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Principles into practice: the EU Level 2 process

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The EU's great cycle of post-financial crisis regulatory reform has reached a critical stage, following agreements between the Council of the EU and the outgoing European Parliament in key financial services legislative dossiers, including: EU Banking Union; the Capital Requirements Directive (CRD IV); the Recovery and Resolution Directive; and the wide-ranging Markets in Financial Instruments Directive (MiFID).

We are now moving to the more detailed and granular rule-making process needed to apply and implement these changes. We are moving from the Level 1 to Level 2 legislative phase.

During Level 1, political agreements and broad principles are hammered out. These are then defined in more detail during Level 2 – a general term for the implementing and technical measures drafted and adopted by the European Commission, following advice from the European Supervisory Authorites (the 'ESAs').

What is comitology?

Level 2 stems from the concept of 'comitology' – the process by which the Commission exercises its implementing powers, conferred on it by the EU's co-legislators (Council and Parliament), and aided by committees of representatives from member states.

Comitology originally developed as a way of applying community wide measures, such as the Common Agriculture Policy (CAP), more rapidly than would be possible if member states had to enact them separately through national laws. Measures can also be updated relatively quickly in response to changing market conditions.

CRD IV is one example of a legislative dossier at Level 2 stage. It comprises both the Capital Requirements Directive (CRD) – which must be enacted at national level – and the Capital Requirements Regulation (CRR), which applies directly to firms across the EU. AFME continues to participate in this Level 2 consultation process.

Heavy lifting for Level 2

The heavy lifting for shaping Level 2 measures is done by the ESAs – also known as Level 3 Committees. They include: the European Banking Authority (EBA); the European Securities and Markets Authority (ESMA); and the European Insurance and Occupational Pensions Authority (EIOPA). The ESAs advise the Commission on the preparation of the various Level 2 measures and also conduct public consultations with stakeholders.

Also prominent are the Level 2 committees of member state representatives; comprising mainly representatives from national finance ministries and central banks.

Most of the Level 2 committees, such as the European Banking Committee, meet in the same building in Brussels: the Albert Borschette Conference Centre on Rue Froissart, not far from other European institutions.
L2 committees advise the Commission on policy issues and are consulted by the Commission when drafting legislative proposals in their policy areas.

**Delegated acts**

Delegated Acts (DAs) and Implementing Acts (IAs) result from the delegation of legislative authority to the Commission to complement or implement Level 1 provisions. They take the form of either Directives or Regulations.

DAs are used to supplement, amend or delete 'non-essential' elements of legislative acts. They often cover sensitive policy issues, and are defined by their associated Level 1 texts in terms of their objectives, content, scope and duration. For this reason, elements of DAs seen as non-essential legally may still have a significant material impact when fully enacted.

Each DA is drafted by the Commission, based on advice it receives from the ESAs. They can enter into force only if no objection has been expressed by the Parliament and the Council within a period predetermined by the Level 1 act.

In financial services legislation, technical aspects of Level 1 rules can be defined in detail through binding Regulatory Technical Standards (RTS), prepared by the relevant ESA. RTS can be seen as a particular type of Delegated act, with the distinction that ESAs have a more formal and central role in the drafting process. Moreover, the 'technical' nature of the act is such that it is difficult for the Commission to diverge from the advice it gets from the ESAs, where technical expertise lies.

**Implementing acts**

IAs are used to implement EU legislation and deal with less controversial and purely technical issues. They are drafted by the Commission based on advice received from ESAs, and can enter into force only if no objection has been expressed by the Level 2 committee responsible for scrutinising the measure.

For the financial sector, technical aspects can be introduced through binding Implementing Technical Standards (ITS), which are prepared by the relevant ESA.

Both IAs and ITS involve extensive consultation exercises run by the ESAs. With CRD IV, for example, this is carried out by the EBA.

**Change of cast**

The shift to Level 2 implies a significant change in terms of actors involved in the decision making process.

At Level 1, the big political bodies – the European Parliament, the Council and the Commission – have the stronger role. During Level 2, however, the national authorities and the ESAs become more prominent.

Yet the political players retain a role at Level 2. The Commission remains central, and the European Parliament and Council retain a 'last resort' influencing power, as they have the right to scrutinise the final outcome of the Level 2 process. However, they exert this influence only in exceptional cases.

All of this adds up to an extremely complex process, but one in which AFME and its members, through constructive engagement with the actors involved, have an important role to play.

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