

## Az Európai Unió Hivatalos Lapjában (2011. november) kihirdetett jogforrások listája, illetve a pénzügyi szolgáltatások szektorral kapcsolatban az Európai Bizottság honlapján közzétett hírek

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## Jogszabályok

### 1.

Jogszabály:

**A BIZOTTSÁG 2011/90/EU IRÁNYELVE (2011. november 14.)  
a 2008/48/EK európai parlamenti és tanácsi irányelv I. mellékletében található, a  
teljeshiteldíj-mutató kiszámításához alkalmazandó további feltevésekről szóló II. rész  
módosításáról**

Megjelent:

L296 (11.15.)

Jogforrás tartalma:

Az 2008/48/EK irányelv végrehajtásával kapcsolatban készült tagállami felmérés során feltárásra került, hogy az irányelv I. számú „Az egyrészről a lehívások, másrészről a visszafizetések és díjak egyenlőségét kifejező alapegyenlet” című mellékletének II. „További feltevések a teljeshiteldíj-mutató kiszámításához” című részében megadott feltevések nem elegendőek a teljeshiteldíj- mutató egységes kiszámításához, valamint nem állnak már összhangban a piacon fennálló kereskedelmi helyzettel.

A piaci gyakorlat és a szabályozás közötti összhang megteremtése érdekében szükségessé vált az I. számú melléklet II. részében említett feltevéseket olyan új feltevésekkel kiegészíteni, amelyek a futamidő nélküli hitelekre vagy az egy összegben, ismételten visszafizethető hitelekre vonatkozó teljeshitel-mutató kiszámítási módját érintik. Indokolt olyan módok meghatározása is, amelyek a hitel eredeti lehívásának időzítésére és a fogyasztó által végrehajtott törlesztésre vonatkoznak.

Az I. számú melléklet II. részére vonatkozó módosító rendelkezéseket az irányelv melléklete tartalmazza.

A tagállamoknak legkésőbb 2012. december 31-ig kell elfogadni és kihirdetni azokat a törvényi, rendeleti és közigazgatási rendelkezéseket, amelyek szükségesek ahhoz, hogy ennek az irányelvnek megfeleljenek. Erről haladéktalanul tájékoztatják a Bizottságot.

A tagállamoknak a rendelkezéseket 2013. január 1-jétől kell alkalmazniuk

Az irányelv 2011. december 5-én lép hatályba.

### 2.

Jogszabály:

**A BIZOTTSÁG 1205/2011/EU RENDELETE (2011. november 22.)  
az 1606/2002/EK európai parlamenti és tanácsi rendelettel összhangban egyes  
nemzetközi számviteli standardok elfogadásáról szóló 1126/2008/EK rendeletnek az  
IFRS 7 nemzetközi pénzügyi beszámolási standard tekintetében történő módosításáról**

Megjelent:

L 305 (11.23.)

Jogforrás tartalma:

A Nemzetközi Számviteli Standard Testület (IASB) 2010. október 7-én közzétette az IFRS 7 *Pénzügyi instrumentumok: közzétételek – Pénzügyi eszközök átadása* standard módosításait (a továbbiakban: a módosítások).

A módosítások célja, hogy segítsen a pénzügyi kimutatások felhasználóinak jobban értékelni a pénzügyi eszközök átadásához kapcsolódó kockázati kitettséget és a kockázatoknak a gazdálkodó egység pénzügyi helyzetére gyakorolt hatását. Céljuk, az átadási tranzakciókkal – különösen a pénzügyi eszközök értékpapírosítását magukban foglalókkal – kapcsolatos beszámolásban az átláthatóság előmozdítása.

A módosításokat minden társaságnak a 2011. június 30. után kezdődő első pénzügyi éve kezdőnapjától alkalmaznia kell.

Az irányelv 2011. november 26-án lép hatályba.

## **Sajtóbejelentések**

1.

### **EUROPEAN COMMISSION - PRESS RELEASE**

#### **Restoring confidence in financial statements: the European Commission aims at a higher quality, dynamic and open audit market**

Brussels, 30 November 2011 - The 2008 financial crisis highlighted considerable shortcomings in the European audit system. Audits of some large financial institutions just before, during and since the crisis resulted in 'clean' audit reports despite the serious intrinsic weaknesses in the financial health of the institutions concerned. Recent inspection reports by national supervisors have also criticised the quality of audits.

Under the proposals adopted today by the European Commission, this situation is to change by clarifying the role of the auditors and introducing more stringent rules for the audit sector aimed in particular at strengthening the independence of auditors as well as greater diversity into the current highly-concentrated audit market. Furthermore, the Commission is also proposing to create a Single Market for statutory audit services allowing auditors to exercise their profession freely and easily across Europe, once licensed in one Member State. There are also proposals for a strengthened and more coordinated approach to the supervision of auditors in the EU. Taken together, all the measures should enhance the quality of statutory audits in the EU and restore confidence in audited financial statements, in particular those of banks, insurers and large listed companies.

Internal Market and Services Commissioner Michel Barnier said: *"Investor confidence in audit has been shaken by the crisis and I believe changes in this sector are necessary: we need to restore confidence in the financial statements of companies. Today's proposals address the current weaknesses in the EU audit market, by eliminating conflicts of interest, ensuring independence and robust supervision and by facilitating more diversity in what is an overly concentrated market, especially at the top-end."*

#### **Background:**

Auditors are entrusted by law to give an opinion on the truth and fairness of the financial statements of the companies they audit. The financial crisis highlighted weaknesses in the statutory audit especially with regards to banks and financial institutions. Concerns around conflicts of interest have been expressed as well as the potential for an accumulation of systemic risk as the market is effectively dominated by four companies ("the Big Four"), namely Deloitte, Ernst & Young, KPMG and PricewaterhouseCoopers.

**Key elements of the proposal:**

The proposals regarding the statutory audit of public-interest entities, such as banks, insurance companies and listed companies, envisage measures to enhance auditor independence and to make the statutory audit market more dynamic. The key measures in this respect are:

*Mandatory rotation of audit firms:* Audit firms will be required to rotate after a maximum engagement period of 6 years (with some exceptions). A cooling off period of 4 years is applicable before the audit firm can be engaged again by the same client. The period before which rotation is obligatory can be extended to 9 years if joint audits are performed, i.e. if the entity being audited appoints more than one audit firm to carry out its audit, thus potentially improving the quality of the audit performed by applying the "four-eyes principle". Joint audits are not made obligatory but are thus encouraged.

*Mandatory tendering:* Public-interest entities will be obliged to have an open and transparent tender procedure when selecting a new auditor. The audit committee (of the audited entity) should be closely involved in the selection procedure.

*Non-audit services:* Audit firms will be prohibited from providing non-audit services to their audit clients. In addition, large audit firms will be obliged to separate audit activities from non-audit activities in order to avoid all risks of conflict of interest.

*European supervision of the audit sector:* In addition, given the global context of audit, it is important that coordination of and cooperation on the oversight of audit networks is ensured both at EU level as well as internationally. Therefore, the Commission proposes that the coordination of the auditor supervision activities is ensured within the framework of the European Markets and Securities Authority (ESMA).

*Enabling auditors to exercise their profession across Europe:* The Commission proposes the creation of a Single Market for statutory audits by introducing a European passport for the audit profession. To this end, the Commission proposals will allow audit firms to provide services across the EU and to require all statutory auditors and audit firms to comply with international auditing standards when carrying out statutory audits.

*Cutting red tape for smaller auditors:* The proposal also allows for a proportionate application of the standards in the case of small and medium-sized companies.

[MEMO/11/856](#)

The proposals can be found at:

[http://ec.europa.eu/internal\\_market/auditing/reform/index\\_en.htm](http://ec.europa.eu/internal_market/auditing/reform/index_en.htm)

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2.

Brussels, 30 November 2011

## Reforming the Audit Market - Frequently Asked Questions

### I. Context and key messages

#### 1. Why is audit important?

The role of audit is to contribute to the credibility and reliability of financial statements. For this reason, it is an integral part of the financial reporting environment and its importance is reflected in statute (Fourth and Seventh Company Law Directives) with a requirement for certain companies to have an audit. Moreover, only approved auditors can undertake these statutory audits.

Statutory audit refers to the mandatory annual audit of companies and is aimed at providing an accurate reflection of the veracity of a company's financial statements to stakeholders.

#### 2. What are the existing rules on audit?

A number of instruments exist at EU level: both binding and non-binding rules for the conduct of audits required by EU law, requirements to be met by auditors and the supervision of the latter.

The main EU instrument, dating from before the 2008 crisis, is the Statutory Audit Directive ([2006/43/EC](#)). The Directive sets out the duties of statutory auditors and introduced a requirement for public oversight of the audit profession and co-operation between regulatory authorities in the EU.

#### 3. What are the main weaknesses facing the audit market?

The audit market faces a number of weaknesses:

- a lack of choice for audit clients resulting from high concentration levels (in essence an oligopoly);
- systemic risk if one of "the Big Four" (Deloitte, Ernst & Young, KPMG and PwC) collapses. In that case, there would be even more concentration at the top end of the audit market;
- possible conflicts of interest and issues around the independence of auditors;
- doubts around the credibility and reliability of the audited financial statements of banks, other financial institutions and listed companies. These came in for heavy criticism during the crisis.

