

NEW CMU ACTION PLAN: OBJECTIVES, CHALLENGES AND MAIN PROPOSALS

Note written by Marc Truchet, EUROFI

1. Context and objectives of the new CMU action plan

The Commission published in September 2020 a new action plan for completing the Capital Markets Union (CMU), a key initiative launched in 2015 aiming to develop and further integrate capital markets in the EU, in order to diversify the funding of EU enterprises and provide investors with better investment opportunities. These objectives are all the more relevant with the increased funding needed for supporting the post-Covid recovery, the EU Green Deal and digital transformation, which cannot be provided solely through public funds and need mobilising significant private investments.

The new CMU action plan completes two previous action plans, which were adopted in 2015 and 2017 and have been mostly implemented. This new plan has a more specific focus on developing retail investment. It also puts forward stronger ambitions in terms of EU capital markets integration (e.g. addressing controversial fragmentation issues such as insolvency regimes or withholding tax, which hamper cross-border investment), although these latter actions were considered to be more a 'medium term' objective by the Ecofin Council in December 2020. There is also the objective of correcting some existing measures with the improvement of instruments that have not delivered all the benefits expected in the previous stages of the CMU, such as ELTIF funds and STS (simple, transparent and standardised) securitisation and a review of insurance and banking prudential requirements in order to reduce their unintended consequences for long term investment.

2. Proposals of the new CMU action plan and priorities established by the ECOFIN Council

2.1 Proposals and timeframe of the new CMU action plan

Three main objectives were put forward by the Commission in the new CMU action plan (*see detail in Appendix 1*):

1. **Developing retail participation:** financial education, inducements and professional qualification of advisors, pension adequacy;
2. **Fostering a further integration of EU capital markets:** common withholding tax system, minimum harmonisation of insolvency regimes, shareholder rights, settlement services, post-trade consolidated tape (CT), investment protection, supervisory convergence;

3. **Making financing more accessible to European companies in order to support a "green, digital, inclusive and resilient economic recovery":** implementation of a European single access point for corporate information (ESAP), SME listing rules simplification, ELTIF review, prudential requirements review, SME referral scheme, review of the securitisation framework.

These objectives largely build on the proposals of the High Level Forum (HLF), a public / private working group put in place by the Commission at the end of 2019 to make proposals likely to be "game-changers" for relaunching the CMU.

The objective of setting up a CT for equity and equity-like instruments, on which the HLF had not reached a consensus was added by the Commission in the new CMU action plan and was completed at the beginning of 2021¹ by a commitment to set up a bond CT. Some recommendations that the HLF made related to digitalisation (standard contractual clauses for the use of cloud service providers, a harmonised open finance regulatory framework, clarification of the application of existing financial legislation to crypto / digital assets) have not been included in the new CMU action plan, but are being addressed in the context of the Digital Finance Strategy also proposed at the end of 2020.

In terms of implementation, the deadlines fixed by the Commission for achieving the related legislative proposals range over 3 years and several proposals of the new CMU action plan are subject to further assessments due to be conducted in 2021 / 2022.

2.2 Priorities established by the ECOFIN (December 2020)

The December 2020 ECOFIN welcomed the new CMU action plan and considered that the next steps towards a 'genuine CMU' require a clear prioritisation of measures.

A clear priority was put on the third set of measures proposed in the CMU action plan, concerning access to capital, particularly for SMEs, which the ECOFIN has urged the Commission to deliver by the end of 2021.

The development of retail investment and some measures likely to encourage cross-border integration of capital markets within the EU (post-trading and supervisory convergence) were also emphasized as being priorities for the short term.

The second set of actions of the new CMU action plan, designed to foster a further integration of EU capital markets, was given a lower degree of priority and considered more as a medium term objective.

1. Communication on fostering openness, strength and resilience of the EU financial system – January 2021

3. Main challenges facing the CMU

Although the previous action plans have helped to enhance the building blocks of EU capital markets in terms of legislation and products, their effects in the market are largely still to come. This is due in part to the length of the legislative processes needed for putting in place the actions proposed and to a limited political support across the Union so far, for actually making a step change in terms of the development of capital markets in the EU. Another challenge is that no single measure or limited set of priorities seems sufficient for achieving the CMU. CMU is at this stage an evolutionary process addressing a broad range of drivers and building on pre-existing market regulations and market structures, all of which make progress lengthy and complex.

The ECOFIN has taken a different approach to this new action plan, setting short and medium term priorities. It is now essential that the short term actions are implemented in the defined timeframe (by the end of 2021) in order for them to have an impact on the post-Covid recovery, which requires a clear timetable and a strict monitoring of implementation. Further clarity will also be needed on the timetable of the actions concerning retail participation and market integration that have been given a lesser degree of priority, but are essential for the development of capital markets in the EU.

