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European Commission,
DG Internal Market,
Unit G1 ("supervision consultation")
B-1049 Brussels

Dear Sirs,

CONSULTATION ON COMMISSION COMMUNICATION OF 27 MAY 2009 ON EUROPEAN FINANCIAL SUPERVISION

Executive summary

The Investment Management Association (IMA¹) is grateful for the opportunity provided by the Commission to contribute to the discussion on the future of the supervision of the financial markets.

We represent an important part of the **buy-side** of financial markets and many of our members' business activities are defined by their **cross-border nature**. IMA members, therefore, have **a strong interest in a harmonised European supervisory framework with powerful European authorities cooperating closely with national supervisors**. The inherent logic of the internal market calls for Community legislation to be accompanied by harmonised EU-supervisory standards, thereby reducing the compliance costs linked with 27 supervisory practices.

IMA welcomes the proposals made by the de Larosière Group on the future supervisory framework, the following European Commission's communications and the agreement by the European Council which set out a clear roadmap for a reform of the financial system. However, we are concerned that by simply following the de Larosière Group's recommendations, the EU might approach the modernisation from a purely banking and insurance perspective, ignoring the securities sector in general and the asset management industry in particular. Experience from recent legislative initiatives seems to indicate a dominant role of the sell-side interests in EU legislation, neglecting the other part of the market, i.e. the buy-side.

¹ The IMA represents the asset management industry operating in the UK. Our members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the managers of occupational pension schemes. They are responsible for the management of £3.4 trillion of assets, which are invested on behalf of clients globally. These include authorised investment funds, institutional funds (e.g. pensions and life funds), private client accounts and a wide range of pooled investment vehicles.

Supervision should aim to encourage the smooth functioning of markets and the development of a competitive industry. However, even competent supervision cannot compensate for failures in financial regulatory policy. Therefore, we deem it necessary not only to comment on the proposals for the future supervisory architecture, but also on the regulatory framework.

At the heart of the debate about how the financial crisis came about, how to deal with it, and how to prevent it in the future lies the question of regulation. The years ahead will witness the most important regulatory reform debate of our time. While there are EU proposals for example on alternative investment fund managers and future supervisory structures, the focus should be on the **regulation of banking**. We need banks which are simpler, more transparent and once again capable of attracting private capital. The last two years have been devastating for the European economy and for its financial infrastructure. It is encouraging to see the EU is addressing the issues with real intent and commitment to reform.

In this context, we take note of the European Commission's intention to further modify the Capital Requirements Directive. In spite of the urgency to act, we urge it to be ensured that changes to the regulatory capital regime for banks do not unintentionally or disproportionately impact other sectors of the industry also subject to CRD, such as asset managers. The business model of banks differs fundamentally from that of asset managers where clients' assets are kept separate from the assets of the managers. Therefore, a one-size-fits-all approach should not be applied.

Stable financial markets and trust among all market participants are a necessary prerequisite for an effective asset management industry. **IMA strongly supports well regulated financial markets. They are to the benefit of investors and hence the investment management industry.** Current regulation of the investment management industry has served the industry and its clients well, and the IMA considers that the fund and asset management sector as a whole has proved fairly robust over the past months in the UK despite the continuing crisis in the financial system. The long term challenge will be to develop equally robust regulatory structures and regimes for other parts of the financial sector.

In conclusion, we are convinced that regulatory reform must be targeted, measured and considered, and regulatory arbitrage must be avoided. Reform should focus on those sub-sectors where regulatory deficiencies have been identified. There must be **no automatic read-across of regulation to the asset management sector** which was not at the origin of the crisis and where existing regulation proved adequate.

IMA'S DETAILED RESPONSE

1 European supervisory structure

1.1 Macro-prudential oversight

We recognise the need for adequate macro-prudential supervision and effective early warning mechanisms. Therefore, we welcome the creation of a European Systemic Risk Board and we share the de Larosière Group's view that **"to be effective macro-prudential supervision must encompass all sectors of finance and not be confined to banks, as well as the wider macro-economic context."** We also welcome the G20 conclusion to reinforce the role of the Financial Stability Forum as it becomes the Financial Stability Board. A good coordination between the two bodies will be essential as the stability issues do not recognise continental borders.

We want to stress that in gathering the data needed by the new body, **a duplication of reporting requirements**, i.e. that the same information has to be provided to various bodies in various formats, **must be avoided**, and that existing information sources should be exploited fully before imposing new requirements. The efficiency and success of the ESRC will depend on the information flow between the ESRC and the micro-prudential, i.e. the future European Authorities and national supervisors. Asset managers should not be required to report the same information to various authorities, instead authorities should agree to exchange this information amongst them. This implies that reporting requirements should be streamlined both in terms of format and content whilst being proportionate and tailored to the specific characteristics of the entities required to report. Indeed, the reporting requirements should not place an unreasonable burden upon market participants in terms of costs and efforts, and an obligation to report each and every transaction should be avoided.

Finally, we believe that **a proper and permanent representation of the asset management industry must be ensured** in a future "European Systemic Risk Board". We welcome Recommendation 16 of the de Larosière report stating that "high-level alternates to the central bank Governors should take part in the discussions, in particular when insurance or securities markets issues are discussed". However, we are concerned that the permission of the high-level alternates to take part only in specific discussions (and not on an ongoing basis) will not sufficiently take into account the importance and needs of the asset management industry as the buy-side in financial markets. We see the risk that macro-prudential supervision will be exercised from a purely banking perspective, which should be avoided.