For example, more recently, there has been considerable media coverage of apparent audit failures (e.g. Anglo Irish Bank, BAE Systems, Lehman, Satyam and Olympus). This would strongly suggest that audit is not working as it should and has seriously dented the credibility of auditors.

#### 4. What are the main objectives of audit reform?

The legislative proposals follow an extensive consultation process which included the Commission's Green Paper on Audit Policy (see [IP/10/1325](#)). The proposals address issues revealed by the crisis and aim to restore confidence in the audits carried out in the EU.

The main objectives of the reform are to:

- clarify and define more precisely the role of the auditor;

- reinforce the independence and professional scepticism of the auditor;
- make the top end of the audit market more dynamic;
- improve the supervision of auditors;
- facilitate the cross-border provision of statutory audit services; and
- reduce unnecessary burdens for SMEs.

[In more detail:](#)

- Mandatory rotation of the audit firm after 6 years (9 years if two audit firms used). A cooling off period of 4 years will be applicable.
- Prohibition of Big 4-only contractual clauses (clauses requiring that the audit is undertaken by one of the Big 4 firms).
- Mandatory tendering for audit mandates.
- Stricter rules on the appointment of auditors with an increased role for the audit committee.
- The audit committee's recommendation for the appointment of an auditor should be discussed at the general meeting of shareholders. The audit committee's independence and technical competence should be reinforced: at least two of its members must be independent and at least one should have knowledge of audit.
- Auditors will be prohibited from providing non-audit services to audit clients. The provision of non-audit services to non-audit clients is allowed.
- Large audit firms will be required to separate their audit activities into pure audit firms i.e. a complete ban on the provision of non-audit services by the large audit firms.
- EU-level cooperation by the European Securities and Markets Authority (ESMA).
- National audit supervisory authorities would be strengthened. The mandate, powers and independence requirements for audit supervisors would be established at EU level, but supervision would be carried out nationally.
- European certification of audit firms recognising their aptitude to perform high quality audits of listed companies. The certificates would be issued by ESMA.
- Regular dialogue will be held between auditors, audit committees and supervisors.
- Mutual recognition of statutory auditors approved in Member States to ensure cross-border mobility of auditors.
- The content of the audit report will be expanded to provide more information to all stakeholders.
- An additional more detailed audit report for the audit entity itself which will provide detailed information on the audit carried out to the audit committee and management.
- Establishing additional requirements on the internal organisation and governance of audit firms.
- Compliance with the International Standards on Auditing (ISAs) by all statutory auditors and audit firms. Member States should ensure that the audit

standards are adapted to the size of the audited entity to ensure a proportionate and simplified audit for SMEs.

### **5. What share of the European audit market do the Big Four have?**

The market share of the Big Four for audits of listed companies exceeds 85% in the vast majority of Member States. In the UK, the Big Four audit 99% of the FTSE 100 companies and more than 95% of the FTSE 350 companies (1995-2004). In Germany, two Big Four firms have the audit mandates for 90% of the companies listed on the DAX 30 (KPMG and PwC). In Spain, all IBEX 35 companies are audited by the Big Four.

### **6. Why propose a regulation and amend the Statutory Audit Directive?**

Public Interest Entities (PIEs)<sup>1</sup> often have cross-border activities and their auditors also operate at EU level. In such cases, audits should be performed on the basis of a harmonised framework and the supervision of audit networks should be carried out at EU level in order to be effective. This can best be achieved through a Regulation which would be directly applicable, therefore providing a higher level of harmonisation and legal certainty.

The amendments to the Directive concern all audits and not just the audits of PIEs.

### **7. Why act now when the existing Directive is only in force since mid-2008?**

Some of the weaknesses, shortcomings and potential failures that came to light during the crisis had not been anticipated by previous legislation and to this extent further revision in this domain has become necessary.

The fact that European and global economies are still experiencing turbulence is all the more reason to take action now, especially if markets are to regain credibility, trust and confidence.

Maintaining the [status quo](#) will not bring about stability in the market. Indeed, the 700 replies to the consultation and other contacts with stakeholders demonstrate that there is an appetite for change, albeit to varying degrees. Many of the proposals will build on or reinforce existing provisions in the Directive.

### **8. Why is the audit reform not being handled under the European Commission's antitrust arm?**

Because we are talking about regulatory changes whereas competition policy is about the enforcement of existing rules to deal with mergers (the Merger Regulation), restrictive practices (Article 101 of the EU Treaty) or suspected abuses (Art 102). In the absence of a merger which would meet the threshold of EU merger control, the European Commission (Directorate-General for Competition) is only entitled to intervene when it has suspicions of antitrust infringements (collusion or abuses of dominant position).

### **9. Why does the reform concern audits of all listed companies and not only banks and financial institutions?**

Considering the importance of listed companies, as well as banks and financial institutions, it is vital that high quality audits are conducted on their financial statements to strengthen investors' confidence in the market as a whole.

## **II. Impact of the proposals**

### **10. Will the proposals damage audit quality?**

Audit quality derives from independence, professional scepticism and technical competence. All of these elements will be enhanced by the proposed reforms and consequently, audit quality as a whole will be improved.

### **11. Will the measures proposed lead to increased costs? What about job losses?**

The Commission's better regulation principles ensure that a rigorous impact assessment is conducted for all legislative proposals.

Some of the measures (such as mandatory tendering and rotation) will entail increased costs for the audited entities but these will be outweighed by the positive effects, such as enhanced independence leading to better quality audits and a more effective audit environment. The proposals will make the top segment of the audit market more dynamic.

The Commission broadly estimates that for public interest entities with a market capitalisation or a balance sheet total in excess of €100 million, costs, depending on the size of the company and the audit committee, could range from €90 000 to €150 000 per annum.

For smaller public interest entities (including those which are SMEs), the additional costs would be less than €10 000 per annum especially as there would be no obligation to either have audit committees or to tender for auditors.

Furthermore, the reform may lead to some restructuring and better allocation of resources. In the case of pure audit firms, audit clients may still use consulting and non-audit services of other providers. The European passport and certificate will facilitate more cross-border opportunities for auditors and firms.

### **12. What are the benefits of the proposals? Who will benefit?**

Although no single component of the financial system can be solely blamed for the financial crisis, it is important to ensure that each component is examined in detail to ensure that improvements are made with a view to the future. The predominance of 'clean audit reports' for banks throughout a crisis during which the European Union committed €4.6 trillion between October 2008 and October 2010 to support banks - such aid amounting to 39% of the Union's GDP for 2009 - renders a serious overhaul of the existing system inevitable.

Many of the benefits of these proposals will accrue at a macro-economic level e.g. stability and confidence in the market.

Furthermore, more informative audit reports will reinforce confidence in robust companies and the latter will eventually enjoy a lower cost of capital and access to better business opportunities when compared to a company where the audit reveals deficiencies. Moreover, such benefits will be of a recurring nature.

The introduction of common auditing standards at the level of the Union should result in total recurring net benefits for the EU economy as a whole through lower costs of capital which are estimated to exceed €2 billion. Since these net benefits are recurring, the present value of the net benefits in perpetuity can be estimated at €40 billion (if using an assumption of a long-term discount rate of 5%).

Stakeholders, investors, shareholders and companies will primarily benefit from better quality audits and restored credibility and confidence in financial information. Next tier audit firms (i.e. those who are not members of the largest networks) will benefit from a reduction in barriers to entry to the top segment of the audit market and new cross-border opportunities. Member States, auditors and supervisors will benefit from more harmonised requirements, legislation and standards. Finally, society as a whole and the European

taxpayer, who is ultimately footing the bill for the bank bailouts, will benefit from the stronger role of auditors in the prevention of future crises.

**13. What is the Commission doing to bridge the expectation gap (the gap between what stakeholders expect of an audit and what auditors actually do)?**

We are making clearer what an audit is and what should be expected of it. Closer cooperation between the auditor, the audit committee and supervisors will also help to clarify and meet the expectations of stakeholders.

The new measures will also require auditors to report more information, including any risks identified, to the management and audit committee of the audited entity. The auditors will also be required to communicate more with supervisors. There should, however, be no confusion between the role of the auditor and that of supervisors, credit rating agencies or market analysts.

**14. Will the proposals stifle competitiveness or hinder growth (of PIEs)?**

These proposals will have a positive impact on the economy and financial stability by strengthening investors' confidence in the financial statements of PIEs. Not only will they not damage growth, they will help to restore confidence in the financial market by increasing the ability of PIEs to attract investment for future expansion and growth.

**15. How will the proposals impact on SMEs?**

SMEs fall into two categories: SMEs who are audited entities and SMEs who are statutory audit providers (the so-called SMPs).

The proposals do not impose any new burdens on SMEs who are audited entities as they are exempt from most measures. Mandatory tendering and rotation will apply to SMEs who are PIEs but these are generally larger SMEs and are generally already subject to additional sector related regulatory requirements. Member States will have to ensure that the application of the auditing standards to the statutory audit of medium-sized companies is proportionate to the scale and complexity of the business of those companies. This could potentially decrease the costs of such audits.

In addition, the on-going revision of the Accounting Directives is proposing simpler accounts for smaller entities as well as increasing the threshold under which an audit is required (see [IP/11/1238](#)). Therefore, there would no longer be an EU requirement for small companies to have an audit.

For SMEs who are audit providers, the proposals will increase the opportunities to provide cross-border services and reduce the associated cost of providing such services. In addition, the measures aimed at lifting market entry barriers will have a positive effect on SME audit providers and facilitate expansion of their activities.

