

EUROPEAN PARLIAMENT OWN INITIATIVE REPORT ON FURTHER DEVELOPMENT OF THE CAPITAL MARKETS UNION

AMAFI'S PROPOSED AMENDMENTS

AMAFI welcomes the ECON's own-initiative draft report "on further development of the Capital Markets Union (CMU): improving access to capital market finance, in particular by SMEs, and further enabling retail investor participation" which highlights a number of key necessary reforms for EU-27 financial markets to contribute to the Union's economic recovery and play a bigger role in the financing of its economy in a post-Brexit environment.

While we are very supportive of the approach taken, we consider that some specific recommendations should be reviewed, and others should be added to fully capture issues at stakes.

AMAFI is grateful for the opportunity to provide comments on the ECON draft report and through the below proposed amendments emphasises the topics it considers crucial to complete the CMU project. Most of the amendments are based on AMAFI's [report](#) "Completing Capital Markets Union: enabling EU-27 markets to play a bigger role in the financing of the Union's economy".



Association française des marchés financiers (AMAFI) is the trade organisation working at national, European and international levels to represent financial market participants in France. It acts on behalf of credit institutions, investment firms and trading and post-trade infrastructures, regardless of where they operate or where their clients or counterparties are located. AMAFI's members operate for their own account or for clients in different segments, particularly organised and over-the-counter markets for equities, fixed-income products and derivatives, including commodities.

1. Revamping the securitisation market

Current text	Proposed amendment
<p>4. Requests the realignment of the treatment of cash and synthetic securitisations, of the treatment of regulatory capital and liquidity with that of covered bonds and loans, as well as with the disclosure and due diligence requirements for covered bonds and simple, transparent and standardised (STS) securitisation;</p>	<p>4. Emphasizes that securitisation has a central role to play in enabling EU-27 financial markets to transition towards a market-based financial system as well as in freeing up banks' balance sheets and enabling them to renew their capacity to distribute credit and in particular to SMEs. Calls on the need to ease the Significant Risk Transfer assessment process. Requests the realignment of the treatment of cash and synthetic securitisations, of the treatment of regulatory capital and liquidity with that of covered bonds and loans, as well as with the disclosure and due diligence requirements for covered bonds and simple, transparent and standardised (STS) securitisation; and calls to review eligibility criteria for assets born of securitisation as collateral for Eurosystem market repo operations and for the ECB's purchase programmes.</p>

Justification

Securitisation has a central role to play in enabling EU-27 financial markets to transition from a bank-based to a market-based financial system.

The current economic context gives new urgency to this issue as it plays a critical role in freeing up banks' balance sheets and in enabling them to renew their capacity to distribute credit, especially when it comes to SMEs financing.

While we support the draft report's call to encourage the development of synthetic securitization as per paragraph 4, we consider that proposed reforms should be broadened.

In particular, the Covid-19 crisis has highlighted the rather limited support from the ECB Purchase Programmes to the securitisation market. If the PEPP launched by the ECB had significantly helped other sectors of the Fixed Income (e.g. covered & corporate bonds), the participation of the ECB in ABS purchases has been very limited.

2. Increasing the production of research on SMEs

Current text	Proposed amendment
<p>5. Calls for targeted measures within securities market legislation to expedite the recovery after the COVID-19 crisis; supports changes in the Prospectus Regulation, the Markets in Financial Instruments Directive (MIFID), the Securitisation Regulation and the Market Abuse Regulation to facilitate investments in the real economy, in particular in SMEs, and to allow newcomers and new products to enter the markets, preserving consumer protection and markets integrity;</p>	<p>5. Calls for targeted measures within securities market legislation to expedite the recovery after the COVID-19 crisis; supports changes in the Prospectus Regulation, the Markets in Financial Instruments Directive (MIFID), the Securitisation Regulation and the Market Abuse Regulation to facilitate investments in the real economy, in particular in SMEs, and to allow newcomers and new products to enter the markets, preserving consumer protection and markets integrity; Calls in particular for the introduction of more proportionality in the inducement regime for SME research and to consider sponsored research as a credible alternative to “traditional” SME research.</p>

Justification

MiFID II rules on research, which had neither been the subject of political discussions by the co-legislators nor been the subject of serious impact studies, have had a negative impact on the production of research in Europe, particularly for SMEs. It can be considered that this piece of legislation was not introduced in a proper manner, and that its impact, while largely predictable, was not properly assessed.

