complex securitisation. In order to bring about an indispensable rebound of this market, an urgent correction of the calibration of Asset Backed Securities capital requirements is required in the various legislations which prevent banks from originating, arranging, and sponsoring securitisations (mainly CRR IV), as well as large potential institutional investors from buying these instruments (Solvency 2, MMF).

We are of the view that pragmatism as well as boldness are both necessary to boost the securitisation market. Although not entirely replicable, lessons from the US experience of disintermediation need to be drawn. And the strong and forward looking will of the American public authorities to develop capital markets activities should be noted. It was a long lasting process starting in the depression era that has driven the US regulatory and institutional framework to provide continuous incentives to the process of banking disintermediation ever since. In particular, a series of regulatory Acts in 1930s-40s aiming to restore confidence in the financial market helped shape up a stable and sustainable backbone of US capital markets. Capital markets development was later accelerated by the establishment of Government Sponsored Enterprises (GSEs) providing a public guarantee for housing loans that continues to allow removing extremely important amounts of housing loans from bank balance sheets through a securitisation process. In this regard, the Commission should study the opportunity of a European backstop for mortgage securitisation, as this could be a critical catalyst to develop a deep (there are very large amounts of housing loans), simple (housing loans are granular and easy to standardise), and safe (housing loans are a low default segment) securitisation market. Such a market would free up capacity in bank balance sheets which banks could use to lend to SMEs instead, as SME lending is less easy to securitise.

Still it should be recalled that SME loan backed securitisations were the second largest asset class for European issuances prior to the crisis. SME securitisation volumes have since collapsed due to severe changes in their regulation and compulsory reference to external ratings in Europe, while at the same time European authorities have explicitly favored the treatment of on-balance sheet SME loans. The regulatory gap before and after securitisation grew to such an extent that those securitisations have almost stopped being issued[2]. Therefore to revive the market in SME securitisations, references to external ratings should be removed, to better align their regulatory treatment with the regulatory treatment of on-balance sheet SME loans. This is particularly important for Europe, as even though some mid-sized companies may be able to move to capital markets, small and most mid-sized companies will continue to rely on bank lending for structural reasons (of which cultural ones, such as lack of appetite for opening up their capital, are not the least).

[1] In 2014, issuances in Europe amounted to €216 bn, compared with €594 bn in 2007, and to €1070 bn in the US where banks' balance sheets represent 1/3 of the European bank's balance sheets

[2] The RWA of the securitized tranches is several times higher than the RWA of the portfolio of the underlying assets.

Removing the compulsory use of agency ratings in the securitisation capital framework should be extended to other key asset classes of the European economy as well, i.e. corporate receivables (loans, trade receivables, leasing,…) and consumer receivables (residential mortgages, autos, consumer loans,…). This could be done in Europe, as a first step in the context of Simple, Transparent and Standardised (STS) securitisations. In all those cases, the regulatory treatment of the on-balance sheet assets should be the basis on which to compute the regulatory treatment of SST securitisations. The presence of rating agencies breaks this fundamental linkage, creating most of the distortions in the European securitisation market, and damaging the European economy.

Preserving the Capital Market Activities of European Banks by removing regulatory barriers to well-functioning capital markets

There are two conditions to develop deep capital markets: a) a deep liquidity ensured by a well-functioning market making capacity and b) a sufficient quantity of long term savings, as the role of capital markets is to mobilize preexisting savings. The first condition comes also as an urgent matter as it is firstly about repairing the economy. Numerous studies (notably one from the New York Fed in October 2014), indicate that bond trading inventories and volumes have been divided by two since the beginning of the financial crisis. Moreover, a recent BIS report points to the reduced risk appetite and risk taking capacity of banks due to the regulatory environment. So here, we would stress that the Green Paper fails to address the regulatory barriers hampering the Capital Market Union and makes no reference to the importance of derivative markets, which are an essential component of capital markets: derivatives are key for efficiently managing all kinds of market and credit risk related to activity in bonds and equity. This is not only true for the market maker, but also for the issuer and the end-investor. In short, modern equity and bond markets could not possibly function without derivatives markets. Moreover, several pending European regulations such as the Regulation on Banking Structural measures or the Financial Transaction Tax will hamper market making, as will the forthcoming European NSFR standard if it does not deviate materially from the BCBS proposal which severely penalizes market making. In both cases, these measures will trigger an increase in the spreads and consequently raise costs, both for investors and issuers alike. In this regard, as is the case for the revision of the Credit Valuation Adjustment charge (CVA), we would caution again that international standards need to be calibrated appropriately, taking into account the specificities of the European market.

CMU will require an evolution of the current institutional framework

The integration of Europe’s capital markets will require regulation and supervision that are much more harmonized and convergent, both in substance and in the enforcement of rules. This will contribute to increasing cost-efficiency and consistency and to reducing fragmentation so that a union of European financial markets, and a level playing field across Member States, can be realised.
To that end, the Commission should consider carefully the options for adapting the current European capital market supervisory and regulatory framework to meet the expanded needs of a true CMU.

In summing up, we would like to stress again the importance of banks to the development of CMU, as liquidity providers (and risk takers) bringing together issuers and investors. The regulatory trend in the past few years has been fully oriented toward reducing bank risks. But CMU will only be a success if this trend is pragmatically redirected and if existing or pending regulations are calibrated in line with the goals of CMU. Otherwise the project will remain an aspiration without concrete achievement and Europe risks going into a third dip. The 2015 recovery could then resemble the 2010 recovery, which was stopped by the first wave of regulation. Finally, political will and vision will be necessary to adapt Europe’s institutions to facilitate the revival of the securitisation market as well as the appropriate and efficient supervision and regulation of its integrated capital markets.

Priorities for early action

Questions

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

A first additional priority is the recalibration of existing or looming regulations and legislative initiatives which may penalize liquidity, market making, and investment: BSR, FTT, NSFR… This must be a priority action as well (LCR, NSFR and TTF). This represents a low-hanging fruit for Europe in order to move quickly in creating a more enabling environment for CMU and for accelerating the economic recovery.

The second one is to put on hold the on-going Basel initiative to completely revamp the RWAs framework as long as a proper governance is not put in place to ensure that the objectives and the supporting proposals strike the right balance between financial stability and growth.

The third one is to systematically undertake a comprehensive assessment of the cumulative impact of post-crisis EU financial regulation on economic growth and employment before enforcing the rules. Here again, policy-makers should ensure that a proper governance is established around those impact assessments.

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?

Improvement of the availability of detailed and reliable financial information is key for SME who intend to benefit from an easier access to capital market through CMU. Nevertheless it must be pointed out that small and very small SMEs will never have access to capital markets and are not looking for it. Authorities could therefore seek to increase transparency of SME activities and performance through mandatory reporting of key financial information to the relevant public registers or public sector authorities.

In France, the publication of key financial information is mandatory for the vast majority of companies. However, companies may ask for a restricted access to the information they provide. In that case, the information will only be available to public authorities including Banque de France. Recently, the legislator decided to alleviate this obligation for very small companies.

The availability of financial information is key for the evaluation of SME creditworthiness. This evaluation can be done by public sector agencies (e. g. FIBEN database run by Banque de France) or the private sector. In the latter case, a clear legal framework should define clear policies regarding the permissible uses of the information that is collected by the public sector agencies and information available in public records.

Regarding other steps, it would be extremely beneficial to develop a website which would provide centralized information for all European SMEs on available loan programs and business planning. While the European Small Business portal represents a useful step in the right direction, we believe the US Small Business Administration (SBA) experience could help enhance the website content and the tools available to European SMEs. A good effort has been made at http://ec.europa.eu/small-business/index_en.htm. However, based on the SBA experience in the United States, we believe the website can be improved.

We think one very useful feature of the US SBA website is that it provides a quick and easy access to a wide variety of simple tools such as business planning, loan availability assessment, etc. The SBA's Business Plan Tool provides SMEs with a step-by-step guide to help them get started. The plan can be saved as a PDF file, firms can update it at any time, making this a living plan to which they can often refer. The business plan can be used to discuss next steps with a mentor or counsellor from an SBA resource partner.

Young, high-growth companies can also get assistance and information about venture capital financing on the SBA website. The website discusses the differences between ordinary loans and venture capital financing, provides information on prospective investors, and describes the steps of the venture capital process in a great detail. In addition it provides a centralized directory of the Small Business Investment Company (SBIC) Program investment funds licensed to provide growth capital to U.S. small businesses. SBICs regulated by SBA, are private, profit-seeking investment companies that make independent investment decisions. However, this directory provides useful contact information needed to learn more about the SBIC Licensees in one's state.The US SBA provides several types of loans to small businesses depending on their particular needs such as to establish a new business or to assist in the acquisition, operation, expansion of an existing business or providing small businesses with long-term financing to acquire and improve major fixed assets, such as owner-occupied commercial real estate and heavy machinery.