**III. More detail on key elements of the proposals**

**16. How will the initiatives encourage new players at the top end of the market?**

The proposals would introduce European certification of audit firms. This will recognise the audit firm's capacity to undertake audits of large listed entities. The certificates would be issued by the European Securities and Markets Authority (ESMA). Regular tendering and rotation of audit firms would give the next tier of audit firms more opportunities to win audit mandates in the top end of the audit market.

**17. What means will the national oversight bodies have to effectively oversee the statutory auditors and audit firms?**

The national oversight bodies will be strengthened, as they will be given more powers such as more investigative powers and their independence from the audit profession will be reinforced i.e. they will no longer be allowed to delegate inspections to the professional bodies.

**18. Why is audit supervision being integrated into ESMA?**

The oversight will still be undertaken at national level in the first instance. However, cooperation and coordination at European level to ensure effective supervision of audit firms operating across the EU is best served by an Authority such as those recently established for supervision in the areas of banking, insurance and pensions. ESMA will take over the current functions of the European Group of Auditor Oversight Bodies (EGAOB). ESMA will also issue standards and guidelines to harmonise supervisory practices. ESMA will additionally be responsible for the issuance of the European Quality Certificate

**19. What is the rationale for proposing mandatory rotation of the auditor?**

There are obvious risks to having the same auditor for 50 or 100 years as does happen today. Such a long professional relationship undermines the auditor's independence and negatively impacts on his/her professional scepticism. Rotation of the key audit partner is an important improvement which was introduced in previous legislation but is insufficient because the main focus remains client retention. A new partner would be under pressure to retain a long standing client of the firm. And it would be unlikely that he/she would criticise the work of the previous audit partner (his/her colleague).

In order that rotation and tendering are carried out with sufficient frequency to ensure enhanced independence and better audit quality, the Commission proposes to set mandatory rotation after 6 years.

Mandatory rotation is the '[sine qua non](#)' of the whole package of proposals as the other measures in isolation will not be sufficient to reinforce independence and professional scepticism.

**20. What is the rationale for mandatory tendering?**

Mandatory tendering will increase transparency and openness in the award of audit mandates. It will give mid-tier firms more opportunities to bid for audit mandates at the top end of the market. It will also facilitate more involvement of the audit committee in the selection of the auditor

**21. Wouldn't a strengthened audit committee be sufficient to address issues of independence?**

Audit committees are currently not always in a position to influence the appointment of the auditor.

A strengthened audit committee will have a positive impact on audit quality by better overseeing the selection and work of the auditor. However, this measure alone will not be sufficient to tackle key shortcomings. The other proposals are necessary to allow the audit committee the opportunity to exercise a stronger role.

**22. Why propose a ban on the provision of non-audit services to audit clients?**

There are obvious issues of potential conflicts of interest when the same audit firm offers both audit and other services to the same client. A ban on the provision of any non-audit services to audit clients will ensure that high quality audits are the primary focus of the audit provider. It will prevent potential conflicts of interest, as well as reinforcing independence and professional scepticism.

### **23. Why are pure audit firms only proposed for the larger audit firms?**

Big firms represent a very large proportion of PIE audits. It is critical that such audits are conducted in an independent manner without any 'pollution' from other commercial interests.

In addition, in the case of a change of auditor, large audited entities can face a limited choice between just one or two audit firms as the others are disqualified by virtue of providing non-audit services. This has resulted in a shift of bargaining power to the large firms remaining in the market. This problem has recently been highlighted in the consultation paper on mandatory rotation by the American auditor supervisor.

### **24. Will pure audit firms be able to attract top talent?**

Yes. Professional training requires minimum periods of supervised audit experience. There would be no limitation on people leaving the audit firm for other lines of business. Currently people can move from audit to other fields within the same firm. People also leave to join other firms.

### **25. Is the modification of the ownership rules incompatible with the measures aimed at enhancing auditor independence?**

Broader ownership rules whereby we eliminate the requirement to keep the majority of the capital of an audit firm in the hands of auditors. This will give audit firms more access to capital which may increase the number of audit providers and encourage new entrants into the market. The requirement that a majority of the members of the administrative or management body of an audit firm are audit firms or statutory auditors will be maintained. This, in addition to other safeguards, will ensure that the shareholders do not intervene in any way that would jeopardise the independence and objectivity of the auditors. Investors should not be able to have a controlling influence on the audit firm.

### **26. Why are the big established players opposed to reform?**

The big players wish to retain the ['status quo'](#) on market-related issues and they fear that the proposals will harm their business. However, it is important to note that the proposals are not an attack on the larger players but an attempt to overcome the lack of perceived independence of such players, to enhance the quality of audits performed in the EU and to remove barriers for smaller players.

## **IV. Wider context**

### **27. Is the reform of audit an isolated event?**

The Commission is working on several fronts to address the problems revealed by the financial crisis. A number of areas have already been reviewed or are under review as part of our objective to ensure that all financial actors are appropriately regulated (e.g. banks, insurance companies, investment funds, credit rating agencies etc.). Audit is an important element of the financial environment and cannot be overlooked if the benefits of all other regulatory changes are to be achieved and maximised.

## **28. Is the Commission acting alone on audit reform?**

While the Commission took the lead when it launched its Green Paper on audit in October 2010, a number of other actors are also examining the needs to reform audit.

The United States of America is considering important changes particularly in the domain of the independence of auditors and transparency of audits. Serious consideration is also being given to the mandatory rotation of audit firms to address what are perceived as grave shortcomings.

In the UK, the House of Lords' enquiry on audit concluded that there were serious problems in the way audits of banks had been carried out during the crisis. The enquiry found the auditors to be "disconcertingly complacent" and even spoke of a "dereliction of duty". Serious concerns were raised about the concentration levels of the audit market.

The UK Office of Fair Trading has referred the market for the supply of statutory audit services to large companies in the UK to the Competition Commission for a market investigation based on concerns that the market is highly concentrated, with low levels of switching and substantial barriers to entry.

The international Financial Stability Board is considering audit as one of its future work streams.

More information:

[http://ec.europa.eu/internal\\_market/auditing/reform/index\\_en.htm](http://ec.europa.eu/internal_market/auditing/reform/index_en.htm)

<sup>1</sup> :

PIEs are banks, other financial undertakings and listed companies in general as defined in the Statutory Audit Directive 2006/43/EC. As the financial sector evolves, new categories of financial institutions are created under EU law and thus the definition of PIEs was amended by the proposal for a Directive amending Directive 2006/43/EC to also encompass investment firms, payment institutions, undertakings for collective investment in transferable securities (UCITS), electronic money institutions and alternative investment funds.

**3.**

**SPEECH/11/766**

**Michel BARNIER**

Member of the European Commission responsible for the Internal Market and Services

**Insurance and pensions: challenges and opportunities for deepening the Single Market**

EIOPA Annual Conference - European Insurance and Occupational Pensions Authority

**Frankfurt, 16 November 2011**

Ladies and Gentlemen,

First of all I should like to thank EIOPA and its Chairperson, Gabriel Bernardino, for organising this first annual conference under the EIOPA banner.

As you know, EIOPA, the successor to the former CEIOPS Committee, came into being on 1 January this year. I have fond memories of the inaugural conference organised by the City of Frankfurt a few months ago. And I am taking this opportunity to thank Gabriel [Bernardino], the Executive Director Carlos Montalvo, and the whole EIOPA team for their dedicated and efficient work which has enabled EIOPA to take off fast.

I wish to thank all of you for being here today.

Your conference focuses on three key issues – Solvency II, occupational pensions institutions, and consumer protection. I will come back to those in a moment.

What I am here to talk about are the challenges and opportunities facing the insurance sector in the Single Market. In the current economic climate it may seem much easier to talk about the challenges facing EIOPA, the insurance and pensions sector, and Europe as a whole.

But I believe that we should not sink into pessimism. When Jean Monnet was asked whether he was an optimist or a pessimist, he usually replied "I am neither. I am merely determined". I think that, if we want to be ready to seize the opportunities that will emerge from this series of crises, the time is ripe for a new determination.

But to get back to our challenges for a moment: the most pressing challenge is to stabilise the European economy — in other words, to address the sovereign debt crisis and restore calm and rationality to the financial markets. The agreement reached by the European Council and the Eurozone Summit on 26 October is a significant step forward.

For the first time we decided to respond to every challenge of the crisis: the future of Greece, of course, but also the challenges of sovereign debt, the banking situation, compliance with the common Eurozone rules, and lastly – perhaps the most crucial issue in the eyes of Europeans – the challenge of a return to growth.

This ambition explains why the decision was a difficult one. It must only strengthen our determination to put the decision into practice. And in every component of this plan, a partial approach would quite simply be ineffective.

We must deal with the emergency. This will require a collective effort by the Commission and by every Member State of the European Union.

Ladies and Gentlemen,

Let us now return to the key topic of your conference. As I have just mentioned, the founding of EIOPA almost a year ago was a crucial step taken in the insurance sector.

In its first year of operation EIOPA too has faced many challenges. I will mention three of them:

- the operational challenges of setting up a new authority – here I am referring mainly to human resources and adjustment to new procedures;
- the challenge of a new mindset, which is necessary if the transition from a committee of supervisors to an authority acting in the interests of the entire EU, with powers of enforcement, is to succeed;
- the challenge of an ambitious work programme. This year, the top two priorities were to prepare to implement Solvency II and the request for an opinion sent to EIOPA on the revision of the IORP [Ai:O:R:P] Directive on institutions for occupational retirement

provision. I shall return to these two important initiatives by also saying something about the current discussions in global terms. And I shall end with the revision of the Insurance Mediation Directive, which is a key issue for consumers.

