European Commission

EU - US TRANSATLANTIC TRADE AND INVESTMENT PARTNERSHIP (TTIP)

Cooperation on financial services regulation

The EU aims at establishing a framework for regulatory cooperation on financial services in the TTIP. The goal is not to define the substance of international standards, which shall be discussed in the respective fora outside the TTIP negotiations. The goal is to create an institutional framework of EU and US regulators to make sure the EU and US rules work together, which shall contribute towards preventing future crisis.

Introduction

In July 2013, the EU and the US launched negotiations on a Transatlantic Trade and Investment Partnership (TTIP). The two parties recognised the objective of the negotiations as the conclusion of a comprehensive agreement that addresses a broad range of bilateral trade and investment issues, including regulatory issues[1].

The need to address regulatory barriers is particularly evident in the financial services sector. The financial crisis showed in stark clarity that financial markets are global and deeply interconnected. The global nature of financial services allows systemic risks to be transmitted across national borders. Financial stability is not served by a fragmented regulatory approach, inconsistent rules and a low level of co-operation among supervisors.

The EU and the US have both been advocates of high international standards for global regulation through the G20, the Financial Stability Board, the Basel Committee and other international bodies.

Although the EU and the US have sought to implement these principles consistently, significant differences have arisen in the process of implementation in a number of

[1] Final Report of the High Level Working Group

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areas. Some of these differences are due to differences in EU and US market structures and are unavoidable. Others cannot be fully justified on prudential grounds. The inconsistencies are not only significant barriers to trade and investment, but they also undermine the global financial stability that both the US and EU are seeking to achieve. In too many instances, international standards have been implemented in a way that does not allow regulatory systems and the relevant regulators and supervisors to work together. This situation can lead to regulatory arbitrage and to the duplicative application of rules. Inconsistent rules fall short of the internationally agreed objectives. The regulatory fragmentation weakens the resilience of financial markets and makes it much more difficult for economies to recover.

The EU and the US already participate in regulatory discussions within the framework of the Financial Markets Regulatory Dialogue (FMRD). In addition, both parties are engaged in detailed discussions on rules for derivatives, insurance and a number of other areas including bank resolution and audit. These dialogues are clearly important and have achieved some important successes over their lifetimes. However, in the post crisis era where we have fundamentally upgraded financial regulation on both sides of the Atlantic, we should also seek to upgrade the mechanisms for regulatory co-operation. Especially as we continue to shift our focus from agreeing high level international standards to implementing them in detailed regional and domestic rule making. It is inevitable that regulatory difference would occur given the differences between our market structures and legislative frameworks, but we should work together, at an early stage in the legislative process to ensure that we aim for consistent rule making, and where consistency is not possible, we mitigate the unintended consequences of inconsistency. For example, in July 2013 the Commission and the CFTC concluded an agreement on derivatives. The process leading to the agreement was far from optimal. Talks commenced shortly before the rules entered into force, causing significant uncertainty on the market, and making it challenging to meaningfully reflect the substance in the final cross-border rules, and to consult accordingly. Implementing the agreement remains uncertain and details are yet to be released.

The EU believes that financial regulation is too important to be discussed ad hoc, in informal settings at the very last minute, under market pressure. To respond to these concerns, the EU proposed that the TTIP establishes a framework for regulatory cooperation in financial services.

The EU proposal

The EU proposes to establish, within the TTIP framework, a transparent, accountable and rule-based process which would commit the two parties to work together towards strengthening financial stability. The regulatory cooperation would be based on a number of principles:

- Joint work to ensure timely and consistent implementation of internationally-agreed standards for regulation and supervision.
- Mutual consultations in advance of any new financial measures that may significantly affect the provision of financial services between the EU and the US and to avoid introducing rules unduly affecting the jurisdiction of the other party[2].
- Joint examination of the existing rules to examine whether they create unnecessary barriers to trade.
- A commitment to assessing whether the other jurisdiction's rules are equivalent in outcomes.

These general principles would be backed up by specific arrangements for the governance of the EU-US regulatory cooperation, guidelines on equivalence assessments and commitments to exchange necessary and appropriate data between regulators.

The core element of the EU proposal is the commitment to outcome-based assessments of whether the other party's regulatory and supervisory framework is equivalent. This could potentially lead to mutual reliance on the rules of the other party. It should be stressed that the EU does not envisage each party making binding declarations of the equivalence of the other's entire regulatory and supervisory framework, but rather carrying out a detailed assessment of the consistency of the implementation of each standard.

This approach is fully in line with G20 commitments aimed at promoting transparent and continuously functioning financial markets. The G20 leaders' declaration from September 2013 states with respect to trade in derivatives that "jurisdictions and

[2] Unless there are overriding prudential reasons.

regulators should be able to defer to each other when it is justified by the quality of their respective regulatory and enforcement regimes, based on similar outcomes, in a non-discriminatory way, paying due respect to home country regulation regimes." This approach allows the parties to respect each other's regulatory models and legal traditions, without changing the existing legislation and without slowing down the current regulatory process. At the same time this approach can ensure, if certain conditions are met, that different rules can work together, provided that they are made consistent.

Under the EU proposal, regulators would still have the possibility to take the necessary measures to protect financial stability. Regulators and supervisors on both side of the Atlantic would keep the prerogative to take measures for prudential reasons. Regulators would only be bound by the principle of good cooperation and would need to take into account the potential impact of the rules on the other party when making a proposal. They would need to factor in the negative implications for the other party and explain the choices made if such implications were to remain in the final rule.

The aim of the EU proposal is not to negotiate within the TTIP on the substance of the international standards, on the on-going implementation of these standards or on other elements of on-going regulatory reforms (e.g. the Volcker rule, or rules on foreign banking organisations) that are being currently implemented. Discussions on these subjects may continue in parallel with, but outside of, the TTIP negotiations.

The EU proposal is forward looking and it aims to achieve consistent and high level of regulation across the Atlantic, on the basis of the internationally agreed standards. The new accountable regulatory cooperation framework, to be established by the TTIP, would provide the right setting in which to continue the joint EU/US work and dialogue on substance of financial regulations. Currently, both the EU and the US are similarly advanced in overhauling financial regulation in response to the crisis and are implementing the same set of standards. In fact, the pre-condition for the joint framework for enhanced regulatory cooperation is that both jurisdictions have equally robust financial regulation in place and that both jurisdictions work together to strengthen financial standards, not to weaken them. The EU is proposing this EU/US regulatory cooperation on the premise that the US shares the EU's ambition to advance global regulatory reforms and that both parties will continue to implement high-quality regulatory standards.

The EU proposal offers the opportunity to lay the long-term foundations of an integrated and stable financial market. Without this framework, in a few years' time, when the crisis has passed from memory, there is a risk that financial regulation could again be dominated by predominantly national considerations, leading once again to regulatory divergence and opening the door to financial instability.

Conclusion

The EU believes that it is in the interests of both the EU and US to agree within the TTIP on a framework for regulatory coherence in financial services. The benefits of transatlantic integration are clear:

- It would strengthen financial stability, as potential problems would be spotted together and addressed jointly. Furthermore, greater coherence could significantly reduce instances of regulatory arbitrage.
- By bridging regulatory divergences we would create a larger and more efficient market place for EU and US financial firms.
- It would improve the ability of the integrated financial system to provide financing to the real economy.
- Finally, an integrated transatlantic marketplace would have a major global impact on financial markets and regulation and would solidify the leading role that the EU and the US play in financial regulation.