European Stability Mechanism

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GREEN PAPER – BUILDING A CAPITAL MARKETS UNION

PUBLIC CONSULTATION

EUROPEAN STABILITY MECHANISM'S RESPONSE *

The European Stability Mechanism (ESM) welcomes the opportunity to respond to the public consultation on the Commission's "Green Paper – Building a Capital Markets Union" whose objective is to foster jobs and growth in Europe by finding efficient solutions to link savers with investors and entrepreneurs.

Building a Capital Markets Union (CMU) is a key initiative in the work programme of the Commission to develop deeper and better integrated capital markets in the EU to complement bank financing and to further the integration of the single market. Deeper and better integrated capital markets promote financial stability and economic growth by creating alternative funding channels for SMEs and corporates beyond bank financing. As a lender to euro area Member States and financial institutions, the ESM is naturally interested in promoting financial stability across the EU. In addition, the ESM - as well as the European Financial Stability Facility (EFSF) – are benchmark issuers in the financial markets with large funding volumes. Some of the elements of the CMU can therefore be directly relevant for the EFSF and ESM as issuers. The developments of the CMU can also be relevant for the flow of securities that both the EFSF and ESM may provide to support member states and/or financial institutions.

The ESM sees the CMU as essential for building resilient and efficient financial markets in the EU. The development of truly pan-European capital markets is limited by many factors, not all of which are due to regulation or solvable through it (lack of retail investor knowledge, certain cultural idiosyncrasies, etc.). Even though a large amount of regulatory integration measures have already been taken (MiFID, AIFMD, UCITS, MAD, etc.) which, together with the Banking Union, set the stage for more integrated capital markets, there is still scope for regulatory action in some areas that could contribute to further integration and a true capital markets union. Building on this, the ESM has prepared the following response.

Beyond the five priority areas identified for short-term action, what other areas should be prioritised?

The five priority areas identified for short term action in the Green Paper cover a wide spectrum of issues regarding which the ESM has specific suggestions and recommendations. In addition to those areas, and based on the obvious synergies with the global objectives of the Green Paper, the ESM recommends that the Commission should focus its attention on the following topics:

- Encouraging Member States towards pension system reform and creating incentives to channel savings towards funded pension schemes;

* *Only questions related to the ESM's scope of activities were addressed*

- Promotion of greater harmonisation of insolvency laws and legal enforceability of cross-border claims;

- Withholding and savings tax harmonisation as they apply to debt securities held in clearing systems (but not only): an effort should be made to eliminate the few known exceptions to the current framework of withholding tax exemptions for listed bonds. The extension of withholding tax exemptions to unlisted bonds issued by SMEs should also be considered;

- Finding an adequate solution to reduce the incentives favouring debt financing to equity financing;

- Reviewing existing and new regulation that affects key players in financial markets to verify that there are no undue obstacles to the stated aims of the Capital Markets Union. In particular, we refer to rules that could hamper the revival of the securitisation market and rules that could further reduce market-making abilities of intermediaries; and

- Measures to increase efficiency of the post-trade function to create a more effective single market for securities and to progress with the harmonisation of securities law.

What further steps around the availability and standardisation of SME credit information could support a deeper market in SME and start-up finance and a wider investor base?

The standardisation of SME credit information is one step in the right direction. The European Commission should contribute to developing a standardised template (for data collection) which lists the key financial data of SMEs. It should be possible to apply this template across jurisdictions without exception. Such a template should warrant complete comparability of companies in different jurisdictions.

Furthermore, another aspect of relevant information surrounding the creditworthiness of SMEs regards the legal framework under which they operate. A broader harmonisation of company law would be beneficial. Particular attention should be dedicated to reforms that promote greater harmonisation of insolvency laws and legal enforceability of cross-border claims. The lack of harmonised insolvency regimes and the cumbersome procedures involved in recovering debt through court proceedings have been major impediments to reducing private sector debt. Many reforms have happened in programme countries, but not so in others. In addition to the other aspects mentioned in the Green Paper, the lack of harmonised insolvency regimes hinders the possibility of pooling claims (of SME credits, for example) on a cross-border basis. Because the insolvency rules and recovery procedures are different, the risks of the claims in different jurisdictions are not homogeneous, hence, they cannot be pooled. If this cross-border pooling was facilitated, the channelling of funds to SMEs would be easier and the effects on growth of the "high quality securitisation" initiative would be greater.

