

Opinion of the European Economic and Social Committee on the ‘Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the European Central Bank — Regulating financial services for sustainable growth’

COM(2010) 301 final

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On 2 June 2010, the European Commission decided to consult the European Economic and Social Committee, under Article 304 of the Treaty on the Functioning of the European Union, on the:

Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the European Central Bank — Regulating financial services for sustainable growth

COM(2010) 301 final.

The Section for the Single Market, Production and Consumption, which was responsible for preparing the Committee’s work on the subject, adopted its opinion on 1 February 2011.

At its 469th plenary session, held on 16 and 17 February 2011 (meeting of 16 February), the European Economic and Social Committee adopted the following opinion by 164 votes with one abstention.

1. Conclusions and recommendations

1.1 ‘More and more has to be done in the area of international supervision. You can have the best regulation in the world but if its implementation is not supervised, it will not be of any use (1).’

1.2 The European Economic and Social Committee (EESC) welcomes the Commission’s communication and sees the new regulation of the financial markets as the crucial instrument needed for re-launching a sustainable economy.

1.3 The EESC thinks that these matters are attracting ever less attention and that the need for measures to be taken urgently is perceived differently in each country and no longer appears to be a shared priority.

1.4 The EESC emphasises and reiterates the importance of redoubling efforts and reaching an international agreement. Nevertheless, it considers it essential and indispensable that the course embarked upon by the European institutions themselves be brought to a swift and positive conclusion and not sidelined in favour of a framework of international agreements which – as we have unfortunately seen again only recently – are far from being achieved.

1.5 The EESC takes a positive view of the measures proposed and awaits those that are still being finalised and which it will be called upon to comment on in due course, such as the projected revision of the MiFID – important to guarantee the soundness and transparency of the markets as well as the trust of investors.

1.6 The EESC supports the Commission’s endeavours to see the legislative process through to its conclusion. The Commission could give the EESC the responsibility of promoting the proposals under discussion, as well as subsequent draft regulations, to social and economic organisations and financial services consumer organisations at national level.

1.7 The United States did a great deal to set the pace in this area with the promulgation of the Dodd-Frank Act, the law to regulate the US financial markets, which lay the foundations for greater convergence across the globe. This legislation addresses many issues with only a regulatory framework, leaving the final form of the rules to the competent authorities or subsequent work on the details. In the case of the European Commission, on the other hand, the individual provisions are already worked out in detail. The two approaches should achieve the same objectives in the end.

1.8 The EESC welcomes some of the innovative choices made in the US legislation and proposes that the Commission undertake an in-depth study of the proposal to establish a financial services consumer protection authority. The Committee thinks, however, that a more autonomous position for such an authority should be considered.

1.9 It is also worthwhile evaluating decisions taken on the other side of the Atlantic on how to deal with ‘too big to fail’ institutions, which can lead to moral hazard in risk management. The EESC asks the Commission to consider very carefully the possibility of adopting similar measures, which appear to be incisive and to act as a deterrent to the imprudent and particularly risky conduct of some financial institution managers and can help to achieve better risk management in financial institutions.

(1) Dominique Strauss-Kahn, Agadir, 1 November 2010.

1.10 The whole process of regulatory update should be finished by 2011 and be fully running from 2013. This will indeed be possible if no problems crop up and everyone sticks to the schedule. However, the EESC has its concerns and fears that this may not happen. The Commission should ask the European Parliament and the Council to fast-track all actions related to the regulation of financial markets. The financial crisis erupted in 2007 and the need to take strenuous action to regulate the markets was broached even back then. Since then, more than two thousand billion dollars have gone down the drain, numerous businesses have gone to the wall and at least thirty million jobs have been lost, with a further four hundred million losses in sight, according to the director of the IMF. In the financial sector alone, at least half a million people have lost their jobs worldwide. Others are still losing theirs and more will join them.

1.11 The EESC calls for a strong, comprehensive, efficient and balanced regulation. In order to avoid negative consequences, the EESC recommends that a profound study on the cumulative regulatory initiatives be undertaken for the necessary measures on the financial system and the capital market. A stable and efficient system should promote financial stability and liquidity for the real economy.