It is important to note that credit availability might not be the only issue constraining small business expansion. The US experience suggests that during the last recession weak demand for credit likely resulted from weak demand for small business goods and services as the economy was slow to recover. Therefore, government efforts to increase credit availability for small businesses should have been taken in the contex of low demand for SMEs goods and services. In the beginning of the current recovery, Federal Reserve noted the need to rely on surveys' data to analyze small business developments. In addition, to get a better insight, the Fed then initiated a series of meetings to gather intelligence they use to facilitate the flow of credit to small businesses.

The survey data could help reveal issues small businesses are facing and therefore target government response. For example, since the beginning of the last recession, 'poor sales' was the most important problem for small businesses for a long period of time. However, 'government requirements' has been steadily rising as of late, and has become the most important problem for small businesses after taxes, reflecting elevated levels of political and regulatory uncertainty. Following the passage of the Patient Protection and Affordable Care Act (Obamacare), small businesses will bear the brunt of increasing health care costs as they will be required to offer health insurance or pay a penalty. As such, small businesses were slow to expand for the reasons other than the lack of credit supply. Government efforts to promote credit availability alone might not be helpful if there is no demand for credit on the part of the SMEs.

3) What support can be given to ELTIFs to encourage their take up?

The ELTIF is a concrete step towards meeting Europe's pressing needs for growth and long term financing. However, in order to achieve this goal, the new regulatory framework needs to ensure that the interests and needs of different types of investors are met while avoiding a one-size-fits-all approach and that the right incentives are in place for ELTIFs to become a market success.

The trilogue agreement added a number of specific conditions that are now foreseen for the marketing of ELTIFs to retail investors. On two specific additional conditions, i.e. the 10.000 euro minimum participation and the 10% threshold as to the aggregate portfolio of the retail investor, their potential as to the protection of the retail investor and their possibility to be implemented are questionable. BNP Paribas therefore believes that a robust investor protection as provided by the MiFID suitability and appropriateness test is the most efficient safeguard for retail investors in ELTIFs.

There is a certain category of investors, belonging to the category of wealth management, that although falling in the general category of retail investors, possess significantly larger resources and enhanced expertise and understanding of the complexity and risks of an investment. BNP Paribas would urge to allow for a more efficient involvement of this particular group of investors in order to fully explore their significant potential to invest in long-term financing projects. For ELTIFs, not open to retail investors, but only to professional (and semi-professional) ones, additional flexibility regarding portfolio diversification rules and marketing and transparency requirements has a key role to play for ELTIFs to become a sustainable option.

BNP Paribas supports a flexible redemption policy of ELTIFs by leaving the discretion to the ELTIF's manager to create a redemption regime that better fits its investment strategy and underlying assets as long as it is fully disclosed to investors in the ELTIF's rules. The same flexibility and discretion should apply to the choice of the lifetime of each ELTIF.

For Pension funds and insurers, capital and portfolio composition requirements for the portfolios they choose to invest in are very important in determining their interest and ability to invest in ELTIFs. BNP Paribas believes that adjustments to the standard capital requirements of Solvency II and IORPs in view of encouraging in concrete investments in ELTIFs will be essential to the success of ELTIFs.

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?

BNP Paribas fully supports and has been an active participant in industry and public-led efforts to further develop private placement markets in Europe.

In France the Euro PP Market in particular has been an initiative of the French Chamber of Commerce and Industry of Paris, the French Central Bank and the Treasury, with the active support of the industry and its trade associations. It has led to the development of a Euro PP Charter, proposing a code of conduct, best practices, and standard documentation for non-listed bonds and a model agreement for loans. Over the last three years, some €10 bn have been issued through Euro PP. But it is important to note that this financing has been raised mainly by fairly consequential mid-size firms, some of which could access the capital markets directly. So the issue remains how to develop PP markets for smaller SMEs.

In 2014, about 12% of EuroPP issues were by Italian SMEs, following the Italian government's introduction of a decree (now a law) encouraging debt capital markets transactions by expanding favourable tax treatment and allowing institutional and qualified persons to invest directly in SME-issued corporate bonds. Elsewhere, another important development is the Schuldschein Market in Germany which has grown to a volume of about €11bn in 2014. In addition, the US PP market may offer useful lessons for Europe, notably in terms of facilitating the analysis of SME credit risk.

These promising initiatives represent important first steps towards a European PP market, which the EU could complement by considering ways to leverage the Juncker Plan. One possible approach could be the development of a Pan-European hybrid debt fund aimed at providing medium to long-term financing to smaller SMEs, a segment where banks are less present. Such a vehicle would be junior to bank loans and complementary to bank intermediation, and allow SMEs to retain control while accessing longer-term financing. To further this, the EU could also encourage Member States to give favourable tax tratement to investors, as is the case in the Italian and German experiences cited above.

A second axis of reflection could be to study how ELTIFs could be used to finance less liquid SME-issued debt instruments and what would be the appropriate level of information to be given to potential investors. This would offer the advantage of providing a long-term investment opportunity for institutional and even retail investors under a clearly defined and regulated framework involving asset managers.

Finally and as noted in our answer to question 6, the EU should do all it can to enhance the liquidity of financial markets in Europe, in particular calibrating those provisions in Solvency 2 regarding equity investments in unquoted companies (thus SMEs and innovative and high-growth start ups) and CRD IV that may make it prohibitive for insurers and banks to hold these assets.

Measures to develop and integrate capital markets

Questions on Improving access to finance

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

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?

As stated in the introduction to our response we do consider that market making activities need to be preserved as they are key to channel funding across the real economy, i.e., match funding needs with investment needs: Effective economic funding through financial markets necessitates that regulated institutions (ie banks) provide liquidity in secondary markets. Promoting greater liquidity is essential to make progress towards CMU. Liquidity in secondary markets will also be key in determining the funding levels and attractiveness of new debt issuance in the primary markets.

It is important to recap, as a preliminary remark, that market liquidity has decreased steadily since 2007 (i) across all geographies (US, Europe and emerging markets) and (ii) across all types of bonds (corporate as well as sovereign).

In this already worrying context, the utmost priority for EU regulators in our view should be to avoid any regulatory mesures that penalize even more this liquidity and hamper market making.

Market liquidity is heavily dependent on the presence of market makers in a given market. The presence of fewer market makers and/or market makers with reduced trading capacity (if the inventory levels required for active trading cannot be kept) inevitably reduces secondary market liquidity. Now, traditional broker-dealers of banks have become much less able to hold large positions on their balance sheet, overnight or for longer period, as a result of prudential regulation (such as capital requirements, leverage ratio, liquidity ratios) that increases the cost of hedging and funding of inventories held and (ii) by market regulation (the OTC derivatives reform, short selling, the upcoming MiFID II…), that also increases hedging costs as well as execution and operational costs. These regulations shall incentivize the banks to reduce their market making activities.

In this regard we would highlight certain provisions of the NSFR, as well as question the need for the proposed FTT.

Net Stable funding Ratio (NSFR)

As a long-term structural ratio to address liquidity mismatches and provide incentives for banks to use stable sources to fund their activities, the NSFR is due to become a binding minimum standard by 1 January 2018.

Most capital market activities would be subjected to a quite adverse treatment by the NSFR as currently designed, in particular:

- ✓ market making activities will be affected through the penalizing treatment
    - o of security inventories (essential to perform market making),
    - o matched book (key driver of liquidity),
    - o as well as repos (to refinance the inventory).

As a consequence providing market making services will become extremely expensive, and the NSFR compliance cost will be well above the profitability of these activities.The NSFR would require the highest quality sovereign debt to be long term funded for a portion between 5% and 10% of the held amount versus a haircut of 0% allocated to LCR for these securities.

Liquid shares will require 50 % stable funding whereas their actual liquidity at more than 1 year horizon should require a much lower percentage. More generally, NSFR run off factors for liquidity outflows should not be LCR based for liquid assets, such as equitites and securitisations.

The suggested asymmetrical treatment for repos and reverse repos with non-financial counterparties would have a direct detrimental impact on market making activities, including sovereign debt. Indeed, the NSFR would act as a disincentive to enter into reverse repos with non-banks (i.e.: insurers and asset managers) which would limit their responsiveness to meet buy orders.

- ✓ Derivatives activities which are essential to allow market makers to hedge their inventories will be affected :
    - o through the penalizing treatement of initial margin (85% will require one year funding),
    - o the obligation to receive cash collateral to benefit from the netting,
    - o total liabilities after netting with derivatives assets will require 20% stable funding at one year,
    - o and hedging relationship between short term derivatives and securitity inventory which hedge derivatives that is completely disregarded.

As a result, a lot of client activites will be affected: hedging of corporate and institutional clients, investments of institutional and individual clients as well as financing of institutional and corporate clients.

Consequently the NSFR as currently proposed will be detrimental to the inventory, to the repo/reverse repo instruments as well as to the derivatives, rendering market making activites either less profitable for banks or more costly for investors or a combination of both.

This will particularly affect the European economy where disintermediation, which relies on efficient market-making capabilities, is much needed to compensate for the decrease in bank-based financing due to very demanding prudential liquidity requirements.