Is any action by the EU needed to support the development of private placement markets other than supporting market-led efforts to agree common standards?

Given that many European corporates already use US private placement markets, a starting point for the development of a European counterpart along the lines of US best practice could be beneficial.

This would have the advantage that European corporates already know how the market works. The US private placement market is standardised, with a set timeline of usually 12 weeks from taking the initial decision to the arrival of funds and standard documents like the "Offering Memorandum" and the "Note Purchase Agreement".

The Commission could contribute to the development of this market by encouraging Member States to alter national legislation where it stands in the way of such a swift and standardised process, notably in respect of withholding tax restrictions.

As the Green Paper emphasises, ICMA has recently released a guide on a Pan-European Corporate Private Placement (PEPP) market, which describes common market practices, principles and standardised documentation for private placements. According to our assessment, the development of a PEPP market may require some fine-tuning of the EU regulatory framework. One of the main barriers already identified in the Green Paper is the differences in national insolvency laws.

Moreover, the majority of PEPP Notes take the form of unlisted securities. However, as a result of domestic legal requirements, tax benefits and investor preferences, some private placement transactions are currently listed in certain national European markets (for example, the French euro private placement market and the Italian private placement market). Therefore, parties to certain PEPP transactions may also seek to have the relevant instruments listed. In such cases, PEPP transaction participants will need, amongst other things, to carefully review the consequences of relevant national and EU legislation for listed transactions, including in relation to the Prospectus Directive, the Transparency Directive or the Market Abuse Directive.

In light of the above, the Commission should re-examine the adequacy of the current regulatory framework in order to find the right balance between supporting the development of the PEPP market and providing enough confidence to investors by ensuring high execution standards and appropriate risk and credit processes.

What further measures could help to increase access to funding and channelling of funds to those who need them?

i. Simplified accounting standard and credit scoring tailored for SMEs

The development of a simplified, common and high quality accounting standard tailored for SMEs, which is suggested in the Green Paper, would help address information problems and credit assessments. In turn, this will help the private sector develop credit scores for SMEs that will have positive spill-over effects on the market for loan securitisations. It is crucial that costs to SMEs for this purpose are not too high.

ii. Promote usage of credit insurance by SMEs

Beyond this, to break the adverse feedback loop between access to credit for SMEs and the recovery in growth, public policy initiatives that foster the use of credit insurance on accounts receivable by SMEs can contribute to increased bank lending to SMEs. This is because banks tend to make more favourable credit assessments of firms that insure their accounts receivable, which in turn facilitates easier access to credit. The usage of credit insurance by SMEs in Europe, however, remains low – estimates point to its use by less than 20% of SMEs. Low awareness among SMEs in combination with high costs of insurance remain key bottlenecks to wider usage. Policies that promote wider use of credit insurance to manage risk of payment defaults on trade receivables are likely to lower the cost of insurance. At the same time, the use of insurance policies by SMEs can lower borrowing costs as banks will factor this into their credit assessments. Policy initiatives that address potential constraints on the supply of credit insurance on accounts receivable are likely to have a more direct effect on loan supply to SMEs.

iii. Standardisation of markets

The Green Paper discusses the standardisation of markets to kick-start the access to funding and capital for SMEs. The use of SME growth markets (“junior markets”) has increased rapidly in certain countries as a good alternative for SMEs to raise capital in traditional stock exchanges.