### **I – First initiative: Solvency and the international context**

With Solvency II, our aim is to introduce, in all the Member States, a modern, economy-driven solvency regime based on the risks to European insurers and reinsurers. As you know, the Framework Directive was adopted in 2009.

This is an ambitious proposal which we are putting forward in close cooperation with the co-legislators and with EIOPA. I should like to remind you of three points.

1. First point : the timetable. During the discussions on the Omnibus II Directive, Parliament and the Council proposed that the Solvency II Directive be applied gradually.

The Commission supports this smooth transition: the Member States should transpose the Directive before 1 January 2013, but the new regime would not be fully applicable to businesses until 1 January 2014.

The details of this transition are still to be finalised, but it is clear that it is a plus point enabling insurers, national supervisors and EIOPA to prepare better for the new regime's entry into force.

2. Second point : calibrating the Solvency II measures. After more than two years of discussions with the Member States, EIOPA and the industry, the Commission is finalising the preparation of the "level 2" implementing measures.

Our aim is to ensure that Solvency II does not penalise insurance products of high economic and social value, such as retirement savings schemes, civil-liability insurance and medical insurance.

To do this we have examined the results of the fifth Quantitative Impact Study (QIS5) and prepared a set of new proposals aimed at ensuring the viability of long-term guarantee products, eliminating artificial volatility, avoiding pro-cyclical effects and reducing complexity.

3. Third point : equivalence in third countries. For Europe, Solvency II is an opportunity to encourage third countries to adopt a solvency regime based on the risks to insurers.

EIOPA has just completed its assessment of the solvency regimes applicable in Switzerland, Japan and Bermuda. Our aim is not to have third countries adopt a regime identical to Solvency II. But equivalence is in the mutual interest of the EU and third countries, since it will streamline cross-border activities by insurance and reinsurance companies and alleviate the burden on groups which operate internationally.

The Omnibus II Directive is intended to introduce a transitional regime for equivalence with Solvency II. Many third countries have already taken measures to adopt a risk-based regime without yet being able to meet the equivalence criteria. The Commission is determined to work with them.

Over and above our discussions with certain third countries on equivalence with Solvency II, Europe is continuing to play its part in the international insurance agenda.

For example, the Commission is giving support to the development of a common framework for supervising internationally active insurance groups under the umbrella of the International Association of Insurance Supervisors [IAIS].

I know some people feel that this project should be limited to improving coordination and cooperation between supervisors. I, on the other hand, am convinced that this common framework gives us a chance to introduce global minimum solvency standards for groups.

These minimum solvency standards are essential for ensuring that the discussions on the systemic risks in the insurance sector take place on a level playing field worldwide.

Still in the global context, I can see that the G20 discussions on global systemically important financial institutions, or G-SIFIs, need to take into account the special characteristics of the insurance sector.

It is possible that certain criteria used to determine whether a bank is systemically important are not suitable for insurers. For example, the "size" of an insurer is generally a positive factor, since it means better risk diversification and hence more financial stability.

One thing is certain: we will not be able to address the systemic risks in the insurance sector without a more effective form of group supervision. Supervisors ought to be able to identify the risks arising from the group as a whole. Capital requirements will never replace the need for robust group supervision.

This is why the Commission feels that the discussions on financial institutions presenting a global systemic risk cannot be separated from the discussions on the common framework for the supervision of insurance groups operating internationally.

## **II – Second initiative: the revision of the Directive on Institutions for Occupational Retirement Provision**

The financial crisis has made the situation worse for pension systems, which were already faced with the long-term challenge of the ageing population.

We must launch a general discussion on pensions to ensure that our retirement systems are adequate and sustainable. To this end we are about to publish, with Commissioners Andor and Rehn, a White Paper based on the many suggestions gathered by the consultation following the Green Paper on pensions.

The Directive on Institutions for Occupational Retirement Provision, adopted in 2003, laid the foundations for a single market for occupational pensions by allowing pension funds to offer their services beyond national borders.

Despite this, there are still very few cross-border pension funds. We therefore intend to revise the Directive to enable employers to reap the full benefits of the single market.

Now is the time to build a modern and innovative system founded on risk management, corporate governance and effective supervision, inspired by the Solvency II Directive and taking into account the special characteristics of institutions for occupational retirement provision.

The Commission proposal, to be submitted at the end of 2012, will have the advantage of a technical opinion from EIOPA, which is expected in mid-February.

I should also like to take this opportunity to pay tribute to EIOPA's work, which produces contributions of very high quality, sometimes with very tight deadlines.

## **III – Third major initiative: the revision of the Insurance Mediation Directive**

Despite the single passport for insurers and intermediaries, we face the challenge of a highly fragmented European insurance market.

We must strengthen and harmonise the rules on consumer protection. The revision of the Insurance Mediation Directive, which we expect to submit in early 2012, should facilitate cross-border trade, enhance consumer confidence and improve the stability of the financial markets.

The revision of this Directive will level the playing field between the various sellers of insurance products: not only insurance companies, but also banks, brokers, car hire firms and travel agents. The Directive will also give a European passport to those providing specific services linked to insurance, such as claims assessments.

The new Directive will also bring significant improvements to consumer protection standards, particularly where sales of life assurance products combined with packaged retail investment products (PRIPs) are concerned. On this subject, the provisions of the new Directive will reflect the rules we have just introduced with the revision of the MIFID Directive.

Ladies and Gentlemen,

With our proposals on Solvency II, on insurance intermediaries and on institutions for occupational retirement provision, 2012 promises to be at least as challenging as 2011.

Yet these three initiatives also give us a chance to deepen the Single Market by harmonising still further the requirements to be met by the European insurance and pensions sector.

This greater harmonisation will offer opportunities to businesses, which will be able to market their products all over Europe. It will give supervisors better means of comparison. And it will benefit consumers, who will be offered more choice and better protection.

Thank you for your attention.

#### 4.

### EUROPEAN COMMISSION - PRESS RELEASE

#### Commission wants better quality credit ratings

Brussels, 15 November 2011 - Credit rating agencies (CRAs) are major players in today's financial markets, with rating actions having a direct impact on the actions of investors, borrowers, issuers and governments. For example, a corporate downgrade can have consequences on the capital a bank must hold and a downgrade of sovereign debt makes a country's borrowing more expensive. Despite the adoption of European legislation on credit rating agencies in 2009 and 2010, recent developments in the context of the euro debt crisis have shown our existing regulatory framework is not good enough. So, today the Commission has put forward proposals to toughen that framework further and deal with outstanding weaknesses.

Internal Market Commissioner Michel Barnier said: "*Ratings have a direct impact on the markets and the wider economy and thus on the prosperity of European citizens. They are not just simple opinions. And rating agencies have made serious mistakes in the past. I have also been surprised by the timings of some sovereign ratings – for example ratings announced in the middle of negotiations on an international aid programme for a country. We can't let ratings increase market volatility further. My first objective is to reduce the over-reliance on ratings, while at the same time improving the quality of the rating process. Credit rating agencies should follow stricter rules, be more transparent about their ratings*

*and be held accountable for their mistakes. I also want to see increased competition in this sector."*

## **Four main goals of the proposed draft Directive and draft Regulation**

### **1. To ensure that financial institutions do not blindly rely only on credit ratings for their investments.**

Ratings currently have a quasi-institutional role. We need to reduce our reliance on them. Our proposals in July 2011 on the Capital Requirements Directive IV reduce the number of references to external ratings and require financial institutions to do their own due diligence. Today, we are making similar changes with regard to rules relating to fund managers, in a complementary draft directive. And this will be completed by changes to rules on insurance next year. A general obligation for investors to do their own assessment is also included in today's proposal.

In addition, more and better information underlying the ratings would need to be disclosed by CRAs and by the rated entities themselves, so that professional investors will be better informed in order to make their own judgments. For example, CRAs would have to communicate their ratings to the European Securities and Markets Authority (ESMA), which would make sure that all available ratings on the market for a debt instrument are published under a European Rating Index (EURIX), freely available to investors.

At the same time, credit rating agencies will have to consult issuers and investors on any intended changes to their rating methodologies. Such changes would have to be communicated to ESMA which would check that applicable rules on form and due process have been respected.

### **2. More transparent and more frequent sovereign debt ratings.**

Member States would be rated more frequently (every six months rather than 12 months) and investors and Member States would be informed of the underlying facts and assumptions on each rating. To avoid market disruption, sovereign ratings should only be published after the close of business and at least one hour before the opening of trading venues in the EU. The possible suspension of sovereign ratings is a complex issue which we believe merits further consideration.

### **3. More diversity and stricter independence of credit rating agencies to eliminate conflicts of interest.**

Issuers would have to rotate every three years between the agencies that rate them. In addition, two ratings from two different rating agencies would be required for complex structured finance instruments and a big shareholder of a credit rating agency should not simultaneously be a big shareholder in another credit rating agency.

### **4. To make CRAs more accountable for the ratings they provide.**

A CRA should be liable in case it infringes, intentionally or with gross negligence, the CRA Regulation, thereby causing damage to an investor having relied on the rating that followed such infringement. Such investors should bring their civil liability claims before national courts. The burden of proof would rest on the credit rating agency.

