European Commission - Fact Sheet

Questions and Answers on the Mid-Term Review of the Capital Markets Union Action Plan

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What is the Capital Markets Union?

One of the Commission's top priorities is to strengthen Europe's economy and stimulate investment to create jobs. The Investment Plan for Europe helped kick-start this process. However, to strengthen investment in the long term, we need stronger capital markets that can provide new sources of funding for businesses, help increase options for savers and make the economy more resilient.

The EU economic recovery is gaining momentum, with a fifth consecutive year of growth. There are, however, significant downside risks. The contribution of investment to growth remains low and the investment rate is still below pre-crisis levels. This persistent weakness in investment continues to drag on the push for recovery and longer-term growth. That is why President Juncker set out as one of his key priorities, the need to build a true single market for capital – a Capital Markets Union for all Member States.

The Action Plan published in September 2015 set out the actions needed to put in place the building blocks of a Capital Markets Union (CMU) by 2019, removing barriers to cross-border investment and lowering the costs of funding. As part of the third pillar of the Investment Plan for Europe, the so-called Juncker Plan, the CMU should help businesses tap into more diverse sources of capital from anywhere within the EU, make markets work more efficiently and offer investors and savers additional opportunities to put their money to work in order to enhance growth and create jobs. It will offer benefits for all Member States, while also strengthening the Economic and Monetary Union (EMU) by supporting economic and social convergence and helping absorb economic shocks in the euro area.

Why have you conducted a Mid-Term Review of the CMU Action Plan?

Since September 2015, in accordance with the original time-table, the Commission has delivered 20 out of 33 measures announced in the CMU Action Plan. We have been continuously monitoring developments in order to identify any further actions that are necessary to complete the CMU. As part of our efforts to achieve a CMU that has a tangible impact, we also launched a public consultation and held a public hearing to gather views on the next steps for this pivotal project.

The 178 responses to the public consultation on the CMU Mid-Term Review confirmed the importance for this key programme to remain 'fit for purpose'. While the challenges set out in 2015 are still as relevant as ever, more recent challenges to financial integration have arisen, which call for a review of the CMU agenda. In particular, the future departure of the largest financial centre from the EU makes it necessary to re-assess how the CMU can ensure that EU businesses and investors have access to strong, dynamic and more integrated capital markets, while risks to financial stability are properly managed. More effective supervision and measures to ensure the benefits of the CMU are felt across the entire EU are additional challenges that have come into sharper focus. The CMU must also propose ways to harness the transformative power of financial technology and to shift private capital towards sustainable investment.

The Mid-Term Review aims at addressing these challenges through an additional set of actions which complements the outstanding ones under the CMU Action Plan.

What are the benefits of a Capital Markets Union (CMU)?

The CMU will complement Europe's strong tradition of bank financing and will help to:

- **Unlock more investment from the EU and the rest of the world**: the CMU should help mobilise capital in Europe and channel it to all companies, including SMEs, and infrastructure projects that need it to expand and create jobs. It will provide households with better options to meet their retirement goals.
- **Connect financing more effectively to investment projects across the EU**: the CMU is a classic single market project for the benefit of all Member States. Those Member States with the

smallest markets and high growth potential have a lot to gain from a better channelling of capital and investment into their projects. More developed market economies will benefit from greater cross-border investment and saving opportunities.

- **Make the financial system more stable**: by opening up a wider range of funding sources and more long-term investment, reduce the vulnerability of EU citizens and companies to banking shocks, such as those they were exposed to during the crisis.
- **Deepen financial integration and increase competition**: more cross-border risk-sharing, deeper and more liquid markets and diversified sources of funding should deepen financial integration, lower costs and increase European competitiveness.

What does the Mid-Term Review of the CMU Action Plan entail?

The Mid-Term Review reports on the good progress in implementing the 2015 Action Plan and sets the timeline for the next round of outstanding measures that will be unveiled in the coming months. Moreover, it updates and complements the original CMU agenda with some selected new priority measures to respond to evolving challenges, drawing on the responses to the public consultation of January-March 2017.

