

# **EUROPEAN ECONOMIC AREA**

## **STANDING COMMITTEE OF THE EFTA STATES**

Ref 1090920  
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### **Subcommittee II on the free movement of Capital and Services**

#### **EEA EFTA Comment on the proposals concerning financial supervision made in the de Larosière report published on 25 February and in the Commission Communication of 4 March 2009**

#### **1. Introduction**

1. The EEA EFTA States refer to the consultation launched by the Commission on 10 March on the improvement of the supervision of the financial sector in the EU following the report of the de Larosière high level group on financial supervision and the Commission communication from 4 March.

#### **2. Background information on the EEA Agreement and the EEA EFTA States current implication in the EU Financial Services structure**

2. The three EEA EFTA States Iceland, Norway and Liechtenstein are fully integrated into the internal market through the EEA Agreement. In accordance with the Agreement all EEA legal acts relevant to financial services that have been adopted by the EU apply equally to Iceland, Norway and Liechtenstein. In other words rights and obligations ensuing from the single market legislation apply to the three EEA EFTA States to the same extent as to the EU members. The EFTA Surveillance Authority ensures that the acts are interpreted and implemented correctly and in a consistent manner.
3. Regarding the current EU “Lamfalussy” committee structure within Financial Services, the three EEA EFTA States have observer status in the existing Level 2 and most of the Level 3 Committees and have thereby contributed actively to regulatory and supervisory developments and convergence of supervisory practices. The EEA

EFTA States contribute financially to the functioning of the Level 3 Committees on a bilateral basis.

### **3. General Remarks**

4. The EEA EFTA States welcome the opportunity to comment on the recommendations in the de Larosière report and on the Commission's proposals in its Communication with regard to the supervisory framework. The EEA EFTA States would like to contribute to developing a more efficient and pro-active financial regulatory and supervisory structure in the European Economic Area.
5. In general the EEA EFTA States agree with the analyses and the proposals outlined and can endorse the reforms suggested. Regulation and supervision did not succeed in preventing the global financial crisis. Reforms are therefore necessary and needed quickly. The current financial crisis and the consequence for the global financial system have revealed the importance of introducing a macro-prudential approach alongside improved micro-prudential arrangements to EU supervisory architecture. Also the methods of monitoring financial stability need to be improved. In this context, the EEA EFTA States welcome the Commission's initiative to review and further improve the European supervisory arrangements covering all financial sectors.
6. Some of the roots of the crisis may be found in the strong growth of financial products and financial institutions which have not been subject to regulation, prudential supervision and capital requirements. The EEA EFTA States see it as an overarching goal to close these gaps and ensure that the whole financial sector is subject to supervision and regulation, and that regulation between different segments of the market is mutually consistent (based on the principle of 'same risk, same regulation'). All relevant financial actors and all types of financial instruments need to be subject to appropriate regulation and oversight.

### **4. New framework for Macro-prudential Supervision**

7. All the three EEA EFTA States have integrated financial supervisory authorities. Norway was in the forefront of this development with the first integrated supervisory authority established in 1986. After the Nordic banking crisis in the 1990's Norway also saw the need to include macro-economic surveillance into their day to day financial supervision of firms and of the financial market, and has since then had a macro-prudential approach to supervision. The macro-prudential issues are closely related to micro-supervision and provide valuable input to the supervision of firms and the analysis of the situation in the market pertinent to financial institutions. It is therefore based on prior experience that the EEA EFTA States fully support the proposal to bring macro-economic oversight and micro-prudential supervision together at a European level. In our view a financial crisis will always include macro-economic elements as well as elements related to supervision and regulation and it is of great importance to involve financial supervisors in the new macro-prudential framework and the proposed European Systemic Risk Council (ESRC).
8. It is also the view of the EEA EFTA States that in order to achieve the best possible coordination on a macro-prudential level within the whole of the EEA, it is important that the central banks of EU/EEA countries outside the euro zone be given the

opportunity to participate in the ESRC. As long as any financial institution from any country within the EEA can establish a branch in any other country within the EEA, risks can also be transferred to any country within the EEA, and the macro-prudential supervision should hence encompass all countries in the EEA. The EEA EFTA States are of the view that it would diminish the effectiveness of EEA-wide coordination if the EEA EFTA States did not actively participate from the outset in the EU macro-prudential supervisory structure.