Under the currently applicable MiFID framework, junior markets are usually operated as multilateral trading facilities (MTFs). MiFID 2 envisages the creation within the MTF category of a new sub-category of SME growth markets, and the registration of those markets. This should facilitate the development of common regulatory standards for those markets in the EU. As a complementary measure, SMEs should receive support to comply with such regulatory standards. This may be achieved by a combination of:

- ESMA pro-actively issuing Guidelines and Q&As for SMEs regarding such regulatory standards; and
- Efficient communication between ESMA and domestic regulators, to ensure that questions posed to domestic regulators by local SMEs are uniformly approached at ESMA level, and that the answers to those questions are made known to other domestic regulators.

iv. Examining the barriers to the wider use of corporate loan asset-backed securities (ABS)

At a time when access by SMEs to funding is seen as fundamental in the context of promoting economic growth, we should consider – in addition to looking at direct access to capital markets as an alternative to bank financing – ways to help banks be more active in the SME segment. For example, with a more dynamic corporate loan securitisation market, banks would be more ready to extend loans to corporates other than highly rated, quoted public companies. In this respect, possible avenues include reviewing the risk-weighted asset charges applied under the CRR to ABS; creating a uniformly accepted credit-scoring system; and establishing a pan-European framework for high-quality securitisation that allows standardisation and lower transaction costs.

Beyond this, tools as provided by the US Small Business Administration that guarantee 20% losses on the pool as a whole, would also foster securitisation of debt based on pooled loans, making it easier for banks to free up their balance sheets for more lending. However, it must be noted that currently this market is very small, and that the bulk of securitised products in the US comes from the GSEs (Government Sponsored Entities, such as the Federal National Mortgage Association) a model which cannot be replicated in Europe. SME ABS can be a very complex and ambitious product, which was not widely traded even before the crisis. To kick-start the market, ABS backed by simpler cash-flow structures should be the focus, such for instance auto loans, credit cards and other receivables.

At present, European authorities are in the final stages of fine-tuning a number of regulatory measures concerning the risk and capital treatment of several asset classes. Such fine-tuning should be made while bearing in mind the need to preserve liquidity in those asset classes, and avoiding the introduction of pricing distortions due to different regulatory treatment of financial instruments and securities products having the same underlying assets. One example of this is the current capital charges on insurers which make a securitised asset much more expensive to hold than single-credit corporate bonds of arguably similar credit quality.

v. Re-examining the Prospectus Directive (PD) regime

The Commission should re-assess the rules applicable to debt securities listed on a regulated market to consider the creation of a simplified framework for smaller corporates. Two areas where some SME-friendly reform might prove particularly useful are the listing requirements under the Prospectus Directive and the ongoing information obligations set out in the Transparency Directive.

The Commission should aim at finding ways to reduce the costs faced by SMEs in preparing and approving an offer prospectus - possibly by simplifying the content of the prospectus for smaller issuers and/or by raising the exemption thresholds. The development of a simplified, common and high quality accounting standard tailored for SMEs would also be useful in this respect.

The role of financial advisory intermediaries in introducing a company to a regulated market for its shares or fixed income securities should be examined. Regulated markets across the EU differ in this respect. At its best, an intermediary performs a valuable role in both supporting a company in listing for the first time and in advising its senior management on compliance with “continuing obligations”, including the *ad hoc* disclosure regime under the Market Abuse Directive. SMEs which do not have experience or resources to meet the demands of making appropriate market disclosure need this support and guidance. At the same time, such intermediaries must be able to perform their role without being subject to an overly prescriptive regulatory regime, which has the effect of raising the fees intermediaries must charge to cover their legal and compliance costs. Best practice and the views of market participants, from sponsors, brokers and their clients, should be sought, and proposals brought forward to make sure that SMEs can get the support they need at a cost they can afford.

vi. Re-examining the adequacy of the current model for the dissemination of regulated information in respect of SMEs

The discussion about the poor cross-border dissemination of regulated information by smaller listed companies and the low interest shown by analysts and investors in those companies (usually referred to as the "black hole" problem) is not new, but a proper solution still seems to be far from reach. There is a wide consensus about the solution for the so-called “black hole” problem not requiring a legislative initiative. However, in view of the objective to foster interest in smaller listed companies, the Commission should be ready to examine alternatives to the current model.

