Capital Markets Union – Slow start towards an ambitious goal
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Executive summary

I. The Capital Markets Union (CMU) is a large-scale initiative of the European Union and it was officially launched in the Commission’s Action Plan in 2015. The main goal of the CMU is to create a single market for capital, in which companies, in particular SMEs, will have better access to non-bank finance and in which local capital markets will be deepened and better integrated. By complementing banking finance, enhancing private risk-sharing and ensuring overall risk reduction, the CMU should result in a more stable financial system that is better equipped to boost growth, create employment and make Europe more attractive for foreign investment.

II. The 2015 CMU Action Plan and its 2017 Mid-Term Review included a large number of measures, which should have had a cumulative effect of laying down a foundation for the CMU by the end of 2019. Given the high priority attached to this flagship initiative by the Commission and stakeholders, we consider that this report is well-timed to support further development of the CMU. Our report addresses how well the Commission carried out its role and highlights issues, which may have an impact on the CMU’s success now and in the future.

III. The audit examined whether the Commission has been successful in its actions towards building an effective CMU. To address this overall question, we assessed whether the Commission had achieved its objectives of increasing the diversity of sources of company financing; whether it had taken effective action to sufficiently foster more integrated and deeper capital markets; whether it had removed cross-border barriers for market participants, and had appropriately designed and monitored the CMU project.

IV. Our overall conclusion is that the Commission has made efforts to achieve the challenging goal of building a CMU, but the results are still to come. Many of the measures that the Commission was able to take within its remit only addressed narrow areas in the pursuit of the CMU objectives. By their very nature, these measures (for example, soft measures such as carrying out analyses to promote best practice) have not been able to catalyse substantial progress in achieving the CMU. Another limitation that the Commission faced is that many key actions can only be undertaken by the Member States, or with their full support.
The measures to diversify financing sources for companies addressed issues that were too narrow to initiate and catalyse a structural shift towards more market funding in the EU and had only a limited impact. Furthermore, the securitisation legislation, although a positive step, has not yet produced the anticipated recovery in the European securitisation market after the financial crisis and did not help banks to increase their lending capacity, among others to the benefit of SMEs. Transactions remain concentrated within traditional asset classes (i.e. mortgages, car loans) and in certain Member States.

As to the development of the local capital markets, the Commission used its coordination role in the European Semester process. However, the Commission did not develop a comprehensive and clear EU strategy and it had not recommended that all Member States with less developed capital markets implement relevant reforms. The Commission used the demand-driven Structural Reform Service Programme (SRSP) to finance CMU-relevant projects, among others. Although the intervention logic of the SRSP was not formally oriented towards the specific needs of EU capital markets, the objectives of the CMU were addressed at the project level. However, the demand-driven approach was not conducive to providing support to all Member States corresponding to their needs and its results are still to be seen.

We note that the CMU Action Plan did not lead to a breakthrough as regards resolving the main barriers impeding cross-border capital flows. These barriers often emanate from national laws, such as those in the fields of insolvency law and withholding tax or from a lack of financial education. The progress on tackling the barriers was limited, partially due to a lack of support from the Member States.

As regards the design of the CMU, its objectives were not always specific or measureable enough. In addition, no priorities were set before the start of the project. The Commission’s monitoring was limited to progress with legislative measures. It did not regularly and consistently monitor the progress towards achieving the CMU objectives.
In order to improve the effectiveness of the CMU project, we recommend that the Commission should:

(a) propose well-targeted actions to further facilitate SME access to capital markets;
(b) foster deeper and better integrated local capital markets;
(c) address key cross-border barriers to investment; and
(d) develop specific objectives, critical measures and the monitoring of the CMU.

We also invite the Council to consider how to take further the Commission’s proposal to address the asymmetric tax treatment of equity and debt.
Introduction

01. The free movement of capital is one of the four freedoms – along with the free movement of goods, services and labour – and a key objective of the European Union. The importance and benefits of creating a European capital market have long been discussed, including in the 1966 Segré Report, the 2001 Lamfalussy Report and earlier Commission Communications (e.g. from 1996, 1998 and 2011). While the emphasis, dimensions and challenges of the development and integration of capital markets have changed, the EU has never accomplished well-functioning integrated capital markets.

02. There are geographical discrepancies between Member States in the capitalisation, liquidity and depth of their local capital markets. Member States in the west and the north tend to have deeper capital markets and self-reinforcing capital hubs, while Member States in the east and the south are lagging behind (see Figure 1). Up to now, London has been the EU’s most important financial hub. The UK’s withdrawal from the EU represents a challenge to the CMU project.
Despite the efforts made in the aftermath of the financial crisis, most EU Member States’ economies still rely more heavily on bank financing than on capital market financing (e.g. private equity, venture capital, bonds). SMEs in Europe choose comparatively cheaper bank funding, allowing them to keep full ownership. Although non-bank financing has had an increasing relevance over the last decade, bank loans still accounted for around 45% of total non-financial corporation debt financing in the euro area in 2018, down from around 60% in 2007\(^1\). Traditions and culture are an

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\(^1\) ECA on European Central Bank Annual Report 2017, p. 36.
important factor in this respect, as illustrated by the home bias (i.e. a tendency to invest the majority of the portfolio in domestic assets). The lack of easily available information on companies and insufficient levels of financial literacy are further obstacles that constrain investors’ demand for capital market instruments.

The Capital Markets Union (CMU) is a large-scale initiative of the Commission. It was officially launched in the Commission’s Action Plan in 2015. This flagship project was announced as part of the Commission’s ten policy priorities and is an element in the third pillar of the Investment Plan for Europe aimed at improving the investment environment. The CMU is intended to complement the Banking Union by enhancing private risk sharing and ensuring overall risk reduction, and eventually to strengthen the Economic and Monetary Union (EMU).

The need for a CMU has never been as strong as it is today. Brexit has accentuated the political need to build deeper and more integrated capital markets in the EU, as the UK, the biggest and deepest capital market and the most important European hub of start-up finance, officially left the EU on 31 January 2020. Furthermore, global competition is increasing, as illustrated by factors such as innovative European SMEs leaving the EU in search of better financing and an environment, which is more conducive to fund fast-growing firms. In recent months, the Commission has included the economic uncertainty caused by the COVID-19 pandemic in its narrative as a further factor in favour of the CMU, which could potentially mobilise private funding and accelerate the recovery of the economy.
The CMU objectives

06 An important aim of the CMU is to help reduce high dependence on bank funding and cut the cost of raising capital, in particular for SMEs. According to the Commission, this goal should be realised by building a stable financial system in which deeper and integrated capital markets will absorb more of citizens’ savings and play a greater role in business finance. The EU banking sector is also set to benefit from the CMU, which includes measures to revive the European securitisation market.

07 By complementing the Banking Union and spreading risks across market participants, the CMU should contribute to a more stable financial system that is better equipped to boost growth, create employment and make Europe more attractive for foreign investment. Finally, more integrated, liquid and deeper financial markets in Europe would not only increase cross-border investment flows but also support a stronger international role for the euro.

08 The 2015 Action Plan and its 2017 Mid-Term Review included a set of legislative and non-legislative measures divided into seven intervention areas that should have had, amongst others, the cumulative effect of turning fragmented pieces of financial legislation into a cohesive regulatory framework. The legislative framework and non-legislative measures intend to build an investment ecosystem, which stimulates access to capital markets and economic growth. However, the regulation can facilitate the market’s operation but it cannot itself dictate it.

09 The CMU is an unfinished agenda with work ongoing. To date, most of the legislative acts have either not yet been implemented or were only recently implemented. To start preparatory work for a new blueprint, the Commission launched a High Level Forum on the Capital Markets Union made up of 28 high-level capital market experts. The Forum’s final report was published in June 2020 and includes a set of policy recommendations. The Commission published its new Action Plan in September 2020.

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Roles and responsibilities in the CMU

10 Under the subsidiarity principle, certain key policy areas for the CMU (e.g. taxation, insolvency and financial education) are the responsibility of Member States. The success of the CMU initiative depends, therefore, not only on the Commission but also on the political will and ambition of the European Parliament, the Council, and the Member States.

11 Within the Commission, the planning, overall implementation and coordination of the CMU project is in the hands of the Directorate-General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA), though other Commission departments are also involved. The Commission’s Directorate-General for Structural Reform Support (DG REFORM), created in 2020 to replace the Structural Reform Support Service (SRSS), provides technical support through the Structural Reform Support Programme (SRSP)⁴, among other tasks, to reinforce the capacity of Member States’ domestic capital markets. There is no specific budget associated with the running of the CMU.

12 The other key bodies in the functioning of the CMU are three European Supervisory Authorities (ESAs):

— the European Securities and Markets Authority (ESMA), which is the EU securities market regulator proposing implementing measures and specifying technical rules;

— the European Insurance and Occupational Pensions Authority; and

— the European Banking Authority.

Audit scope and approach

13 Given the importance of the CMU, we audited its design, implementation and effectiveness. Our report is intended to inform stakeholders and provide recommendations to the Commission to support further development of the CMU.

14 The actions we looked at relate to four out of seven intervention areas in the CMU Action Plan, namely: (i) financing for innovation, start-ups and non-listed companies, (ii) making it easier for companies to enter and raise capital on public markets, (iii) leveraging banking capacity to support the wider economy, and (iv) facilitating cross-border investment.

15 The overall question of the audit was whether the Commission has been successful in its actions towards building an effective CMU. To address this question we assessed whether the Commission:

(a) helped diversify the financing of companies, in particular SMEs;

(b) helped the development of deeper and better integrated local capital markets;

(c) took effective action to tackle key cross-border barriers; and

(d) equipped the CMU with a convincing performance framework.

16 For the purposes of our audit, we examined documentation available at the Commission and conducted interviews with relevant Commission staff. We reviewed a sample of 10 out of 54 CMU-relevant projects that were financed from the Structural Reform Support Programme (SRSP) and its preparatory action over the period 2016-2019. We used our professional judgement to select this sample (see Annex I for the list of projects) focusing on projects that were located in Member States with less-developed capital markets (see Figure 1). The selected projects were relatively advanced in terms of implementation, thus their results were more likely to be observable.
In addition, to gather information, we met authorities and stakeholders from nine selected Member States, i.e. Bulgaria, Czechia, Estonia, Italy, Lithuania, Luxembourg, the Netherlands, Poland and Romania. We also interviewed staff from the ESMA, the European Investment Bank, the European Investment Fund and the experts and representatives of the Organisation for Economic Co-operation and Development (OECD), the European Bank for Reconstruction and Development (EBRD), a number of business and investor associations, and stock exchanges.

We surveyed the authorities responsible for the regulation and supervision of local capital markets in all Member States (Ministries of Finance, national competent authorities (NCAs) and central banks), European and national business associations, investor associations and bank associations as well as stock exchanges in the EU.

We carried out our audit work from September 2019 to February 2020. Our audit work was completed prior to the outbreak of COVID-19, and therefore this report does not take into account any policy developments or other changes that occurred in response to the pandemic.
Observations

The Commission’s measures to diversify the financing options of SMEs have had no catalytic effect so far

20 In the EU, bank lending has always been the predominant source of funds to finance companies, especially SMEs. At the heart of the CMU initiative has been access to new sources of funding for SMEs, by complementing the bank-based finance with market-based finance (i.e. venture capital, private equity).

21 In recent decades, Europe generated many innovative start-ups, so-called ‘unicorns’, i.e. high-growth start-ups valued at over $1 billion (see Figure 2). An increasing number of companies of this kind, once they have passed the early growth stage, move outside the EU due to growth opportunities. The Commission has tried to stop this trend by supporting listing activities of SMEs through several measures in the scope of the CMU.

Figure 2 – The landscape of European unicorns, 2000-2020

Source: Dealroom.co.
There is large heterogeneity within the SME population, in terms of size, industry, age, activity and ownership, as well as many cross-border differences. Fast growing SMEs constitute around 11% of the 25 million companies in the EU. Facilitating access to a diversity of funding sources for fast-growing SMEs is a longstanding policy for the Commission, starting in 1998 with a Commission action plan on risk capital. The financing problem of SMEs, which varies along their growth stage (see Figure 3), has also been the focus of a number of Commission policies such as a 2011 action plan to improve access to finance for SMEs. The 2015 CMU Action Plan is a continuation of the above-mentioned initiatives (see Annex II).