AMAFI recognizes that the decline in SME coverage was a pre-existing trend to the implementation of MiFID II / MiFIR and that there are geographic divergences about the way investment research is produced and displayed in the UE.

Still, it is assessed in many EU markets that MiFID 2 has had a negative impact¹, in terms both of quantity and quality of the SME coverage. It is not easy to give today quantitative evidence of the decline of the coverage.

On this topic, AMAFI performed, mid 2018 a study on the coverage of French shares by investment analysts between 2005 and 2017. This analysis highlights as well several weaknesses in the supply of financial analysis for small and medium capitalisations:

- The supply is mainly provided by local players, while international players have disengaged from this market segment during the period of observation.
- The supply is more concentrated, creating greater risk of attrition, considering that the 3 more active providers represent 40% of the supply on the capitalisations smaller than 1 Bn €.
- The evolution of this supply appears to be largely dictated by a process of creative destruction leading to the emergence of new players replacing those who disappear rather than a mechanism of elasticity by virtue of which the « stable » players increase or decrease their coverage.

In this environment, the new economic conditions introduced by MiFID II for the financial analysis business pose great risks for the prevalent « Schumpeterian » trend that has prevailed for the last decade. In this case, the disappearance of existing players would not be compensated by the emergence of new players, considering the growing weakening of their business model.

¹ Fang, B., Hope, O.-K., Huang, Z. and Moldovan, R. (2019), 'The Effects of MiFID II on Sell-Side Analysts, Buy-Side Analysts, and Firms,' *Rotman School of Management Working Paper No. 3422155*, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3422155.

In this context, we consider that:

- (i) More proportionality should be introduced in the inducement regime for SMEs research; and
- (ii) The framework for sponsored research – that could constitute a credible alternative to “traditional” SMEs research – should be reviewed to ensure that that issuer-sponsored can qualify as “investment research” and not marketing communication provided that the research provider strictly comply with MiFID II and MAR rules.

3. Supporting market-making activities in EU-27 financial markets

Current text	Proposed amendment
N/A	5bis. Given the importance of market-making in the financing of the Union’s economy by financial markets, calls to preserve the European exemption from holding capital gainst CVA risk on corporate derivatives exposures, to replicate as much as possible US specificities and deviations in the implementation of the final Basel provisions to preserve the competitiveness of EU-27 players; and to provide clarifications on the European implementation of fully phased-in Basel III rules especially regarding the Leverage Ratio (LR), the Fundamental Review of the Trading Book (FRTB), refinements around the implementation of the Standardised Approach for Counterparty Credit Risk (SA-CCR) as well as the use of discretion in the ongoing reform of Credit Valuation Adjustment (CVA).

Justification

Market making is key for the functioning of both primary and secondary markets in three major asset classes: equities, bonds and derivatives, both on organised platforms and over the counter. It is performed by financial institutions to help the economy function properly. Much more than a mere profit-seeking activity, it helps governments and corporates to meet their financing needs and also enables them, along with investors, to hedge risk.

The equity and debt markets are the ones to consider when it comes to financing governments and firms. Market making is pivotal to the orderly operation of bond markets, and also plays an important role in equity markets.

Market making also plays a widely acknowledged role in derivatives markets, which operate as indirect financing markets since they allow risk hedging by economic agents (currency risk, interest rate risk, commodity price risk, etc.) and investors (interest rate and portfolio risk). Furthermore, investors’ ability to hedge their portfolio risk directly affects their appetite for investing in primary and secondary markets for equity and fixed income.