Should measures be taken to promote greater liquidity in corporate bond markets, such as standardisation? If so, which measures are needed and can these be achieved by the market, or is regulatory action required?

Standardisation would certainly promote liquidity in corporate bond markets. Nevertheless, other factors stemming from financial sector regulation are equally relevant with respect to liquidity.

Liquidity requirements can, for instance, affect banks’ willingness to hold adequate inventory of corporate bonds to facilitate market-making. In this case, the benefit to financial stability gained through a reduction in bank balance sheet risk from increased risk weights might have adverse spill-over effects on markets through increased liquidity risk. While financial stability (including that of banking institutions) remains the ESM's foremost concern, one must acknowledge that the minimisation of balance sheet risk brought about by increased risk weighs comes with a cost, and that, as always, the right balance should be struck.

Another factor that impacts liquidity in these markets is whether the future regulatory framework will allow banks to be market-makers in such corporate bond markets. Many brokers are reporting a marked decrease in liquidity, as risk weights and other regulations, such as large exposure limits, mean that it becomes uneconomic for them to hold inventory in less liquid bonds and thus makes it difficult for them to make markets for clients. Some are exiting entire product lines, meaning that investment managers are forced to trade amongst each other and have difficulties in the price discovery process.

Is there value in developing a common EU level accounting standard for small and medium-sized companies listed on MTFs? Should such a standard become a feature of SME Growth Markets? If so, under which conditions?

Yes. See our answer to question 5.

Are there barriers to the development of appropriately regulated crowd-funding or peer to peer platforms including on a cross border basis? If so, how should they be addressed?

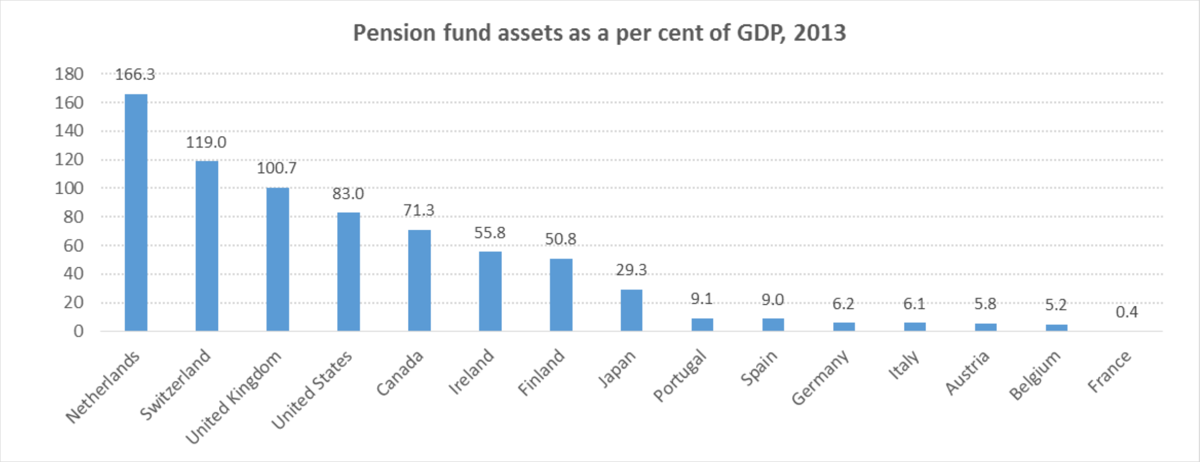
A push towards harmonised company law, in particular insolvency legislation (e.g. creditor seniority, timelines, coordination), would certainly clarify the risks that "crowdfunders" would face when engaging in cross-border investments. Another would be a working group setup to look at the disclosure liability regime, both for professional and non-professional investors and the definition of these categories, which currently does not sit easily within the existing national and EU prospectus liability or misrepresentation regimes.

Ensuring more certainty with regard to cross-border enforcement of claims would also be beneficial.

