# Simpler financial regulation

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The purpose is to discuss the challenge of complexity in the EU's financial regulation and how to advance work on simplifying financial regulation, including possible principles on financial regulation and simplification.

***Context: the need for simpler financial regulation***

Simplifying EU regulation is vital for strengthening European competitiveness, economic performance and security, as underlined in the Budapest Declaration on the New European Competitiveness Deal by EU Heads of State or Government, the European Commission priorities, as well as in the Draghi report on EU competitiveness. The work on the Savings and Investments Union (SIU), which aims to create better financial opportunities for EU citizens and channel the massive European savings to productive investments, will also be guided by considerations of simplification, burden reduction and digitalisation.

Delivering on the simplification agenda within the field of financial services has to be done while safeguarding financial stability and preserve consumer and investor protection. It requires both simplifying existing financial regulation *(a backward-looking approach)* and a stronger focus on reducing complexity in new regulation *(a forward-looking approach)*.

The Danish Presidency has asked New Financial to analyse European financial services regulation in view of the objective of simplification. New Financial has presented its findings in a report on European market outcomes and the complexity of regulation as well as suggestions to simplify existing rules and the creation of new rules.

**The role of the financial sector in the economy**

The global financial crisis and the sovereign debt crisis had severe consequences for the EU economy, public finances and the financial sector. Regulation of the financial sector – globally and within the EU – was rightly strengthened and made more prudent in response. Given the sectors' size and role as an intermediary in the European economy some complexity in financial regulation is unavoidable. However, over time, the regulation has grown increasingly complex. Extensive and complex regulation entails burdens for companies, just as it is also more cumbersome to supervise. As a result, both companies and supervisory authorities risk having fewer resources available to identify and address the most important risks. In addition to the value of reducing burdens, simpler financial regulation can also strengthen the understanding of and compliance with rules by market participants.

The aims of this major overhaul of the financial regulation have been manyfold: ensuring financial stability, protecting public finances from banking crises, investor protection and combatting money-laundering and terror financing activities. Simplification should, as a main rule, not lead to less ambitious regulation, nor the removal of key requirements on e.g. capital, liquidity, resolution, or consumer and investor safeguards. In pursuing such an approach there is room for making regulation simpler and potentially also removing some requirements, while maintaining the purpose of the regulation.

*Principles for simplifying financial regulation*

In light of the need for simplification and inspired by New Financial's analysis, the future work on simplifying financial regulation could be guided by e.g. the following principles, while allowing for flexibility for the EU to act quickly due to crises or other urgent matters:

I. **The key pillars of financial regulation should be preserved**, as they are essential for financial stability and long term economic prosperity. The key pillars - including in particular robust capital requirements, liquidity requirements and resolution frameworks for credit institutions as well as investor protection, supervision, anti-money laundering and terrorist financing - must be preserved and take international standards into account.

II. **A "sense check": Develop better problem statements at the "level 0":**
- Before work on new rules fully starts, the Commission should at "level 0" go through a limited amount of high-level questions in order to sense check whether a new rule is necessary in the first place and to clarify how a potential new rule can be developed and implemented as simple as possible. The statement should focus on what problem any piece of financial regulation is trying to solve, what sort of market outcomes a successful implementation would deliver, and why existing rules and measures are insufficient to achieve these outcomes. And the result may well be that no further work on a new rule is carried out.
- The Commission should discuss these with the Member States for example in relevant Council working parties or expert groups and potentially the European Parliament.

III. **Simplification of the existing stock of regulation** could focus on a thematic omnibus approach to e.g. identify and eliminate duplications and inconsistent definitions, out-dated provisions, a complete check of need to have and not just nice to have reporting requirements and/or on identifying a few "big hitters" with high impact. The work could be guided by principles of achieving political objectives in the most effective and cost-efficient way.

IV. **There is a need for consistent and better impact assessments throughout the legislative process**, and they should as a minimum include:
- **Realistic cost estimates** at both the EU and, subject to data being made available, national level. This includes detailed analyses of IT and digital platforms requirements, which are especially costly both for private and public entities to develop.
- Assessment of **cross border activities** to support why new legislation is needed at EU-level.
- An assessment of **what existing legislation is made redundant or is now considered to be disproportionality burdensome and might be removed** because of the new legislation.