Some of the external challenges that may threaten the success of the CMU will also remain present in the coming months. The possible effects of the current macro-economic and monetary context first need considering. Very low interest rates tend to favour debt financing and to encourage liquidity hoarding at the expense of longer term investment and may also create bubbles. Macro-economic imbalances between EU Member States are also due to persist in the current environment, impeding a further integration of EU capital markets. Finally, Brexit, which introduces new frictions and costs in the access of the EU to the most developed capital market in Europe is a reality now and is both an opportunity and a challenge for the CMU.

Appendix 1: Detail of the new CMU action plan (September 2020)

1. Developing retail participation:

1.1 Financial education: Feasibility assessment of the development of a financial competence framework aiming to develop a common understanding among Member States of financial competence (Q2 2021). Introduction of requirements for member states to promote learning measures supporting financial education in particular in relation to responsible investing (Q1 2022);

1.2 Inducements and professional qualifications: Amendments to applicable rules in the area of inducements in order to ensure that retail investors receive fair and adequate advice (Q1 2022). Introduction of a new category of qualified investors in MiFID II and reduction of the current information and administrative overload for these investors (Q1 2022). Measures to improve the level of the professional qualification of advisors including the introduction of a possible pan-EU competence certificate as part of the MiFID II and IDD reviews (Q4 2021 / Q1 2023);

1.3 Pension adequacy: Development of pension dashboards with indicators for facilitating the monitoring of pension adequacy; development of best practices in the area of pension simulations and tracking (Q4 2021). Assessment of current auto-enrolment practices in occupation pension schemes and identification of best practices across the EU (Q3 2020).

2. Further integrating EU capital markets:

2.1 Withholding tax: Legislative initiative aiming to introduce a common, standardised EU-wide system for withholding tax relief at source, taking into account the OECD TRACE project in particular (Q4 2022);

2.2 Insolvency regimes: Initiative for ensuring the minimum harmonisation or increased convergence of rules in targeted areas of core non-bank insolvency (e.g. definition of triggers, ranking of claims, asset tracing...) (Q2 2022). Regular assessment of the effectiveness of national loan insolvency systems (Q1 2021 / Q4 2022);

2.3 Shareholder rights: Assessment of the possibility of introducing a harmonized EU-wide definition of 'shareholders' as part of the SRD 2 review and of the need for a further harmonisation of rules governing the interaction between investors, intermediaries and issuers (Q3 2023). Assessment of national barriers to digitalisation of this area (Q4 2021);

2.4 Settlement services: Review of the rules concerning the provision of settlement services in the EU in the context of the CSDR review (provision of cross-border services on the basis of CSD passports, conditions under which CSDs are authorised to designate credit institutions or themselves to provide banking-type ancillary services...) (Q4 2021);

2.5 Post-trade consolidated tape: Legislative changes that will support the establishment of an effective

and comprehensive consolidated tape for equity and equity-like instruments in order to create an integrated trading view across the EU and improve competition between venues (Q4 2021);

2.6 Investment protection: Strengthening of the investment protection and facilitation framework in the EU (e.g. rules to ensure protection of intra-EU investments; effectiveness of dispute resolution mechanisms, consolidation of information on rights and opportunities for investors in a single access point...) (Q2 2021);

2.7 Supervisory convergence: Assessment of the need for further harmonisation of capital market rules and further supervisory convergence, possibly through stronger supervisory coordination or direct supervision by the ESAs (Q4 2021).

3. Making financing more accessible to European companies:

3.1 Single-access point to corporate information:

Legislative proposal to set up a European Single Access Point (ESAP) for all relevant corporate financial and sustainability-related information in order to make EU companies more visible to cross-border investors. This will entail streamlining EU legislation on the disclosure of company data to the public (Q3 2021). The ESAP platform will to the greatest extent possible build on existing EU and national infrastructure, as well as existing EU initiatives (such as the European financial transparency gateway (EFTG) pilot project and the business registers interconnection system (BRIS));

3.2 SME listing rules simplification: Possible simplification of public listing rules for SMEs on SME growth markets and regulated markets (e.g. consistency of SME definition, simplification of the market abuse regime, provisions for simplifying for issuers the transitioning from SME growth markets to regulated markets) (Q4 2021);

3.3 ELTIF review: Review of the ELTIF legislation concerning e.g. investment limitations for retail investors, ELTIF marketing rules, the redemption policy and lifespan of ELTIFs, eligible assets as well as diversification rules, portfolio composition, limits on cash borrowing (Q3 2021);