Financial Transaction Tax (FTT)

The FTT contradicts two fundamental objectives of the Capital Markets Union project:

- firstly, the objective to achieve the free movement of capital within the EU 28 Member States: it needs to be stressed that the FTT applied to 11 Member States over 28 will necessarily accentuate the fragmentation of the internal market. Trades would be treated differently depending on their territory, creating (instead of removing, which should be one of the objectives of CMU) additional barriers to cross-border investments;
- secondly, the objective to diversify the sources of financing and make financial markets work more efficiently for the benefit of the appropriate funding of the economy: the FTT would (i) hamper the smoothness of the market financing; (ii) reduce market liquidity which is already damaged by the effect of prudential and market regulations (inventories and trading volumes have been halved during the recent years); (iii) lead to the exit of participants from parts of the market; and (iv) increase the cost of financing through the markets since the tax would inevitably be passed on to the end-users (i.e., corporates).

As a concluding remark, it should be noted that the regulatory environment is still moving with new rules looming (Fundamental Review of the Trading book, moving from IRB approaches to standard models) where the calibration could introduce very adverse effects on the EU economy. All these changes still to be transposed in Europe need to be carefully assessed in the light of CMU. This environment will still prove challenging for European banks in their ability to contribute efficiently to the CMU.

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?

BNP Paribas actively supports the development of ESG investments. The Group recently arranged, for example, the first green bond issue on the US market in the form of a private placement. The deal went towards financing a wind farm in Australia, and is remarkable for being the first multi-currency private placement of a green bond for a single asset, and for giving the client access to services including structuring and placement, as well as forex and interest rate hedging. The offer was three times over-subscribed.

This transaction and similar ones by other financial institutions demonstrate that there is significant investor appetite for these types of investments. The EU can support their development in Europe by adopting measures aimed at enhancing the visibility and tranparency of this asset class. A pan-European “Green label,” for instance, could be considered for investment funds that meet relevant required criteria, as certified by independent auditors.

Similarly, the EU could define a European standard and nomenclature of ESG economic activities to launch an ESG label for SMEs and mid-size companies active in those sectors. In addition, the EU could study the possibility of providing seed money to ESG funds within the framework of the European Strategic Investment Fund, which at present has a social impact accelerator criterion but not one dedicated to environmental impacts. This ESG transparency at all level of the value chain would allow for these funds to attain the critical size, visibility, and sustainability necessary to attract institutional investors.

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

Yes.

Addressing information problems is a key step forward to improve access to finance by SMEs and mid-size companies in Europe. Developing a simplified, common EU level accounting standard tailored to companies listed on multilateral trading facilities would increase transparency and comparability and help them attract investors, in particular across borders, which is one of the expected benefits of the capital markets union project.

The emphasis of such a standard, however, should be on the word "simplified" to foster its use and enhance its accessibility to SMEs, making it easier for them to produce their accounts. Importantly, the accounting standard needs to be designed for all users including the management of these companies, in particular the issuers of securities and not only short term investors. It should also be neutral and not pro-cyclical.

The above considerations would preclude the adoption at European level of the IFRS standard for SMEs, which, in addition to carrying over--and amplifying—some of the weaknesses of IFRS (conceptualized as they are on valuation as an instant market value and being investor-biased, to cite but two issues), is too complex for SMEs and would not meet their needs. One example of a real, simplified accounting norm for SMEs would be for them to be able to account for equity and debt instruments they have bought at cost rather than at market value. To prepare the growth of these entities and the potential use of IFRS for SMEs or full IFRS, this simplified accounting standard should be based on a simplified version of IFRS for SMEs. But this standard should be drafted under EU control by a EU accounting standard setter – EFRAG could be a candidate.

With regard to SME Growth Markets, were a common and simplified EU standard to be developed, it should naturally become a key feature since as envisaged under MiFID2, one of the main objectives of these markets is to lessen the administrative burden and provide greater incentives for SMEs to access capital markets.

In addition to accounting standards, harmonisation of reporting for SMEs seeking cross-border funding would enhance their access to financing. Advantages for investors would in particular include better comparability and frequency of reporting.

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?

There is today a multiplicity of initiatives taking very different forms, including within each Member State. Obviously the business model of this financing channel is not stabilized yet.

As regards lending activity specifically, two trends can be observed:

- all traditional banking activities are now targeted (consumer loans, SME loans, factoring, infrastructure financing…), and
- market share is at the very heart of the platforms business model, generating a race for critical mass.

Therefore a European passport is probably a key factor to the development of this financial channel. This issue is of crucial importance for euro zone platforms which currently cannot benefit from the volume of this market.

As a consequence it is necessary to set a European regulatory status appropriate to the risks these new actors generate which are twofold: consumer/investor protection and financial stability.

It is crucial that potential losses are incurred by investors that are aware of the risk they take (which certainly means consumer protection but also strong educational efforts) and unleveraged (notably investment funds). It is also crucial that institutional investors do not fully dominate this financing channel at the risk of exposing it to a "wholesale funding risk" well-known by banks (opportunistic investment funds can massively and abruptly withdraw their funding thereby destabilizing all the actors of the financing channel, starting with borrowing firms from the real economy).

Regarding legal protections, investors will only be attracted in investing in crowdfunding or peer to peer platforms if they trust them. In order to give confidence to investors and encourage small and medium sized companies to use crowdfunding or peer to peer platforms, investor protection must be ensured.

A wide range of requirements, including enhanced investor protection rules, are already applicable to investment firms providing investment services and banks. This raises the question of the opportunity of introducing new measures governing crowdfunding platforms or applying them the set of rules already governing Investment firms and banks since the financial instruments which can be acquired through investment firms and crowdfunding platforms are the same.

The application of the existing rules (for example: categorization of clients, minimum capital or disclosure information requirements under MIFID) to crowdfunding participants (investors, operators of crowdfunding platform, project owners seeking finance) could be a barrier to the development of crowdfunding or peer to peer platforms. Nevertheless, investor protection is a key issue and the application of the existing rules to crowdfunding participants may mitigate risks in particular the risks of bad advice, fraud, hacking, loss or money laundering.

Crowdfunding process involves a wide variety of actors and crowdfunding services are provided using a large number of different business models, which explain why different pieces of EU financial regulation could potentially apply.

It is essential to the development of appropriately regulated crowdfunding or peer to peer platforms to clarify how crowdfunding fits into existing rules and others introducing specific requirements.

The introduction of potential specific requirements must be analysed in relation to the existing rules and regulations applicable to Investment firms and banks but also those about to be adopted.

The adoption of specific rules applicable to crowdfunding or peer to peer platforms would permit to use a common terminology across Member States to refer to the various actors of crowdfunding or peer to peer platforms and to clarify the roles and responsibilities of crowdfunding platforms and other actors of capital markets.

(See Annex for detailed recommendations on the regulation of crowdfunding platforms)

Developing and diversifying the supply of funding: Questions on Boosting Institutional Investment

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?

Policy measures that incentivize and remove obstacles to the development of pension funds in Europe would be key to creating a deeper institutional pool of long term financing. Likewise for insurers, achieving the right calibration of Solvency 2 capital requirements, which at present penalize investments in equities, in particular those of unlisted ones (i.e. , SMEs), will be essential to achieving this objective.

In addition, an important factor which limits Institutional investments in funds dedicated to SME financing in equities is the size of these funds. Funds investing in small "early bird" companies (venture capital) are too small for big Institutional investors. As a matter of fact, investments in such funds cannot exceed 10/15 mln EUR. This forces institutional investors to make numerous small investments in many funds, which is very difficult to manage (and too costly). There are larger funds on the market, but they invest in larger and more mature companies (LBO funds), so this is not the same target. The solution could be pan-european funds on venture capital which, with a much larger territorial basis, would be of course much bigger.

Another element that could help Institutional investments in pan-European venture capital funds could be the support/backing of European actors such as the European Investment Bank / the European Investment Fund, that could perhaps provide a partial guarantee on investments.

In other areas, the context of the review of accounting rules represents an opportunity to give particular attention to their impact on long-term investment and financing as in their present form they have led to short-terminism behaviour due to over reliance on mark to market valuation methods.

Also, encouraging Member States to promote long-term investment in SMEs and high growth start-ups through ensuring certainty and an attractive tax treatment is also crucial in this regard. This is an even more important rationale than current macroeconomic perspectives and the weakness of the economy. To this end, guidelines at European level could be developed regarding favourable tax policies that encourage long term investment.

Finally, measures at EU and national level to facilitate investment in infrastructure such as improving the legal framework, drafting a pan-European definition of infrastructure as an asset class, standardizing information, and amending accounting and regulatory treatment to increase attractiveness for investors would also be highly beneficial.

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?

A first course of action would be to review the additional costs and obstacles imposed on fund managers by UCITS V and AIFMD requirements, as in some cases they are likely to exceed the benefits to be achieved from greater consumer protection. These include the obligation to register funds in every single country where they are marketed and not just in the country of listing (where the passport is requested), in addition to the heavy attendant tasks involving the translation, regular update, and diffusion of investor information, and compliance with mandatory tax transparency rules that employ different calculation methods in the different Member States, such as in the UK, Germany, and Austria. The net impact for producers is that their costs are increasing, in particular for the more sophisticated funds (the exception is plain-vanilla funds, for which production costs have decreased), ultimately lowering profitability and therefore market offer.