1.2 Micro-prudential oversight

1.2.1 Establishing a European System of Financial Supervision

IMA's members provide asset management services, distribute investment funds and act as investors in the securities markets of all the 27 EU Member States. A harmonised regulatory and supervisory framework is therefore of crucial interest to us. ***It is very expensive and inefficient to operate under 27 different sets of rules/ differing interpretations of the EU rules.*** So far in many areas of

financial markets regulation and especially supervision national differences remain strong beneath a thin layer of European harmonisation.

There has also been all too much gold-plating of the EU rules, national regulators adding requirements on top of the EU requirements as they see fit. There are a lot of examples on this for instance in the area of MiFID and UCITS Directive. The simplified prospectus for UCITS funds is a good example where the benign intentions of European legislators to achieve a short, harmonised document to be used across Europe failed completely because of the diverse implementation and gold-plating by national regulators. This necessitated a review of these requirements in the UCITS IV package and again expectations are high that Europe gets it right this time, but only national implementation will tell whether the aims will be achieved this time around.

The 3L3 Committees (CEBS, CEIOPS and CESR) have reached their limits, not only in terms of resources, but also legal powers. Therefore, we strongly support the strengthening of the 3L3 Committees and transforming them into European Authorities (European Banking Authority, European Insurance and Occupational Pensions Authority and European Securities and Markets Authority) with real powers whilst leaving day-to-day supervision to national supervisors, thus making full use of their local knowledge. This will help to reduce significantly the huge compliance costs faced by IMA members who operate on a cross-border basis in the securities markets of all 27 EU Member States.

In particular, we welcome the proposal that the future authorities should be able to adopt binding technical level 3 interpretation and supervisory standards. This will help to prevent Member States and national regulators from gold-plating of EU rules. In this context, we stress the need for timely interpretation of EU rules, meaning that for each project, deadlines should be fixed by which binding technical level 3 interpretation and supervisory standards have to be issued in order to ensure coherent interpretation across Europe, legal certainty and a smooth functioning of the internal market.

We strongly support the Commission's proposed actions to introduce a far more consistent set of supervisory rules. We also support the proposed overall supervisory structure, establishing a European System of Financial Supervision, with national supervisors still responsible for the day-to-day supervision but with a strengthened coordination at the European Level. Local knowledge is needed to apply the rules to the supervised entities, but more and more the aim should be one set of rules so strong coordination of the supervisors at European level is needed. We support the strengthening of the 3L3 Committees and transforming them into European Authorities with real powers. Our members need certainty of the rules applicable.

1.2.2 Mediation and arbitration

In addition to the new legally binding mediation mechanism between national supervisors and the new legally binding technical level 3 interpretation that will be issued by the future Authorities, we would welcome a **legally binding arbitration mechanism** covering disputes between an individual firm and its national supervisor. Such disputes should include diverging views between a national supervisor and an individual firm on national interpretation of an EU Directive.

1.2.3 Accountability

IMA agrees with the de Larosière Group's view that governance and accountability of the three future Authorities will be crucial, and that the **right balance** must be found between **accountability** on the one hand and a **high degree of independence** on the other.

1.2.4 Cross-sectoral cooperation

In addition, we fully endorse the emphasis placed on cross-sectoral cooperation. It is of very important to establish a formal structure for mutual understanding, cooperation and consistent supervisory approaches of the three Authorities. An overarching steering committee and the possibility to participate as an observer in the meetings of other European Supervisory Authorities are sensible proposals.

Cross-sectoral cooperation is, for instance, highly needed in the area of Occupational Pensions. Historically linked to insurance products, pensions products such as defined contribution schemes based on asset management products have become used more widely. Therefore, the **Commission should examine whether it is still justified that occupational pensions are exclusively within the remit of EIOPA and that no role is given to ESMA.**

2 Global crisis calls for global solutions

It cannot be stressed enough that financial markets are global and their problems are global, but the regulation/ supervision remains mainly national. We urge Europe to coordinate with the key non-EU jurisdictions the regulatory measures to address the crisis. ***Future EU actions should be consistent with the G20 decisions.***

We believe that protectionism would be very harmful in the long run for Europe's financial markets and European market participants. There have been worrying examples of this like the Commission proposal for a Regulation of Credit Rating Agencies which as originally proposed would have allowed European market participants only to invest in rated issues if the rating is European. Also the proposed Alternative Investment Fund Managers Directive carries the risk of resulting in increased protectionism as it introduces a three year delay before third country funds can have a European passport, and the whole value chain of European managers is subjected to overdetailed EU rules making it very difficult if not almost impossible, for third countries to achieve equivalence.

We do not believe that taking the view that only European regulation can protect investors is valid or beneficial for Europe's financial markets. The position of third countries must be carefully taken into account in a balanced manner. For example the UK/ European asset management industry is a major exporter of EU harmonised investment funds (UCITS) into Asia and Latin America. Closing Europe's borders is not an option in the globalised economy. ***We agree the Europe can and should take the lead, but it must act responsibly and in coordination with other continents.***

Yours sincerely

A handwritten signature in black ink, appearing to read 'Jarkko Syyrilä', with a long, sweeping flourish extending to the right.

Jarkko Syyrilä
Director, International Relations