3.4 Prudential requirements: Review of Solvency II (risk-margin calculation, valuation of insurers' liabilities, eligibility criteria for the long-term equity asset class...) for promoting long-term investment by institutional investors (Q3 2021). Review of CRR/CRD aiming to avoid the undue impact of Basel III requirements on banks' investment in long-term SME equity and on market-making activities conducted by banks and investment firms (Q1 2021);

3.5 SME referral scheme: Feasibility assessment of a scheme requiring banks to direct SMEs whose credit applications have been rejected to alternative funding providers and vice versa (Q4 2021);

3.6 Securitisation: Review of the STS and non-STS securitisation framework (concerning the appropriateness of disclosure requirements, the prudential treatment of cash and synthetic securitisation, the process for recognising

significant risk transfer...) to help banks lend more to the real economy with a particular focus on SMEs and the green transition (Q4 2021).

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Appendix 2: ECOFIN conclusions (December 2020)

The ECOFIN welcomed the new CMU action plan and considered that the next steps towards a genuine CMU require a clear prioritisation of measures.

Highest priority – to be delivered by the end of 2021

The actions, that are important to improve the funding of the economy and particularly of SMEs and have the potential to support a swift economic recovery in the context of COVID-19 pandemic, were deemed most urgent at this juncture by the ECOFIN. They should have the highest priority and should all be delivered by the Commission as soon as possible, but not later than by the end of 2021. These correspond to the third set of measures of the CMU action plan (Making financing more accessible to European companies):

- Facilitating access of corporations, in particular SMEs, to financing on capital markets by streamlining and simplifying the current rules for listing on regulated markets and admission to trading on MTFs and by supporting financial ecosystems that can foster enhanced SME access to equity (3.2);
- Setting up an EU wide «single access point» for financial and non-financial company information. This data hub should include environmental, social and governance (ESG) data (3.1);
- Strengthening the role of insurers, banks and other institutional investors as long term investors and assessing ways to incentivise long-term investments (3.4);
- Reviewing the appropriateness of the current securitisation framework with a view to enable capital markets to absorb more exposure from banks, thus freeing up lending capacities of banks (3.6);
- Improving the regulatory framework for long-term investment vehicles by reviewing the European Long-Term Investment Fund (ELTIF) Regulation (3.3);
- Exploring the benefits and drawbacks of a referral scheme to direct SMEs to providers of alternative funding when their credit application has been turned down.(3.5);

Measures to be delivered as soon as possible:

The measures that are considered most important for mobilising private capital and stimulate more investment activity should also be delivered as soon as possible, according to the ECOFIN.

- Empowering citizens to take well-educated investment decisions through enhanced financial literacy (1.1);

- Enhancing data availability and transparency by further assessing how to tackle the barriers to establish a consolidated tape in the EU (2.5);
- Streamlining existing disclosure rules for the various capital market products and assessing the quality and fairness of investment advice provided to retail investors as well as the benefits and drawbacks of readjusting the current investor categorisation (1.2).

Measures to be delivered in the short term:

The ECOFIN emphasized the need to make tangible progress towards a globally competitive CMU with unhampered cross-border capital movement in order to unlock the potential of a deep integrated capital market that is attractive for the movement and retention of external capital and expertise, to the advantage of investors and capital raisers. These actions should be assessed in the following order:

- Explore options for optimising the investment climate within the single market and to propose a Union framework that clarifies, strengthens and supplements the rules on the protection of cross-border investment within the Union;
- Explore ways to enhance the cross-border activities of post trading infrastructures, particularly in the area of settlement (2.4);
- Promote further supervisory convergence by working towards a more harmonised legal framework for regulated capital market activities. (2.7).

Medium term actions:

The Commission was encouraged by the ECOFIN to look at the more complex and time consuming structural reforms and to deliver the respective initiatives in the medium term, in the following order:

- Assess ways to simplify the withholding tax relief procedure for cross-border investments (2.1);
- Assess legislative or non-legislative initiatives to increase convergence of the outcome of insolvency procedures in different Member States (2.2);
- Assess the need for further action to strengthen the confidence of investors and facilitate cross-border investments by, for instance, evaluating possible deficits in the areas of rules on enforcement of financial reporting of listed companies and supervision or oversight on technology providers in finance (2.6);
- Assess ways to support raising citizens' awareness as regards their future retirement income by developing best practices for, e.g. national tracking systems (1.3);
- Assess the possible benefits and drawbacks of a harmonised definition of «shareholder» (2.3).