With regard to the achievement of economies of scale, a priority would be to lower where feasible national-level barriers such as the tax transparency rules mentioned above and removing any redundant administrative requirements that may exist. This would definitely facilitate the cross-border marketing of funds and contribute to allowing them to reach critical size. It would also help in guaranteeing a single market with a level playing field.

Finally, the potential restriction of separating the asset management and custody functions within financial groups would entail important costs which are very likely to be ultimately borne by UCITS unit holders and appear to be disproportionate in comparison to the benefits they would enjoy in terms of increased protection.

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?

Boosting institutional investment in infrastructure is a major and necessary step towards developing and diversifying the supply of funding to the real economy in Europe. In this regard, infrastructure investment is particularly well suited to meet the needs of the pension and insurance sectors as their long-term liabilities require matching with long-term, low-risk, and inflation-protected assets. Moreover, banks and insurers are naturally complementary in this area, with the former more geared to deal structuring and short to medium term financing and the latter able to take up the long term phase of the investment.

BNP Paribas would thus welcome the introduction of a tailored treatment of infrastructure investments in the calibration of capital requirements for banks and insurers in CRD IV/CRR and Solvency II. One option could be to develop a definition of an asset sub-class for high-quality, low-risk infrastructure investments (akin to the work being done on high quality securitisation) applying a set of criteria to mitigate risks (e.g., projects that are in OECD countries; are brown field rather than green field; use proven technologies; have the participation of multi-lateral banks; mitigate political risks, etc.). The qualifying assets could then benefit from lower capital requirements, whereas under the current rules they are treated in the same manner as corporates.

A complementary approach could be to leverage on the Juncker Plan, which is already up and running and is likely to do a fair amount of infrastructure financing. As the Plan provides a known and stable framework – thereby lowering legal, fiscal, regulatory and political risks-- and greater visibility to investors, projects approved for financing by the decision committee could be given a "Juncker Plan infrastructure investment label" that would enable them to be treated in a less stringent manner under the capital requirement rules. One obstacle to this, however, is that the Plan's duration is only three years. The label and calibration would have to be undertaken in the very short term, requiring building a political consensus very rapidly.

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

The introduction of a standardised pension product is an old issue (cf. the so called "29th regime") that could help channel retirement savings and enhance the capital market union, but this seems very difficult, if not impossible, to reach within a short to medium time period for many reasons.

We believe a standardised product as the EPP would reduce the current barriers for the cross border activity of pension providers. It would solve the different rules on product notification and design, marketing and distribution. While removing some of the existing legal obstacles, the creation of an EU legislative framework to regulate a new pension product would not interfere with the existing personal pension products that already exist in each member state. Providers would have access to more markets and would be able to generate considerable economies of scale, particularly in the investment portfolio.

The creation of an EPP would allow consumers to continue their pension contributions wherever they move to in the EU. Consumers would also benefit from the cost reduction deriving from both higher competition and from a wider offer of different types of pension products.

Standardisation would mean that prudential, financial, governance, distribution, or consumer protection rules should be the same or equivalent in order to avoid unfair competition and to guarantee to the future retirees the best and efficient product. But for example it is must recognized that for the moment, pension funds and insurers, do not apply the principle of "same risks, same rules" for occupational pension products.

In addition, the present landscape is very fragmented and there are strong cultural and technical differences between the available products in the EU. So, we are of the view that improving the EU passport with a better harmonisation of prudential rules, for instance for occupation pension activity, would be a better solution in the short to medium term to give larger choice to customers and improve competition between financial service providers.

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?

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?

There are two types of measures that should be considered:

- Measures to increase the size of assets available for Private Equity and Venture Capital by promoting long term investments, through encouraging the development of the ELTIF regime, finding an appropriate and more accurate approach to valuing long term assets (which are illiquid), making available EU venture Capital Regulation to venture capital funds outside the EU to provide European professional investors with full access to global investment opportunities, and providing tax incentives to encourage investment decisions. However, this directory provides useful contact information needed to learn more about the SBIC Licensees in one's state both for the longer-term and in emerging growth companies.

- Measures to promote later stage access to finance to enhance exit opportunities for venture capital investors by lowering the barrier to entry and the cost of capital of “emerging growth companies”, reducing the costs of listing for companies, enhancing the availability of EU data and research by standardizing and improving data collection in order to enable both companies and investors to better understand services provided by capital markets, creating a single market for retail investors to directly access public equity markets cross-border Europe, promoting the financial education of both investors and companies, and promoting the so-called alternative markets (AIM, ISDX, Alternext, etc …) with more flexible and calibrated requirements than the main markets.

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

Due to their economic and social responsibility as deposit collectors, banks are professional risk takers and managers. They are regulated and supervised to do so. We can probably assume that they are the safest harbours to perform this function for the economy despite current ways of thinking.

The activities of non-banks are mainly based on markets. Markets cannot provide all the answers: they are volatile and therefore sometimes destabilizing; they are nonetheless useful for the economy and can be complementary to the banking function (notably on long term maturities).

The activities of non-banks should certainly be monitored, and they actually almost are in Europe (but new "digital" actors such as crowdfunding platforms are clearly not yet monitored enough), even though more effective macro supervision might be needed.

Currently, regulations (both existing and proposed) are essentially designed to protect investors/consumers of financial products and depositors. This dimension is important but should be supplemented by a broader vision of the finance channels of the European economy (so as to guarantee a level playing field between banks and non-banks) and the risks that threaten the financial system as a whole.

From this perspective, the European Commission should focus on:

- first, making sure that regulations are consistent and based on the general principle that same functions or same activities must call for equivalent regulations (not necessarily identical regulations) whatever the nature of the performer of the activities in order to address the same objectives and have the same effects and consequences;
- secondly, keeping control of the systemic risks that may be generated by non-banking entities, or between these entities and banks while making sure that we do not smoother economic growth in trying to ensure financial stability.

Developing and diversifying the supply of funding: Questions on Boosting Retail Investment and Attracting International Investment

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

The two cross-border retail markets are the US market (50% of the global fund market) and the Asian market benefiting from a fast growing rate compared to the developed markets.
UCITS remains the strongest brand in Asia. Since 2008, all years have seen positive inflows in UCITS in Asia including strong inflows in 2013. Other open ended funds in Asia have been negative since 2000.

Interest in Asia is particularly strong, reflecting the region's huge potential for long-term savings growth. This is only being heightened by the emergence of three proposals for Asian cross-border fund distribution. In fact, mutual recognition is likely to be expanded in the future in Asia (HKCMR). China may be open to reciprocity with other markets in Asia or beyond, but we expect Hong Kong to enjoy at least a few years of exclusivity. Asian passporting (ASEANC, ARFP) remains a long way off, with proposed schemes facing significant technical and political hurdles. For now their major impact is likely to be to add to asset managers' strategic uncertainty. The proposed changes are likely to disrupt the existing role of UCITS in Asia.

The Asian markets are becoming critical not only as markets for distribution but also as major hubs of production. As a result, it becomes essential for Europe to explore opportunities to engage in strategic partnerships in the local initiatives to preserve the strong UCITS footprint and enhance European shares in the future outlook and openness of each individual market.

On the US distribution side, European asset managers are facing major difficulties to distribute open ended funds. The US market represents around 50% of the global distribution market but there is no European actors being part of it due to major barriers of entry for foreign providers.

Among different barriers, the SEC compliance regime and the US 40 act funds requirements are the two most important. Minimum size of the funds (~250M$) brand recognition, local investment bias (12% of AuM are invested outside the US) as well as marketing and sales investments are part as well of the different existing barriers. On the other side, AIFMD and UCITS include third party recognition and the third country passport which lead to important distribution synergies for US providers in Europe. Thanks to higher margin in their domestic market, US actors may propose more aggressive pricing strategies in Europe with the benefit to enlarge their business thanks the corresponding economies of scale.

Already in difficulty to preserve their market shares in Europe, European asset managers are facing major difficulties to distribute in the US market due to these different barriers of entry. When GSAM decided to distribute asset management products in the US, the marketing and sales development required 10 years of investments of which 6 of them where negative in terms of profitability. To limit the erosion of European actors' market shares and to lower barriers of entry in for the US distribution, it is essential to include asset management's services in the TTIP discussions to establish a minimum of level playing field and set- up the basements of reciprocity between the two first markets.

18) How can the ESAs further contribute to ensuring consumer and investor protection?