**Figure 3 – Sources of funding concerning the growth stages of a company**

*Source: European Commission.*

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In the CMU Action Plan of 2015 and its 2017 update, the Commission aimed to improve access to finance for SMEs by focusing on two intervention areas: (i) financing for innovation, start-ups and non-listed companies and (ii) making it easier for companies to enter and raise capital on public markets. The regulatory changes proposed were mainly revisions of previous rules (prospectus, SME growth markets, European venture capital funds (EuVECA)).

The Commission’s other intervention area was (iii) strengthening banking capacity to support the wider economy, which included covered bonds and securitisation. This policy action is not directly linked to the financing of SMEs, but addresses the possibility for banks to deleverage (i.e. to reduce their balance sheets) without cutting credit provision to the private sector.

In order to examine whether the measures under the CMU achieved their objective of diversifying the financing for SMEs, we assessed whether the Commission:

(a) enhanced the possibilities for companies to finance expansion in their growth stages before going public (see Figure 3; including venture capital and private equity);

(b) improved the access of SMEs to public markets (i.e. going public stage);

(c) reduced information barriers that prevent SMEs from identifying sources of funding and prospective investors from investment opportunities; and

(d) enabled banks to free up their lending capacity to support SMEs.

Partial results in supporting venture capital and equity financing

Within the CMU Action Plan, the Commission launched a package of measures to support venture capital and equity financing in the EU. The measures include regulatory reform, establishing a pan-European funds-of-funds and promotion of best practices on tax incentives (see Table 1).
Table 1 – Selected audited measures under the CMU aimed at supporting venture capital and equity financing

<table>
<thead>
<tr>
<th>Measures</th>
<th>Type</th>
<th>Action completed at the Commission’s level</th>
<th>ECA observations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Establishment of a pan-European venture capital funds-of-funds</td>
<td>Injection of funding</td>
<td>YES</td>
<td>Fundraising and investment operations advancing with three funds-of-funds; amount invested expected to be leveraged by the Commission be five times (not reached yet)</td>
</tr>
<tr>
<td>Changes to the EuVECA and EuSEF Regulation</td>
<td>Legislative measure</td>
<td>YES In force since March 2018</td>
<td>Increased registration of venture capital funds only in those Member States with already attractive, integrated and well-developed venture capital markets</td>
</tr>
<tr>
<td>Study and promotion of best practices on tax incentive schemes for venture capital and business angel investments</td>
<td>Non-legislative measure</td>
<td>YES</td>
<td>Presentation of the study in two workshops to promote the results among tax administration of Member States; no further impact at Member State level</td>
</tr>
<tr>
<td>Legislative proposal on Common Consolidated Corporate Tax Base (CCCTB)</td>
<td>Legislative measure</td>
<td>YES</td>
<td>The CCCTB proposed in 2011 (too ambitious for Member States to agree); proposal relaunched in 2016, no agreement so far</td>
</tr>
</tbody>
</table>

Source: ECA.

27 EU venture capital and private equity markets are still characterised by big differences among Member States, as regards both the size of the SMEs’ financing gap and the availability of funding sources, in particular as regards institutional investors. Indeed, there is a huge fragmentation of the markets between the centres and peripheral parts of the EU in terms of venture capital and private equity investments (i.e. the localisation of the portfolio companies receiving the funds); these are mainly concentrated in a few Member States (i.e. France, Germany, the Netherlands, Denmark and Sweden).

28 The review of the regulations on EuVECA and European social entrepreneurship funds (EuSEF) was the first legislative measure included in the CMU Action Plan to promote cross-border oriented venture capital companies and support development of less developed areas among the European venture capital market. However, this measure only effectively increased the number of registrations of EuVECA funds in those Member States with well-developed venture capital markets (e.g. France and the Netherlands).
Our data analysis on EuVECA and EuSEF newly registered funds and our interviews with market participants and stakeholders have revealed that the EuVECA and EuSEF labels are still not used by the majority of venture capital funds and proved not to be decisive for the market expansion and the financing of SMEs. The results of our survey conducted among EU public authorities show that 22% of respondents do not believe that the 2017 amendments to EuVECA regulation increased the level of investment in EU venture capital enterprises, whereas 45% of them consider that it is too early to assess.

The establishment of the pan-European venture capital funds-of-funds represents a potential injection of €410 million in the market through the EU budget. This measure is the only funding action within the CMU Action Plan. Outside of the Action Plan, the Commission is also active in financing SMEs providing significant funding through centrally and shared managed programmes. Although the expectation of raising €2.1 billion from private or public investors (i.e. to leverage the amount injected to the fund by five times) remains to be fulfilled, the fundraising and investment operations with three funds of funds are advancing with the effect of attracting private investments and increasing the size of the EU venture capital market.

To support private equity and venture capital markets, the Commission also published a report on tax incentives schemes for venture capital and business angel investment including best practice and presented this report in two workshops. There was no further follow-up to this action in the Member States.

The Commission made a legislative proposal to address the so-called debt-equity bias. In most Member States, interest on debt and the return on equity capital are treated differently, which prevents development and integration of markets. Because interest is deductible from the corporate tax base while returns to equity are not, there is a tax advantage for debt financing which influences financial decisions made by companies and investors. Because of this, the cost of capital for equity was estimated to be 45% higher than the cost of capital for debt.

The Commission has tried to address this issue under the CMU by proposing the introduction of a corporate tax offset allowance for equity issuance as part of the Common Consolidated Corporate Tax Base (CCCTB) proposal. However, the proposed

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8 ECA special report 17/2019, paragraph 20.

solution has not yet been implemented due to the lack of agreement from the Council, which remains solely responsible for taxation matters.

SMEs’ access to public markets has to be improved

Raising equity financing on the public market is more difficult for SMEs than for larger companies because they fear losing ownership, and do not have the same capacity to comply with disclosure requirements and bear the associated costs (even up to 15% of the amount raised). The Commission has set an objective of making it easier and less costly to issue bonds and equity in the public markets, while ensuring the protection of investors. For this purpose, the Commission launched a package of measures (see Table 2).

Table 2 – Selected audited measures under the CMU aimed at strengthening access to public markets for companies

<table>
<thead>
<tr>
<th>Measures</th>
<th>Type</th>
<th>Action completed at the Commission’s level</th>
<th>ECA observations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulation to review the rules on the issuance of prospectus</td>
<td>Legislative measure</td>
<td>YES</td>
<td>Proposal rejected in first instance by the Commission’s Regulatory Scrutiny Board as to why the second revision within 5 years was expected to be successful; proposal accepted after rushed re-submission; prospectus still considered as expensive and too complex for SMEs; no exemption for secondary issuance; no significant increase of IPOs observed since July 2019</td>
</tr>
<tr>
<td>New regulation to support the SME growth markets, introduced by MiFID II</td>
<td>Legislative measure</td>
<td>YES</td>
<td>Positive message to the SME ecosystem that EU policymakers were ready to introduce proportionality in the texts for the benefit of SMEs</td>
</tr>
<tr>
<td>Monitor progress on International Accounting Standards Board commitment to improve disclosure, usability and accessibility of IFRS</td>
<td>Ongoing non-legislative measure</td>
<td>YES</td>
<td>No tangible result of the monitoring activity on the market</td>
</tr>
</tbody>
</table>

Source: ECA.
Macroeconomic conditions, such as liquidity on the market, investors’ appetite, interest rate level, expected economic growth rate, expected tax rate and inflation rate, can have a bigger impact than the costs of publishing a prospectus and determine a company’s choice to proceed to an IPO or not. In the aftermath of the financial crisis, the number of IPOs in the EU fluctuated, reaching a total of 90 IPOs in 2019, but it did not recover since 2009 (see Figure 4). The largest total number of IPOs in the EU was recorded in 2011, when the number of recorded IPOs reached 415\(^{10}\).

**Figure 4 – Total number of IPOs in the EU 2009-2019**

![Graph showing total number of IPOs in the EU from 2009 to 2019](image)


The access to public markets for SMEs has so far not been significantly strengthened or become cheaper, as evidenced by our interviews and surveys. The costs associated with the publication of a prospectus only slightly decreased and the process is still burdensome and lengthy. In addition, the cost of advisory services as regards issuing a prospectus determines the bulk of costs associated with its publication, which is not easily influenced by the Commission’s actions.

Moreover, the changes in the regulation and the lack of harmonisation of national rules for issuances below the threshold under which a prospectus is not required, creates scope for regulatory arbitrage. Indeed companies planning to raise up to €8 million and established in a country where the obligation for a prospectus is

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\(^{10}\) IPO Watch Europe 2011 and IPO Watch Europe 2019.
above €1 million can make a cross-border equity issuance online (i.e. equity crowdfunding) through a platform established in another country with no prospectus obligation for issuances up to €8 million.

38 We note also that, when preparing the 2015 Action Plan, the Commission did not consider injecting any funding in support of SME IPOs, for instance in the form of a public-private fund. However, in March 2020 the Commission announced its intention to set up a public-private fund investing in public offerings.11

39 Another measure of the CMU Action Plan, the Regulation on SME Growth Markets, included amendments to the Market Abuse Regulation and further changes to the rules on prospectuses to make it easier for SMEs to issue equity and debt on the SME growth markets. Furthermore, the Commission proposed additional rules to facilitate the registration of multilateral trading facilities as SME growth markets and to foster the liquidity of publicly listed SME shares to make these markets more attractive for investors, issuers and intermediaries. The legislative measure was adopted in 2019 and entered into force in January 2020. The enactment of this measure has sent a positive message to the SME ecosystem that EU policymakers are ready to introduce changes to the benefit of SMEs.

Limited impact in overcoming information barriers

40 Information barriers represent one of the main obstacles that affect the demand and the supply side of the SMEs funding market. On the demand side, SMEs face difficulties in determining the funding options available. On the supply side, investors have difficulties in assessing the creditworthiness of SMEs. The Commission has tried to address both of these issues (see Table 3).

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Table 3 – Selected audited measures under the CMU aimed at overcoming information barriers for the financing of SMEs

<table>
<thead>
<tr>
<th>Measures</th>
<th>Type</th>
<th>Action completed at the Commission’s level</th>
<th>ECA observations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Encouraging an agreement between bank federations and SME associations on high-level principles on feedback given by banks rejecting SME credit applications</td>
<td>Non-legislative measure</td>
<td>YES</td>
<td>Application of high-level principles in the hands of the bank federations</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Agreement non-binding for banks</td>
</tr>
<tr>
<td>Support a pan-European information system for investors</td>
<td>Non-legislative measure</td>
<td>YES</td>
<td>Commission concluded that EU intervention would not bring added value unless local and national authorities find solutions first</td>
</tr>
</tbody>
</table>

*Source: ECA.*

41 On the demand side, the Commission encouraged a non-binding agreement between banks federations and SME associations on high-level principles to provide feedback by banks on rejected SME credit applications. We note that the initiative entirely depends on the uptake by the industry. The principles are still not yet known by the whole banking sector and such feedback would not have a massive impact on the loan applications of SMEs, as only 6 % of them were rejected in the euro area in 2019.

42 On the supply side, the attempts made to develop a pan-European information system containing information on SMEs were stopped, since a lack of budget and expertise made them unfeasible. The Commission concluded that EU intervention would not bring added value unless local and national authorities found solutions first.

43 We note that the establishment of an EU-wide digital access platform to companies’ public financial and non-financial information, the European Single Access Point (ESAP), has been under discussion since the adoption of the Transparency Directive in 2013. Even if the project could be highly relevant for the CMU to overcome information barriers, the Commission did not include it in its Action Plan but delegated it to ESMA. In 2017, ESMA deprioritised the project due to lack of budget, lack of comparability of company data from Member States and lack of mandate to validate company data submitted by Member States.
Actions to generate new bank lending to SMEs have had no observable effect

With its CMU measures under the intervention area to leverage banking capacity, the Commission aimed at facilitating bank financing of companies and the wider economy. We examined whether the Commission’s actions regarding the securitisation framework, covered bonds and European Secured Notes were effective in supporting banking capacity to support EU companies (see Table 4).