The Review is built around a new set of priorities focused on: more effective supervision by the European Securities and Markets Authority (ESMA), ensuring a more proportionate regulatory environment for SME listing on public markets, simplifying cross-border investment and developing capital market ecosystems throughout the EU; and exploring ways to harness the transformative power of financial technology and to shift private capital towards sustainable investment.

The measures identified here, along with the outstanding CMU work-stream, constitute the basis for a decisive and lasting contribution to laying the foundations for a true CMU by 2019. The consolidated set of measures aiming to put the CMU building blocks in place by 2019 is presented in the Annex to the Communication.

Has there been any progress in implementing the measures of the CMU Action Plan?

Yes, the Commission has delivered more than half the measures (20 out of 33) announced in the CMU Action Plan:

- **Venture capital**: The European Parliament and Council reached an agreement in principle on 30 May 2017 on the European Venture Capital Funds (EuVECA) Regulation and the European Social Entrepreneurship Funds (EuSEF) will make it easier for investors to invest in small and medium-sized innovative companies. The selection procedure for managers for one or more private sector-led pan-European Venture Capital Funds-of-Funds will be finalised in the next months. The Commission has also reviewed national tax incentives for venture capital and business angels, and a study setting out good practices is being published today.
- **Companies entering and raising capital on public markets**: The December 2016 agreement by the European Parliament and Council on a modernised EU Prospectus Regulation will start to apply from mid-2019. The Commission has also taken steps to address the bias in the tax system in favour of debt over equity, as part of its October 2016 proposal for a Common Consolidated Corporate Tax Base (CCCTB).
- **Bank capacity to lend to the real economy**: To free up capacity on banks' balance sheets, and so generate additional funding for the economy, on 30 May 2017 the European Parliament and the Council reached an agreement in principle on Simple, Transparent and Standardised (STS) securitisation, alongside a review of capital requirements for banks. In November 2016, the Commission proposed an amendment to the EU's capital requirement rules for banks, empowering it to exempt the entire credit union sector of a Member State. The proposal is now with the Council and European Parliament.
- **Infrastructure investment**: The Solvency II delegated act was amended in September 2015 and entered into application in April 2016, making it cheaper for EU insurance companies to invest in qualifying infrastructure projects. Today the Commission is also presenting measures to review risk calibrations for investment into infrastructure corporates. To encourage private investment by banks in infrastructure projects, we proposed in November 2016 to amend the capital requirements legislation (Capital Requirements Regulation and Directive, CRR/CRD IV). This would create a more risk-sensitive regulatory environment to promote high-quality infrastructure projects and reduce risks for investors.
- **Institutional and retail investment**: In March 2017 the Commission presented its Consumer Financial Services Action Plan, which sets out ways to provide consumers with greater choice and

better access to retail financial services across the EU. The Commission is also gearing up work with the European Supervisory Authorities (ESAs) on increasing the transparency and comparability of costs and performance of retail investment and pension products.

- **Preventive restructuring and second chance for entrepreneurs**: In November 2016, the Commission proposed rules on preventive restructuring, to avoid the liquidation of viable companies with financial difficulties and give entrepreneurs a chance to re-enter business life after bankruptcy. The proposal also lays down rules to enhance the efficiency of insolvency procedures, to make them more predictable, less costly and speedier.
- The Commission's Report of March 2017 sets out a roadmap for **removing national barriers to the free movement of capital**. The Economic and Financial Affairs Council endorsed this roadmap on 23 May 2017.
- **Financial stability**: Following its consultation in 2016, the Commission will now work to ensure that the European Systemic Risk Board (ESRB) has the capacity to monitor potential risks to financial stability arising from market-based finance.

What are the new actions and proposals?

