

## Financial services: what to expect from the European Commission



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The financial services sector is a cornerstone of the European Union Single Market. The sector is a driving force for economic prosperity, it unquestionably affects all EU citizens, it is a source of innovation and entrepreneurship, and its health or weakness influences all areas of activity. This notwithstanding, financial services have traditionally represented one of the most challenging sectors to integrate due to several factors, including differences in national culture and business practices, and the wariness of some EU member states which view market integration as an encroachment of national sovereignty.

The appointment of Frenchman Michel Barnier as commissioner for the internal market including financial services was controversial and some member states viewed it with scepticism. They were concerned that his appointment signalled a turn towards a heavier regulatory approach. Barnier's situation was not helped by French President Sarkozy's comments following the nomination, which implied that the commissioner's independence of national influence – a prerequisite for all members of the commission – might be less than total. Barnier, himself a former member of the commission, has worked hard, and successfully, to dispel these doubts. He has a reputation as a conscientious and experienced politician and a team player. These qualities will stand him in good stead as he moves forward with his new responsibilities.

### The priorities

Commissioner Barnier's first occasion to outline his priorities in the financial services sector was at the February 16 meeting of EU ministers of economic and finance. This event took place one day before the first meeting of the new College of Commissioners ("Barroso II"). In the post-meeting press conference, he identified five tasks as requiring immediate attention:

1. The establishment of an effective EU financial supervisory system.
2. To identify and close existing regulatory loopholes in financial services and, more broadly, internal market, legislation.
3. To contribute to agreeing common rules at international level to guarantee strength and stability in the global financial sector.
4. To improve the risk management and internal control dimensions of corporate governance.
5. To develop safeguards to prevent and manage future crises.

These objectives are challenging by any standards all the more so in the current economic climate. They are not, however, new, as commissioner Barnier largely inherits the dossier of legislative projects, many of which have formed part of the EU Financial Services Action Plan which has evolved over the past decade. There is renewed urgency in seeing these challenges met.

### A closer analysis of the priorities

The proposed framework for financial supervision was inspired by the conclusions of the report prepared by Jacques de Larosière, whose recommendations have been transformed into EU regulatory proposals to introduce greater control of the principal financial services sectors in relation to banking, securities, and insurance and pensions. This would be achieved by reinforcing and expanding the role of the existing "Lamfalussy Committees",

among other things, by including them more actively in the preparation of technical standards, strengthening their coordinating role and, in some instances, exercising direct supervisory powers or giving them decision-making powers. As regards macro-economic supervision, a proposal to establish a systemic risk board would complete the regulatory framework. Indicative of the urgency of putting this new financial architecture in place is the fact that the Council of Ministers agreed a “general approach” on these proposals within three months or less of their being proposed. There is optimism that the proposals, now under discussion in the European Parliament, can be adopted and in place before the end of this year.

Commissioner Barnier has vowed aggressively to identify and close existing regulatory loopholes which weaken the financial system. In doing so, he applies his principle (stated during his hearing with members of the European Parliament in January), that “... no market, no territory and no institution [should] escape supervision”. Initiatives which may be expected in this connection are: revision of the Markets in Financial Instruments Directive, the standardisation of derivatives and the thorny issue of short-selling. This latter practice is the subject of a Committee of European Securities Regulator’s report expected any day and the commission is expected to announce an EU-wide consultation on short-selling disclosure rules in mid-2010. “Regulatory loopholes” also, importantly, concern tax matters (e.g., tax havens or regarding prudential matters). On this topic, the commissioner aims, as stated in this post-Ecofin press conference, to take determined action against non-cooperative tax jurisdictions.

Bearing in mind that the European Commission is a college of commissioners whose decisions are taken as a college and in which there are inevitable areas of shared responsibility. On the issue of tax avoidance, commissioner Barnier will be working closely with Algirdas Semeta, commissioner responsible for tax and customs, audit and anti-fraud.

The G20 is prominent in pressing for the strengthening of global financial sector stability, and commissioner Barnier has made clear his support for its initiatives and his intention to ensure that the EU plays a leading role within this forum. Illustrative of the commission’s desire to spearhead initiatives to strengthen stability is the proposed, and controversial, Alternative Investment Fund Managers Directive. Such an initiative had been discussed in the context of recent G20 meetings, but it was the commission which was first in introducing draft legislation on this financial product. The proposal originated under the previous commissioner, Charlie McCreevy; there is no indication, however, that commissioner Barnier will not work for its adoption.

On the establishment of common international rules for the financial sector, commissioner Barnier had an opportunity recently to present his views to the press. When asked about the suitability of proposed reforms that the US administration recently announced, he noted that these could not be transferred to a European environment as the structure and administration of the two financial systems were in many ways quite dissimilar. He said, rather, that the importance of the US and EU initiatives was that they shared a determination to realise the goals of the G20 on both sides of the Atlantic. On more than one occasion, commissioner Barnier has stated his intention to introduce stronger rules on financial remuneration in the financial services sector as part of efforts to improve risk management and corporate governance. This, like rules that govern alternative investment funds, is a frequently debated issue with opinions strongly divided and the commissioner will face a challenge to bring any form of discipline to the practice.

Finally, commissioner Barnier shares the goal of the entire commission in ensuring that an effective structure, accompanied by appropriate rules and a realistic enforcement mechanism, are put in place to prevent future economic crises. Commissioner Barnier has set himself a number of challenges in the months to come. Achieving his goals will require the support and cooperation of the European Parliament, whose new “post Lisbon” powers strengthen its voice in the legislative process. In this respect he has the twin advantages of being a former member of the European Parliament himself and the parliament’s general enthusiasm following his January hearings. Based upon his performance during his (admittedly) short period as member of the commission, it may be assumed that he will adopt a determined stance in ensuring the progress of EU financial services initiatives, while at the same time being even-handed in his approach.

*This article first appeared on [www.complinet.com](http://www.complinet.com) on 4 March 2010.*