All proposals should be **accompanied by an impact assessment** when presented by the Commission. In the event that a proposal from the Commission is not accompanied by an impact assessment, the relevant working party could discuss if this is duly justified as the first order of business. If not duly justified, the Presidency could refuse to take the negotiations forward until a comprehensive accompanying impact assessment has been put forward. Both the Council and the European-Parliament should also consider to classify more amendments in the legislative process as "significant" and carry out impact assessments of their amendments.

**V.** **Better coordination on implementation and new reporting requirements may only enter into force once a year:** Coordination, timing and implementation of legislative files should be improved in order to ease the implementation burden on market participants. Moreover, new or revised reporting requirements should only take effect once a year. This should apply for both level 1 and level 2.

**VI.** **A regulatory time-out through fewer and more targeted review clauses:** New regulation should be given time to take effect before further rules are introduced. Review clauses with full evaluations after a certain number of years, which focus more on *when* to review legislation than *why* to review, tend to lead to more new legislation rather than finding that the current legislation is sufficient. Instead review clauses should

- Be fewer in number and more clearly justified
- Be targeted towards specific parts of the legislation
- When used, leave time for new regulation to have effect and generally apply five years after implementation, unless sector-specific needs justify otherwise.

This approach reduces administrative burdens and avoids diverting Commission resources from more urgent priorities. At the same time, the Commission with its right of initiative can propose changes any time, if needed.

**VII.** **A clearer legislative hierarchy:** Many different stakeholders are involved in financial regulation, and every stakeholder has a responsibility in adding complexity. The complexity seems to be a *feature of the system, not a bug*. To ensure well-functioning financial markets, the rulebook must be clear, stable and easy to navigate and with an accessible overview. As a general principle

- <u>Level 1 acts</u> should contain essential political choices, be clear on objectives and measures of success of the rules, and provide fewer and clearer mandates to level 2.
- <u>Level 2 acts</u>:
    i. Should be used more sparingly, be better justified in level 1 and remain focused and technical in nature, within the clearly defined mandates.
    ii. After a political agreement is initially approved by Coreper, the Commission should critically assess the level 2 mandates it has been given and whether new rules at level 2 are actually needed. This analysis should be presented to the co-legislators before the final adoption of the legislative act, in order to highlight possible deficiencies and unjustified complexity and give the co-legislators an opportunity to reflect.

iii. The ESA's should implement their mandates with a view to ensure a clear, simple and focused outcome.

- Level 3 measures (guidelines etc) should be used more sparingly and with a view to deliver a clear and focused outcome.

With guidance from the ministers and central banks, the 2026 report from the Commission on the banking system in the Single Market, including the evaluation of competitiveness, could also contribute to a way forward on how to advance simplification.

**Questions for discussion:**
*Do you agree that there is need to simplify the existing* ***stock*** *of financial regulation, and do you agree on the principles outlined above? If so, do you have any suggestions for concrete action and potential "big hitters" in the existing stock, e.g. simplifying and strengthening usability of capital buffers, reducing reporting requirements or the amount and complexity of consumer and investor information?*

*Do you agree that there is a need to ensure that the* ***flow*** *of new financial regulation is simpler, and do you agree on the principles outlined above? In particular, do you agree on the idea of a 'sense-check' addressing overall questions on the value-added etc. of new regulation ahead of possible proposals, and the suggestion to have more clarity on objectives and material rules at level 1 and more focus on fewer and shorter technical standards at level 2 and guidelines at level 3?*

*Do you support that the Council should work on principles to guide the Commission, co-legislators and Member States in simplifying existing and new financial legislation? Do you support laying down such principles in Council conclusions and what principles would you consider especially important?*

*Would you support Council conclusions asking the Commission to provide an analysis of how the legislative process for financial regulation could be improved, and possibly a proposal on how to institutionalise a process, which reduces the amount and complexity of level 2 mandates?*