1.12 Civil society at European and national level must continue to press the authorities and public bodies to swiftly adopt new rules in the financial sphere. The Commission could task the EESC with advocating in the Member States the need to take quick and comprehensive decisions on the regulation of financial markets, via public initiatives on the ground involving the social and economic players and financial services consumer organisations.

2. The Commission Communication

2.1 In its Communication 'Regulating financial services for sustainable growth', the Commission sets out the goals attained and a schedule for future legislative initiatives, elucidating the four guiding principles on which its work is based: transparency, effective supervision, enhanced resilience and financial stability, and consumer protection.

2.2 'A safer, sounder, more transparent and more responsible financial system, working for the economy and society as a whole and able to finance the real economy, is a precondition for sustainable growth. It is the essential complement to the efforts Europe is undertaking to consolidate public finances and undertake the structural reforms that will deliver a vibrant economy in the future.' These are the guiding principles behind the Commission's legislative work.

2.3 In the present document, the Commission recaps the stages, since the major crisis of September 2008, that have led to the creation of a new and coherent regulatory framework.

2.4 As far back as November 2008, a group was set up under the chairmanship of Jacques de Larosière and urgent

measures such as the revision of the Directives on Capital Requirements and Deposit Guarantee Schemes have been taken. A Regulation on Credit Rating Agencies has also been adopted and two recommendations on remuneration principles have been presented.

2.5 The Commission has adopted a series of proposals in line with those in the group's report. Many of these are still being discussed by the Union's policy-making bodies, the Council and Parliament.

2.6 The Commission wishes to see a coordinated legislative push to ensure that all the proposed provisions are processed and transposed by the end of 2012.

3. The Committee's comments

3.1 The European Economic and Social Committee (EESC) has expressed its views in several opinions about provisions the Commission intended to adopt, starting with the package proposed by the de Larosière group and going on to the individual provisions that followed.

3.2 Many of the Committee's suggestions and comments on a range of issues have been taken on board, producing results that appear appropriate and sufficient. However, will all of this restore trust in the markets and supervisory authorities, as well as in public authorities, which have to some extent in the past supported an ultra-liberal model in the conviction that the market would regulate itself? This illusion affected not only most Member States, but also some senior figures in the European Commission. Markets have an innate tendency to fluctuate irrationally between risk aversion and risk-taking. Reining in these fluctuations without destroying markets is no easy matter.

3.3 With this Communication, the Commission is implicitly acknowledging the errors of the past – errors which the EESC had promptly pointed out – and setting out a sound and virtually comprehensive road map to redesign the architecture for the supervision, stability and transparency of markets. This is an important piece of work and one which, as the Committee readily acknowledges, has so far been done well.

3.4 The European Parliament has done a lot to beef up and improve the drafts, in some cases advocating the same changes as the Committee, resulting in regulations and directives that appear to be effective and coherent.

3.5 The application phase, however, is beset by a number of problems. For example, in the case of the European Insurance and Occupational Pensions Authority (EIOPA), which oversees the insurance market and pension funds, it is vital that the distinct characteristics of the two sectors are recognised and safeguarded; in particular, it is crucial that the supplementary pensions branch is accorded the same respect as the insurance branch.

3.6 The Council has, unexpectedly, played a less positive role, obliging the Commission to re-examine some good proposals, as in the case of supervisory authorities. Nevertheless, thanks to the work of the Parliament and the Commission, the compromise reached has been a good one, although more could have been done and done earlier if particular provisions had not fallen foul of mutual vetoes.

3.7 However: has everything been done that needed to be done and was it done at the right time?

3.8 The United States gave an apparently comprehensive and more prompt response to the calls for regulation and protection from the weakest parts of the market – consumers – with the Dodd-Frank act ⁽²⁾, promulgated on 21 July 2010. Clearly, one has to bear in mind the slower decision-making process in Europe and the fact that European measures tackle the various facets in detail, while the US law provides the framework for subsequent laws and regulations. It is important that these processes move forward in equilibrium and at a similar pace in order that new regulation is approached organically.