The Commission will now quickly move forward with three legislative proposals, which are central to the creation of a CMU:

1. A legislative proposal on a **Pan-European Personal Pension Product (PEPP)** by **end of June 2017.**
2. A legislative proposal specifying **conflict of laws rules for third party effects of transactions in securities and claims in the cross-border context in the fourth quarter of 2017.**
3. A legislative proposal for an **EU-framework for covered bonds, a key long-term funding tool to help banks finance their lending activity, in the first quarter of 2018.**

In addition, the Commission is also advancing with its preparatory work on the following measures to implement the commitments in the original Action Plan:

- Amendments to the Delegated Regulation supplementing Solvency II **in 2018** to **review the prudential treatment of private equity and privately placed debt**;
- **Recommendation on private placements** (building on the experience of well-functioning national regimes) – **in the fourth quarter of 2017**;
- **Communication on a roadmap for removing barriers to post-trade market infrastructure** (building on the recommendations of the EPTF – the European Post Trade Forum) – **in the fourth quarter of 2017**;
- **Communication on corporate bond markets** (building on the recommendations of the Expert Group on Corporate Bond Market Liquidity) – **in the fourth quarter of 2017**;
- **Code of Conduct to simplify withholding tax procedures**, with a focus on refunds – **by end 2017**.

How can strengthened supervision of capital markets contribute to the objectives of the CMU?

Many respondents to the CMU Mid-Term Review consultation commented on the need for more regulatory harmonisation and convergence to overcome real and perceived cross-border barriers. Respondents from a wide range of stakeholder groups favoured strengthening the mandates of the ESAs with the objective to increase supervisory convergence.

Another recent consultation on the operations of the ESAs also showed that the rules under which the ESAs operate need to evolve to increase the effectiveness of supervision. Stakeholder feedback to this consultation pointed to the need to adjust the regulatory framework to improve the ability of the ESAs to supervise the financial sector and better deliver on their objectives. Responses pointed to a need to strengthen ESMA's ability to identify and tackle weaknesses in national supervision and to identify areas where ESMA's direct supervision may be warranted.

This is why we will propose **amendments to the functioning of the ESAs in the third quarter of 2017,** as mandated by their founding Regulations (Article 81). In targeted areas, the Commission will strengthen ESMA's powers including, where warranted, granting direct supervision to support a functioning CMU.

How will the CMU further enhance SMEs access to finance?

The EU has already made good progress in making easier for companies to enter and raise capital on public markets. For instance, the December 2016 agreement by the European Parliament and Council on a modernised EU Prospectus Regulation will apply from mid-2019.

But more needs to be done to ensure that European companies and investors can reap the full benefits of access to public markets. The number and volume of initial public offerings (IPOs) are much lower than before the crisis, having decreased by 56% and 49% respectively between 2007 and 2016. In particular, public listings of SMEs remain low in the EU. In 2016, smaller companies only represented 6% of the total IPO market. In addition, the amount of equity raised on SME-dedicated markets decreased by €9 billion compared to pre-crisis levels.

Many respondents to the recent CMU consultation called for a proportionate review of the different obligations placed on non-financial issuers, especially SMEs. Those obligations may be too burdensome and can deter these issuers from seeking a listing. The objectives of such a review should be to assess whether the disclosure requirements bring useful information to investors, as well as consider the opportunity to repeal unnecessary disproportionate provisions and create a more balanced regulatory environment for small and mid-cap quoted companies.

The Commission will review the regulatory barriers to SMEs admission to public markets as set out in the Call for Evidence. The review will focus on how **targeted amendments to relevant EU legislation can deliver a more proportionate regulatory environment to support SME listing** on public markets, which could lead to a legislative **proposal in the second quarter of 2018.**

Why is the Commission looking at investment firms in the context of the CMU Mid-Term Review?

Investment firms play an important role in capital markets, and provide a range of services which give investors access to securities and derivatives markets. These services include investment advice, portfolio management, brokerage, execution of orders, proprietary trading and underwriting. Their authorisation and conduct rules are set out in MiFID, and they are subject to EU prudential requirements (CRR and CRD IV).

Respondents to earlier consultations argued that the application of some rules under CRR/CRD IV are not tailored to the business models of investment firms. In particular, it was argued that the CRR/CRDIV should better distinguish between the capital requirements imposed on large, bank-like investment firms and those imposed on smaller investment firms. Some respondents to the CMU Mid-Term Review consultation also emphasised the importance of decreasing the regulatory burden for local investment firms offering their services to SMEs.