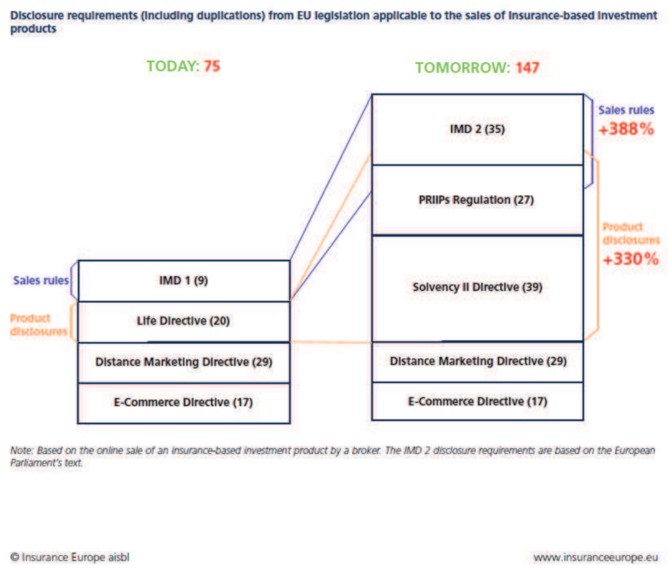
Current investor protection provisions within the European Union financial landscape

The current regulatory framework encompasses numerous investor protection provisions, which embrace most challenges to the investor/ consumer protection that were identified in the aftermath of the financial crisis.

The rules that have been enacted, with regards to the protection of the investor/consumer are in particular MiFID2, the proposal for IMD2, PRIIPS, the Payment Services Directive, the Credit Mortgage Directive, and Solvency 2. Amongst these pieces of legislation/ regulation, MiFID 2 is considered a cornerstone for the protection of investors in financial products. Other regulations such as Solvency 2 and IMD2, are similarly enhancing considerably the protection of consumers of insurance products.

At the same time, however, it is necessary to avoid a cumulative effect and duplication of requirements. For example[3], the amount of pre contractual information that insurers will be required to provide to consumers will dramatically increase: currently a consumer purchasing an insurance-based investment product online from a broker must be provided with 75 different pieces of pre-contractual information under existing EU legislation. With PRIIPs, Solvency II and the European Commission's proposal for the IMD2, consumers will end up being provided with 147 different pieces of pre-contractual information (see figure below). This is far from the "smart regulation" wanted by the European Commission.

[3] See Insurance Europe : "ensuring consumers are appropriately informed"
http://www.insuranceeurope.eu/uploads/Modules/Publications/insight-briefing---information-overload.pdf



In this particular context, a few questions are currently pending with regards to the potential role and the relevance of the ESAs as to consumer and investor protection

A call for minimum investor/consumer protection standards

Considering the investor protection objective granted to ESAs and taking into account the large number of investor/consumer provisions, it can be envisaged that ESAs could contribute to ensuring consumer and investor protection by advancing the codification[4] of consumer and investor protection rules

This CMU consultation could be a springboard to the creation of a concise and comprehensive corpus of rules relating to the consumer/ investor protection, which would nurture our progress in this domain and strengthen it. The review of the New European System of Financial Supervision (Part 1) took the lead of this proposal, by suggesting a codification of rules composed of a Prudential Code and a Consumer/Investor Code[5]. The single rulebook could therefore include for instance general provisions on:

- The prevention and management of conflicts of interests
- Inducements (prohibition and restrictions of inducements)
- Common information standards given to investors/ consumers
- The suitability and appropriateness tests
- The cross-selling of products
- Acting in the best interests of clients

However, codification should be appropriate to each type of investor, product, sector and actor. The market structures and product characteristics make it more suitable that some specific sectorial requirements are set out in sectorial bodies of rules or that the single Rulebook provides for exceptions according to the specificities of the sector.

Positive effects of codification

[4] Review of the New European System of Financial Supervision (ESFS): Part 1, A structured Single Rulebook (page 15)
[5] Paragraph 22, page 120, Review of the New European System of Financial Supervision (ESFS)

The implementation of a single Rulebook relating to the protection of investors and consumers could lead to positive consequences and repercussions. Codification could contribute to the increased effectiveness of markets, because of the simplification of the legislation, and to a better integration of the market and in consequence strengthen the Single Market. Finally, codification of rules aiming at the protection of investors and consumers could also reinforce the control of actors and therefore lead to better supervision.

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

These past years, a lot has been done at UE level regarding investor protection (MiFID I & II, PRIIPS, IMD2…). An extensive assessment of those regulations should be made against European households behavior regarding their savings. Compared to American households, the European have always had a strong preference for liquid assets. We are of the opinion that many of the requirements included in the aforementioned regulations will not favor the risk appetite essential to long term investment. We strongly oppose against the widely spread idea that complexity is by design associated with risk and is therefore not suitable to retail investors. The latter is basically interested by two key questions: what return can I expect and what are the risks. The options taken by the manufacturer are not essential to the investors. Some complex design may be intended to reduce the risk.

The distribution of financial products is subject to more and more constraints. At the same time, business models are under pressure from legislators and regulators. The pros and cons of such policies should be weighed carefully against the ambition of developing long term investment.

In addition, measures aimed at boosting awareness and education of consumers and also of policy makers should also be undertaken at European level (see our answer to question 32).

We call for a full implementation of the ongoing regulations and recommend that the Commission does not consider any additional rules regarding retail financial products before the impact of the recent requirements have been assessed.

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

French best practice: Euro PP

In France the Euro PP Market in particular has been an initiative of the French Chamber of Commerce and Industry of Paris, the French Central Bank and the Treasury, with the active support of the industry and its professional associations. It has led to the development of a Euro PP Charter, proposing a code of conduct, best practices, and standard documentation for non-listed bonds and a model agreement for loans. Over the last three years, some €10 bn have been issued through Euro PP. But it is important to note that this financing has been raised mainly by fairly consequential mid-size firms, some of which could access the capital markets directly.

EU best practice to enlarge to other sectors: UCITS

The objective of the original UCITS Directive, adopted in 1985, was to allow for open-ended funds investing in transferable securities to be subject to the same regulation in every Member State without further authorization. There are approximately 36 000 UCITS operating accounting for more than €8 trillion assets under management. This success is the result of a cleverly designed framework benefiting for European households. UCITS is also regularly sold to investors outside the EU where they are highly valued due to the high level of investor protection they embody. It is internationally recognised that UCITS is a successful cross-border product (40% are cross-border assets).

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

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

Improving market effectiveness – intermediaries, infrastructures and the broader legal framework

Questions:

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?

Major regulations in the field of the functioning and liquidity of the markets have recently been adopted and/or are in the course of finalisation: EMIR, MIFID II etc. It will be of utmost importance to monitor their forthcoming implementation and draw the appropriate lessons once the market has fully absorbed their impact.

This being said, it shall be highlighted again here that market liquidity is not only crucial on the principle (for the issuers as well as for the investors and not only for the intermediaries) but already strongly weakened by recent prudential regulations.

So high cautiousness is necessary when considering BSR, FTT and NSFR projects in particular to be sure they do not kill the market making capacity in Europe.

It can also be underlined that banks are highly regulated but are not the only market intervenants: it is important that regulators progress to make sure the so-called shadow banking system does not endanger the functioning and liquidity of markets.

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

In recent years, a number of very important elements of post-trade and FMI harmonisation have taken place. Among these, the Settlement Finality Directive (SFD), the Financial Collateral Directive (FCD), EMIR, CSDR as well as market standards on corporate actions and the market standards on general meetings brought important progress.

Furthermore, Target2Securities (T2S) is expected to facilitate cross-border settlement and importantly to minimise the cost differences between a cross-border and a domestic settlement.

T2S will also reduce operational uncertainties in the settlement of cross-border transactions, as well as remove the “cross-border” aspect of settlements between participating CSDs.

Within this context it is important to implement EMIR and CSDR, which is not yet the case. Unanimously (or amost), market participants and associations have expressed concerns about:

- the settlement discipline regime under CSDR that leads to important inefficiencies in the settlement of fixed income and less liquid assets, including SME issued securities;
- the same asset classes are affected by burdensome transparency rules under MiFID 2;

- the capital surchage put on banks that provide banking services to CSDs. For example, where a CSD of one country wishes to offer settlement of securities issued in another country and another currency, such a services is made as good as impossible as no payment bank will be in a position to actually provide such services;

When it comes precisely to those less liquid asset classes, which include SME growth markets, it is particularly important to put in place rules that are adapted to their lower liquidity.

Legal aspects are discussed under question 26 below.

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?

BNP Paribas acknowledges the important work accomplished by the ESAs. ensuring an effective and convergent supervision, preventing regulatory arbitrage and promoting equal conditions of competition throughout Europe.

On an international level, BNP Paribas welcomes the presence of the ESAs, acting alongside other European institutions, in international organisations such as IOSCO. It contributes to better regulation and supervision. Nonetheless, further studies could be undertaken in order to improve the defense of the European financial model in international fora, by ensuring that European representation is always coordinated and consistent to enhance its impact.

BNP Paribas welcomes the transversal approach of the ESAs and the Joint Committee's role. In fact, it is important to have such an approach to clarify and simplify the regulatory and supervisory framework and give some legal visibility to the various stakeholders.
However, in order to develop a capital markets union, the ESA's approach should consider the following points:

- Specific characteristics of different products and sectors.
- Proportionate actions, depending on the level of risks and complexity.
- A global review could be useful to identify the areas where there are regulatory deficiencies or ambiguities, particularly when there are cross-references and interactions between several legal texts. This work could be carried by the Commission with the help of the ESAs, which could bring their expertise and the experience they gained from their supervisory and regulatory roles.
- Carefully align guidelines (in particular cross-sector guidelines) and draft technical standards with level 1 legal texts (notably with their implementing date).