Table 4 – Selected audited measures under the CMU aimed at leveraging banking capacity

<table>
<thead>
<tr>
<th>Measure</th>
<th>Type</th>
<th>Action completed at the Commission’s level</th>
<th>ECA observations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Securitisation Regulation</td>
<td>Legislative measure</td>
<td>YES In force since 2019</td>
<td>Long legislative process (2 years); process for the potential inclusion of synthetic securitisation in considerable delay; delays in secondary legislation and guidelines which had a negative impact on STS securitisation issuance in the short-term</td>
</tr>
<tr>
<td>Directive on Covered Bonds</td>
<td>Legislative measure</td>
<td>YES Applicable from 2022</td>
<td>Too early to assess</td>
</tr>
<tr>
<td>European Secured Notes</td>
<td>Non-legislative measure</td>
<td>YES</td>
<td>The European Banking Authority report on the European Secured Notes published, no follow-up action</td>
</tr>
</tbody>
</table>

Source: ECA.

Given that SMEs usually have no direct access to the capital markets, a functioning securitisation market allows the transformation of illiquid loans into marketable securities. It can therefore be considered as an indirect financing instrument for SMEs. The measure under the CMU Action Plan, the new Simple, Transparent, and Standardised (STS) securitisation framework, was an initiative driven by both the regulator and the industry to essentially create a “gold standard” indicating the highest quality securitisations.

Although the Commission considered its proposal as a “low-hanging fruit” within the CMU Action Plan, the legislative process required more than two years. While the STS Securitisation Regulation has been in effect since January 2019, the majority of the secondary legislation and guidelines that are required in order to interpret and ensure compliance with the Regulation came into effect only in September 2020.
47 We note that in its impact assessment for the Securitisation Regulation, the Commission did not provide any data or an estimate as to which share of the European securitisation market would meet the new STS criteria. The lack of legal clarity, caused by delays in the adoption of secondary legislation and guidelines, negatively affected the STS transactions in the short-term\(^\text{12}\) (i.e. the first STS transaction was conducted on 21 March 2019, almost three months after the application date), but the situation gradually improved with 143 securitisations within the same year. By June 2020, a further 165 notifications were made making 308 in total.

48 In 2019, the new STS label covered almost half of the EU market share (46 % with around €100 billion; see Figure 5) but the overall securitisation market did not show signs of growth. Securitisation transactions remain largely concentrated within traditional asset classes such as mortgages and car loans.

**Figure 5 – European securitisation issuance, 2010 – 2019 (in billion euros)**

![Graph showing European securitisation issuance from 2010 to 2019](source)

With regard to the results achieved, we note that SME securitisation issuance is still suffering from the 2007/2008 financial crisis and remains at low levels (10.6 % of total issuance in 2019, see Figure 6). In 2019, the overall issued volume of SME deals (€23 billion) was below the 2007/2008 levels and the pre-CMU period of 2014/2015 and the securitisation of SME loans made up only 1 % of STS transactions as of

\(^{12}\) EUROFI Regulatory Update – April 2020, Relaunching securitisation in the EU, p. 21.
June 2020. Moreover, the SME securitisation is concentrated in a few Member States (Belgium, Italy and Spain, based on outstanding volumes as of June 2020).

**Figure 6 – European SME securitisation issuance, 2000-2019 (volume in billion euros and share as % of total securitisation)**

**NB.** In Q1 2020, there were no SME securitisations.

*Source:* ECA based on Association for Financial Markets in Europe and OECD data.

We note that in December 2019, the Council asked the Commission to assess whether to establish EU labels including "SME securitisation", "SME European Secured Notes (ESNs)", "SME investment funds" and loan originating funds with a view to improving the funding conditions for SMEs. Moreover, the Commission, in association with the EIB Group, introduced securitisation vehicles to help finance SMEs, mostly in the Central, Eastern and South-eastern Europe (CESEE) region. Nevertheless, these transactions have not triggered an increase in private participation.

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Shortcomings in the efforts to develop local capital markets

51 Well-functioning local markets offer to support private-sector financing and investments, ultimately leading to economic growth and job creation. The EU capital markets remain heterogeneous and concentrated in Western and Northern Europe (see Figure 1).

52 The CMU Action Plan is aimed at developing local capital markets by reinforcing their specific capacities and facilitating their integration. Nevertheless, the policy measures taken need to fully observe the subsidiarity principle. National and regional authorities are responsible in the first place for developing local markets.

53 The Commission also provides funding sources (such as venture capital or loan guarantees) to support SMEs either via programmes managed centrally by the European Commission (such as the Competitiveness of Enterprises and SMEs programme – COSME) or via the European Structural and Investment Funds under shared management (i.e. funds whose management is shared between EU and the Member States). These actions do not fall under the CMU Action Plan. EU support covers a variety of different financial instruments (equity and debt, loan guarantees and venture capital, capacity building and risk sharing facilities).

54 Another way for the Commission to foster the development of local capital markets is through the European Semester, an annual cycle of economic and fiscal policy coordination introduced in 2010 to improve the EU’s economic and social sustainability. Each year, the Commission performs an analysis of each country’s plans for budgetary, macroeconomic and structural reforms and then provides Member States with country specific recommendations (CSRs) for the next 12-18 months that are endorsed and formally adopted by the Council.

55 Under the SRSP, the EU provides technical support to EU Member States for institutional, administrative and growth-enhancing reforms, including the development of their capital markets. The SRSP is demand-driven; in other words, the Member States choose whether or not to submit project proposals for funding to the Commission.

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We assessed whether:

(a) the Commission has a comprehensive strategy to foster the development of local capital markets;

(b) the European Semester was used to support CMU-related reforms in Member States; and

(c) technical support provided under the SRSP effectively helped to develop capital markets.

Lacking a comprehensive strategy for the development of local capital markets

In the CMU’s Mid-Term Review in 2017, the Commission planned to prepare a comprehensive EU strategy on local and regional capital market developments across the EU. This was one of nine new priority actions in the CMU agenda. The Commission did not issue a distinct strategic report, as it did for example for sustainable finance and Fintech in March 2018. It rather just reported with a delay of nine months on actions that could be taken at national and regional level to develop capital markets. This fell short of the expectations created by the Mid-Term Review (see Annex III). It was not a strategy in the sense of presenting a long-term perspective covering comprehensively all capital market segments, and did not include any concrete actions to be taken by the Commission.

In our survey, the majority of the Member States’ authorities were of the opinion that the CMU Action Plan largely adopted a ‘one size fits all’ approach and that it did not specifically foster the development of local markets (see Table 5).

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Table 5 – Comments by the Member States about the CMU approach for local and regional capital markets

<table>
<thead>
<tr>
<th>Western and Northern Europe</th>
<th>Southern Europe</th>
<th>Central and Eastern Europe</th>
</tr>
</thead>
<tbody>
<tr>
<td>• “The CMU Action Plan aimed at fostering convergence among EU capital markets and ease cross-border capital flow rather than foster the development of local markets specifically. In our view, it aims at increasing liquidity and market depth globally.”</td>
<td>• “It was more like a “one size fits all” approach”</td>
<td>• “CMU legislative actions were not proportionate and were not taking into account size of less-developed capital markets”</td>
</tr>
<tr>
<td>• “There did not seem to be a particular focus on this. Some proposals even would have put at risk well established and functioning national or regional segments of capital markets”</td>
<td>• “We could expect further measures for local capital markets”</td>
<td>• “Interests of small and less developed markets could be taken into account more”</td>
</tr>
<tr>
<td>• “It was more like a “one size fits all” approach”</td>
<td>• “We could expect further measures for local capital markets”</td>
<td>• “The CMU initiative actually aims at centralisation, in our opinion, thus heavily focusing on most developed markets”</td>
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<tr>
<td>• “We could expect further measures for local capital markets”</td>
<td>• “The CMU initiative actually aims at centralisation, in our opinion, thus heavily focusing on most developed markets”</td>
<td>• “CMU initiatives were targeted more to developed larger markets and smaller, less developed markets benefited less. Also small companies (micro) did not get the expected benefits (less regulatory burden)”</td>
</tr>
<tr>
<td>• “There is a need to prepare measures in a way which would benefit not only the already strong financial centres but also capital markets of smaller economies in the EU”</td>
<td>• “There is a need to prepare measures in a way which would benefit not only the already strong financial centres but also capital markets of smaller economies in the EU”</td>
<td>• “In practical solutions the principle of local needs has not been realised”</td>
</tr>
</tbody>
</table>

NB. Ten illustrative replies out of the 17 Ministries of Finance that responded to our survey; similar replies were provided by NCAs and central banks.

Source: ECA survey.

The European Semester is not used to its full potential to foster capital markets reforms

59 We examined whether the Country Reports identified important risks with regard to the development of capital markets and whether the Commission addressed country-specific recommendations (CSRs) to Member States with underdeveloped capital markets.

60 In our sample, we found that the Country Reports identified important risks and served as a good basis for formulating CSRs aiming at the development of capital markets and better access to alternative sources of financing for companies. However, there were some cases where challenges in areas such as market developments, governance and supervision could have been better reflected in the 2018 or 2019
Country Reports. Moreover, no Country Report in our sample included specific indicators referring to the domestic capital markets.

61 We observed that nine Member States during the 2016-2019 period, i.e. after the adoption of the CMU Action Plan, were requested to implement reforms aiming at capital markets and better access to non-bank finance. Annex IV provides the list of the recommendations that we took into consideration.

62 Our analysis of the less developed capital markets within the EU showed (see Annex V) that, for at least four consecutive years, the Commission did not recommend the implementation of directly related reforms in ten Member States, although these Member States still have a less developed capital market than the EU average. In five out of these cases (Bulgaria, Croatia, Greece, Latvia and Slovakia), the Commission proposed recommendations on broader challenges affecting the financial sector, such as supervision of financial services or the judicial system which can have an impact on the local capital market, albeit mostly indirect. Thus, for five Member States with less developed capital markets, no CSRs were issued that were either directly or indirectly relevant to the CMU objectives.\footnote{Czechia, Estonia, Hungary, Poland and Romania.}

63 While we acknowledge that the capital market topic is only one of many policy challenges to be addressed in the European Semester process, the criteria and rationale for prioritising the areas on which to propose CSRs is not clearly documented by the Commission\footnote{ECA special report 16/2020, paragraphs 49-50.}. Moreover, we did not find specific recommendations aiming at promoting cross-border integration of local capital markets for the design and implementation of pertinent reforms.

64 In line with the ECA’s Special Report on the European Semester\footnote{ECA special report 16/2020 – Box 5.}, we also noticed that within one CSR, CMU-relevant reforms were mixed with other policy areas, even unrelated ones (e.g. employment, social inclusion). Furthermore, CSRs related to capital markets lacked targets against which to benchmark progress based on a clear timetable for implementation\footnote{ECA special report 16/2020, paragraphs 51, 63 and Recommendation 4.}.

65 With regard to the CMU-related CSRs from 2016, 2017 and 2018, we noted that the Commission’s assessment had found that the progress made by the end of 2019...
had been partial. None of the Member States involved had fully or substantially implemented the recommended reforms, suggesting that the timeframe was too short or there had been an issue of national ownership by Member States to implement CSRs.

Technical support is largely appreciated, but the results are still to come

66 We assessed whether the Member States with less developed markets benefited from projects under the SRSP and whether the projects provided added value and led to positive results in the Member States.

67 In the CMU Action Plan, the Commission committed to developing a strategy for providing technical support to Member States to support capital markets’ capacity by Q3 2016, an additional measure to the EU’s comprehensive strategy on local and regional capital markets (see paragraph 57). However, in September 2016 and pending the adoption of the SRSP Regulation, the Commission reported that it had developed capacity to provide technical support and would work with Member States to identify priority areas but that it had not published any strategic documents.

68 The SRSP support is demand-driven and does not require co-financing from Member States. It covers the entire process cycle from the preparation and design to the implementation of a project. Over the period from 2016 to 2019, the SRSP and its preparatory action financed 54 CMU-relevant projects with a budget of €14.31 million in 20 Member States.