What policy measures could incentivise institutional investors to raise and invest larger amounts and in a broader range of assets, in particular long-term projects, SMEs and innovative and high growth start-ups?

The Green Paper appropriately emphasises that growing capital markets in the EU will require policies that promote a greater inflow of institutional investor funds into these markets, including in instruments that fund long-term infrastructure projects. In this context, the Commission staff working document notes that *further developments of funded pension schemes would have a positive impact on the size of EU capital markets*. This point is worth exploring further, considering that a majority of retirement plans in the euro area are set up a "pay-as-you-go" (PAYG) schemes with no capital stock backing such pension commitments. Netherlands, which has a fully funded pension scheme, is a notable exception to this. Finland also has a funded pension scheme to complement a minimum state pension. The size of funded assets as a per cent of GDP that back pension commitments across several countries is shown in Graph 1.

Graph 1



Source: OECD

A progressive shift away from PAYG pension schemes towards funded pension schemes can unlock significant funding to support the growth of long-term financing in the EU. The Commission staff working document recognises this and notes, *capital market development in the US was in part spurred by the development of a private pension system*. Indeed, as of end-2013 US retirement plans (individual retirement accounts and employer sponsored defined contribution plans such as 401(k) plans) held U.S. $6.5 trillion of mutual fund assets making up nearly 43 per cent of all mutual fund assets. The increased equity ownership of US households relative to households in the EU can be largely attributed to their participation in private pension plans rather than any stark differences in cultural attitudes.

Promoting private pensions in Europe, however, will face significant challenges as alternative financing arrangements to honour contractual commitments on existing PAYG schemes will have to be made. This is because pension contributions of employees transferred to the funded scheme will not be available for making the pension payments. Yet, developing deeper and better integrated capital markets in the EU will depend on whether pension systems in a number of countries in the EU can be reformed to include an additional funded private pension scheme element, managed by professional asset managers. For example, the funded private pension schemes in the United States complement the social security system that provides the first pension pillar. In Switzerland, a second pillar of privately funded pension scheme (with option to have an additional third pillar) complements the first pillar of minimum state pensions. In the Netherlands, this has been achieved by the favourable taxation of pension fund contributions and investments, which channel savings to the pension industry. To the extent that these large funds include allocation to alternative asset classes, such as private equity and venture capital, they will contribute to the growth of these markets.

Developing privately funded pension schemes that are portable across borders can also alter labour market mobility and positively impact jobs and growth in the EU.

In this regard, Commission’s initiative to strengthen the single market in pension provision through the introduction of a standardised and portable pension product, and removing the existing obstacles to cross-border access, deserves strong support.

What steps could be taken to reduce the costs to fund managers of setting up and marketing funds across the EU? What barriers are there to funds benefiting from economies of scale?

The European mutual funds industry can play an important role in attracting new funding channels to SMEs and corporates. However, the relative small size of (regulated) mutual funds in Europe (versus, for example, US funds) seems to prevent such role. Without an adequate size, it is virtually impossible for mutual funds to invest in longer-term (less liquid) projects while maintaining the necessary liquidity to address the redemption requests from its investors. Closed funds may not be the best way to address this issue, as their lack of liquidity may hinder their attractiveness for investors. Tax policies could also be used to better align incentives for longer-term investments. In view of the above, measures to facilitate the existence of larger mutual funds could be beneficial in this respect.

Should work on the tailored treatment of infrastructure investments target certain clearly identifiable sub-classes of assets? If so, which of these should the Commission prioritise in future reviews of the prudential rules such as CRDIV/CRR and Solvency II?

It is important that CRDIV/CRR and Solvency II create incentives to risk-pooling and risk-sharing. Originators of loans should be able to issue securitised products in which they retain a risk slice to ensure interest alignment and obtain sufficient capital relief to make the transaction viable. From an investor point of view, this is beneficial as risks in infrastructure investments otherwise would be too concentrated and long-dated to manage appropriately in a portfolio.

Would the introduction of a standardised product, or removing the existing obstacles to cross-border access, strengthen the single market in pension provision?