## **Background**

The EU Regulation on Credit Rating Agencies (CRA)<sup>1</sup>, (in force since December 2010), was part of Europe's response to the commitments made by the G20 at the November 2008 Washington summit. This Regulation was amended in May 2011, to adapt the Regulation to the creation of ESMA<sup>2</sup>.

The existing CRA Regulations focus on registration, conduct of business and supervision of CRAs:

(1) *registration*: in order to be registered, a CRA must fulfill a number of obligations on the conduct of its business (see (2)) intended to ensure the independence and integrity of the rating process and to enhance the quality of the ratings issued. The European Securities and Markets Authority (ESMA) is entrusted since July 2011 with the responsibility for registering CRAs in the EU; 28 CRAs (of which some belong to the same group) are now registered with ESMA.

(2) *conduct of business*: the existing Regulation requires CRAs to avoid conflicts of interests (for example, a rating analyst employed by a CRA should not rate an entity in which he/she has an ownership interest), to ensure the quality of ratings (for example, requiring the ongoing monitoring of credit ratings) and rating methodologies (which must be, *inter alia*, rigorous and systematic) and a high level of transparency (for example, every year, CRAs should publish a Transparency Report).

(3) *supervision*: since July 2011, ESMA exercises exclusive supervisory powers over credit rating agencies registered in the EU and has comprehensive investigative powers including the possibility to demand any document or data, to summon and hear persons, to conduct on-site inspections and to impose administrative sanctions, fines and periodic penalty payments. This centralises and simplifies the supervision of CRAs at European level. Centralised supervision ensures a single point of contact for registered CRAs, significant efficiency gains due to a shorter and less complicated registration and supervisory process and a more consistent application of the rules for CRAs. CRAs are at present the only financial institutions which are directly supervised by a European supervisory authority.

EU rules would apply to ratings of public entities within the EU but also outside the EU provided that the sovereign ratings are issued by a CRA registered in the EU.

Today's proposals now pass to the European Parliament and the Council (Member States) for negotiation and adoption.

See also [MEMO/11/788](#)

#### **More information:**

[http://ec.europa.eu/internal\\_market/securities/agencies/index\\_en.htm](http://ec.europa.eu/internal_market/securities/agencies/index_en.htm)

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<sup>1</sup> :

Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies , OJ L 302, 17.11.2009. Regulation (EC) No 1060/2009 is often referred to as CRA I Regulation.

<sup>2</sup> :

Regulation (EU) No 513/2011 of the European Parliament and of the Council of 11 May 2011 amending Regulation (EC) No 1060/2009. Regulation (EU) No 513/2011 is often referred to as CRA II Regulation:

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:145:0030:0056:EN:PDF>

5.

**MEMO/11/788**

Brussels, 15 November 2011

**Frequently asked questions: legislative proposal on credit rating agencies (CRAs)**

**I. GENERAL CONTEXT AND APPLICABLE LAW**

**1. What is a credit rating?**

A credit rating is an opinion issued by a specialised firm on the creditworthiness of an entity (e.g. an issuer of bonds) or a debt instrument (e.g. bonds or asset-backed securities). This opinion is based on research activity and presented according to a ranking system (e.g. AAA, BBB. For full list, please refer to the annex attached to this memo.)

**2. What is a credit rating agency?**

A credit rating agency (CRA) is a service provider specialised in the provision of credit ratings on a professional basis. The three biggest rating agencies are Standard & Poor's, Moody's and Fitch. They cover approximately 95% of the world market. Smaller rating agencies make up the remaining part. For a list of all European CRAs already registered under the CRA Regulation, see:

<http://www.esma.europa.eu/popup2.php?id=7692>

**3. Why do we need to regulate credit rating agencies?**

CRAs have a major impact on today's financial markets, with rating actions being closely followed and impacting on investors, borrowers, issuers and governments: e.g. sovereign ratings play a crucial role for the rated country, since a downgrading has the immediate effect of making a country's borrowing more expensive. A downgrading also has a direct impact for example on the capital levels of a financial institution.

The financial crisis and recent developments in the context of the euro debt crisis have revealed serious weaknesses in the existing EU rules on credit ratings. In the run up to the financial crisis, CRAs failed to appreciate properly the risks inherent in more complicated financial instruments (especially structured financial products backed by risky subprime mortgages), issuing incorrect ratings that were far too high.

The market for structured finance products grew rapidly, and CRAs were happy to both advise the issuer on the design of these innovative structures and afterwards rate them. These conflicts of interest were poorly managed, contributing further to rating inflation.

The 2008 crisis highlighted how far many of these instruments had been overrated.

The large majority of the ratings that large CRAs made on instruments linked to subprime in 2006 had to be downgraded between mid-2007 and mid-2008 causing substantial losses for investors.

In this context a number of legal proceedings have been launched in particular in the US by investors accusing CRAs of issuing misleading ratings.

#### **4. What do applicable EU rules on credit rating agencies say?**

The G20 summit in Washington (2008) aimed to ensure that no institution, product or market was left unregulated at EU and international levels.

The EU Regulation on Credit Rating Agencies (CRA Regulation)<sup>1</sup>, in force since December 2010, was part of Europe's response to these commitments. The Regulation was amended in May 2011 to adapt it to the creation of the European Securities and Markets Authority (ESMA)<sup>2</sup>.

The current CRA Regulation focuses on:

- registration: in order to be registered, a CRA must fulfill a number of obligations on the conduct of their business (see below), intended to ensure the independence and integrity of the rating process and to enhance the quality of the ratings issued. ESMA is entrusted since July 2011 with responsibility for registering and directly supervising CRAs in the EU;
- conduct of business: the existing Regulation requires CRAs to avoid conflicts of interest (for example, a rating analyst employed by a CRA should not rate an entity in which he/she has an ownership interest), to ensure the quality of ratings (for example, requiring the ongoing monitoring of credit ratings) and rating methodologies (which must be, inter alia, rigorous and systematic) and a high level of transparency (for example, every year the CRA should publish a Transparency Report); and
- supervision: ESMA has comprehensive investigatory powers including the possibility to demand any document or data, to summon and hear persons, to conduct on-site inspections and to impose administrative sanctions, fines and periodic penalty payments. This centralises and simplifies the supervision of CRAs at European level. Centralised supervision ensures a single point of contact for registered CRAs, significant efficiency gains due to a shorter and less complicated registration and supervisory process and a more consistent application of the rules for CRAs. CRAs are at present the only financial institutions which are directly supervised by a European supervisory authority.

The current CRA Regulation, however, does not regulate the use of credit ratings and their impact on the market. The use of external ratings by financial institutions is regulated in sectoral financial legislation (e.g. in the Capital Requirements Directive).

#### **5. What has already been proposed to reduce the risk of overreliance in the banking sector?**

The Commission's proposal for a new Capital Requirements Directive (CRD IV) of July 2011 proposed measures to reduce reliance on ratings. In that proposal ([IP/11/915](#)) it is envisaged to reduce to the extent possible reliance by credit institutions on external credit ratings by:

- requiring that all banks' investment decisions are based not only on ratings but also on their own internal credit opinion,
- that banks with a material number of exposures in a given portfolio develop internal ratings for that portfolio instead of relying on external ratings for the calculation of their capital requirements.

## **II. THE INTERNATIONAL CONTEXT**

### **6. What is the situation at international level? Are the proposed measures in line with regulatory approaches of other jurisdictions and international standard setting bodies?**

The Commission's efforts are broadly in line with the policy developed by our international partners within the Financial Stability Board (FSB) and the Basel Committee.

The Financial Stability Board (FSB) endorsed in October 2010 principles to reduce authorities' and financial institutions' reliance on CRA ratings. The G20 approved the FSB's principles on reducing reliance on external credit ratings (Seoul Summit, 11-12 November 2010).

The FSB principles cover five types of financial market activity: 1) prudential supervision of banks; 2) policies of investment managers and institutional investors; 3) central bank operations; 4) private sector margin requirements; and 5) disclosure requirements for issuers of securities. The goal of the principles is to reduce the cliff effects from CRA ratings that can amplify procyclicality and cause systemic disruption. The principles call on authorities to do this through:

- removing or replacing references to CRA ratings in laws and regulations, wherever possible, with suitable alternative standards of creditworthiness assessment;
- expecting that banks, market participants and institutional investors make their own credit assessments, and not rely solely or mechanically on CRA ratings.

The Basel Committee on Banking Supervision has also proposed to reduce reliance on credit rating agencies ratings in the regulatory capital framework.

In the USA, the Dodd-Frank Wall Street Reform and Consumer Protection Act<sup>3</sup> has strengthened rules on CRAs. Among other things section 939A of the Dodd-Frank Act requires federal agencies to review how existing regulations rely on ratings and remove such references from their rules as appropriate. As a consequence, the Securities and Exchange Commission (SEC) is currently exploring ways to reduce regulatory reliance on external credit ratings and replace them with alternative criteria. Some references have already been replaced in US legislation.

Apart from over-reliance, there are other areas of change being proposed by the European Commission which are also being reviewed by third country regulators, including in the US. This concerns, for example, the question of how conflicts of interests due to the "issuer-pays" model can be efficiently mitigated or how transparency of structured finance instruments can be improved. The debate on some of the issues has not yet been finalised at the global level. However, the Commission believes that the measures it proposes are a suitable way to tackle the problems identified and that its proposal can provide an important contribution to the international debate.