This is why the Commission will present a **legislative proposal to review the prudential treatment of investment firms in the fourth quarter of 2017.** A more effective prudential and supervisory framework calibrated to the size and nature of investment firms should improve investors' access to new opportunities and better ways of managing their risks. It should ensure that any relocation of investment firms is not driven by regulatory arbitrage or differences in the supervisory framework.

Will the Commission promote FinTech solutions in the CMU?

With the CMU Mid-Term Review the Commission is assessing how financial technology (FinTech) can contribute to deepening and broadening EU capital markets. The recently launched Action Plan on Consumer Financial Services already seeks to harness the potential of FinTech to bring about better financial services for consumers. Examples of financial innovations that can make the EU capital markets broader and deeper include: crowdfunding and other alternative funding tools; supply chain finance; online shareholder voting; and the possible application of block chain technology in post-trading.

Respondents to the CMU Mid-Term Review consultation underlined that technology and digitalisation have already shown they have a role to play and can overcome some of the barriers and current gaps in consumer financial services. FinTech primarily benefits retail investors by offering a wider choice of services at potentially lower costs. The majority of respondents called for a level-playing field between traditional actors and FinTech companies. Many respondents also believed that the application of FinTech innovations must ensure appropriate investor and consumer confidence and protection.

In addition, the Commission has also launched a targeted consultation to gather feedback on the impact that new technologies are having on financial services. It will provide the Commission with valuable input on: whether new, more proportionate licensing arrangements for FinTech activities and firms in areas such as crowdfunding are needed; how to support FinTech firms, registered in one EU country, doing cross-border business without requiring further authorisation in each EU country ('passporting'). The Commission will assess the **case for an EU licensing and passporting framework for FinTech activities in the fourth quarter of 2017.**

How can the CMU strengthen bank lending and the stability of the EU

banking sector?

Capital markets can help European banks to overcome the challenges of non-performing loans (NPLs) which are weighing heavily on some national banking systems. NPLs have a significant adverse impact on banks' profitability and their ability to lend, including to SMEs.

Many respondents to the CMU Mid-Term Review consultation considered that it would important to foster an EU-wide secondary market for NPLs. They pointed out that this market is currently hindered by high transaction costs.

Secondary markets for NPLs would allow banks to sell their NPLs to a larger pool of investors potentially at prices that better reflect the underlying value of the assets. This will lead to cleaned-up balance sheets and credit institutions better prepared to provide new credit flow to the economy.

The Commission services will shortly launch a public consultation on potential EU action to foster these secondary markets.

More efficient and predictable loan enforcement and insolvency frameworks designed to enable swift value recovery by secured creditors will benefit the management of NPLs. A benchmarking of national enforcement and insolvency systems will be completed in the fourth quarter of 2017. This benchmarking work underscores the challenges facing banks and other secured creditors posed by the lack of efficiency in the legal frameworks for enforcing collateral in order to recover value from non-performing loans.

Therefore, the Commission will launch **an impact assessment to consider a possible legislative initiative in the first quarter of 2018 to strengthen the ability of secured creditors to recover value from secured loans to corporates and entrepreneurs.** This will complement and reinforce the Commission proposal of November 2016 on the effective functioning of the pre-insolvency/restructuring systems.

How will the CMU strengthen the EU's leadership on sustainable finance?

The EU is fully committed to putting sustainability at the heart of its policies. The Paris climate agreement marked a watershed in global commitments to tackling climate change. Providing sustainable finance for investments that lead to a more sustainable economy is therefore essential. In particular, reorienting private capital flows to more sustainable investments requires a comprehensive and deep rethinking of our financial framework.

The market for green bonds has been expanding rapidly over recent years, with the amount of green bonds outstanding more than doubling between end-2014 and end-2015. However, this market still remains marginal, representing less than 0.1% of the global outstanding debt securities market. Respondents to the CMU Mid-Term Review consultation urged the Commission to reflect on steps that could be launched now to begin the recalibration of the EU financial policy framework. Examples of issues that were identified include:

- clarification that fiduciary duties of asset owners and asset managers includes integrating Environmental, Social and Governance (ESG) considerations into decision-making;
- ensuring that sustainability is more central to corporate governance;
- promoting better integration of ESG performance in issuer ratings and key market benchmarks.

