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EU auditors call to address essential limitations of ESAs

The EU was plunged into a pool of uncertainty this year with regards to the financial sector as it continues to try and find tools to offset the massive economic fallout of the coronavirus crisis – which could likely require a global effort. The negative impact of the pandemic on the financial markets is evident, pushing to obscure transformations and making future structural changes inevitable (as of now). However, a need for sound supervision will surely stay instrumental, and thus, past lessons in building a harmonized approach to the EU-wide financial sector still need to be learned.

Common rules for the entire EU financial sector, or the single rulebook, are meant to ensure a more effective level playing field and prevent negative cross-border spillovers stemming from possible regulatory arbitrage. However, despite a large number of regulations and directives put in place since 2009, the bulk of direct supervisory controls and enforcement responsibilities still rest with national competent authorities and supervisors. As a result, even with more intensive coordination and approximation of national laws to reinforce the internal market, the rule framework remains fragmented due to different transposition or interpretation of rules, different supervision approaches, and most importantly, very limited EU level enforcement instruments.

So far, all three ESAs acting within their mandates can be praised to have indeed effectively contributed to a smoother functioning Single Market for financial services. At the same time, we can observe that in terms of the types of possible response to various developments in the financial area, the EU is constrained in its competences defined within the Treaties, although notably, EU legislators enjoy ample degree of flexibility in these issues. At present, strong national interest and a legally permissible degree of arbitrage (in setting national regulations, supervisory practices or enforcement approaches) related to the financial sector limit the possibility to take fully effective and proactive measures at EU level, because a difficult consensual approach in many cases has to be applied. Therefore, to overcome persisting strong national borders and to make the single rulebook work, ESAs should evolve from being "de jure" authorities to "de facto".

The mandate and role of ESAs as centralized bodies for capital markets and conduct-of-business supervision were discussed intensively recently. In its audits of EIOPA and EBA, the European Court of Auditors has identified a number of serious, systemic gaps in the supervision of the EU's banking and insurance sectors. In our work, for example, we pointed out a too limited role of ESAs, especially EIOPA and EBA, in supervisory colleges (for cross-border groups). The complicated functioning model of supervisory colleges and even the lack of proper arrangements concerning information exchange could bring about vast inefficiencies.

We called upon EU legislators to adjust accordingly the respective regulations and frameworks. We recommended, among other measures, to rethink both the governance and powers of the ESAs. Of course, another question is what should come first: whether it would be optimal to grant ESAs more powers before fixing identified issues in their governance and resources.

Along with the banking and insurance sectors, we also feel there are similar issues in the area of securities markets, investment funds, etc. Thus, we are about to start an audit of performance of the EU framework for non-bank finance intermediation to be able to provide a more detailed picture of it to EU legislators. ■