69 As regards the reasoning provided by the national authorities to apply for technical support, all 10 requests of our sample referred to the implementation of the CMU as a Union priority. In half of the cases (five requests), the authorities claimed that the request was in line with their own reform agenda. Only one Member State from the sample (Lithuania) had received a CMU-relevant CSR and the project request referred to this CSR as a relevant circumstance. Two other Member States (Bulgaria and Italy) had received wider CSRs (relating to insolvency and supervision) but their requests were not linked to those CSRs.

70 Figure 7 presents the number of projects approved and their budget in each Member State. The figure shows that there are significant divergences among countries with less developed capital markets (e.g. Croatia and Romania in comparison to Bulgaria, Hungary and Slovakia).
Figure 7 – Number of CMU-relevant projects approved and their budget per Member State, 2016-2019

Source: ECA based on SRSS data.

The SRSS succeeded in supporting more than one CMU-relevant project in nine Member States. However, we found that six Member States (Slovakia, Bulgaria, Hungary, Greece, Cyprus and Austria) with less developed capital markets had implemented zero or one CMU-relevant projects. Three of them had submitted either a low number of requests (one each by Slovakia and Bulgaria) or none (Austria).

Although the intervention logic of the SRSP was not formally oriented towards the specific needs of EU capital markets, the objectives of the CMU were addressed in each individual project. Furthermore, the selected projects clearly demonstrated a link with the identified national needs. They also addressed most of the priorities for policy actions identified by the Vienna Initiative in 2018. We noted that within the group of the CESEE countries, only one out of six submitted requests relating to financial

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literacy, which is a key issue for less developed capital markets (see paragraph 82), was selected (Czechia). The others were rejected partially due to a lack of project maturity.

73 The SRSS intended to adopt a three-stage/step-by-step approach in sequencing interventions, i.e. first comprehensively analyse the current state of capital market development, then assist to improve access to market infrastructure and, finally, support efforts in deepening and widening of capital market access. For this purpose, the SRSS set seven broad areas and 26 types of CMU-relevant projects to be potentially supported. The document stating this approach was provided to selected Member States visited on the spot in 2017 and 2018.

74 In six out of 13 Member States with relatively less developed capital markets (Lithuania, Slovenia, Slovakia, Hungary, Greece and Cyprus), the SRSS did not closely follow this approach. However, this does not imply that the projects selected were not relevant or that they did not foster the development of capital markets. While a capital markets diagnostic or strategy did not exist for those Member States, the SRSS approved projects submitted by these countries that were addressing particular sectors of their capital markets.

75 By March 2020, only two multi-country requests were submitted by Member States, both of them by Estonia, Latvia and Lithuania (see Box 1). These were approved under the SRSP. Despite significant challenges to coordinating such projects across all Member States involved, their potential results and impact on the region can be significant.

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Box 1

Covered bonds – legal and regulatory reforms

The SRSS (presently DG REFORM), together with the EBRD, is supporting the Baltic States with the introduction of a pan-Baltic covered bond framework, contributing towards well-functioning and larger capital markets in the region, opening up long-term funding options for banks, and increasing the level of lending to economies. It is envisaged that each Baltic State will have its own covered bond law and secondary regulations, and so the pan-Baltic covered bonds issuance will be achieved on the basis of the overall framework. In Estonia, the law on covered bonds was adopted by the Parliament in February 2019 but further amendments are required to fully include the pan-Baltic angle and align it with the EU covered bond legislative package. The following diagram illustrates how the covered bond framework will operate:

Source: EBRD.

As regards the timely delivery and respect of milestones, we found several shortcomings with regard to projects in our sample. In almost all these projects, the contracting and implementation phases lasted longer than initially estimated and there were delays in the submission of the final deliverables compared to the initial schedule in the SRSS analysis. Five projects have taken (or are expected to
take considerable time in order to be finalised from the submission of the requests (between 30 and 40 months), mostly due to the abovementioned delays.

77 When it comes to results achieved, a conclusion is not yet possible as most projects were still under implementation at the end of the audit. Similarly, in our survey, the majority of Member States’ authorities (57 %) did not comment on the importance of the technical support provided to them as they consider that more time is needed to reach a solid assessment. Nevertheless, we noted that the results so far were mixed within our sample. For half of the eight completed projects (i) not all recommendations initially suggested by the contractor were eventually included in the final report or considered for implementation by the national authorities and (ii) the overall implementation of recommendations included in the studies is rather low.

78 As required by the SRSP Regulation, the SRSS monitors the results of the technical support it provides. In this context, the SRSS sends out two questionnaires to the beneficiary authorities. Market participants not involved in the project implementation are not asked to participate, even though they are in a position to provide independent, practical and broader feedback.

The Commission has taken some action within its remit but has not fully tackled key cross-border barriers

79 Cross-border investments are impaired by the fragmented European market along national boundaries. The lack of market integration is reflected by the low proportion of assets held by collective investment funds (UCITS and AIFs) that are registered for sale in more than three countries. Statistics show that while the market for collective investment funds in Europe has grown, market activity is concentrated in a few countries24. As of June 2017, approximately 70 % of all assets under management were held by investment funds registered for sale only in their domestic market25.

80 In their report of 24 March 201726, the Commission and the Member States identified three types of barriers that impede cross-border capital flows at different stages of the investment cycle. The report resulted in a Joint Roadmap of actions.

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which included only those barriers that Member States were ready to address. As part of the CMU Action Plan, the Commission set up an expert group in 2016, the European Post-Trade Forum (EPTF), to undertake a broad review of the progress made in the field of securities post-trading and in the removal of Giovannini barriers (inefficiencies in the cross-border clearing and settlement arrangements identified in 2001 and 2003)\textsuperscript{27}. Some of the barriers identified by the Commission and Member States were also flagged up by the EPTF in its subsequent report of 15 May 2017\textsuperscript{28}. Both reports suggest that many of the barriers impeding cross-border capital flows have remained unresolved for decades.

Based on the two reports, the Commission has proposed legislative as well as non-legislative measures to alleviate barriers to cross-border capital flows. We audited measures under the CMU relating to financial literacy of investors and particularly SMEs, insolvency law and withholding taxes (see Figure 8).

**Figure 8 – Action taken to address barriers to cross-border investment**

- **Financial Education**
  - Non-Paper on Financial Literacy prepared by a Sub-Group of 18 Member States led by Croatia

- **Insolvency Law**
  - Directive on preventive restructuring and second chance
  - Proposal for a regulation on the law applicable to the third-party effects of assignments of claims
  - Communication on the applicable law to the proprietary effects of transactions in securities

- **Withholding Tax**
  - Code of Conduct on Withholding Tax
  - Follow-up Monitoring and Workshops with Member States

*Source: ECA.*

The Commission could have done more to promote financial literacy among SMEs

OECD surveys of financial literacy confirm that levels of financial literacy measured in terms of financial knowledge, behaviour and attitudes remain heterogeneous across the EU. They also show that gender, age, digital skills and

\textsuperscript{27} The Giovannini Group (November 2001), Cross-Border Clearing and Settlement Arrangements in the European Union.

\textsuperscript{28} COM(2015) 468 final.
financial resilience matter for financial literacy. The aforementioned heterogeneity in levels of financial literacy is also evident amongst SMEs. The Commission and European Central Bank’s SAFE survey shows that most small companies’ managers do not feel confident in talking to equity and venture capital providers rather than banks about finance. This appears more pronounced in Central and Eastern Europe than the rest of the EU.

While the CMU Action Plan did not contain any specific commitment to address financial literacy, the Commission and Member States identified insufficient levels of financial literacy as a barrier that deters investors from maintaining or increasing their cross-border exposure. They committed in the joint roadmap of actions to "start exchanging best practices on financial literacy programmes, taking into account the cross-border dimension".

In line with this commitment, a sub-group of 18 Member States chaired by Croatia took up the task and produced a non-paper in 2018 that was endorsed by the joint Commission and Member State Expert Group on barriers to the free movement of capital. Amongst others, the non-paper recommends that Member States measure financial literacy levels and implement evidence-based and accessible financial education programmes. It also states that initiatives tackling the cross-border dimension of SMEs are lacking. Further, “the cross-border dimension of SME financial literacy would be difficult to address since there is still much to be done at national level”. Some Member States called for the EU to address this important issue.

In the area of financial education, the primary competence lies with the Member States. The recommendations of the non-paper leave open how the EU should exercise its competence to support Member States in fostering financial literacy, including among SMEs. The Commission has not yet decided how to move forward. In our survey of public authorities, 73 % were of the opinion that the Commission, alongside Member States, should have proposed and financed concrete actions within the CMU initiative to increase financial literacy among retail investors and entrepreneurs. However, at the same time there was a lack of support from Member States, which is


why the Expert Group on barriers to the free movement of capital was put on hold in 2018.  

86 We note that the Expert Group’s non-paper on financial literacy did not systematically consider how existing EU funding programmes and platforms including the Enterprise Europe Network and the European Investment Advisory Hub are already being used to foster financial literacy and how they could potentially be used more effectively to this end. For instance, the Enterprise Europe Network launched by the Commission in 2008 is intended to help businesses innovate and grow on an international scale, among other things by providing advice on finance and funding. Similarly, the services available via the European Investment Advisory Hub include financial advice to enhance companies’ ability to access adequate sources of financing.

The Commission’s actions are unlikely to lead to a substantial convergence of insolvency proceedings

87 Strong and efficient insolvency frameworks are conducive to cross-border capital market transactions. According to the CMU Action Plan, the inefficiency and divergence of insolvency laws currently makes it difficult for investors to assess credit risk, particularly in cross-border investments. The Commission states that a convergence of insolvency and restructuring proceedings would facilitate greater legal certainty for cross-border investors and could thus encourage more cross-border activity.

88 As announced in the CMU Action Plan and the Mid-Term Review thereof, the Commission proposed two legislative initiatives and one non-legislative measure on the issue of insolvency.

— The Directive on early restructuring and second chances mainly establishes minimum standards for procedures that restructure viable companies before they go insolvent and for procedures leading to a discharge of debts.

31 Minutes of the Financial Services Committee of 3 May 2018.
32 https://eiah.eib.org/about/index.
33 Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and
The Proposal for a regulation on the law applicable to the third-party effects of the assignment of claims\textsuperscript{34} seeks to introduce uniform conflict of law rules that clarify which laws assignees must observe in order to acquire legal title over the assigned claims.

The Communication\textsuperscript{35} on the applicable law to the proprietary effects of transactions in securities clarifies that there are different ways of determining where a securities account is maintained or located and that all definitions are equally valid for the purposes of determining which conflict-of-law rules apply in the event of insolvency or another dispute.

While the two legislative acts are still pending approval by the Council or transposition into national law, neither of the actions is suited to bring about a substantial convergence of insolvency proceedings, as they largely address issues faced by market participants prior to entering into insolvency proceedings, such as the restructuring of viable companies and clarifying ownership rights. They also support market participants with the consequences resulting from insolvency, such as a debt overhang and the difficulty of starting a new business venture. While a convergence of insolvency proceedings is not one of the main objectives of the CMU, the Commission has stated its intention to foster such a convergence in the CMU Action Plan\textsuperscript{36}.

So far, the Commission has refrained from taking further action on harmonising core elements of insolvency proceedings. This is because substantive insolvency law remains the sole competence of Member States, and the EU’s role is limited to developing judicial cooperation in civil matters with cross-border implications. According to interviews with the Commission, during the Council negotiations on the proposal for the Restructuring and Insolvency Directive, and already in pre-meetings consulting Member States before the actual proposal, the reluctance of Member States to address core areas of insolvency laws was obvious.

However, a comparative study on substantive insolvency law in the EU\textsuperscript{37}, contracted by the Commission in 2016 suggested that there was room for harmonising discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency) (OJ L 172, 26.6.2019).

\textsuperscript{34} COM(2018) 96 final.
\textsuperscript{35} COM(2018) 89 final.
\textsuperscript{37} EU publication, Study on a new approach to business failure and insolvency, 2016.
aspects of insolvency proceedings. On the one hand, the study revealed that there are vast differences in national insolvency frameworks, which make it difficult to arrive at a common approach onto which to harmonise. On the other hand, the study raised issues that are deemed appropriate for the EU legislator to consider taking forward, including qualifications and training of insolvency practitioners, the ranking of claims and order of priorities, avoidance and adjustment actions and procedural issues relating to formal insolvency proceedings.