## **III. THE PROPOSAL: WHY IS IT NEEDED**

### **7. Why is a reform of the CRA Regulation needed?**

Because there are weaknesses in the existing EU rules on credit ratings that have been highlighted both by the financial crisis and more recent euro debt crisis:

- non-transparent sovereign ratings: Downgrading sovereign ratings has immediate consequences on the stability of financial markets but CRAs are insufficiently transparent about their reasons for attributing a particular rating to sovereign debt. Given the

importance of ratings on sovereign debts, it is essential that ratings of this asset class are both timely and transparent. While the EU regulatory framework for credit ratings already contains measures on disclosure and transparency that apply to sovereign debt ratings, further measures are needed such as access to more comprehensive information on the data and reasons underlying a rating, in order to improve the process of sovereign debt ratings in EU;

- investors' over-reliance on ratings: European and national laws give a quasi-institutional role to ratings. For example, the amount of capital that banks must hold is determined in some cases by the external ratings given to it. Furthermore, some investors rely excessively on the opinions of CRAs, and don't have access to enough information on the debt instruments rated or the reasons behind the credit rating which would enable them to conduct their own credit risk assessments. Measures are needed to reduce references to external ratings in legislation and to ensure investors carry out their own additional due diligence on a well-informed basis;

- conflicts of interest threaten independence of CRAs and high market concentration: CRAs are not independent enough from the rated entity that contract (and pays) them: e.g. as a rating agency has a financial interest in generating business from the issuer that seeks the rating, this could lead to assigning a higher rating than warranted in order to encourage the issuer to contract them again in the future. Furthermore, a small number of large CRAs dominate the market. The rating of large corporates and complex structured finance products is conducted by a few agencies that also happen to have shareholders that sometimes overlap;

- (absence of) liability of CRAs: CRAs issuing credit ratings in violation of the CRA Regulation are not always liable towards investors that suffered losses. National differences in civil liability regimes could result in credit rating agencies or issuers shopping around, choosing jurisdictions under which civil liability is less likely.

## **8. What is the Commission proposing to address these issues?**

The Commission is proposing targeted, but nevertheless far reaching amendments to the current CRA Regulation. The major initiatives are the following:

- More transparent and timely sovereign ratings:

CRAs will need to provide more information on the reasons behind sovereign ratings, explaining why it takes a specific rating action, and will need to update the ratings every six months (rather than 12 months at the moment)). This will make sovereign ratings more transparent and reliable. CRAs will have to publish those ratings outside the European working hours of the stock exchanges, so that traders have some time to assess them before starting to trade. The rule in the current CRA Regulation requiring CRAs to inform the issuers in advance of the rating and of the principle grounds on which the rating is based is specified in order to grant issuers appropriate time to react to the rating notification. CRAs shall inform issuers during working hours and at least one working day before publication of the rating.

- More transparency and less investors' reliance on ratings:

Investors will have to conduct their own assessment on the creditworthiness of the debt instruments in which they invest. For this, they will have access to more information from issuers (issuers will have to disclose specific information on structured finance products on an ongoing basis) and rating agencies (e.g. guidance explaining methodologies and underlying assumptions will be extended from structured finance products to all asset classes).

A horizontal provision in the CRA Regulation will oblige all regulated financial institutions (banks, insurance companies, investment fund managers...) to make their own credit risk assessment without solely or mechanically relying on credit ratings.

Changes to UCITS and the Alternative Investment Fund Managers Directive introduce the principle that investment managers should not rely solely and mechanically on external credit ratings in those sectoral legislations and empower the Commission to further specify this principle in delegated acts.

A general provision will require the European Supervisory Authorities (ESMA, EBA and EIOPA) to avoid external ratings in their guidelines where those would enhance the risk of overreliance and to review and if possible remove existing references. A similar provision is addressed to the European Systemic Risk Board (ESRB).

- More diversity and independence of CRAs

CRAs will have to become more independent vis-à-vis the entities they rate, in particular:

- an agency should not issue ratings for a period of more than three years on an issuer that pays the agency for that rating. However, there would be special rules in case an issuer, voluntarily or on the basis of the applicable legal provisions, requests ratings from more than one CRA (for more details on the rotation rule please refer to the replies to questions 13-15 below);
- lead analysts should not be involved in the rating of an entity for more than 4 years;
- cross-shareholdings in CRAs will be limited: a shareholder with a sizeable stake (more than 5%) in a credit rating agency should not simultaneously be a major shareholder (5% or more) in another credit rating agency unless both CRAs belong to the same group;
- CRAs will be prohibited from rating an entity in which its largest shareholders (those holding more than 10% of the capital or the voting rights or otherwise in a position to exercise significant influence) have a financial interest;
- Shareholders holding more than 5% of the capital or the voting rights in a CRA or otherwise in a position to exercise significant influence over the business activities of a CRA shall not be allowed to provide consultancy services to the entities rated by that CRA;
- ratings from two different CRAs will be required for structured finance products where such ratings are paid by the issuer .

- Liability of CRAs

Investors will be able to sue a credit rating agency which, intentionally or with gross negligence, fails to respect the obligations set out in the CRA Regulation, thereby causing damage to investors.

In this context, and given that it would often be difficult, for the investor, to prove what the reason for the breach of the Regulation was and whether this breach was due to gross negligence of the CRA, we are also proposing that it will be for the CRA to prove that it applied the necessary care. The investor only has to provide facts that suggest that there was an infringement.

#### **IV. WHAT WILL CHANGE?**

##### **9. Who will be affected by the proposed changes and how?**

The following categories of market participants will directly be affected by the proposed changes:

- Corporate and sovereign issuers:

They will benefit from more choice of rating providers which may lead to lower rating fees in the medium term. Sovereign issuers (e.g. states and municipalities) will benefit from the improved transparency and process of issuing sovereign ratings.

From now on, a **corporate issuer should regularly change CRA** (maximum period for using the services of a certain CRA would be three years). However, where the issuer – voluntarily or because it is legally obliged to do so – mandates more than one CRA to rate its creditworthiness or its instrument, only one of the CRAs will have to rotate. Nevertheless, the maximum contractual relationship with any CRA should in these cases never exceed six years.

All issuers, including sovereigns, will enjoy **additional time to react to ratings** before they are being made public. The current rules already provide for ratings to be announced to the rated entity 12 hours before their publication. In order to avoid that this notification takes place outside working hours and to leave the rated entity sufficient time to verify the correctness of data underlying the rating, the new rules will require that the rated entity should be notified a full working day before publication of the rating or of a rating outlook. This information shall include the principal grounds on which the rating or outlook is based in order to give the entity an opportunity to draw attention of the credit rating agency to any factual errors.

The publication of sovereign ratings will be done in a manner that is **least distortive on markets**: these ratings will only be published after the close of stock exchanges and at least one hour before their opening in the EU.

- Investors:

They will be in a **better position to evaluate the credit risk** of financial instruments themselves, including complex structured instruments. They will have free access to a European Rating Index (EURIX) and harmonised rating scale developed by ESMA where all ratings regarding a specific company or financial instruments can be found and compared. In addition, investors will benefit from an increase in the quality of ratings as conflicts of interests due to the "issuer-pays" model and the shareholder structure will be reduced. Investors' right of redress against credit rating agencies having infringed the CRA Regulation will be enhanced.

- Credit rating agencies that will need to :
  - **be more transparent notably regarding their pricing policy and the fees they receive.** Their fees should be non-discriminatory based on costs incurred for the rating (e.g. the issuer should not pay more with a view to get a better rating) and should not be dependent on the outcome of the work performed (e.g. not dependant on whether the rating is triple A or not);
  - **be more transparent about how they conduct their process of rating and reach their conclusions:** CRAs will need to disclose information on methodologies, underlying assumptions etc. However, there is no attempt made in the Commission's proposals to second-guess ratings;
  - **change their long-term business relations** with issuers and be ready to regularly change clients and share them with other CRAs;
  - **be more independent from their shareholder base and from other CRAs:** e.g. important shareholders of a CRA cannot, at the same time, be important

shareholders of another CRA. CRAs will be prohibited from rating an entity in which its relevant shareholders (those holding more than 10% of the capital or the voting rights) have a financial interests and

- **be liable towards investors when breaching intentionally or with gross negligence the CRA Regulation** thereby causing damage to investors. Investors' claims will be brought before national courts. Liability towards investors does not exclude administrative fines. According to the current rules in place, CRAs can already be subject to administrative fines for infringements to the CRA Regulation. Those fines are imposed by ESMA and, depending on the infringement, can reach approximately €1.5 million.

- ESMA:

Its role will be reinforced regarding supervision of sovereign ratings. In addition, ESMA will be entrusted with new tasks e.g. it will have to draft a number of new technical standards for adoption by the Commission.

For instance, ESMA should establish a European Rating Index (EURIX) so as to allow investors to easily compare all ratings that exist with regard to a specific rated entity and provide them with average ratings. ESMA will need to develop draft regulatory technical standards to specify the content and the presentation of the information to be provided by CRAs to EURIX as well as to specify a harmonised rating scale to be used by CRAs when providing such information.

#### - **Regarding the new rating methodologies:**

ESMA will have to verify that methodologies and changes to methodologies comply with regulatory requirements set out in Art 8 (3) and the ESMA technical standards, i.e. methodologies must be rigorous, systematic, continuous, and subject to a validation test based on historical experience, including back-testing before they are applied. However, ESMA will not be allowed to second guess specific ratings or to interfere with the content of methodologies.