3.9 In examining the Commission's proposals, the EESC will compare the two approaches, weigh up the various responses given to particular issues and consider the expediency of incorporating some aspects of the US approach into our own regulations.

3.10 One example worth looking into is the creation of a federal authority for consumer protection (the Bureau of Consumer Financial Protection). The EESC calls on the Commission to undertake an in-depth study of the possibility of establishing a similar authority in the European legal system.

3.10.1 The authority set up in the United States falls within the Federal Reserve and has ample powers that cover a large part of the functions previously carried out by other regulators under consumer protection legislation. This authority will have exclusive powers to oversee compliance with the rules on activities carried out by intermediaries with assets over ten billion dollars and it will have joint powers, along with other supervisory authorities, in the case of intermediaries with assets below that amount.

3.10.2 The EESC thinks that the following points, in particular, should be studied:

— In the United States, the Bureau falls within the Federal Reserve. This can be justified by the need to contain the authority's administrative costs, but could, nonetheless, prejudice its autonomy and independence. The EESC therefore thinks that a more autonomous position for such an authority should be considered.

— The powers of the authority could in some circumstances conflict with those of the financial intermediaries supervisory authorities. A hierarchy of priorities must be established ex ante that will help to contain any possible controversy, since although the stability of intermediaries and markets is of prime importance, so too is the protection of retail investors. The need for investor protection cannot be subordinated to any other principle. In fact, we can only talk about sustainable growth if the needs and protection of the weakest individuals are put at the hub of the system.

— It is important that the focus is put on financial services and products rather than simply on financial institutions. The authority must have its own jurisdiction and be able to intercede any time that financial services or products are offered to the public, even when these do not primarily involve financial intermediaries already subject to other forms of supervision.

3.11 Another important point that must be looked at is the body of rules geared to countering the moral hazard of institutions deemed too big to fail. The options taken by the US legislator in this matter are incisive and far-reaching: the possibility of intervening pre-emptively, ordering the sale of parts of a business to avoid systemic risks, and the requirement of a plan to dismantle conglomerates with a range of activities or so large that any intervention becomes problematic. There is also provision for components established in other countries also being subject to the same measures, therefore influencing the activity of some important EU-based players.

3.11.1 The creation of the European Systemic Risk Board (ESRB) is a move in this direction. Limiting the power of large groups is healthy in many respects. As well as cutting systemic risk, which will let badly managed banks go to the wall, it would help competition, which in turn should keep interest rates under control, making credit more accessible for clients. These ideas have been raised in the past and the regulators should no doubt have paid them greater heed, especially given the particular nature of the finance business, which does not even have the physical limitations of other forms of production.

3.11.2 Although size is of prime importance, it should not be forgotten that this does not alone determine the systemic relevance of an intermediary, which also depends on the functions it performs within the system, how easy it is to replace and how closely interconnected the group is both nationally and internationally. Despite being unduly large, some intermediaries could nevertheless crash together because they share the same risks.

⁽²⁾ Pub.L. 111-203, H.R. 4173.

3.11.3 Regarding financial regulation, the EESC emphasises the need to adopt a balanced approach. The EESC emphasises the substantial benefits in the long term of stricter regulation of financial institutions for the financial stability, economic growth and efficiency of the real economy.

3.12 Some of the measures included in the new US financial regulations are: an early warning system for major systemic risks, regulation of the non-bank system, creation of a council for financial stability, effective legislation on credit rating agencies (CRAs), measures of transparency and credibility for non-standard instruments, including over-the-counter (OTC) markets, and securitisations with asset-backed securities (ABS) and hedge funds.

The European Union's first step was to react to the crisis and champion the need for international coordination, a prerequisite for guaranteeing a level playing field internationally.

3.13 We need to ask ourselves whether the authorities in the different countries are as a whole responding in a similar and joined-up way, since one of the major problems has been caused by regulatory mismatch between the various financial markets.