The Commission established a High-Level Expert Group in December 2016 to advise it on how to integrate sustainability considerations into EU financial regulation and financial markets practices. The Group has met on a regular basis throughout the first half of 2017. It will produce an interim report in the summer of 2017 that will frame the principal issues and approaches that could be put in place. The report will be finalised in December 2017 and will contain a set of operational recommendations for integration of sustainability considerations in EU financial regulation. Both the interim and the final report will be made public.

The Commission **will follow up, by the first quarter of 2018, on the recommendations of the High Level Expert Group on Sustainable Finance**. In particular, it will set in motion work to improve disclosure and better integrate sustainability in rating methodologies and supervisory processes, as well as in the investment mandates of institutional investors and asset managers. A more sustainable approach should also be applied in upcoming legislative reviews of financial legislation.

How will the CMU knock down barriers to cross-border investment in the EU?

In spite of the progress made in recent years to create a Single Market for capital and financial services, investors continue to face significant barriers when investing across borders in the EU.

In addition, investment funds in the EU are still small and less cost-efficient than in some other jurisdictions. The distribution of funds also remains geographically limited in Europe. The evidence collected during the public consultation shows that a significant barrier is the lack of regulatory and supervisory convergence, including divergent national requirements on the notification, distribution and use of the marketing passport under the UCITS and AIFM Directives, as well as differing requirements for administrative arrangements such as local agents.

Greater cross-border distribution and in particular digital cross-border distribution would allow funds to grow, allocate capital more efficiently across the EU, and compete within national markets to deliver better value and greater innovation.

The Commission will launch an **impact assessment with a view to considering a possible legislative proposal to facilitate the cross-border distribution and supervision of UCITS and AIFs in the first quarter of 2018.**

A stable investment environment is also crucial for encouraging more cross-border investment within the EU. Greater clarity on existing EU investor rights is important not only for the investors themselves, but also for national administrations, stakeholders as well as for national court judges. In the first quarter of 2018, the Commission will adopt an interpretative Communication to provide guidance on existing EU rules for the treatment of cross-border EU investments.

How will the Commission support the development of local capital market ecosystems in the EU?

The maturity of capital markets differs considerably among EU Member States. In particular, capital markets in countries from Central, Eastern and South-Eastern Europe (CESEE) are one third as developed as the EU average. For instance, non-financial firms' access to capital markets in this region is lower that the EU average (6% versus 21% for the EU). The Vienna Initiative has agreed to establish a Working Group on Capital Markets Union in a bid to promote the diversification of investment finance in the region.

The Vienna Initiative was founded at the height of the global financial crisis of 2008/09 as a private-public sector platform to secure adequate capital and liquidity support by Western banking groups for their affiliates in the CESEE region. The Commission will also provide technical support to Member States through the Structural Reform Support Programme, which entered into force on 19 May 2017. The programme will contribute to institutional, administrative and growth-enhancing structural reforms in Member States by providing support to national authorities. Under the programme, the Commission has so far received over fifty requests for technical support in the financial sector from thirteen Member States, with a high focus on support for the development of capital markets.

By the second quarter of 2018, the Commission will propose a comprehensive EU strategy on steps that could be taken at EU level to support local and regional capital market development across the EU. This will build on the report of the Vienna Initiative's CMU Working Group and will take account of experience through the growing delivery of on-demand technical support under the Commission's Structural Reform Support Programme.

Who will implement the CMU actions?

Over the past two years, in accordance with the original timetable, the Commission has delivered 20 out of 33 announced in the CMU Action Plan. But the Commission cannot build a CMU alone. Its success will depend on the level of political commitment from the Member States, the European Parliament and market participants. National authorities and market participants hold the key role to building the market segments, as well as the legal, fiscal and technical infrastructure needed to dismantle barriers to EU integration and develop a true Single Market for capital.

For More Information

Communication on the CMU Mid-Term Review

MEMO on Solvency II Delegated Regulation

MEMO on study on tax incentives for venture capital and business angels

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