CRAs shall inform ESMA of detected errors in methodologies and/or their application. This should facilitate ESMA's oversight.

#### - **Regarding existing ratings: EURIX**

CRAs will have to communicate to ESMA all credit ratings they issue. ESMA will make them available to the public on a website. ESMA will also disclose an aggregated rating index for any rated debt instrument (EURIX). As a result, investors, issuers and other interested parties should have an easy access to up to date rating information enabling them to compare all existing ratings with regard to a specific rated entity. EURIX should also help smaller CRAs to gain visibility.

#### - **Regarding rating scales**

ESMA will develop a harmonised rating scale to be used by CRAs for the publication of ratings on EURIX. This will ensure that ratings can be compared more easily by investors. This measure will make EURIX more useful.

### **10. Why is the Commission proposing specific rules for sovereign ratings?**

- Sovereign ratings include ratings of countries, regions and municipalities. Sovereign ratings are very important for the rated public entity. For instance, the conditions of access to external funding very much depend on the rating received. In addition, rating actions with regard to specific countries can have impacts on companies

located in that country, on other countries and even on the stability of financial markets.

- Due to this specific role the Commission believes that it is particularly important that sovereign ratings are accurate and transparent so that investors can fully understand rating actions regarding sovereigns and their wider implications.
- On the issue of possible suspension of sovereign ratings in exceptional circumstances to ensure the stability of financial markets, further work is needed on the details of how this could work in practice. The European Commission will analyse the options further and make proposals in due course, if appropriate.

#### **11. Will ESMA have a veto power on CRAs methodologies?**

No. ESMA already carries out this verification in the registration process and as part of the ongoing supervision. However, in the interest of legal certainty and the stability of the markets, it should be ensured that these methodologies comply with legal requirements *before* they can be used to issue ratings.

#### **V. OTHER:**

#### **12. Why is the Commission not proposing to set up a European CRA?**

- The Commission believes the CRA market is too concentrated, and more diversity would be positive. In November 2010, the Commission consulted on different options for how diversity in the rating industry could be increased, including establishing a new independent European CRA. The Commission assessed the feasibility of this option in the impact assessment accompanying this proposal. This analysis showed that setting up a credit rating agency with public money would be costly (ca €300-500 Mio over a period of 5 years), could raise concerns regarding the CRA's credibility especially if a publicly funded CRA would rate the Member States which finance the CRA, and put private CRAs at a comparative disadvantage.
- For these reasons, the Commission has at this stage decided to not pursue the idea further but is taking action to promote diversity in the market (see reply under question 8 above).

#### **13. The rotation rule will undermine quality of ratings. Why is the Commission proposing it?**

Credit rating agencies provide a service of particular importance to investors. Therefore, it is important that they are, and are seen as being, independent from the entity they rate or the entity that issued the financial instrument they rate. This independence is even more important in a business environment where the rated entity selects and pays the credit rating agency (so-called "issuer-pays" model).

Limiting the time period during which a CRA can be engaged and paid by a rated entity will mitigate the following risks:

- a long-term relationship could result in incentives for the CRA to issue overly favourable ratings in order to maintain the business relationship with the rated entity and therefore secure regular revenues;
- the prevailing practice of long-term relationships between the rated entity and the CRA also increases **the risk of potential lock-in effects on the rated**

**entities:** these entities may refrain from changing credit rating agency as this may raise concerns of investors regarding the entity's creditworthiness;

- **long-term relationships increase the familiarity threat:** CRAs may not remain vigilant enough on the risks they are assessing which would negatively affect the quality of their ratings.

These threats are, by nature, less important where an issuer – voluntarily or because the applicable legal provisions require it to do so – uses two or more CRAs in parallel to rate its creditworthiness or its instrument(s). In such cases, only one CRA shall rotate. However, also in these cases the business relationship with one particular CRA should not be permanent. We are proposing a maximum duration of six years. In addition, lead analysts should not be involved in the rating of an entity for more than 4 years.

#### **14. How will the rotation rule work in practice?**

The general rule is that CRAs shall not rate corporate issuers for a period exceeding three years.

Concerning the rating of a debt instrument, the same rule would normally apply. However, the period after which the CRA should stop issuing credit ratings may be shorter in the following case: once the CRA has rated 10 consecutive debt instruments of the same issuer, it should also stop issuing credit ratings on this issuer's instruments. However, if the rating of the 10 debt instruments was completed in less than 12 months, the CRA can continue its activity until 12 months of engagement have been completed).

Where an issuer has employed more than one CRA to rate its creditworthiness or its instrument, only one of the CRAs would have to respect the three years' limitation. However, this exception should not lead to any contractual relationship exceeding a total duration of six years.

That CRA could rate this issuer again after a *cooling-off period* of four years has elapsed.

The rotation rule does not apply in the case of unsolicited ratings, or in the case of sovereign ratings, where the issuer-pays model is less common and therefore conflicts of interests are less relevant.

#### **15. Rotation is not workable, in particular where you have an issuer issuing a high number of structured finance instruments.**

The exception from the rotation rule in case of multiple ratings for the same issuer or products mitigates the effects of the rule for these issuers (see also reply to question 17 above).

In addition, we ensure that the contract between the issuer and the CRA should not be shorter than one year, independently from the number of credit ratings issued on the financial instruments of that issuer within that year (see also reply to question 17 above).

Furthermore, the objective of any proposal on rotation is in the first place to increase the independence of CRAs and therefore the quality of ratings. However, a second objective is to make the credit rating market more dynamic and increase the number of participants and the choice for issuers.

The proposal will be accompanied by other measures to reach that aim (such as the support for the creation of a network of smaller CRAs.) We therefore expect the market to develop in the future. ESMA and the Commission will monitor that development. If the market does not develop as expected, appropriate transition rules relating to rotation could be put in place.

Some issuers already use multiple ratings for their structured finance products. This is something we support as it improves information for investors and the quality of the overall information available for these complex products. It is consistent with our intention to propose double ratings for such products as an obligation for issuers. As explained above, if an issuer has employed more than one CRA on the same matter, only one of them would have to respect the short rotation period.

The quality of rating will not be undermined because of the use of small CRAs. Given the new market opportunities, small CRAs will grow and develop their capacity and expertise. They will be tightly monitored and supervised. In any event, given their records regarding the rating of structured products, large CRAs cannot really pretend that their quality is above market standards.

#### **16. What will happen when issuing complex structured finance instruments?**

In recent years, many structured finance instruments rated with the highest ratings have become toxic assets. For example, a major CRA had to downgrade 83% of its AAA ratings issued in 2006 on mortgage-backed securities. The subsequent downgrades of these products meant that investors such as pension funds incurred massive losses, in some cases billions of euros.

Therefore the present proposal reinforces the rules and requires issuers of complex structured finance instruments to substantially change the way they provide investors with information on the creditworthiness of those instruments. The ratings of CRAs will no longer be the only channel to assess such creditworthiness. Issuers will need to be more transparent towards the market, to enable investors better to judge, by themselves, the creditworthiness of these complex instruments

Two provisions in the proposal will deal with this matter:

- Issuers of structured finance products shall provide more information (e.g. on the credit quality and performance of the individual underlying assets of the structured finance instrument, the structure of the securitization transaction, the cash flows and any collateral supporting a securitisation exposure) on their products to the market, so that investors can make their own judgements and not rely systematically and mechanically on ratings to assess the creditworthiness of those instruments. This will also allow other CRAs to issue unsolicited (and independent) ratings;
- Issuers of structured finance products will have to engage two CRAs to rate their products in parallel and independently from each other, to provide more reliable ratings to investors. The two CRAs will need to be independent from each other in terms of ownership and management.

#### **17. What rules does the Commission propose to mitigate possible conflicts of interest of a CRA with regard to its shareholders?**

The Commission proposes that a credit rating agency should abstain from issuing credit ratings (or should disclose that the credit rating may be affected) where a shareholder who is in a position to significantly influence the business activity of that agency:

- is a member of the administrative or supervisory board of the rated entity,
- has invested in the rated entity.

Where a shareholder of a CRA is in a position to influence the business activity of the CRA, he shall not provide consultancy or advisory services to an entity rated by this CRA or its related third party.

### **18. Why does the Commission propose to extend certain rules of the CRA Regulation to rating outlooks?**

A rating outlook provides an opinion regarding the likely direction of a credit rating in the short and medium term. Rating outlooks can be 'stable', 'negative' or 'positive'. A negative outlook means that the CRA is considering downgrading the rating in the short to medium term. The relevance of credit outlooks for investors and issuers and their effects on markets can be comparable to the effects of any "normal" rating decision. Therefore, the procedural requirements of the CRA Regulation which ensure that ratings are accurate, transparent and understood by investors should also apply to rating outlooks.

### **19. What does the proposal say about the possibility of investor pays models?**

The proposal allows the investor pays models but the use of the investor pays model is not compulsory; it will continue to coexist with the prevalent issuer pays model. Making the investor-pays model compulsory risks resulting in a lower number of credit ratings issued, therefore leaving the market without credit ratings on certain issuers or financial instruments.

### **20. Are all ratings going to be disclosed? If so, why not just wait for others to pay them?**

Ratings issued under the investor pays model are only disclosed to the investors who pay for them. But all ratings under the issuer pays model will be disclosed and aggregated on Eurix.