92 The results of our survey of public authorities show that over 50% of the respondents believe the Commission should prioritise finding common ground in particular on: a) the conditions for opening insolvency proceedings, b) the definition of insolvency, and c) the ranking of insolvency claims (see Figure 9). 23% of respondents indicated that the Commission should lay down common ground for avoidance actions.

Figure 9 – ECA survey question on the harmonisation of insolvency law

In order to lay down common ground for convergence of insolvency regimes, the European Commission should attempt to harmonise the following core aspects:

- Conditions for opening insolvency proceedings: 54%
- The definition of insolvency: 54%
- The ranking of insolvency claims: 51%
- No opinion: 32%
- Avoidance actions: 23%
- Other: 7%

Multiple answers possible

“The current patchwork of national insolvency and securities law continue to give raise to legal uncertainty and transaction costs discouraging investments into the EU capital market. A more holistic approach seeking broader harmonisation of national laws in these areas would seem to be both necessary and affordable (at least on an opt-in basis).”

“A convergence of insolvency regimes in the European Union is difficult to achieve. The respective insolvency regimes in EU Member States are very different. In particular, there are inter-relations among the relevant insolvency laws and other areas of the national law of EU Member States (i.e. commercial law, labour and social security law, tax law), which are only randomly harmonised at EU level. As a first step, it is advisable for the Commission to focus on harmonising the conditions for the opening of insolvency proceedings.”

Source: ECA.
The Commission issued a sound Code of Conduct on Withholding Tax but it is not binding

93 A withholding tax is a direct tax levied on passive income including interest, dividends, royalties and capital gains. The tax is withheld by either the resident or the source country or both, and the investor must apply to reclaim the tax or obtain a refund. In their report on cross-border barriers (see paragraph 80), the Commission and Member States identified discriminatory and burdensome procedures for claiming relief from withholding taxes as hampering cross-border investment. Similarly, the EPTF flagged inefficient withholding tax collection procedures as a priority for action to improve the post-trading environment in the EU38.

94 To address these issues the Commission published on 11 December 2017 a Code of Conduct on Withholding Tax. It mainly recommends that governments take steps to implement simplified tax refund procedures among which a standardised and harmonised system for providing tax relief at source so that treaty entitlements and exemptions are directly applied and are put in place. However, the Code is non-binding and not firm enough in places, for example on deadlines by which tax authorities in Member States must process requests for reclaims.

95 While the Commission has been active in promoting simpler withholding tax procedures within the EU, it has so far refrained from proposing more than a non-binding code of conduct as the legal and political hurdles of doing otherwise would be high. In particular, also in the light of difficult discussions at international level, it did not propose a directive based on Article 115 TFEU because doing so would require:

— the Commission to show that its lack of action directly affects the proper functioning of the internal market, and

— unanimity in the Council and a special legislative procedure.

96 Since 1975, the Commission has attempted to find a common solution concerning withholding tax on dividends based on Article 115 TFEU but has not been successful. A more recent Commission Communication proposing a step-by-step transition towards qualified majority voting in the area of taxation39 was rejected by a majority of Member States.

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Instead, the Commission has monitored the implementation of the code of conduct through a questionnaire and workshops with Member States. Both highlighted, among others, the following areas for further improvement:

— digitalising the submission of refund claims, and
— introducing the possibility of accepting alternative proofs of tax residence.

Further, in the framework of the Tax Administration EU Summit, Member States’ tax administrations agreed in May 2020 that the Commission will organise a dedicated stream of work to explore legislative and non-legislative initiatives to address the current challenges on WHT procedures, including a potential relief at source system.

On 15 July 2020, the Commission issued an Action Plan for fair and simple taxation. As tax barriers to cross-border investment persist despite the Withholding Tax Code of Conduct, the Commission announced that it would propose a legislative initiative for introducing a common and standardised, EU-wide system for withholding tax relief at source, accompanied by an exchange of information and cooperation mechanism among tax administrations. In 2022, the Commission intends to produce an impact assessment possibly leading to a Commission proposal for a Council directive introducing a system of relief at source.

The CMU lacked a convincing performance framework

We examined whether the Commission:

(a) set up specific, measurable, achievable, reasonable and timely objectives and sufficiently prioritised the measures;

(b) communicated clearly with the public about the CMU; and

(c) put a comprehensive monitoring system in place.

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40 COM(2020) 312 final.
The objectives of the CMU were rather vague and the priorities were set late

101 The CMU Action Plan and its Mid-Term Review were accompanied by a detailed economic analysis. As regards the consultation process for the Commission’s 2015 Green Paper on the CMU and for its 2017 update, the Commission organised the process well and communicated well on the results; this was confirmed by our survey. The CMU mainly evoked the interest of the financial sector and of four big Member States. There was less interest from other businesses/SMEs and Member States with less developed capital markets.

102 The CMU Action Plan builds on three levels of objectives: two overarching, three strategic and three operational. Under the operational objectives, the Action Plan is split into seven areas of intervention, which are in turn split into 25 specific objectives. The specific objectives are implemented through a total of 71 measures. This intervention logic (i.e. objectives tree; see Figure 10) was presented in a general way only in the Mid-Term Review. The links between the four audited intervention areas, their multiple specific objectives, underlying measures and their cross-impacts were not explained in any Commission document, although required under the Better Regulation framework.  

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41 Tool 16 “How to set objectives” of the Better Regulation Tool Box.
A prioritisation and sequencing of actions would have been important for the project from its very beginning, as both the Action Plan and the Mid-Term Review contained a large number of measures. The measures were not all of the same weight: some were preparatory, administrative or monitoring in nature, while others related to legislative proposals or other non-legislative measures, which were intended to be strategic in nature. The Commission did not set explicit priorities amongst the actions of the 2015 Action Plan. Instead, prioritisation was only implicit through the timing of the various actions, reflecting feasibility and need for preparatory work.
This was due to the fact that the Action Plan was prepared as a matter of urgency and thus there was no analysis upfront of whether any of the measures would have a stronger effect than others. Nine priority actions were introduced only in the 2017 Mid-Term Review. Our surveys and interviews revealed that the narrative of the CMU project was not fully clear and its visibility was limited to the specialised audience. Further, even the specific objectives for each area of intervention were vague and not measurable.

To support the CMU objectives, the Commission used general estimates in some cases (see Box 2).

**Box 2**

**An example of the securitisation estimate used in the CMU**

As regards securitisation, the Commission estimated the revival of the EU-28 securitisation market in 2015 at between €100-150 billion in order to rebuild issuances to the pre-crisis average. This estimate has not been reviewed by the Commission since then and was considered in April 2020 by market participants as inappropriate for the current needs of the EU-27 (e.g. in view of the anticipated impact of Basel III and the EU goal for sustainable finance). More specifically, they concluded that the EU-27 target alone should be set considerably higher, i.e. at a minimum level of €235-240 billion of new securitisations per year.

The CMU Action Plan did not necessarily list all actions that were ongoing or under reflection by the Commission and which matched the project objectives. An example is the ESAP (see paragraph 43).

The CMU measures could not realistically fulfil the high expectations raised by the Commission.

The launch of the CMU and the communication around this flagship project were perceived by market participants as a substantial commitment by the Commission to induce a significant positive impact. The communication on the project

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43 Ian Bell et al., Relaunching securitisation in the EU in the Eurofi, Regulatory Update, April 2020, pp. 20, 22-24.
raised expectations that were higher than it could realistically achieve with the measures it proposed and that are within its remit.

108 The Commission intended with its 2015 Action Plan to lay down the foundations for a well-functioning CMU by 2019. The EU companies’ reliance on bank finance and deficiencies in development of EU capital markets are a reflection of various structural factors, which cannot be alleviated or shifted by an action plan over a few years. In March 2019, the Commission nevertheless announced in its progress report that it delivered on its promise within the timeframe.

109 However, analysis from public bodies (International Monetary Fund, European Central Bank), private associations (Association for Financial Markets in Europe, European Banking Federation), industry-led initiatives (Market4Europe) and think tanks (Bruegel, Centre for European Policy Studies, Eurofi) provide an indication that the CMU is far from being completed and a lot of work still remains to be done. This indication is backed up by high-level market indicators, such as the European Central Bank’s financial integration indicators, the debt to bank lending ratio, or households’ composition of financial assets. In fact, these indicators have not moved much compared to the time before the launch of the CMU Action Plan.

110 The opinions among the respondents to our surveys are split whether the CMU Action Plan and its update were overambitious, not demanding enough, or well thought out and in line with its objectives. The respondents who criticised the CMU as overambitious primarily cited its complexity that negatively affected its feasibility. Second, they stated that the Commission underestimated the time required to get the CMU and Mid-Term Review measures approved by the co-legislators. As repeatedly mentioned by the stakeholders that we interviewed, the ambitions for the CMU should be high and driven by the Commission but at the same time, the project should be realistic and feasible enough to make progress.

111 The key actions and levers depend on other actors, in particular the co-legislators and Member States. As indicated above (e.g. paragraphs 85, 90 and 96), the support of Member States is crucial as regards areas that are of national competence. The Commission stated in the CMU Action Plan and the Mid-Term Review that it cannot build the CMU alone and that the success of the project depends also on the political will of the Member States and on the uptake by the industry.

112 In terms of legislative measures, the Commission focused on a rather limited legislative programme comprising 13 initiatives (see Annex VI). However, in several cases, the Commission had to significantly scale back its initial ambitions in order to
reach an agreement among the co-legislators, as for instance in the case of the review of the ESAs, or leave out of the CMU politically controversial issues such as the European safe asset.

In some other cases, even when the Commission tabled its legislative proposals for CMU measures largely on time, the legislative process lasted longer than expected (see paragraph 46). Similarly, the Commission’s proposal for a directive on a CCCTB, which is important to overcome the debt-equity bias, stalled in the Council (see paragraph 33). Overall, 12 (out of 13) legal measures have been adopted and entered into force by now, mostly towards the end of the CMU timeline. Only five of those entered into force are already fully or partially applied, while the remaining seven are to be gradually applied and will become effective by mid-2022, or even later (see Annex VI).

The majority of the non-legislative measures (i.e. expert studies, best practices, consultations) were useful for knowledge building and sharing as regards specific market segments and, in some cases, led to legislative proposals (e.g. crowdfunding, covered bonds). However, due to their preparatory and non-binding nature, they could not make real change. An example is the Commission’s Communication on the law applicable to the proprietary effects of transactions in securities, which did not significantly improve legal certainty compared to the status quo.

We audited if the Commission has put in place adequate arrangements for monitoring the implementation of the CMU overall. This includes the choice of indicators used to monitor CMU developments and the data used to report on them. Monitoring is necessary to allow policy makers and stakeholders to check if policy implementation is “on track” and to generate information that can be used to evaluate whether it has achieved its objectives. Monitoring can take place at different points in time (at the point of implementation, during or after policy implementation) and with varying frequency (annually, quarterly etc.).

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The Commission did not regularly monitor overall progress towards achieving the CMU objectives. Monitoring is necessary to allow policy makers and stakeholders to check if policy implementation is “on track” and to generate information that can be used to evaluate whether it has achieved its objectives. Monitoring can take place at different points in time (at the point of implementation, during or after policy implementation) and with varying frequency (annually, quarterly etc.).

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Annex VI
The Commission has so far used a number of tools (see Figure 11) to review and report on CMU actions as well as developments on capital markets. However, neither of the tools have been specifically dedicated to regularly monitor overall progress on the CMU’s seven areas of intervention.

Figure 11 – The Commission’s reporting on CMU

<table>
<thead>
<tr>
<th>Reporting on policy implementation</th>
<th>Reporting on CMU objectives</th>
<th>Internal monitoring of market developments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commission Communications 2016 and 2018</td>
<td>ECB Financial Integration Reports</td>
<td>Financial Markets Pulse</td>
</tr>
<tr>
<td>Mid-Term Review 2017</td>
<td>Economic Analysis accompanying the CMU Mid-Term Review 2017</td>
<td>Bond Markets Monthly</td>
</tr>
<tr>
<td>Status report 2019</td>
<td>Annual reporting on DG FISMA Strategic Plan 2016-2020</td>
<td></td>
</tr>
</tbody>
</table>

Source: ECA.

