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Enhancements to the EU equivalence framework

Effective cross-border regulation and supervision is an essential prerequisite for the development of strong, efficient and safe global financial markets. In this regard, open access to financial markets needs to go hand-in-hand with an effective supervisory toolbox for authorities, in both home and host jurisdictions.

The financial market regulatory framework in the European Union (EU) offers market access by market participants from third countries based on equivalence and recognition regimes. While not available to all sectors, these regimes still constitute, from a global perspective, the most extensive application of the “deference” principle agreed back in 2013 by the G20.

Internationally active market participants have benefitted in the past years from the aforementioned European approach, and market fragmentation has been kept limited in areas such as securities trading and clearing.

With the United Kingdom leaving the EU, which has Europe’s largest capital market, the EU needed to accelerate the improvement of third-country arrangements as they were designed many years ago. In January 2020, a number of important changes in the EU equivalence and recognition frameworks became applicable, without, however, changing the main underlying principles of these frameworks.

Firstly, ESMA will continue to play an advisory role to the European Commission regarding the assessment of non-EU regulatory and supervisory frameworks in order to facilitate equivalence determinations. In addition, ESMA will take up the important task of monitoring relevant developments in those areas and jurisdictions where equivalence has been declared. To this end, ESMA will strengthen its ongoing cooperation with non-EU regulators and seek to better understand their domestic frameworks as well as their effectiveness. The revised ESMA Regulation requires ESMA to report on its monitoring activities to the European Institutions on an annual basis.

Secondly, in relation to CCPs, the EU introduced a more proportionate framework for the recognition and supervision of non-EU market participants. In particular, EMIR 2.2 sets out an enhanced recognition regime for systemically important third-country CCPs, whereby such CCPs will have to comply with EMIR requirements and be subject to certain supervisory powers of ESMA’s. The current arrangement with ESMA’s full reliance on non-EU supervision will continue to apply with regards to all non-systemic third-country CCPs. The final legal framework allowing ESMA to distinguish between sys-

temically important and non-systemic CCPs has however yet to be established.

Thirdly, enhancements were also introduced regarding non-EU Investment Firms (under the Investment Firms Review legislation), and here ESMA will receive improved monitoring and information powers as of mid-2021 in relation to firms from equivalent jurisdictions.

Fourthly, and finally, the revised ESMA Regulation contains a requirement for the European Commission to provide, in due course, a report regarding the need to enhance equivalence arrangements, with a possible supervisory role for ESMA, in relation to non-EU trading venues and CSDs.

Looking at these examples, it is clear that the EU equivalence regimes are changing. On the one hand, the equivalence frameworks will continue to be an important arrangement allowing to avoid market fragmentation while preserving open markets and a level-playing field between global market players active in the EU. On the other hand, a more proportionate approach to systemic and non-systemic non-EU market players is needed, combined with direct supervisory powers at European level, in the interest of EU financial stability and investor protection. ●