3.14 Europe should avoid any further delay in completing its reform process – which should be transposed into national legislation starting in 2013 – in order not to penalise companies and the European financial system, which international investors perceive as being poorly governed because of the differences between Member States and the inefficacy of the legislative model.

3.15 Notwithstanding all the Commission's efforts to regulate the single market in a uniform manner, powerful economic and political interests make it ever more difficult to create an effective and far-reaching European supervisory system.

3.16 Having only recently restated the need to swiftly strengthen the legislative and regulatory framework, the EESC backs the Commission's efforts to this end. Civil society at European and national level must continue to press the authorities and public bodies to swiftly adopt new rules in the financial sphere. The EESC has a truly important role to play, both directly and through the organisations of its members, which should promote a serious and informed debate in the Member States. The future of a new sustainable economy and of financial markets dedicated to balanced development and sustainable growth will depend mostly on the

quality of financial regulation. Better and tighter rules are needed so that the market reintroduces an ethical dimension into business as its code of conduct.

4. Specific comments

4.1 The Communication says nothing about the involvement of stakeholders in the impact assessment process or about the measures that have been adopted, except to note that this process has taken place. But who are the stakeholders? Does this refer to the usual electronic consultation, which has doubtlessly involved the industry and some expert group or other (invariably appointed by the financial system), but only peripherally workers and consumers? If so, there is still no real balance of various interests that can be enlisted as soon as the reform process gets off the ground.

4.2 The EESC calls on the Commission to give greater heed to civil society bodies and to making sure they are meaningfully involved. The EESC calls on the Commission to deploy its own resources more effectively to achieve better international coordination between the institutions of democracy in all the EU Member States. There needs to be a serious programme, appropriately funded, to get Europe's citizens involved and to inform them about some difficult but necessary changes.

4.3 The cumulative effects of the various legislative initiatives are not made clear, not least because the measures are not discussed in context and some (Basel III, future international accounting standards) will be in the hands of third parties, such as the Basel Committee and the IASB ⁽³⁾.

4.4 The EESC calls for a strong, comprehensive, efficient and balanced regulation. In order to avoid negative consequences, the EESC recommends that a profound study on the cumulative regulatory initiatives be undertaken for the necessary measures on the financial system and the capital market. A stable and efficient system should promote financial stability and liquidity for the real economy. The Commission will have to face the difficult task, in the context of a complete overhaul of the entire architecture for regulating the markets, of seeking the best balance between prudential measures, increased capital requirements, better risk coverage and classification, and economic development. It will have to do this in a situation in which the financial and economic crisis has been gravely exacerbated by budget consolidation measures.

4.5 The EESC calls on the Commission to redouble its efforts to make common cause with the authorities in the major countries, especially with the G20 countries.

⁽³⁾ International Accounting Standards Board.

4.6 According to the Commission, thirty more legislative proposals are awaiting debate and adoption by the end of next year, but have yet to be allocated time on the Parliament's agenda. The EESC is very concerned and has its doubts whether the programme will actually come to fruition. The next two presidencies of the Union will have their work cut out and the role of the president of the Union, which is intended to bring continuity and effectiveness to actions, has yet to get off the ground. The Commission should ask the European Parliament and the Council to fast-track provisions to regulate markets, which have been too long coming.

4.7 The EESC is ready to support the Commission in this process and to contribute to better regulation through its opinions and ongoing direct consultation. The Commission could task the EESC with advocating in the Member States the need to take quick and comprehensive decisions on the

regulation of financial markets, via public initiatives on the ground involving the social and economic players and financial services consumer organisations. The EESC, together with the network of national and international ESCs, can make an enormous contribution to the positive outcome of the process with action focused on:

- keeping the issue in the spotlight,
- bolstering European and international coordination,
- disseminating the proposals under discussion in the European debate,
- making available its own experience and competence.

Brussels, 16 February 2011.

The President
of the European Economic and Social Committee
Staffan NILSSON