In order for EU-27 investment firms to remain competitive especially with regards to their US counterparts, the European implementation of the “fully phased-in Basel III package” should make sure, while ensuring the control of systemic risk, not to unduly penalise European market activities. With this in mind, it is

particularly striking that the implementation of the final Basel III rules is set to induce a significant increase in the required capital for European banks (by 20% to 25%)². It would be at odds with the expectations expressed by the Council in July 2016³, all the more as it will be neutral for non-European banks.

The EU transposition of the Basel III package is critical to enable financial markets to play a bigger role in the financing of the Union's economy. To that end, we recommend the following approach:

- (i) Preserve the European exemption from holding capital against CVA risk on corporate derivatives exposures;
- (ii) Replicate as much as possible US specificities and deviations in the implementation of final Basel provisions (notably, target a capital neutral implementation of FRTB, set the alpha-factor at 1 with end-clients in the Standardised Approach for Counterparty Credit Risk, etc.);
- (iii) Provide clarifications on certain topics for the European implementation of fully phased-in Basel III rules (treatment of repos and reverse repos under the Leverage Ratio, treatment of derivatives hedges under NSFR, implementation of FRTB, refinements in the implementation of SA-CCR, use of discretion in the ongoing reform of Credit Valuation Adjustment, level of the Internal Loss Multiplier in the implementation of provisions related to operational risk).

4. Reducing the cost of market data

Current text	Proposed amendment
N/A	5ter. Calls on the enforcement of the Reasonable Commercial Basis (RCB) principle by simplifying and harmonising tariffs grids, contracts and audit procedures of trading venues. Market actors should be able to compare prices more easily and regulators to determine when the reasonable commercial basis principle is not respected. Considers that the scope of the RCB principle should be extended to include the activities of data vendors, index and benchmark providers, as well as Credit Rating Agencies.

Justification

MiFID II contains provisions aiming at improving the quality and availability of market data and reducing the costs for market participants. In order to reduce costs MiFID II requires trading venues to make pre-trade and post-trade data available separately and to make them available on a reasonable commercial basis (RCB).

Market participants believe that so far MiFID II has not yet delivered on its objective to lower the prices of market data.

Consequently, market participants face increased costs in the acquisition and management of data and the compliance to complex auditing procedures.

Most Trading Venues acknowledge that the revenue they make from market data services is at least stable or has just increased by low single digit percent every year. This paradoxical effect can be explained by the

² <https://eba.europa.eu/eba-updates-estimates-impact-implementation-basel-iii-and-provides-assessment-its-effect-eu-economy>

³ <https://www.consilium.europa.eu/en/press/press-releases/2016/07/12/conclusions-banking-reform/>

fact that most investment firms have implemented significant optimisation programs with a view to reduce their overall costs of market data. Those programs have led to a huge decrease of the number of front office users having access to real time market data from trading venues.

All in all, it appears that, in order to maintain the same level of revenues, trading venues tend to compensate the decrease in the number of users by increasing the costs for each client, which constitutes a vicious circle for all market participants.

Besides, data vendors/aggregators as well as credit rating agencies and index benchmark providers have a natural monopoly with no regulatory constraints on prices have been contributing to the significant rise of market data costs.

In order for market data to be available on a reasonable commercial basis, AMAFI considers that it is necessary to bring more transparency in the methodology used by trading venues to calculate the price of the data they sell. Tariff grids, contracts and audit procedures should be simplified and harmonised. Data aggregators, index and benchmark providers as well as credit rating agencies should be included in the scope of the RCB principle.