## **ANNEX**

**Fitch Ratings** and **Standard & Poor's** use a system of letter sliding from the best rating "AAA" to "D" for issuers already defaulting on payments.

- **Investment Grade** add explanation of what investment grade means
  - **AAA** : best quality borrowers, reliable and stable without a foreseeable risk to future payments of interest and principal
  - **AA** : very strong borrowers; a bit higher risk than AAA
  - **A** : upper medium grade; economic situation can affect finance (what is meant by finance?)
  - **BBB** : medium grade borrowers, which are satisfactory at the moment
- **Non-Investment Grade**
  - **BB** : lower medium grade borrowers, more prone to changes in the economy, somewhat speculative (what is meant by speculative)
  - **B** : low grade, financial situation varies noticeably, speculative
  - **CCC** : poor quality, currently vulnerable and may default
  - **CC** : highly vulnerable, most speculative bonds
  - **C** : highly vulnerable, perhaps in bankruptcy or in arrears but still continuing to pay out on obligations
  - **CI** : past due on interest
  - **R** : under regulatory supervision due to its financial situation
  - **SD** : has selectively defaulted on some obligations

- **D** : has defaulted on obligations and S&P believes that it will generally default on most or all obligations
- **NR** : not rated

Moody's ratings follows a different system:

- **Investment Grade**

- **Aaa**: Obligations rated Aaa are judged to be of the highest quality, with the "smallest degree of risk"
- **Aa1, Aa2, Aa3**: Obligations rated Aa are judged to be of high quality and are subject to very low credit risk, but "their susceptibility to long-term risks appears somewhat greater".
- **A1, A2, A3**: Obligations rated A are considered upper-medium grade and are subject to low credit risk, but have elements "present that suggest a susceptibility to impairment over the long term".
- **Baa1, Baa2, Baa3**: Obligations rated Baa are subject to moderate credit risk. They are considered medium-grade and as such "protective elements may be lacking or may be characteristically unreliable".

**Non-Investment Grade**

- **Ba1, Ba2, Ba3**: Obligations rated Ba are judged to have "questionable credit quality."
- **B1, B2, B3**: Obligations rated B are considered speculative and are subject to high credit risk, and have "generally poor credit quality."
- **Caa1, Caa2, Caa3**: Obligations rated Caa are judged to be of poor standing and are subject to very high credit risk, and have "extremely poor credit quality. Such banks may be in default..."
- **Ca**: Obligations rated Ca are highly speculative and are "usually in default on their deposit obligations".
- **C**: Obligations rated C are the lowest rated class of bonds and are typically in default, and "potential recovery values are low".

- **Others**

- **WR**: Withdrawn Rating
- **NR**: Not Rated
- **P**: Provisional

1.

Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies , OJ L 302, 17.11.2009. Regulation (EC) No 1060/2009 is often referred to as CRA I Regulation.

2.

Regulation (EU) No 513/2011 of the European Parliament and of the Council of 11 May 2011 amending Regulation (EC) No 1060/2009. Regulation (EU) No 513/2011 is often referred to as CRA II Regulation.:

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:145:0030:0056:EN:PDF>  
3.  
<http://www.sec.gov/about/laws/wallstreetreform-cpa.pdf>

6.

SPEECH/11/721

**Michel BARNIER**

Member of the European Commission, responsible for Internal Market and Services  
**European financial regulation: time for delivery**

Conference on Financial Regulation and the Dynamics of Saving and Investment Markets

**Cumberland Lodge, London - 4 November 2011**

Ladies and gentlemen,

I am very pleased to be with you today. And I would like to thank you for inviting me.

**These are difficult times.**

As our global leaders meet in Cannes, we are all acutely aware of how big and deep the crisis we are facing still is. And its multiple facets. Which are all interdependent.

Like you, I hope today's summit can conclude on long lasting measures which will bring back stability. **Stability which is essential for a return to long term growth.**

The largely peaceful protests by anti-capitalists – in London and across the world – should not be underestimated. **They highlight that if we don't get change right, the situation could quickly turn.**

Despite the ups and downs of recent months, the fact is that **we are making progress.** We are demonstrating our determination to overcome together the current difficulties. And to take all the necessary steps towards a deeper economic union: **it is the only solution if we want to keep our monetary union.**

But our task is not only to deal with immediate crises. **We must not lose sight of the financial regulation agenda.** Because we need financial services back at the service of the real economy. And because **we cannot afford another crisis like this one.**

This agenda for financial stability was decided by the G20 members. And the EU played a key role in the G20 advocating it.

**Now is the time for delivery.** We only have a small window of opportunity.

We need to get down to the hard work of finalising technical details and making the new framework work.

If we don't, lending to the real economy will slow. **The already fragile recovery will stutter to a grinding halt.** With catastrophic consequences on employment.

## **I – Where do we stand on financial regulation?**

The **three new European supervisory authorities** for banks, financial markets and insurance and pensions started working on the 1st of January.

Beyond supervision, our agenda aims to achieve **four main objectives**:

### ***1. First objective: reinforcing stability and improving the governance of financial institutions***

For **banks**, we proposed in July to increase capital and liquidity requirements in compliance with Basel III.

Capital requirements will also become stricter, more precise and more risk-sensitive for **insurance**, with the "Solvency II" directive taking effect in 2013.

Measures were also agreed for **hedge funds** who will now be obliged to act in a more transparent way.

On **credit rating agencies**, our first regulation did not go far enough. In a few weeks, we will table a proposal addressing outstanding issues: over-reliance on ratings, conflicts of interest, the lack of competition and the specificities of rating sovereign debts.

### ***2. Second objective: improving financial markets' effectiveness, integrity and transparency***

A few weeks ago, we finally agreed on new rules for **short-selling** and **credit default swaps**.

I also hope there will be a final agreement to increase transparency on **OTC derivatives**. A market that is huge – but largely hidden – accounting for 600,000 billion euro a year.

We tabled a few days ago a proposal to revise the Markets in Financial Instruments directive (**MiFID**). Our proposal will regulate new trading venues and technological developments, such as high frequency trading. It will also address excessive price volatility in commodity derivatives markets, an issue that is being discussed in Cannes today.

Finally, our new proposals on **Market Abuse** will help better prevent, detect and punish market manipulation and insider dealing.

### ***3. Third objective: restoring confidence in the financial sector by enhancing consumers' and investors' protection***

On this, let me mention briefly 5 initiatives:

- We hope to see swift agreement on **Deposit Guarantee Schemes** – guaranteeing up to £85 000 per account – and **Investor Compensation schemes**;
- As well as on our proposals to better **protect those who take out residential mortgages**;
- We are also making progress towards greater **financial inclusion**. Today 30 million adult Europeans don't have a bank account, including 7 million because of a bank's refusal. This is not acceptable;

- The proposal on retail investment products [**PRIPs**] that we make early next year will ensure customers have access to concise, targeted and clear information on investment opportunities;
- And I will also make proposals on the **transparency of bank fees**, so consumers can better compare offers on the market.

**Together, these measures will hope restore trust in financial services that consumers and investors have completely lost.**

#### ***4. Last objective: a framework for crisis resolution in Europe.***

This is perhaps the most important piece of the jigsaw puzzle.

Since 2008, Member States have massively supported the banks. 4,600 billion euro have been committed to the financial sector, either through direct funding or guarantees.

**But the financial sector can no longer be underwritten by taxpayers.**

Taxpayers cannot and should not have to tolerate such a burden again.

Our new framework will equip supervisory authorities with the tools to prevent and manage banking crises.

Ladies and Gentlemen,

One last word to remind you that **financial regulation alone is not enough**. I also have responsibility for the Single Market. And there are real opportunities there for more growth. The UK economy's trade with the EU remains multiples higher than with the USA or any other trading partner

But to exploit this potential, **the economy needs to be based on a sound and healthy financial system.**

I am confident our new rules will allow **the financial sector to once again fulfil its role of financing the real economy.**

On all these issues, I am fully aware of the criticisms I face. "You're undermining the City of London's competitiveness." "You're trying to promote Paris and Frankfurt over London".

**All this is nonsense.**

I've repeated this many times before and will do so again.

- I see the City of London as an asset to the European financial sector and to the EU economy in general. This is my conviction.
- I also believe in efficient and intelligent regulation. It is not a threat to London's financial centre. And I have seen no evidence that our rules, which the UK government has always signed up to, undermine the City's competitiveness.
- On the contrary, the right regulation will be a significant asset for the competitiveness of the industry. And it will contribute to Europe's attractiveness for investors.

- But there can be no return to business as usual in the financial sector. I continue to hope the financial sector will lead the way with a more ethical and **responsible approach in the ways they operate.**

I also hear a great deal about concerns we are undermining the single market for financial services. This is also untrue.

If anyone has done well out of the single market for financial services, it is the UK.

And I hope the UK, and the City in particular, will continue to do well out of it. It's in all our interests.

You can count on the European Commission to uphold a Single Market for all 27 Member States, whether in or out of the Eurozone.

A real single market means a European framework and common European supervisory standards.

On which note, I thank you and look forward to your questions.

**A sajtóbejelentések elérhetőek:**

[http://europa.eu.int/rapid/searchResultAction.do?search=OK&query=markt&use\\_rname=PROF&advanced=0&guiLanguage=en](http://europa.eu.int/rapid/searchResultAction.do?search=OK&query=markt&use_rname=PROF&advanced=0&guiLanguage=en)