Guidelines can bring clarification and reinforce the consistency of supervision (both at EU and national levels) but they must however be sufficiently adapted to different situations and supplement with value added the level 1 and 2 texts. It seems appropriate to clarify their legal regime. Indeed, even if they are non-binding instruments, they can in practice produce legal effects.
Therefore their use should be restricted to limited cases defined in the regulations in order to clearly precise the legislative powers.

In order to develop a capital markets union and to restore confidence of the various stakeholders, a more effective, transparent and participatory process of ESA public consultations should be implemented. It would also help stabilizing the legal and regulatory framework. In this regard:

- The timeframe for consultations should be lengthened in order to give stakeholders more time to carry out a meaningful impact assessment that is necessary to the adoption to a proportionate and focused regulatory action.
- It would be helpful to have, in addition to the ESAs' working programs, a provisional consultation calendar for stakeholders to anticipate and prepare in advance.

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?

Whilst "securities law" provides for the very existance of securities that are no longer printed in certificated form, it is paramount to stress that the various European legal systems pursue the same objective of investor protection against insolvency, title transfer by debit and credit of securities accounts and ensuring negotiability (thus the concept of Trust in the UK, ownership in France and Italy for example, co-ownership in Germany, Belgium, Netherlands and others).

Legal differences are not a source of legal uncertainty. BNP Paribas Securities Services is an active custodian in as good as all Member States of the European Union and we do not suffer legal uncertainties or other practical differences from different legal regimes within the EU. The high-level explanation that we have for this is that all legal systems pursue the same economic objective.

Changing ownership rules in securities touches upon a vast range of other legal aspects and can be a source of legal uncertainty. For example, the fact that the Bank of England takes collateral by control agreement and the Banque de France by title transfer arrangements are both legally efficient. Introducing questions of priority and ranking between control agreements and title transfer arrangements causes lenghty and sterile legal discussions.

We are therefore not in favour of any changes to the securities ownership rules. It is important to take stock of the important changes that have been initiated and not yet entirely implemented (cf. question 24 above).

However, we do favour an approach where the factual situation of account holders and account providers is made clearer through regulation, but without touching upon securities legislation.

As part of changes that would be welcome, the upcoming Regulation on the transparency of securities financing transactions (SFTR) is expected to greatly clarify how ownership in securities materialises, i.e. through a credit of securities to securities accounts.
There still is residual place for improvements, namely by providing that:

- As a general rule, the credit of securities to a securities account corresponds to the title of the account holder in the securities or holding of those securities for the account holder's clients. As currently under discussion, such a rule is foreseen only in respect of re-used collateral in SFTR (art. 15.2);
- As a general rule, the law applicable to securities credited to a securities account is the law of the country where the relevant account is located. This rule is currently provided for in the SFD, the FCD and the Winding-Up Directive. It was discussed in the legislative process of CSDR. Although, not many (if any at all) cases of uncertainty have arisen around this question, other than in the field of collateral, a general conflict of law rule would be welcomed;
- In the case of an intermediary's (account provider) insolvency:
    - Account holders do not compete with any of the insolvent intermediary's creditors,

- Account holders may instruct the insolvency administrator to transfer the securities to another securities account held with another intermediary and
    - In case of securities shortfall, the intermediary's proprietary securities are in priority affected to the insolvent intermediary's clients that suffer from the shortfall.
- Title transfer takes place at the moment of settlement in the securities settlement system or, alternatively, at the moment to transferee's securities account is credited;
- Intermediaries must on a continuing basis reconcile the securities positions they hold for clients with the amount of securities held upper-tier (with another intermediary or with a CSD). This corresponds to art. 37 of the CSD Regulation.

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?

There are three areas where specific measures could be undertaken to address issues affecting the cross-border flow of collateral in Europe:

1 Resolving issues regarding the use of credit claims as collateral:
Collateral can inter alia be in the form of claims (receivables). The use of credit claims as collateral may be implemented by pledge or assignment (security over lender's right). However, as soon as there are different jurisdictions and governing laws involved, the constitution of a collateral security over credit claims may become a complex matter and raises international private law issues. In international private law, a pledge or a transfer present an element of foreign origin as soon as the pledgor/ transferor, the pledgee/ transferee or the debtor are not located in the same country. Due to this element of foreign origin, it is necessary to determine the conflict of law rules applicable to (i) the relationship between the pledgor/ transferor and the pledgee/ transferee, (ii) the relationship between the pledgor/ transferor and the debtor, (iii) the enforcement of the pledge/ transfer towards third parties.

These issues are not insurmountable, however they are often complex and, need to be analysed, assessed (in term of legal risks) and resolved (administrative rules, such as notification and registration obligations) leading to less efficient cross border collateral mechanisms[6]. Therefore, we consider there are significant gaps or lack of harmonisation in the European legislation, which are tend to weaken the use of all collateral within the framework of cross-border transactions.

These obstacles are in addition to the fact that the contractual documentation relating to the receivables intended to be subject to the collateral security may contain restrictions on the right of a

[6] For instance, we note that Regulation (EC) no. 593/2008 of the European Parliament and of the Council dated 17 June 2008 on the law applicable to contractual obligations ("Rome Regulation") is silent as to the binding effect of a pledge or a transfer against third parties, and the conflict of law rule of the Financial Collateral Directive concerns only assets credited to securities accounts, thus not claims. This issue is of utmost importance in case the pledgor/ transferor is the subject of bankruptcy proceedings where the pledge or transfer have to be recognised as such by the bankruptcy administrator and by all creditors of the pledgor/ transferor in order to become enforceable. Consequently, the binding effect of a collateral security in credit claims would have to be assessed in accordance with the conflict of law rules determined by the courts of each jurisdiction. The conflict of law rules depend greatly on the law/ case law of the Court hearing the case, which results in a high level of uncertainty.

We also note that, pursuant to article 14 of the Rome Regulation, the relationship between a pledgee or a transferee and the debtor of a claim over which the relevant pledge has been created or which has been transferred, the conditions under which such pledge or transfer can be invoked against such debtor and whether its obligations have been discharged are governed by the law governing such claim.

lender to transfer or create a security interest over such receivables. Subsequently, the creation of the collateral security in credit claims requires the completion of a preliminary legal analysis of contractual documentation in order to identify any contractual constraints which may need to be complied with, such as, requesting the consent of the underlying debtor and/or guarantor(s), or delivering an information notice.

In order to facilitate the use of eligible collateral consisting of credit claims, it is important to eliminate any administrative requirements, such as notification and registration obligations, that would make the pledge or transfer of credit claims impracticable. Similarly, in order not to compromise the position of collateral takers, debtors should be able to validly waive their set-off rights vis-à-vis creditors. The same rationale should also apply to the need to introduce the possibility for the debtor to waive bank secrecy rules, because otherwise the collateral taker may have insufficient information with which to properly assess the value of the underlying credit claims. In the same way, debtors should be given the possibility to waive bank secrecy rules which could otherwise hinder the collateral taker's access to sufficient information with which to properly assess the value of the underlying credit claims.

These were the aims of two main EU Directives. However, these Directives are not applicable for all collateral and between all parties since they have a limited purpose (please refer to (ii) below). The European framework for the provision of collateral on a cross border basis was substantially improved and harmonised through the implementation of Directive 2002/47/EC on Financial Collateral Arrangements in member states, which removed many major obstacles for cross border use of collateral, envisaged clear, effective and simple regimes for financial collateral arrangements, and sought to limit administrative burdens on the creation and enforcement of collateral (the "**Collateral Directive**"). Directive 2009/44/EC of the Parliament and of the Council of 6 May 2009 then further amended the Collateral Directive, as well as Directive 98/26/EC on "settlement finality in payment and securities settlement systems" (the "**SFD Directive**"). The main aims of this 2009 amendment were to enable the use of credit claims as eligible collateral in the Eurosystem (in addition to cash and securities) under the Collateral Directive and to provide for the introduction of interoperable systems (clearing, payment or settlement systems which link with each other) into the scope of the SFD Directive.

If the use of credit claims as collateral were to be further facilitated, consumers and debtors would also benefit, as the use of credit claims as collateral could ultimately lead to more intense competition and better availability of credit, and increase the pool of available collateral.

The Collateral Directive was to create a uniform community legal framework for the cross-border use of financial collateral and thus abolish most of the formal requirements traditionally imposed on collateral arrangements. The use of credit claims should have increased the pool of available collateral.