5. Managing the implications of a hard-Brexit

Current text	Proposed amendment
N/A	<p>13bis. Underlines that if no equivalence decision is being granted for UK trading venues, EU-27 investment firms will face detrimental consequences related to MiFIR trading obligations;</p> <p>Calls that in such situation ESMA provides supervisory forbearance for the execution of orders on shares listed both in the UK and in the EU-27, and for UK branches of EU-27 investment firms when they trade with non-EU clients;</p> <p>Calls, as part of the upcoming general revision of MiFID2/MiFIR, on the Commission to integrate specific provisions for double-listed shares and to clarify that MiFIR trading obligations has no extraterritorial implications.</p>

Justification

A hard-brexit could have detrimental implications on EU-27 investment firms capacity to access UK infrastructures and provide their clients with the same quality of services as they used to.

If the recent European Commission Communication⁴ indicates that the temporary equivalence should be extended, issues around the share trading obligation (STO) and the derivative trading obligation (DTO) have not been addressed.

⁴https://ec.europa.eu/info/sites/info/files/brexit_files/info_site/com_2020_324_2_communication_from_commission_to_inst_en_0.pdf, p.13.

Absent of an equivalence decision, EU-27 firms will face two main consequences:

- (i) They will not be in a capacity to execute orders with a proper quality of execution on at least 40 double listed shares of which 16 have more important liquidity on the London listing than on the EU-27 one;
- (ii) They will face a conflict of law both for shares and derivatives that are subject to MiFIR trading obligations as they will have to comply with both the UK and the EU-27 trading obligations. This will have a major impact on their competitiveness.

Considering that no equivalence decisions will be granted, AMAFI would recommend to:

- (i) Change the scope of the STO for double-listed shared to enable the execution of orders on UK trading venues;
- (ii) Clarify that the MiFIR STO and DTO have no extraterritorial reach and therefore do not apply to UK branches of EU-27 investment firms when they trade with non-EU clients.

6. Increasing retail participation in EU-27 financial markets

➤ *Facilitating the opt-in of sophisticated retail clients as professional clients*

Current text	Proposed amendment
<p>17. Urges the Commission to make clear the differentiation between professional and retail investors on all levels of MIFID, making it possible to tailor the treatment of clients according to their knowledge and experience on the markets; requests that the Commission consider the introduction of a category of semi-professional investors to better respond to the reality of participation on the financial markets;</p>	<p>17. Urges the Commission to make clear the differentiation between professional and retail investors on all levels of MIFID, making it possible to tailor the treatment of clients according to their knowledge and experience on the markets; requests that the Commission consider the introduction of a category of semi-professional investors to facilitate the opt-in of sophisticated retail clients as professional clients to better respond to the reality of participation on the financial markets;</p>

Justification

AMAFI agrees that within the retail clients category there is a large diversity of clients' profiles: on one hand some clients are wealthy and have a very good knowledge and understanding of financial markets while on the other hand some do not have a lot of resources and / or a very limited knowledge of financial markets. This heterogeneity raises several issues.

Firstly, the current categorisation may prevent, in some limited cases, access to some products (which are dedicated to professional clients and eligible counterparties). This is the case for wealth management clients who can have a good knowledge of financial markets and a significant amount of money to invest (for diversifying their portfolios) but cannot access to sophisticated products (such as private equity funds or hedge funds). Secondly, this situation also raises some issues with certain corporate clients (which do not fall within the criteria of professional clients per se) but perform sometimes a lot of transactions, notably for hedging purposes. As they are considered as "retail clients", for instance, investment firms have to provide them "suitability report" for each and yet very similar transactions which is time consuming.

More globally, MiFID II client protection rules for retail are quite heavy and if globally well fit for retail clients with low to intermediate knowledge are considered too burdensome and excessively constraining for those sophisticated "retail" clients. It is true that some so-called retail clients are too sophisticated to benefit from

all investor protection rules designed for retail. In particular those sophisticated clients – that should be upgraded more easily into professional category – should be applied mitigated rules on notably costs and charges.

To tackle those issues, AMAFI does not support the creation of a new category of “semi-professional” clients but rather suggests modifying the “opt-in” process for “clients who may be treated as professionals on request” to facilitate the opt-in of sophisticated retail clients as professional clients.