The design of existing pension plans in the EU tend to discourage worker mobility across the national borders. These plans are incompatible with today’s mobile workforce, which requires schemes that are easily portable when workers change employers, and an integrated European economy. The introduction of a standardised funded retirement savings scheme that is portable across borders can act as a catalyst to foster both greater integration of capital markets as well as labour markets. For example, the standardised pension product could be structured to share some features with the 401(k) plan in the United States, which is portable across employers and states. The introduction of such a standardised pension product, for example through a pan-European or 29th regime, would contribute to strengthening the single market in pension provision.

Complementary to the overall legal regime facilitating the portability of pensions, the development of specific products and harmonization of related legislation may play a role. Facilitating the use of suitable investment instruments, such as N-bonds (“Namensschuldverschreibung”), through standardized European level framework would facilitate cross-border investment and accessibility. Similarly, harmonized taxation, e.g. for withholding and income taxes, would facilitate cross-border investment. Strengthened investment opportunities would in turn offer better opportunities for pension funds to structure their portfolio and provide products across borders, and thereby the provision of pensions in a single market.

How can the EU further develop private equity and venture capital as an alternative source of finance for the economy? In particular, what measures could boost the scale of venture capital funds and enhance the exit opportunities for venture capital investors?

Venture capital is the start of the cycle in order to develop a stronger market for private equity, equity capital markets and debt capital markets. In Europe, however, venture capital investment is still 4.5 times smaller than in the US.[1]

Some of the issues related to venture capital (VC) investment in Europe currently being discussed are:

i) The existence of few truly European funds: in fact, the majority of the VC funds are still of US origin;

ii) Geographic concentration: European VC funds are mainly clustered around London (and, to a lesser extent, Berlin, Amsterdam and Barcelona);

iii) The role played by public sector entities: governments and other public sector institutions can play a crucial role in terms of taking steps to create or promote regulatory frameworks and entrepreneurial ecosystems in which VC investment can thrive. For example, the European Investment Fund, has a very positive mandate, but the applicable framework tends to favour established bank funds rather than new venture funds (e.g. by requiring at least 10 years of VC experience, which, by their nature, new funds do not have);

iv) Cumbersome legislation: in some countries, for example, the legal framework requires the entrepreneur not to have had significant business failures previously (which is very common in new ventures, as it is a trial and error, entrepreneurial approach).

Mitigating the elements above could boost European VC investment and ease the exits to private equity. A stronger VC sector could also contribute to the transparency usually required for retail investors directly to invest in post-venture capital firms at the IPO stage.

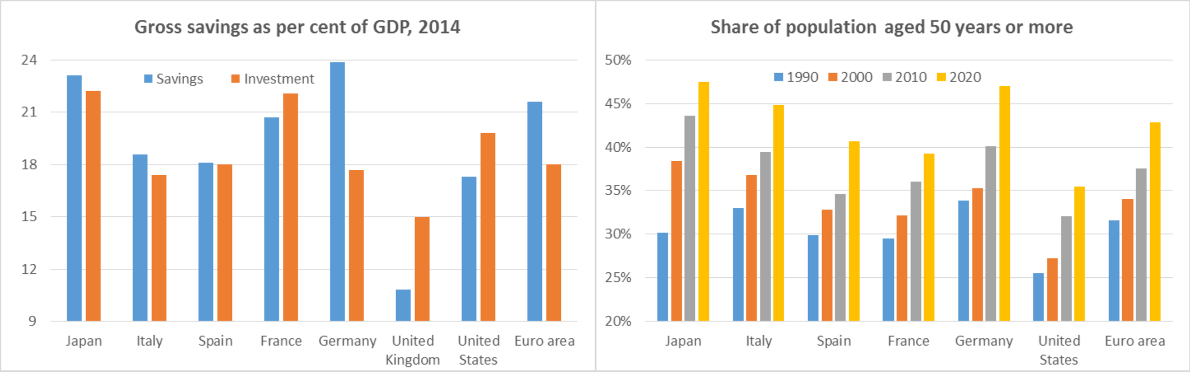
How can cross border retail participation in UCITS be increased? Also, What policy measures could increase retail investment?