2- <u>Extending and clarifying the application of the Collateral Directive</u>:

From the perspective of a financial institution, there is a willingness to carry out business on a cross border basis with a variety of counterparts, including non-financial institutions. Corporates in a number of jurisdictions may also wish to enter into collateralisation arrangements with other non-financial institutions. With reference to the opt-out available in Article 1(3) of the Collateral Directive (arrangements where one party is an unincorporated firms or partnership), we note that whilst no member states have currently applied the full opt-out, a number have applied a partial opt-out, eg, by limiting the scope of the Collateral Directive to arrangements where one party is a financial institution or similar regulated entity (in keeping with the spirit of Article 1(2)(e) of the Collateral Directive), such as France, Germany, Greece, Cyprus or Italy. Others have introduced nuanced limitations (for example the Slovenian implementation excludes companies which are not defined as "large corporates" under Slovenian commercial company legislation). Certain jurisdictions have extended the scope of application to a wider group than that foreseen by the Collateral Directive. This means that continued due diligence is necessary on a case by case basis to ensure that a collateral agreement with a given counterparty type is able to benefit from the Collateral directive regime, as long as such opt-out provisions exist. The personal scope of application should be harmonised and ideally any opt-out should not exist, or be limited.

3- MIFID II – title transfer collateral arrangements with retail clients:

As regards the Investor Protection related provisions of MIFID II; we note Recitals 52 and Article 16(10) provide that investment firms shall not conclude title transfer collateral arrangements with retail clients for the purpose of securing or covering present or future, actual or contingent or prospective obligations of clients. This potentially restricts the scope of small and medium sized companies to access the title transfer collateral markets as regards derivative transactions.

As regards close-out netting arrangements:

Close out netting is an important counterparty risk mitigant and contributes to the reduction of settlement and liquidity risk.

Article 7 of the Collateral Directive requires member states to ensure that close-out netting can take effect in accordance with its terms, but does not provide any guidance to member states as to the principles that should underlie the close out netting regime (or provide for the direct implementation of a close out netting regime). Close out netting itself therefore generally needs to be dealt with in separate legislation. Experience has shown that a number of European jurisdictions have implemented netting legislation in a manner which raises a number of issues or grey areas, or alternatively have not implemented it at all, meaning that to examine the enforceability of netting for counterparties in such jurisdictions, we may only rely on the Collateral Directive (which they have implemented), which cannot be considered to constitute comprehensive netting legislation in its own right (for example, Croatia). Close out netting may therefore not be considered fully enforceable vis à vis counterparties in such jurisdictions, or only enforceable as against those which have also entered into a collateral arrangement.

We are aware that ISDA leads a number of initiatives together with local regulators and local counsel in various emerging market jurisdictions where no netting legislation exists, to encourage the implementation of efficient close out netting legislation, based on ISDA's model netting act provisions. We fully support these efforts and regret that not all jurisdictions have implemented comprehensive close-out netting legislation providing for a clear carve-out from any cherry picking rights under the existing insolvency regime (for example, Bulgaria, Romania) despite having implemented the Collateral Directive upon joining the EU.

We therefore consider there is scope for improving the legal framework relating to the cross border flow of collateral and close out netting arrangements. This is however a complex exercise impacting key legislation (insolvency, security regimes, conflict of interest) on a national and European level.

It should also be borne in mind that reforms in relation to the derivatives market in particular should not limit or unnecessarily restrain liquidity (see answers to Question 23), which would in itself hinder the availability and flow of collateral generally. In this respect and in relation to EMIR in particular, we note as regards the requirements for margining of non-cleared derivatives that the draft RTS in relation to margining of uncleared derivatives already limit the re-hypothecation of initial margin in line with BCBS/IOSCO recommendations. It should now be ensured, in line with the various comments made by market participants generally, that the rules are implemented in a coherent and workable manner and according to a realistic timetable, in order to avoid market disruption generally. In this respect we note that for the margining obligation, revised draft RTS should be published sooner rather than later (hence any further consultation completed as soon as possible) in order that parties can fully benefit from the time afforded by the revised implementation date proposed by BCBS/IOSCO (from 1st December 2015 to 1st September 2016).

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?

1. **Corporate governance**

We consider that it is important to link long term shareholder engagements with efficient corporate governance. Indeed, shareholders engaged in long-term perspective will be more sensitive to corporate governance issues within the company.

Recently, many European initiatives have been launched regarding corporate governance and corporate law (ex: The revision of the shareholder rights directive and for banks, CRD IV and MIFID2). Among other things, these initiatives are intended to comfort investors. For instance, the role of the management body in banks has been strengthened which is very positive.

Nevertheless, in practice, these initiatives should not have anti-competitive effects. For instance, it seems that, at the European level, the trend is to require more and more shareholders votes on decisions that would, under national law, be under the management's competence. We think that such a trend can entail problematic issues for companies which may need rapid decision-making for business reasons.

Moreover, the risk is to heavily complicate the life of a company and put European companies in an anti-competitive position. We nonetheless think that informing shareholders is very important and that it should be the preferred way to improve governance in that respect.

Here it should be recalled that the respective roles and missions of the general meeting, the board of directors and the executive management are clearly defined in national laws. Moreover, shareholders have already an opportunity of voting against any resolutions which fall under their competence (power of nomination/revocation of board members if for instance they do not agree with the strategy of the company; possibility to submit draft resolutions…).

2. **Corporate law**

There are two main obstacles which companies have to face in their cross-border mobility and restructurings. First, any cross-border restructuring within the Union includes a negotiation process around employees' participations, even when the company to be merged does not have employees. The process includes the formation of the Special Negotiation Body (SNB) with the employees' representatives through a complex set-up procedure that has no relevance when only the surviving company has employees. There should be an exception to the set-up of the SNB when the merged company does not have any employee between the publication of the merger documents and the effective date of merger.

Furthermore, the European Company, designed to allow a company based in the EU to move the place of incorporation from one member state to another, does not fulfill its role efficiently: the

European company may transfer its registered office within the Union from one member state to another. Such transfer requires however the drawing up of a transfer proposal, a report justifying the legal and economic aspects of the transfer and the issuing, by the competent authority in the member state of registration, of a certificate attesting the completion of the required acts and formalities. To facilitate the cross-border movements of companies within the EU, the process of creation of a European company and its transfer from one member state to another should be simplified.

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

The emergence of a pan-European capital market implies a necessary degree of predictability and certainty. As highlighted in the Commission Recommendation of 12 March 2014[7] "differences between domestic insolvency laws may hamper the establishment of an efficient internal market", and therefore discourage the timely restructuring of viable companies in financial difficulties and often lead to liquidation rather than providing the ability to restructure as an ongoing concern. The high restructuring costs for small and medium size companies and the lack of transparency regarding their solvability for investors constitute the main obstacles to the emergence of a European "CMU".

While progress has been made on the harmonization of conflict of laws rules throughout the forthcoming adoption of the EC Insolvency Regulation recast, a full harmonization of the substantial insolvency laws amongst Member States seems unlikely due to its complexity. Reaching a consensus among member states on a set of principles and/or best practices generally accepted would be a more efficient way of providing the UE with a non-binding regulatory framework on insolvency, thereby preventing detrimental discrepancies between domestic laws.

To achieve that goal, several proposals might be suggested:

- More predictability and transparency with respect to the companies' solvability could be obtained by:
    - The implementation of a centralized European e-justice Portal linking publically accessible electronic register, in which information concerning domestic and cross-border ongoing company insolvency proceedings would be available for investors;
    - For investors to fully understand the accurate state of an enterprise, the creation of a harmonized and standardized terminology should be considered. This would contribute to create a level playing field as to the meaning of the various insolvency procedural steps across Member States.

- Further harmonization is needed regarding preventive restructuring proceedings so as to change the global perception of insolvency proceedings and avoid the stigma attached to insolvency, which is generally seen as a preventable failure.
    - Promote early negotiations led in good faith between creditors and debtors through out-of-court and hybrid procedures with a view to mitigate the role of courts in the proceedings, thereby reducing the procedural costs for SMEs and its negative impact;
        - <u>Ex:</u> The Company Voluntary Arrangements (CVA) in the UK whereby a restructuring proposal can be brokered by the company through a voting mechanism.

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[7] "Commission Recommendation on a new approach to business failure and insolvency", 12 March 2014, C(2014).

    - Soften the proceedings initiation conditions by encouraging debtors to voluntarily introduce restructuring proceedings.
        - Ex: Chapter 11 of the US insolvency law which provides for voluntary or involuntary procedure initiation.

- Simplify and clarify the insolvency procedure.
    - Harmonizing the various procedural periods in order to enhance the predictability needed by investors, especially with respect to stays and discharged periods;
    - Setting up standards on the possibility for a minority of creditors to be bound by the restructuring plan voted by the majority of creditors.

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?

Removing withholding taxes

Withholding taxes on interests and dividends paid to residents of other member states of EU create barriers to cross- border flows between Member States and a segmentation of Europe's Internal Market. A removal of withholding taxes on dividends and interests would facilitate intra-Union trade and the creation of an efficient CMU.

Improving the access to tax treaties' benefits

Double taxation is an obstacle to cross border flows. Despite the Tax treaties which aim to eliminate the double taxation, this latter remains a concern for taxpayers. This is because the eligibility to tax treaties benefits is complex. It is often complex and costly for an investor to obtain the tax relief that he is legally entitled. This leads to disincentive cross-border investment in capital markets. Moreover, the procedures put in place in order to obtain the reimboursment of withholding taxes can be long, costly and with administrative and practical obstacles.