Creating a new category of clients would be too disruptive and costly:

- the costs to implement changes would be extremely high, IT systems would have to be totally reviewed as well as all firms’ documentation, repapering, product governance’s target markets, etc., which have already been modified by MiFID II.
- both investment firms and clients need regulatory stability, the current clients’ categories have been implemented since MiFID I. Creating a new one today would be very disruptive and confusing for everyone and would require new training of staff and distributors.

➤ *Setting up a European certification requirement for staff providing investment advice*

Current text	Proposed amendment
19. Calls for amendments to legislation to ensure access to independent advice by financial intermediaries while avoiding promotion of the institution’s own financial products and ensuring a fair marketing of financial products;	19. Calls for amendments to legislation to ensure access to independent qualitative and pertinent advice by financial intermediaries while avoiding promotion of the institution’s own financial products and ensuring a fair marketing of financial products by setting up a European certification requirement for staff providing investment advice ;

Justification

Overall, AMAFI does not consider the ban of inducements or the promotion of “independent advice” as the best means to facilitate the access of individuals to capital markets.

Current rules are already quite demanding and, in our view, sufficiently protective of the clients’ interest. MiFID II strengthened the previous inducement regime and makes sure that the client is informed precisely and properly of any inducement and requires a quality enhancement test that ensure that firms act in the best interest of their clients.

For all the above reasons, and for the sake of regulatory stability, inducement rules do not need to be changed in relation to commercialisation of financial instruments.

AMAFI sees merits in setting up certification requirement for staff providing investment advice and other relevant information if such certification is considered as an appropriate way to comply with the requirement to assess knowledge and competence of staff providing investment advice and other relevant information.

It is the case in France. Indeed, the French NCA (*Autorité des marchés financiers* - AMF) already set up and put in place, since July 2010, a certification mechanism aiming at checking the minimum level of knowledge of current and prospective employees of investment service providers. This exam certified by AMF constitutes a tangible recognition of a core of professional knowledge and strengthens the quality and consistency of the investment advice given to clients in France.

7. Promoting EU champions in the energy transition field

Current text	Proposed amendment
N/A	25bis. Calls on a targeted support from EU authorities to create the relevant regulatory framework to establish a common language including with regards to transition strategies and the data collection & disclosure, to promote international standards consistency, to create a pan-European CMU ESG system, to develop product neutral approaches on labels and frameworks to onboard retail clients, to create incentives to redirect capital flow toward sustainable activities while ensuring that usual risk analysis are performed.

Justification

Proactive positioning has made the EU a standard-setter in regulations related to sustainable finance, and a global leader in this domain. While this position is a geopolitical asset for the Union, there is a risk that decisions taken in the internal market become constraints for European companies when they compete outside the Union's borders, and paradoxically reduce their contribution to the mitigation of climate change.

Typically, the efforts produced by the European Commission on the taxonomy are very welcome but need to go further by completing the approach with a framework that could help in assessing the transition efforts made at companies level, which are key to achieve the EU's 2050 climate-related objective. It would also help to reward companies which are engaged into a robust science-based transition pathway and ensure that the energy transition will be as inclusive as possible.

In addition, the development of the market requires to make available better-quality data from more numerous stakeholders. In that sense, the Non-financial Reporting Directive (NFRD) regulation review is key in getting more stakeholders to publish on their non-financial performance, while adapting the disclosure requirements for smaller counterparties. Moreover, ESG-related data collection could be organised and centralised at the EU level to ensure a fair and reasonable access while trading them with non-EU players where relevant.

Onboarding the retail clients will be key in the development of the sustainable finance market: there needs to be simple, easy to understand and product neutral tools and processes at their disposals in order to match their increasing demand for sustainable products. If the Ecolabel will help achieve that, additional standards or frameworks could be developed.

Finally, sustainable regulation/standard fragmentation at international level should also be addressed in order to level the playing field, and to ensure that EU stakeholders can continue to play a significant role in financing energy transition of the emerging economies.