## **5. Enforced and New Framework for Micro-Prudential Supervision**

9. Based on the active participation of the EEA EFTA States in the existing Level 2 and 3 Committees as outlined in the introductory remarks, the EEA EFTA States assume that any change in the current regulatory and supervisory architecture in the EU, regardless of the model which eventually would be chosen, will provide for the opportunity for all EEA EFTA States to participate as observers. At the moment this opportunity is not fully provided for all EEA EFTA States, given that Liechtenstein is not allowed to participate and contribute to the work of CESR. In the light of the extended powers, which the future EU supervisory "authorities" will presumably assume, the opportunity for participation of all EEA EFTA States will be even more fundamental. We expect that experts from all EEA EFTA States will be invited as observers in the appropriate authorities within the new European System of Financial Supervision in addition to being present in the to be established European Systemic Risk Council.
10. With regard to the timing of the reforms, the EEA EFTA States support the Commission's intention to set up the new supervisory framework in the course of 2010. We agree that there is a need to move swiftly and to merge phase 1 and phase 2 of the supervisory reforms suggested by the de Larosière group.
11. With regard to the possible merger of the existing Level 3 Committees into a new authority, based on their longstanding and positive experience with integrated financial markets and integrated supervision, the EEA EFTA States support a merger of the current "sectors" of EU supervision into one authority. A single market conduct and prudential authority would in our view ensure the best possible coordination of financial market supervision in the future, thus avoiding possible regulatory and supervisory gaps.
12. Merging the current Supervisory Committees into one would also result in cost efficiency, decreasing the burden on each national supervisor as regards representation and reducing the Secretarial resource needed.

## **6. Role and responsibility of the new EU supervisory "authorities"**

13. The EEA EFTA States agree that the day-to-day supervision of domestic financial institutions must remain the responsibility of the national authorities. We agree with the proposal to give the new European securities authority the responsibility for licensing and supervising specific EU-wide institutions such as credit rating agencies and post-trading infrastructures.

14. We understand that it is the Commission's intention that the new EU Authorities shall play a significant role related to mediation and shall set up legally binding mediation mechanisms. They shall be charged with oversight and ultimate decision making powers regarding colleges of supervisors for cross-border financial groups. We underline the importance of ensuring a fair balance of power between the home country supervisory authorities and the host country supervisory authorities. The competence must ultimately remain with the competent authorities responsible for the institution in question.
15. One important issue is the supervisory responsibilities for branches vs. subsidiaries, including the supervisory power for the host country authorities and its influence on supervision of branches. The host country authorities should have access to mechanisms to influence the supervision of the branches. Such measures should be investigated, i.a. powers to require conversion into subsidiaries for systemically important branches.
16. The Commission proposes that the authorities be mandated to adopt legally binding standards. At national level, supervisory authorities have different mandates and are not always empowered to adopt laws and regulations. Hence it might be a challenge to give the EU authorities the mandate to adopt decisions that are binding on the national supervisory authorities. This would pose a legal challenge to the EEA EFTA States as long as they are not included in the decision-making process.
17. In addition, the authorities shall play a coordination role in a crisis situation. These new roles cannot be assumed overnight as they require major legislative amendments. We agree that the authorities shall play a key role in early warning mechanisms and crisis management, in cooperation with the ESRC.

## **7. Concluding remark**

18. The financial system is in acute need of reform. The EEA EFTA States are of the opinion that the recommendations by the de Larosière group and the measures and proposals signalled by the Commission in its Communication should be followed up swiftly and without undue protectionist resistance by national governments or authorities, as such a reform would be in the long term interest of the whole EEA. However, a new supervisory architecture cannot be superimposed on a still fragmented and unharmonised legal framework. In order for this new supervisory structure to work according to the intention, extensive legal reforms are needed.
  19. The EEA EFTA States hope that their comments are found useful and that they will be taken into consideration in the Commission's preparations for the proposal for a future EU Supervisory Architecture. The EEA EFTA States and their relevant authorities are prepared to take part in future work at EEA level to ensure harmonised improvement of the supervision for the financial services sector in the EEA.
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