While the Commission started to assess capital market developments relevant to the seven areas of intervention of the CMU45 in the 2016 edition of the Economic and Financial Stability and Integration Review – a general-purpose publication first initiated in 2007 – it did not update this framework going forward. Furthermore, many of the key indicators of the 2016 EFSIR lacked baseline measures and target values.

45 The seventh area of intervention – “strengthening supervision” – was separated from the “facilitating cross-border investment” area in the 2017 Mid-Term Review.
The Commission’s main reason for not maintaining the monitoring system set up with the 2016 EFSIR was the nascent stage of the CMU, with many of the policy measures still in the process of being enacted, and the substantial time lag within which changes in financial structures become visible in quantitative statistics. However, these issues should not have precluded the Commission from setting up monitoring arrangements and developing them over time.

In 2020, i.e. five years after the start of the CMU and on the invitation of the Council, the Commission contracted a study with a view to developing a dashboard of key performance indicators for monitoring progress on the CMU. In line with the proposal, the contractor attempted to establish an evidence-based intervention logic. In this approach, the contractor sought to determine how changes in more immediate outcomes of CMU policy measures (e.g. costs of listing) affect the main CMU objectives (e.g. the relative share of non-financial corporations’ listed equity and debt financing relative to bank lending).

In its draft final report, the consultant suggested over 50 indicators on four areas for possible inclusion in the dashboard and recommended that the Commission give further thought to purpose, user group, structure and maintenance when designing its dashboard of KPIs. Meanwhile, the Commission has taken steps to develop additional indicators, for example on market integration, as the contractor’s work showed that many of the more immediate outcome indicators needed for the intervention logic are either not available or not suitable in the sense that they crossed one of the three red lines.

In order to report on indicators, suitable data is needed. We note that the data required to monitor progress on individual CMU policy measures was sometimes not available or not available in sufficient quality and granularity. This may also hinder prospects of trying to measure progress on CMU implementation overall. In particular, the lack of reliable information on the cross-border distribution of investment funds is a well-known data gap that was acknowledged by ESMA during the course of our audit.

The four areas are 1) Financing firms on public equity and debt markets, 2) Financing innovation, start-ups and non-listed companies, 3) Using capital markets to strengthen banking capacity, 4) Fostering retail participation.

Indicators were rejected if they crossed one of three "red lines": non-replicability, lack of geographical coverage and a lack of time series and cross-country variation.
In the set-up phase of the CMU, the Commission has tried to make the best of the situation by accumulating data from a number of sources, including from ESMA. For instance, while ESMA keeps information on the number of EuVECA and EuSEF registered funds, other data such as funds raised and investments made were acquired from non-Commission sources such as Invest Europe. Furthermore, ESMA largely relies on private sources (e.g. BAML) for its estimations of the non-STS securitisation market. The reliance on private data suppliers can be problematic, as assembling the data is time-consuming, often costly in monetary terms and the Commission may not be in a position to judge its quality.

The Commission has taken steps to include data clauses in relevant CMU legislation to ensure the information needed for monitoring and evaluation purposes – if not available and accessible through other sources - is being collected. For instance, new CMU legislation\(^{48}\) obliges ESMA from 2022 onwards to host an EU-wide register with data on cross border distribution for UCITS, AIFMD and other funds. The Commission has stressed that additional reporting requirements imposed on industry have to be carefully justified.

\(^{48}\) Article 12 (1) of Regulation (EU) 2019/1156.
Conclusions and recommendations

125 The EU has a predominantly loan-based financial system relying strongly on bank-based financing. The Commission made efforts to move towards more market-based financing and to supplement the Banking Union by a CMU. The main goals of the CMU were to foster the development and integration of EU capital markets and to increase alternative funding for SMEs. Our overall conclusion is that the Commission has made first steps towards this challenging goal, but the results are still to come.

126 Many of the measures that the Commission was able to take within its remit are small steps towards its objectives, but were not able to act as a catalyst for change in the EU so far. Although non-binding soft measures, such as reports or best practices contributed to knowledge-building on specific capital market segments, many of them had rather a limited impact due to their nature. A limitation the Commission also faced is that many of the key actions can only be undertaken by the Member States or with their full support.

127 The 2015 CMU Action Plan has been done in continuum with the previous plans, mainly taking up earlier ideas and including measures already in the pipeline or proposing calibration of the existing regulations (i.e. prospectus, EuVECA), in order to progress on specific segments of the capital markets. Many of the policy measures towards the objective of diversifying funding sources for SMEs were addressing issues too narrow to initiate and catalyse a structural shift towards more market funding in Europe (see paragraphs 20-39).

128 Despite the Commission’s efforts under the CMU Action Plan, its actions to overcome information barriers for the financing market for SMEs have had a very limited impact as regards facilitating the matching of market players’ interests. The Commission did not include a relevant project in the CMU Action Plan, ESAP, which was under discussion before the 2015 CMU Action Plan. As a result, information barriers on the demand and supply side still prevail (see paragraphs 40-43).

129 Regarding the challenge of bank financing, the Commission took initiatives to improve their capacity to provide credit to EU companies. While the STS initiative was a positive step, it has not yet produced the anticipated effect in the European securitisation market and facilitated the financing of SMEs. Securitisation transactions remain largely concentrated within traditional asset classes (i.e. mortgages, car loans) and in certain Member States (see paragraphs 44-50).
Recommendation 1 – Propose well-targeted actions to further facilitate SME access to capital markets

The Commission should provide:

(a) measures to increase the attractiveness of equity financing and public issuance for companies, in particular SMEs;

(b) measures to reduce the impact of the information asymmetry between suppliers and users of capital, in particular SMEs (e.g. by establishing the ESAP); and

(c) amendments to the legal framework to make SME securitisation issuance more attractive while duly considering the potential risks.

Timeframe: Q1 2022

The Commission had declared its ambition to promote the development of Member States’ capital markets, in particular in the countries with high catch-up potential. For this purpose, it used broader EU coordinating processes (European Semester) and financing tools, such as the SRSP, but not within a specific, comprehensive and clear EU strategy (see paragraphs 51-58).

The European Semester mostly identifies CMU-relevant challenges. However, in spite of the adoption of the CMU Action Plan in 2015 and the increasing relevance of the subject after Brexit, the Commission had not recommended to ten Member States with less developed capital markets that they implement directly relevant reforms (see paragraphs 59-65).

While the Commission provides technical support under the SRSP with a low level of financial and administrative burden to the Member States, this support is not embedded in a specific strategy. The demand-driven model of the technical support was not conducive in providing support to Member States corresponding to their needs. Moreover, multi-country projects are still the exception under the SRSP. Most projects were still ongoing or recently finished. Nevertheless, our sample showed mixed results in terms of scale and progress of reforms. Furthermore, in most cases, the initial timetable of implementation was not respected and the SRSS analysis did not properly reflect the implementation risks (see paragraphs 66-78).
Recommendation 2 – Foster deeper and better integrated local capital markets

The Commission should:

(a) develop a comprehensive strategy to address the needs of local capital markets;
(b) issue CSRs for Member States that need to progress in market-based financing; and
(c) enhance the current demand-driven model of the technical support to reach those Member States with the highest needs, while focusing on results.

Timeframe: Q4 2022

133 Many of the barriers impeding cross-border capital flows have remained unresolved for decades. The Commission identified that such barriers often emanate from national laws, including in the fields of insolvency law and withholding tax or from a lack of financial education. Accordingly and based on a request from the Council, it devised a roadmap jointly with Member States for addressing them, which meant that only barriers that Member States were willing to tackle were included (see paragraphs 79-81).

134 The Expert Group on overcoming national barriers to capital flows recommended in 2018 that Member States measure financial literacy rates and implement financial education programmes in line with OECD principles. The Commission has not yet stated if and how it will support Member States in their efforts, for example, by reviewing relevant EU funding programmes with a view to better fostering financial literacy of consumers, investors and SMEs across Europe (see paragraphs 82-86).

135 The Commission’s actions on the issue of insolvency have the potential to clarify ownership rights, facilitate early restructuring and give entrepreneurs a second chance. However, they are unlikely to lead to a convergence of insolvency proceedings. As substantive insolvency law remains in the sole competence of Member States, the Commission has little leeway to move ahead without their support (see paragraphs 87-92).

136 The Commission’s Code of Conduct on Withholding Taxes proposes best practices to tackle burdensome relief and reclaim procedures. However, it relies on voluntary commitments from Member States and a more binding approximation of
national practices based on the recommendations of the Code require unanimity in the Council. Previous attempts to reform withholding tax procedures on this basis have not been successful (see paragraphs 93-99).

**Recommendation 3 – Address key cross-border barriers to investment**

The Commission should:

(a) assess how it can better promote financial literacy, including among SMEs, and support Member States’ efforts in this area;

(b) assess scope for convergence or harmonisation of elements of national insolvency proceedings such as the criteria for opening insolvency proceedings, the hierarchy for ranking claims, the order of priorities and avoidance actions, and promote concomitant reforms; and

(c) depending on the outcome of an impact assessment, propose to the Council a Directive on a system of withholding tax relief at source.

**Timeframe: Q4 2022**

137 The Commission’s CMU objectives were in many cases vague. The priorities were set only late in the process. The Commission’s communication around this project raised expectations that were higher than what it could achieve with its own actions. In some cases, the co-legislators significantly scaled back the ambition of the Commission’s initial proposals or the proposals stalled in the Council due to lack of consent (see paragraphs 100-114).

138 The Commission’s monitoring was limited to progress with legislative measures, it has not regularly and consistently monitored if it is progressing in accomplishing the main CMU objectives. Furthermore, it is currently unable to assess to what extent its policy actions – both legislative and non-legislative measures – are contributing to progress on CMU objectives. Further, assembling the data required to monitor progress on CMU objectives is time-consuming, often costly in monetary terms and the Commission may not be in a position to judge its quality. Not all data is readily available in sufficient quality and detail. These shortcomings are particularly detrimental in view of the release of the second CMU action plan in September 2020 (see paragraphs 115-119).
Five years after the start of CMU, the Commission has taken steps to develop a dashboard of indicators. A dashboard can be used to assess the success of CMU as a whole. It should be rooted in an evidence-based intervention logic and be based on the selection of suitable indicators. Data to compile indicators should be made available, keeping in mind the need to keep reporting burdens on industry to a necessary minimum (see paragraphs 120-124).

Recommendation 4 – Develop specific objectives, critical measures and the monitoring of the CMU

The Commission should:

(a) define specific objectives and address the critical measures which are effective for achieving the CMU objectives early on;

(b) regularly monitor and report on progress towards achieving the CMU objectives; and

(c) select indicators that are suitable and based on reliable, timely and available data.

Timeframe: Q4 2021

This Report was adopted by Chamber IV, headed by Mr Alex Brenninkmeijer, Member of the Court of Auditors, in Luxembourg on 20 October 2020.