Some of the challenges of transforming savings into investments (for example, through the mutual funds industry) have their roots in a wide policy concern: the EU's aging population and its natural aversion to risk taking. This has implications for retail participation in UCITS.

Gross savings in the euro area have exceeded total investment as a per cent of GDP by 2.8% annually on average over the period 2010-14. By contrast, investment exceeded savings as a per cent of GDP by 2.8% in the United States and 3.3% in the United Kingdom in the same period. One might be inclined to think that measures promoting cross-border retail participation in UCITS or other investment vehicles would help finance the investment needs in the euro area through reallocation of the excess national savings across the single market (Graph 2, left panel).

[1] Ernst & Young, Adapting and evolving Global venture capital insights and trends 2014, p. 2.

Graph 2



Source: Haver Analytics

However, the role of the traditional banking sector in intermediating this is likely to remain fundamental and difficult to replace. This is because the savings-investment balance and the decision to transform savings into investments will be affected by risk attitudes as well as demographics. For example, gross savings as a per cent of GDP has been consistently higher in Germany compared to the United States. This reflects both risk attitudes as well as a more ageing population in Germany (Graph 2, left panel). Indeed, studies based on microeconomic data tend to support the hypothesis that the desire to dis-save is not there among the elderly. Savings behaviour also do not appear to be affected by the rate of return or the level of interest rates so that zero or even negative interest rates in the euro area may not change behaviour. On investments, empirical studies point to a fall in investment as the population ages.

In an ageing society as in the euro area, risk aversion will remain entrenched, creating excess demand for financial instruments that are both risk-free and liquid. Insured deposits offered by banks to its customers meet such criteria. Transforming the short-term deposits to fund riskier investments or long-term infrastructure projects will remains a core function of banks. This will have to be a focus of new initiatives in this area.

What policy measures could increase retail investment? What else could be done to empower and protect EU citizens accessing capital markets?

Cross-border legal transparency and certainty seem the main obstacle for retail investors to invest abroad. In particular retail investors do not normally have the resources to engage in large scale investigations of a foreign legal system. In this respect a harmonisation would of course be the best solution. As a second step, the ability to enforce cross-border claims in a simple and unitary way would also be important.

More specifically, the harmonisation of securities laws would certainly enhance legal certainty in the retail segment. Currently, an account holder's (that is, investor's) legal position from the moment a security is posted to their account varies substantially. In some countries, the account holder has full and undivided ownership. In other countries, they have an "inferior" legal position, i.e. they hold an indirect interest in a property or just a claim against the account provider, possibly governed by the law of a different jurisdiction.

Also see our comments on SME credit information in question 2.

Are there mechanisms to improve the functioning and efficiency of markets not covered in this paper, particularly in the areas of equity and bond market functioning and liquidity?

In this context, we would emphasise again (i) measures to enhance efficiency of clearing systems (see our response to question 26) and (ii) the benefits of developing of a pan-European regime for prospectus liability (please see our response to question 25).

Do you think that the powers of the ESAs to ensure consistent supervision are sufficient? What additional measures relating to EU level supervision would materially contribute to developing a capital markets union?

The gradual convergence of supervisory regimes for market regulation of securities is crucial for the operation of the single market in securities. Supervisory authorities across the EU should follow an increasingly consistent approach to exercising their discretionary powers in order to decrease transaction and custodial costs in cross-border investment. ESMA has an important role to play here, both as a forum for promoting convergence and, in time, by having its mandate gradually extended.

Specifically, the development of a pan-European regime for prospectus liability would materially facilitate cross-border investments and hence contribute to developing a capital markets union. This is also true when thinking about the attractiveness of the European market towards investors in third countries, especially the United States. Part of the reason that large investors in the US private placement and public securities markets are reluctant to invest in securities issued in the EU market is the uncertainty over the liability in damages of the companies issuing those securities compared to their own jurisdiction.

