Finance Watch welcomes the opportunity to review the European System of Financial Supervision (ESFS). We consider the system of supervision to be a key driver in ensuring the financial stability and good functioning of the EU markets. In order to ensure that the European financial system operates in a way that protects consumers, investors and taxpayers we need strong European supervisory authorities that are appropriate staffed, financed and given strong mandates.

However, we are disappointed that there is a lack of ambition in the Commission proposal. Following the public consultation on the review, Finance Watch believed that the Commission was planning a significant change to the operation of the European Supervisory Authorities (ESAs). Instead, the proposal leaves the fundamental structures of the ESAs unchanged. The lack of ambition in the current proposal means that there is a need to consider a deeper review in the future. Any such review should also be based on the input of experts who have deeply considered the structure of the ESFS. The current proposal is largely based on responses to a series of public consultations. The lack of expert input leaves the proposal open to undue influence of stakeholders who may have vested interests shaping how the system is constructed. Finance Watch is concerned that this allows the industry to write its own rules. Therefore, we would like to see a revival of the High-Level Expert Group on financial supervision to inform a future review.

This blueprint sets out the features that Finance Watch would like to see from a ESFS that serves the needs of European society.

A system that works for consumers

Finance Watch believes that ensuring proper consumer protection across the Union is incredibly important. Consumers are increasingly affected both by the impacts of new product designs and distribution practices, but also by the effect that these changes have on the overall financial system through increased complexity in the market place. Enhanced consumer protection is vital to preserve consumer welfare in these increasingly complex markets, where decision making can become more difficult and the consequences of poor decisions can be great. Ensuring better consumer and investor protection at the European level is also needed if we are to continue with developing capital markets in Europe including engaging more retail investors and creating cross boarder financial products for retail consumers.

Therefore, we would like to see an enhanced role for the ESAs in the area of consumer protection. We believe that the ESAs should have a role in promoting a convergence in the application of conduct of business rules in order to ensure all financial service users are treated fairly across the Union. This should include the development of binding technical standards on conduct of business, and the power to coordinate enforcement actions on the basis of those standards. In order to ensure that these consumer protection objectives are met, the ESAs must dedicate proper resources to them. We suggest that at least 20% of the authorities’ budgets are dedicated to consumer protection issues.

We would also like to see the ESAs’ ability to prohibit financial activities extended to include cases where the financial activity leads to consumer detriment. We believe it is as important to empower the ESAs to act in cases where consumers in the EU are at the risk of potential detriment as it is to allow them to act to protect financial stability. Preventing widespread consumer detriment is important to ensuring a well-functioning, integrated European financial system.
A system that addresses systemic risk

Finance Watch believes that the active role of the ESAs, as well as the development of the Single Supervisory Mechanism under the European Central Bank has led to a lot of progress in the harmonisation of micro-prudential supervision in the Union. However, there remains a gap on the side of macro-prudential supervision. Finance Watch would like to see a much stronger role for the ESRB as an authority.

We believe that the ESRB should have a coordinating role to ensure a more consistent application of macro-prudential tools across Member States. In particular, the designation of Other Systemically Important Institutions (O-SIIs) remains at the discretion of the National Competent Authorities (NCAs). Despite the EBA guidelines on the designation of O-SIIs there remain significant national differences in the risk assessment on the systemic importance of these institutions. These differences can also be seen in the application of the countercyclical capital buffer and the systemic risk buffer. A robust approach to systemic risk in the Union implies a more consistent and harmonised approach than currently exists.

In light of this, Finance Watch believes there is a role for the ESRB to act as a coordinating authority with regards to macro-prudential tools. We believe the ESRB should therefore be empowered to monitor the use of macro-prudential tools across Member States, and to intervene in cases where their analysis suggests a misuse of these tools.

A system that serves all stakeholders

Finance Watch is also concerned about the influence that industry stakeholders have over the rules they are subject to. A clear example of this is the composition and power of the ESA stakeholder groups. Finance Watch has long recognised the difficulties non-industry stakeholders have in participating in the ESAs’ stakeholder groups, not least because their financial resources are much lower than that of the industry lobby. We believe it is very important that the feedback received by the ESAs from these stakeholder groups represents a balanced view that represents the views of all affected parties. Understanding the impact on financial consumers and end-users is very important for the ESAs’ work.

Finance Watch notes that the rules on the composition of ESA stakeholder groups state that they should be composed in “balanced proportions” between industry, their employees’ representatives as well as academics, consumers, users of financial services and representatives of SMEs. However, there is also a requirement that at least 10 members represent the financial industry. This means that the industry remains over-represented compared to other groups. Therefore, Finance Watch would like to see changes to the proposal that promotes the inclusion of non-industry participants in these stakeholder groups – in particular to ensure that for every financial industry participant there is an equivalent participant representing the views of financial consumers and end-users. Without a truly balance composition, these group run the risk of once again allowing the industry to write its own rules by influencing the direction that the ESAs take in their work.

Finance Watch is particularly concerned with the new proposal that to give the power to the stakeholders groups to challenge the ESAs guidelines and recommendations where two thirds of the group agree. In the first instance, Finance Watch does not believe that this power is in line with the mandate of the stakeholder groups; their purpose is to provide feedback on the ESAs’ regulatory work and to act as an advisory group. This power is also problematic given the current composition of the stakeholder groups, as the two-thirds majority means that even if all 5 consumer representatives object to the reasoned opinion, they can be overruled. Nevertheless, even if the composition of these groups improve, Finance Watch cannot support this new power as we believe it oversteps the competences of the stakeholder group.
A system that works cross-border

Finance Watch believes the **ESAs have a role to play in resolving cross-border disputes**, a fact which has also been recognised by the Parliament. However, in order to do this the authorities’ toolkit must be strengthened. In tackling these cases, EIOPA has established collaboration platforms to facilitate exchanges between the national competent authorities involved. Finance Watch believes these are useful structures and they should be formalised under the coordination function of the ESAs.

A system that is sustainable

Finance Watch believes that it is important for regulators and supervisors to need to consider **the purpose of finance that goes beyond prudential supervision and consumer protection**. In particular, there should be a role for the ESAs to support the European Commission initiative under the CMU to properly consider environmental, social and governance (ESG) factors in financial services legislation. We recognise that the Commission proposal includes an amendment that requires the ESAs to take account of ESG factors when performing their tasks, however Finance Watch believes that the ESAs should take a stronger role in this area. The ESAs are uniquely positioned to be able to take a European view on how ESG considerations are treated in across the Union.

To this end, Finance Watch would support a **clear mandate for the ESAs to conduct analysis on a European-wide basis of ESG factors**. This would include producing a report on ESG factors, to take account of NCA enforcement of requirements related to ESG included in existing and future EU financial services legislation. The ESAs should also have the power to issue opinions to identify and propose areas where ESG factors can be better taken in account in EU financial services legislation. These opinions should be submitted to both the EU institutions and the new European Observatory being proposed by the HLEG on sustainable finance. Overall, we believe the ESAs should be able to use its powers to address ESG factors themselves, not just as a consequence of its other tasks.