For the Court of Auditors

Klaus-Heiner Lehne
President
## Annexes

### Annex I – Overview of the audited CMU-relevant SRSP projects, 2017-2018

<table>
<thead>
<tr>
<th>Member State</th>
<th>SRSS ID</th>
<th>SRSP Project</th>
<th>Main output as of March 2020</th>
<th>Budget in EUR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bulgaria</td>
<td>SRSP2017/445</td>
<td>Development of a single entry point for disclosure and distribution of information by market participants ('single entry point')</td>
<td>Single entry point system ‘blueprint’ technical specifications and operational plan (21 February 2020)</td>
<td>425 000</td>
</tr>
<tr>
<td>Czechia</td>
<td>SRSP2017/360</td>
<td>Analysis of Czech business angels and promotion of business angels</td>
<td>Study capturing the status quo of angel investment activities in the country (16 October 2018)</td>
<td>70 000</td>
</tr>
<tr>
<td>Estonia</td>
<td>SRSP2017/344</td>
<td>Capital market diagnostic</td>
<td>Diagnostic report on the Estonian capital market (15 February 2019)</td>
<td>100 000</td>
</tr>
<tr>
<td>Lithuania</td>
<td>SRSP2017/444</td>
<td>Improvement of investment environment for institutional investors</td>
<td>Diagnostic study (July 2018) and presentation (September 2018)</td>
<td>150 000</td>
</tr>
<tr>
<td>Poland</td>
<td>SRSP2017/42</td>
<td>Drawing up a strategy for capital market development</td>
<td>Capital Markets Development Strategy for Poland (adopted on 1 October 2019)</td>
<td>150 000</td>
</tr>
<tr>
<td>Lithuania</td>
<td>SRSP2018/31</td>
<td>SME Equity Support Instrument</td>
<td>Draft legislation and implementation plan including operational changes (7 August 2019)</td>
<td>65 000</td>
</tr>
</tbody>
</table>

*NB. The beneficiary in all cases was the national Ministry of Finance or similar (Italy: Ministry of Economy and Finance; Romania: Ministry of Public Finance).*  

*Source: ECA based on SRSS.*
### Annex II – The Commission’s 2015 Action Plan on CMU and its predecessors – selected actions focused on access to finance

<table>
<thead>
<tr>
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<tbody>
<tr>
<td>Prospectus – one passport procedures for large companies and SMEs</td>
<td>Amendment of the Prospectus Directive for a proportional disclosure regime for SMEs</td>
<td>EU Prospectus Regulation (in force as of July 2019)</td>
</tr>
<tr>
<td>Detailed examination of costs to firms of raising debt and equity finance across Europe</td>
<td>SME growth markets label in MiFID</td>
<td>SME growth markets regulation amending MAR</td>
</tr>
<tr>
<td>Venture Capital funds: Community legislation covering specific closed end funds</td>
<td>First legislative proposal of EuVECA/EuSEF Regulation (not adopted)</td>
<td>EuVECA/EuSEF Regulation review (adopted and in force since 2018)</td>
</tr>
<tr>
<td>Taxation of Venture Capital funds – Clarification of tax Environment</td>
<td>Examination of tax obstacles to cross-border venture capital investment</td>
<td>Study on tax incentives for venture capital and business angels</td>
</tr>
<tr>
<td>Examine taxation of debt equity</td>
<td>No action</td>
<td>Legislative proposal on the Common Consolidated Corporate Tax Base addressing debt-equity bias</td>
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<tr>
<td>No action</td>
<td>Single access point to regulated information at EU level</td>
<td>Investigate how to develop pan-European information systems</td>
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<tr>
<td>No action</td>
<td>Equity funding for SMES: Equity financial instrument under COSME and Horizon 2020 – Funds-of-Funds; EIB/EIF securitisation of portfolio of SME debt</td>
<td>Pan-European Venture Capital Funds-of-Funds programme, Venture EU under EIB/EIF</td>
</tr>
<tr>
<td>No action</td>
<td>Reinforce the Enterprise Europe Network to provide SMEs with better information</td>
<td>European high-level principles on feedback to be given by banks to SMEs with declined credit applications</td>
</tr>
<tr>
<td>No action</td>
<td>Review of SME lending market, incl. transparency mechanism</td>
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</table>

*Source: ECA.*
Annex III – CMU action for the development of local capital markets

Box 3: Commission’s deliverable on local and regional capital markets

**Priority action No 9 under the Mid-Term Review:** “By Q2 2018, the Commission will propose a comprehensive EU strategy on steps that can be taken at EU level to support local and regional capital market development across the EU. This will build on the report of the Vienna Initiative’s CMU Working Group and will take account of experience through the growing delivery of on-demand technical support under the Commission’s SRSP.”

On top of its late publication (March 2019) compared to the CMU Action Plan (September 2015), the Commission’s deliverable inter alia:

- Does not constitute a strategy per se, i.e. a detailed, long-range plan but rather an indicative, non-exhaustive list of available policy responses;\(^\text{49}\);
- Does not identify the specific needs of Member States’ capital markets based on a prior analysis of the status quo at national level;\(^\text{50}\);
- Does not comprehensively cover all capital market segments and available topics or options;
- Does not prioritise the reform areas with the greatest potential to improve the local capital markets and does not provide guidance about sequencing (implementation steps);
- Does not analyse the potential impact of the measures nor highlight the potentially high fiscal cost of particular options (see, for instance, the use of investment saving accounts in Sweden);\(^\text{51}\);
- Does not offer best practices implemented at a more global level (for instance in countries with advanced financial markets such as the US, Canada, Japan, Switzerland, Australia, or Singapore) but only within the EU;

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\(^{49}\) “To inspire and motivate public and private market players to further grow and integrate capital markets in their respective Member States and regions”.

\(^{50}\) It makes only a general reference to the finding of the 2018 EFSIR that the CESEE countries account for 8% of the EU’s GDP, but only 3% of the EU’s capital market.

\(^{51}\) A 2018 audit of the Swedish NAO found that these accounts might have cost almost €4 billion (SEK 42 billion) in forgone tax revenue.
- Does not reflect on major exogenous factors (e.g. Brexit, monetary policy, economic cycle);
- Lacks provisions about its own review or evaluation after a certain period that could pinpoint the remaining gaps and how to create the required solutions;
- Lacks a specific EU budget for the purposes of the CMU and the development of local and regional capital markets in addition to the already existing EU-funded financial instruments as well as the SRSP that are however out of DG FISMA control despite having the most relevant mandate for the CMU.

Source: ECA.
Annex IV – Overview of direct CSRs issued to all Member States, 2014-2019

<table>
<thead>
<tr>
<th>Before the CMU</th>
<th>After the adoption of the CMU Action Plan (September 2015)</th>
<th>MS</th>
<th>Programme</th>
<th>Programme</th>
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<tr>
<td>Belgium</td>
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<td>Greece</td>
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<td>Slovakia</td>
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<tr>
<td>Finland</td>
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</tr>
<tr>
<td>Luxembourg</td>
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<tr>
<td>Latvia</td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Lithuania</td>
<td>x</td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Hungary</td>
<td>x</td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Malta</td>
<td>x</td>
<td>x</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Netherlands</td>
<td>x</td>
<td>x</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>England</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>10 out of 26</td>
<td>7 out of 26</td>
<td>MS with</td>
<td>6 out of 27</td>
<td>6 out of 27</td>
<td>7 out of 27</td>
<td>4 out of 28</td>
</tr>
<tr>
<td>38 %</td>
<td>27 %</td>
<td>CMU-relevant CSR</td>
<td>22 %</td>
<td>22 %</td>
<td>26 %</td>
<td>14 %</td>
</tr>
<tr>
<td>157</td>
<td>102</td>
<td>Total CSRs</td>
<td>89</td>
<td>78</td>
<td>73</td>
<td>97</td>
</tr>
</tbody>
</table>

Source: ECA based on CESAR database; European Parliament’s EGOV Briefing, CSRs: An overview, September 2019.
## Annex V – Overview of direct and broader CSRs issued to less developed Member States, 2016-2019

<table>
<thead>
<tr>
<th>Rank</th>
<th>MS</th>
<th>Direct CSRs</th>
<th>Broader CSRs</th>
</tr>
</thead>
<tbody>
<tr>
<td>28</td>
<td>Lithuania</td>
<td>Access to finance (2016)</td>
<td>NONE</td>
</tr>
<tr>
<td>27</td>
<td>Romania</td>
<td>NONE</td>
<td></td>
</tr>
<tr>
<td>26</td>
<td>Slovenia</td>
<td>Access to finance (2016-2019)</td>
<td>NONE</td>
</tr>
<tr>
<td>25</td>
<td>Slovakia</td>
<td>NONE</td>
<td>Justice (2017)</td>
</tr>
<tr>
<td>23</td>
<td>Latvia</td>
<td>NONE</td>
<td>Insolvency (2016)</td>
</tr>
<tr>
<td>22</td>
<td>Estonia</td>
<td>NONE</td>
<td></td>
</tr>
<tr>
<td>21</td>
<td>Hungary</td>
<td>NONE</td>
<td></td>
</tr>
<tr>
<td>20</td>
<td>Croatia</td>
<td>NONE</td>
<td>Insolvency (2017)</td>
</tr>
<tr>
<td>19</td>
<td>Greece</td>
<td>NONE</td>
<td>Insolvency (2019)</td>
</tr>
<tr>
<td>18</td>
<td>Poland</td>
<td>NONE</td>
<td></td>
</tr>
<tr>
<td>17</td>
<td>Czechia</td>
<td>NONE</td>
<td></td>
</tr>
<tr>
<td>15</td>
<td>Austria</td>
<td>Access to finance (2017-2019)</td>
<td>NONE</td>
</tr>
</tbody>
</table>

**NB.** (1) The ranking is based on the depth of local capital markets by Asimakopoulos and Wright, A new sense of urgency: The future of Capital Markets Union, New Financial, November 2019; (2) As ‘direct CSRs’, we considered the Commission’s internal taxonomy, mainly ‘access to finance’ and ‘reduce the debt-bias’. In order to avoid a ‘CMU over-labelling’, we classified the recommendations addressing issues also targeting the banking sector as ‘broader CSRs’, for example insolvency regimes, supervision of the financial sector and sale of non-performing loans; (3) Due to the economic adjustment programmes until 2018, Greece received CSRs only in 2019.

**Source:** ECA based on the Commission’s CESAR database.
## Annex VI – Overview of CMU legislative measures as of July 2020

<table>
<thead>
<tr>
<th>Measure</th>
<th>Deadline</th>
<th>COM</th>
<th>EP</th>
<th>Council</th>
<th>Adoption</th>
<th>Application as from</th>
</tr>
</thead>
<tbody>
<tr>
<td>EuVECA/ EuSEF review</td>
<td>Q3 2016</td>
<td>July 2016</td>
<td></td>
<td></td>
<td>October 2017</td>
<td>March 2018</td>
</tr>
<tr>
<td>Prospectus Regulation (review)</td>
<td>Q4 2015</td>
<td>November 2015</td>
<td></td>
<td></td>
<td>June 2017</td>
<td>July 2019</td>
</tr>
<tr>
<td>STS securitisation Regulation</td>
<td>Q3 2015</td>
<td>September 2015</td>
<td></td>
<td></td>
<td>December 2017</td>
<td>January 2019</td>
</tr>
<tr>
<td>Pan-European Personal Pension Product (PEPP)</td>
<td>Q2 2017</td>
<td>June 2017</td>
<td></td>
<td></td>
<td>June 2019</td>
<td>12 months after publication of delegated acts</td>
</tr>
<tr>
<td>European Supervisory Authorities review, including AML rules</td>
<td>Q3 2017</td>
<td>Adopted on 20.9.2017</td>
<td>Negotiating mandate obtained in December 2018</td>
<td>Negotiating mandate obtained in February 2019</td>
<td>December 2019</td>
<td>January 2020 and January 2022</td>
</tr>
<tr>
<td>Crowdfunding</td>
<td>Q4 2017 (IA) Q1 2018</td>
<td>Adopted on 08.3.2018</td>
<td>Negotiating mandate obtained in November 2018</td>
<td>Negotiating mandate obtained in June 2019</td>
<td>Q4 2020</td>
<td>Q4 2021</td>
</tr>
<tr>
<td>Covered bonds</td>
<td>Q1 2018</td>
<td>Adopted on 12.3.2018</td>
<td></td>
<td></td>
<td>November 2019</td>
<td>July 2022</td>
</tr>
<tr>
<td>Cross-border distribution of investment funds</td>
<td>Q1 2018 (IA) Q2 2018</td>
<td>Adopted on 12.3.2018</td>
<td></td>
<td></td>
<td>June 2019</td>
<td>August 2021</td>
</tr>
<tr>
<td>Measure</td>
<td>Deadline</td>
<td>COM</td>
<td>EP</td>
<td>Council</td>
<td>Adoption</td>
<td>Application as from</td>
</tr>
<tr>
<td>------------------------------------------------------------------------</td>
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<td>--------------------</td>
<td>--------------------------------</td>
</tr>
<tr>
<td>Rules to give SMEs easier access to growth markets</td>
<td>Q2 2018 (IA) Q3 2018</td>
<td>Adopted on 24.5.2018</td>
<td></td>
<td></td>
<td>November 2019</td>
<td>December 2019 or January 2021</td>
</tr>
<tr>
<td>Preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures (DG JUST)</td>
<td>Q4 2016</td>
<td>Adopted on 22.11.2016</td>
<td></td>
<td></td>
<td>June 2019</td>
<td>July 2021, July 2024 and July 2026</td>
</tr>
<tr>
<td>Law applicable to third party effects of transactions in claims (DG JUST)</td>
<td>Q4 2017</td>
<td>Adopted on 12.3.2018</td>
<td>Negotiating mandate obtained in February 2019</td>
<td>Not agreed yet</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: ECA based on the European Commission.
Acronyms and abbreviations

**AIF:** Alternative Investment Fund

**AIFMD:** Alternative Investment Fund Manager Directive

**BAML:** Bank of America Merrill Lynch

**CCCTB:** Common Consolidated Corporate Tax Base

**CMU:** Capital Markets Union

**CSR:** Country Specific Recommendation

**EFAMA:** European Fund and Asset Management Association

**ESAP:** European Single Access Point

**ESMA:** European Securities and Markets Authority

**EuSEF:** European social entrepreneurship fund

**EuVECA:** European venture capital fund

**IPO:** Initial public offering

**SME:** Small and medium-sized enterprise

**SRSP:** Structural Reform Support Programme

**SRSS:** Structural Reform Support Service (now DG REFORM)

**STS securitisation:** “Simple, Transparent, and Standardised” securitisation

**UCITS:** Undertaking for Collective Investment in Transferable Securities
Glossary

Alternative Investment Funds (AIFs): All investment funds that are not covered by the EU Directive on UCITS and instead fall under the Alternative Investment Fund Manager Directive (AIFMD). This includes hedge funds, venture capital, private equity funds and real estate funds.