Taking into account past experience, are there targeted changes to securities ownership rules that could contribute to more integrated capital markets within the EU?

Europe should strive towards a simple and less layered architecture with strengthened legal certainty. A simple system is easier to understand, which increases the confidence of investors and issuers. Many costs and interdependencies generated by the current multi-layer system could then be reduced. See also our response to question 19.

In view of integration and investor confidence it would be useful to consolidate the information on holders of each marketable security issued in the EU in a single register that establishes the legal right of every final investor (that is, potentially at the level of private citizens). This could be done by creating a European bond and shareholder register and connecting it to the ECB's Target2-securities settlement service to be launched soon.

This would provide means to improve transparency on EU securities for both the issuers and public authorities such as supervisors, judicial systems and tax authorities. It is cumbersome and costly for issuers to obtain reliable information on the final holders of the securities issued by them, which may have implications on corporate governance as often only the largest holders are identified and can affect corporate strategies. Investors do not have control of the account relationships of their service providers (therefore risks).

Currently, stocks are held through a (sometimes lengthy) chain of custodial account relationships across borders. The reliable functioning of records in every link of the chain becomes an operational risk and a potential complication since they may be subject to laws under different jurisdictions. The burden from resilience requirements on intermediary accounts could be alleviated, as they provide no legal proof of ownership, and costs reduced.

The register could be operated under a public mandate by either a public authority or a private company. To avoid conflict of interest, it could be a different entity than the one operating the settlement engine. Investors could be provided browsing access to their own centralised accounts, and they could grant access to the account to selected intermediaries as necessary. As a result, an investor would be able to sell securities with a different intermediary than the one through whom they were bought (without resorting to additional securities transfers).

It would also ensure that no securities are used for multiple purposes (e.g., as collateral before final title transfer) simultaneously, which strengthens the system in terms of financial stability. Such proof of ownership through a register would also separate fully risks arising from the underlying security and the service provider, which would also be a matter of importance.

What measures could be taken to improve the cross-border flow of collateral? Should work be undertaken to improve the legal enforceability of collateral and close-out netting arrangements cross-border?

Acknowledging the existence of the financial collateral directive, the question arises whether further improvements can come from operational and technical fields to ensure efficient and prompt means to mobilise securities while securing certainty on securities interest, such as a pledge on a security, and eliminating the risk of multiple use of the same securities. We refer to our response to question 26, suggesting a consolidated register at final investor level, which would also accommodate the booking of securities interests other than legal and/or beneficial ownership.

Within the Target2-securities project, the ECB can play a key role in bringing all EU securities depositories on board by ensuring a pricing that provides a truly level playing field for the national depositories, irrespective of their size and volumes and the extent to which securities issued in the country are mostly held domestically or cross-border. Moreover, the underlying technology platform should eliminate unnecessary procedures from links between EU central securities depositories.

Moreover, many banks have difficulties in accepting collateral located in another EU jurisdiction. This applies especially to retail clients and non-financial assets, such as real estate. It is presumably related to lack of knowledge of local insolvency legislation, national language and cost of liquidation. It could be examined whether the legal ownership in assets such as real estate could be transformed economically into a form of a security that could be mobilised through CSDs, or if national registers on real estate and land could be harmonised and connected efficiently similar to CSDs.

What specific aspects of insolvency laws would need to be harmonised in order to support the emergence of a pan-European capital market?

In order to support the kind of cross-border risk pooling needed for high-quality securitisation that truly shares risk across the EU, the following aspects of insolvency law should be harmonised:

- Ranking of unsecured claims;
- Categories of secured, preferred claims, and the nature and extent of their rights against the insolvency estate;
- Legal consequences of insolvency in contractual relationships; and

- Hardening periods and claw back rights.

Harmonisation of insolvency laws in all EU Member States is a difficult endeavour. As an initial step, the Commission should consider conducting a study on how the above-mentioned compare across EU jurisdictions, to determine if any standard may be used for harmonisation.