In order to improve the access to tax treaties' benefits, to eliminate double taxation, and thus to facilitate non-residents investments:

- the tax authorities should provide sufficient guidance to ease treaty access to foreign investors, with simpler rules,
- it should be adopted within the EU simplified relief at source procedures,
- the EU members States should put in place rationalized, efficient and simple procedures to reclaim excessive whithholding taxes in accordance to tax treaties.

Thin capitalisation rules and debt financing

Banks must comply with a set of binding rules, mainly provided by Basel III, Banks should be excluded from any tax measures which may interfere with these regulatory rules, and may disrupt their aim. In particular, the Banks should be excluded from any measure to restrict interest deduction

Improving the EU VAT system

The lack of harmonization of EU VAt system, creates tax inefficiencies and discreppancies that impact the intra-Group flows. In the area of financial services, it prevents efficient implementation of a single European market. In order to improve VAT system, the administrative burden on economic operators should be reduced. In order to harmonize the EU VAT system, EU should develop a doctrine whith common definitions

Creating a tax-attractive environment in the EU

It is essential to create a tax-attractive environment in the EU, which means stable, simple and non burdensome tax rules. Generally speaking, stable tax rules are important so that the economic actors can invest in an environment ensuring a legal security.

Avoiding a Tax on Financial Transactions

As explained in our response to question 6, the FTT would have very negative consequences for the development of CMU and to the integration of capital markets in Europe.

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?

New technologies are changing in many ways how business is done in finance. Through analytics and predictive modelling, new technology enables to analyse, explain, anticipate clients or market trends. It can also be applied from capital markets to credit scoring, regulatory stress testing, etc… They can provide enhanced structural hardware infrastructures modifying and improving operating processes such as cybersecurity, trade matching, clearing houses, Know Your Client procedures… Technologies finally tend to challenge traditional bank business models with new technology favoring disintermediation of financial services through credit (P2P lending) and trading platforms as well as new currency and payment platforms that develop away from traditional banking infrastructures.

Initiatives from financial industry to develop incubators / accelerator programs or to create in-house or external venture capital funds dedicated to Fintech need to be encouraged. Activities that are developed away from the banking system but perform the same functions as banks should be carefully monitored in order to develop a regulatory framework that is preventing systemic risk and malfunctioning of the financial system. Regulators, academia and financial institutions need to work together in partnerships in order to develop ecosystems where new disruptive technology developments can be tested, understood and efficiently nurtured for the benefit of improving the functioning of financial system while reducing the costs and risks associated with financial transactions.

The EU should ensure that “laboratories” and ecosystems in the Fintech sector develop within different member states, by favoring the development of multiple clusters spread within the EU territory, in order to take advantage of the centers of excellence that already exist in member states (prestigious academia, engineer schools, leading financial institutions, etc…), benefit from the diversity of talents and take advantage of the proximity of leading institutions in banking, asset management, insurance, etc… The regulatory framework should be appropriate in order to attract and develop long-term commitment from EU investors but also from institutionals outside the EU. Regulators should also participate actively in the ecosystem in order to understand new disruptive developments, identify and prevent potential risks related to continuing changing technology such as fraud and cybercrime.

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?

Financial literacy has been increasingly considered by policy and decision makers as a life skill of the 21st century necessary to enable individuals to achieve a long term financing of the economy. The importance of financial education has also been recognised at the highest policy level by G20 Leaders as a complement to financial consumer protection and inclusion with a view to achieving financial stability.

Prior to the 1980s, Social Security and employer-sponsored defined benefit (DB) pension plans were the primary sources to support retirement. Today employers, and therefore employees, are increasingly turning to defined contribution (DC) plans and Individual Retirement Accounts. The transition to the DC retirement saving model has the advantage of permitting more worker flexibility and labour mobility than in the past, yet it also imposes on employees a greater personal responsibility to save, invest, and accumulate retirement wealth sensibly. Furthermore, the spread of DC plans means that workers today are directly and immediately exposed to financial market risks.

The focus on individuals and households' long-term saving is deemed essential to balance the lack of saving and in some countries mounting debts' levels of governments and corporations. At the same time, investment in specific types of assets and in the real economy is more and more important to help sustaining economic activities as well as the strengthening infrastructure and deepening research in innovative areas.

Research has clearly identified the pressing need for greater financial literacy, but the challenge is not yet being met. A review of studies and surveys in the United States and other countries shows that the level of financial literacy among the population is very low. Moreover, financial literacy does not seem to be improving over time. Financial illiteracy is both widespread and particularly severe among specific demographic groups. This has consequences for both individuals and society as a whole because financial literacy plays an important role in financial decisions.

Financial consumer protection should be reinforced with investor education policies. Such initiatives need to be embraced by Public authorities, industry associations and investment advisors/managers. The public authorities have a leading role to promote investor education, especially in school. The authorities can rely on industry associations to co-ordinate common actions. Investment advisors/managers understand that promoting investor education is a component of their social responsibility and that they can bring useful contribution to investor education initiatives.

Derivatives and CMU

The green paper does not adequately address the essential role that derivatives play in global capital markets. Derivatives are critical for many of the stated objectives of the CMU project, from revitalizing the securitization market in Europe, to attracting additional financing for infrastructure, or making Europe a more attractive market for international investors.

In this respect derivatives are key for the various types of market participants to mitigate their specific risks as to interest rate, foreign exchange, inflation, credit risk etc.:

1. the investor looking for safe and stable returns on his investment;
2. the issuer looking to optimize his funding levels and better match investor's preferences; and
3. the market maker looking to hedge risk when assuring secondary market liquidity in financial instruments.

We would therefore urge the Commission to carefully calibrate all pending regulation such as transparency matters under MiFID II and initial margins under EMIR, to make sure that derivative markets can continue to function in an effective and cost-efficient way. We would also call for further exploring new initiatives that could improve the functioning of derivatives markets in Europe as a main component of the CMU project.

Annex:

Recommendations on the regulation of crowdfunding platforms (in reference to question 9)

A distinction between crowdfunding models based on donations, non-monetary rewards or lending on one hand, from crowdfunding based on investment on the other hand could be made.

Within Crowdfunding models based on investments, an option could be given to allow Investment-based platforms to choose between the status of Investment Firm or a dedicated legal status.

An Investment-based platform having the authorization to operate as an investment firm constitutes an essential guarantee to ensure the protection of investors in case of platform failure. Indeed, an Investment-based platform having the authorization to operate as an investment firm should be registered in public and official register, have organizational arrangements in place and respect minimum capital requirements, and obtain the approval of the competent prudential authority.

In addition, a crowdfunding platform which has obtained an authorisation to provide investment advice services will have to comply with the suitability test that will permit it to assess whether the projects meet the investment objectives of the investor or not.

Furthermore, an Investment-based platform having the authorization to operate as an investment firm will benefit from European Passport and, depending on a pre-defined minimum share capital, be allowed to receive funds collected from investors.

Conversely, an Investment-based platform which is not qualified as an Investment firm does not offer the same guarantee of protection to investors and should therefore be required to comply with a set of specific rules. For this purpose, specific legal status, minimum capital requirements, prohibition to receive the funds collected from investors could be established.

In order to address risk of bad advice, Crowdfunding platforms which are not qualified as Investment firms could also be required to select projects on the basis of pre-defined and transparent criteria, to comply with the rules regarding the suitability/appropriateness test and to assess whether the projects meet the investor’s investment objectives. Furthermore, a common approach on information disclosure could be adopted.

Finally, an Investment-based platform which is not qualified as an Investment Firm should not benefit from the European passport.

It should also be noted that (i) the legal framework and the scope of public offers of securities should be adapted (specific thresholds dedicated to financial instruments subscribed via an Investment-based platform for the issuance of a prospectus), (ii) Investment-based platforms must be included in the scope of anti-Money Laundering Directive.

The principle to act at all times in the best interest of the investors should be applied to investment-based platform.

Within Crowdfunding models based on Lending-based platforms

- In order to develop appropriately regulated crowdfunding platforms, categories of lenders and borrowers could be established and specific criteria for categorisation have to be considered.

- Individuals who are acting for purposes which are outside their profession could be allowed to provide remunerated loans to project owners seeking finance. The other lenders could only be allowed to provide non-remunerated loans.

- In order to ensure the protection of borrowers, lending-based platforms should have specific legal status, be registered and be subject to supervision and/or oversight by a national competent authority. In addition, lending-based platforms could ensure that lenders are aware of the potential risks of crowdfunding operations. A common approach in information disclosure may encourage crowdfunding activities regarding costs, risks, projects, conflict of interests…
  Capital, organizational and conduct of business requirements shall also apply to lending-based platforms. Lending-based platforms must be included in the scope of anti-Money Laundering Directive. Lenders could only be permitted to lend a maximum amount per project, within a certain period of time. Furthermore, the project owner seeking finance could only be allowed to borrow a maximum amount per project.

- Finally, when a lending-based platform is a Payment service provider, rules governing Payment service providers should be applied.

Within Crowdfunding models based on donations or rewards

- Donations-based platforms or rewards-based ones could be allowed not to have specific legal status or not being submitted to specific requirements regarding their organization, capital and conduct of business.