CMU Working Group: Platform formed under the Vienna Initiative to support the exchange of information on financial trends in central, eastern and southeastern Europe and thus develop local capital markets, comprising representatives from the public and private sectors in the countries concerned and from international institutions, with the Commission as coordinator.

Common Consolidated Corporate Tax Base (CCCTB): A single set of rules for calculating companies’ taxable profits in the EU.

Covered bond: Type of secured bond issued by a bank or other credit institution, that is usually backed by mortgages or public-sector loans.

Debt-equity bias: Economic distortion caused by the fact that interest payments on debt are tax-deductible in most corporate income tax systems, but dividend payments for equity financing are not.

Deep capital market: A market in which securities are traded at a high volume, with only a small difference between buying and selling prices.

European Semester: Annual cycle which provides a framework for coordinating the economic policies of EU Member States and monitoring progress.

European Single Access Point: A planned EU web portal for fast and easy access to listed companies’ statutory information.

European Social Entrepreneurship Fund (EuSEF) Regulation: A regulation providing the basis for a voluntary EU-wide passport for qualifying alternative investment schemes that focus on social enterprises.

European Venture Capital Fund (EuVECA) Regulation: A regulation providing the basis for a voluntary EU-wide passport for qualifying venture capital funds and fund management companies.

Fund of funds: A pooled investment fund that invests in other funds rather than investing directly in securities.
Initial public offering: The first sale of a company's shares to the public.

Market depth: Indicator of the volume of trading in a market.


Multilateral trading facility: A self-regulating facility for trading financial instruments, which provides an alternative to traditional stock exchanges and, unlike these, can be operated not only by an authorised market operator, but also by an investment company.

Relief at source: A form of tax relief applied at the moment tax is deducted at source.

Securitisation: The practice of pooling various types of illiquid financial assets such as mortgages, loans and leases, and selling them to investors as liquid marketable securities such as bonds.

SME growth market: A type of multilateral trading facility for shares issued during the previous three years by companies with an average market capitalisation of less than €200 million.

Structural Reform Support Programme (SRSP): EU programme that provides tailor-made support for Member States' institutional, administrative and growth-enhancing reforms, without the need for national co-financing.

Undertaking for Collective Investment in Transferable Securities (UCITS): An investment vehicle that pools investors’ capital and invests it collectively through a portfolio of financial instruments such as stocks, bonds and other securities. UCITSs, which are covered by an EU Directive, can be distributed publicly to retail investors across the EU based on a single authorisation from one Member State.

Unicorn company: A privately held start-up with a value of over $1 billion, so called due to the rarity of such ventures.

Venture capital fund: An investment fund that manages money from professional investors seeking to invest in SMEs with strong growth potential.

Vienna Initiative: Forum established in January 2009 that brought together all the main public and private stakeholders in the EU banking sector to help emerging European economies weather the global economic crisis.
REPLIES OF THE EUROPEAN COMMISSION TO THE EUROPEAN COURT OF AUDITORS SPECIAL REPORT

“CAPITAL MARKETS UNION – SLOW START TOWARDS AN AMBITIOUS GOAL”

EXECUTIVE SUMMARY

I. Common Commission reply to paragraphs I-III.

Efforts to put in place a genuine single market for capital started with the Treaty of Rome more than fifty years ago and intensified with the free movement of capital freedom enshrined in the Maastricht Treaty (1992) and the Financial Service Action Plan (1999). This ultimate objective has not yet been achieved largely because difference in legal traditions and practises across the EU Member States have prevented establishing a fully harmonised legal framework in the EU for governing financial activity. The only way forward is step-by-step, in all areas where barriers to free movement of capital still exist, whilst keeping in mind the global vision and overall objectives. Building Capital Markets Union (CMU) is therefore a gradual process, based on delivering many detailed, but important changes.

IV. Common Commission reply to paragraphs IV-VII.

The Commission delivered all the actions announced in the 2015 CMU Action Plan and the 2017 Mid-term Review. The European Parliament and the Member States have agreed on 12 out of 13 CMU legislative proposals although not all of them have maintained the level of ambition proposed by the Commission. The Commission considers the effectiveness of CMU will be measured by the effectiveness of the actions undertaken. As hardly any of the recently adopted legislative proposals have been in application for sufficient time, and some of them have not started to apply yet, it is difficult to assess as of yet their effectiveness in accomplishing their narrow goals as well as their contribution to the specific CMU objectives. Catalysing progress towards CMU requires support from the European Parliament and Member States at the highest level and from technical experts in public administration. It also requires that market participants make good use of these measures. The EU can offer tools and put in place supporting conditions, but it is for national authorities to implement them on the ground, and for private actors to take the initiative, seize business opportunities and innovate.

VIII. The Commission concurs with the ECA that the CMU objectives were broad. Since building the CMU is a gradual process, based on making many detailed and often technical changes, it was deemed important to establish sufficiently general and comprehensible objectives in order not to lose sight of the global CMU vision.

IX. While the Commission accepts the general direction of all recommendations, some of them are fully accepted, others partially accepted. The Commission did not accept only one sub-recommendation. See Commission replies to recommendations 1, 2, 3 and 4.

INTRODUCTION

08. The 2015 Action plan aimed to overcome the fragmentation of capital markets along national lines. The Commission agrees with the ECA to the extent that that fragmentation of legislation refers to differences in national legislation.
09. The Commission agrees with the ECA that work on CMU needs to continue. It carefully considered the report of the High Level Forum on CMU and the feedback received thereon. The work continues with the 2020 Action Plan, in which it presents measures, most of which of legislative nature, that will further transform the EU financial system and contribute to completing CMU.

12. The Commission notes that the European Central Bank has played a very important and supportive role in the CMU project.

OBSERVATIONS


SME funding remains an important concern. The measures that target SME funding under the 2015 Action Plan and the 2017 Mid-term review have been agreed with co-legislators and are implemented. The Commission is confident that the concrete effects will materialise over time. While there is not yet evidence that the measures had a significant impact on SMEs funding behaviour, it is notable that the Survey on Access to Finance showed that the SME financing gap disappeared in early 2019 in 10 of the 11 Member States that contribute to the survey.

The economic impact of Covid-19 has however reversed the positive trend of declining financing gaps, which underscores companies of all sizes, and in particular SMEs, need solid market-based funding sources. The Capital Market Recovery Package of July 2020 already proposed targeted amendments to the prospectus regime and Markets in Financial Instruments Directive II (MiFID II) that will facilitate the market funding of firms. As further part of this package, the Commission proposed targeted amendments to securitisation rules to strengthen banks’ capacity to lend to SMEs. The Commission has proposed further measures to this end as part of its second CMU Action Plan.


Better access to market funding, notably equity, will enable companies to innovate, reap the benefits of new technologies and avoid that, in search of capital, innovative start-ups or scale-ups decide to relocate outside the EU or scale down their ambition, greatly harming the EU’s future growth potential and productivity. Past measures under the CMU have not been a game changer in this regard. Progress was nevertheless notable. European intervention in the pre-initial public offering (IPO) phase, particularly in the venture capital (VC) field, has been successful in attracting private institutional investors into VC funds, thanks to the catalytic effect of European Investment Fund (EIF)-backed intervention and other EU initiatives. While in the immediate aftermath of the 2008-2009 crisis public/government support to VCs in Europe was higher than 35%, the percentage has declined to 20% in 2019 while private support has increased. Also, the average size of VC funds in EU has progressively increased over the years since the financial crisis. The COVID-19 crisis severely altered the EU’s economic landscape and there is therefore a need for renewed ambition to support the financing of smaller companies and innovative scale-ups.

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4 COM(2020) 590.
34. To address the urgency of access to market funding caused by the consequences of the Covid-19 pandemic, the Commission has adopted legislative proposals in the “Capital Market Recovery Package”. One of such measures is the introduction of a time-limited ‘EU Recovery prospectus’. This new prospectus will be available for secondary issuances of shares of companies listed on a regulated market or an SME Growth market.

36. The Prospectus Regulation introduced a new type of prospectus – the EU Growth prospectus – that contains alleviated disclosures requirements targeted to SMEs and mid-caps. These are lighter than for a full prospectus and are expected to decrease costs and burdens for SMEs while maintaining the confidence of investors to invest in small companies. Since the Prospectus Regulation has been in application only for one year, there are not yet sufficient data to assess whether this prospectus has achieved its objectives. Notwithstanding this, and building on the measures already taken, the Commission will seek to simplify the listing rules for public markets.

37. The possibility for Member States to set different thresholds depends on the different size of capital markets throughout the EU. However, such exemption is only available for offers of securities to the public that do not require passport to other Member States and the exemption does not apply to the admission of securities to trading on a regulated market.

38. To support the recovery following the COVID-19 crisis, and building on work carried out under the SME strategy, the Commission is currently working on creating an SME IPO fund to make it easier for small and high-growth companies, in particular in sectors of strategic importance to the EU, to raise capital and finance their growth.

39. In particular, as regards the prospectus, the regulation on SME Growth Markets has introduced the ‘transfer prospectus’ to facilitate the transition from an SME growth market to a regulated market: under certain conditions, issuers whose securities have been admitted to trading on an SME Growth market for at least two years are allowed to draw up a simplified prospectus for secondary issuances to seek admission to trading on a regulated market.


The right balance between providing relevant information about investment opportunities to investors and minimising the burden for companies to report this information is key to facilitate access to market funding. To make companies more visible to cross-border investors, the Commission will tackle the lack of accessible and comparable company data for investors. It also aims at targeted simplification of existing listing rules to reduce compliance costs for SMEs.

57. Common Commission reply to paragraphs 57 and 58.

In March 2019, the Commission presented its views on local capital markets developments in the “Communication on Capital Market Union: Progress on building a single market for capital for a strong economic and monetary union” and in the accompanying Staff Working Document. Admittedly, these do not establish a detailed action plan. They communicated the strategic vision, namely that local capital markets are important. This was not obvious at the time. Furthermore, the

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directions were outlined on three levels, namely national, regional and European with at each level actions to undertake.


The EU semester is an important means to coordinate Member States’ economic policy and since boosting investment is among its goals, the Commission gives solid consideration to the role of structural reforms towards better local capital markets in supporting this goal. Given that the Commission can issue only a limited number of country-specific recommendations to a Member State, trade-offs are unavoidable and choices have to be made between the policy domains that can be covered by a recommendation to a given Member State. In this context, the Commission stresses that the ranking of priorities at country level is an equally important criterion to determine the choice of recommendations as the cross-country consistency within a policy field.

60. The Commission considers that the most important issues were tackled in the Country Reports taking into account the format, the conditions and the need for setting priorities under which the assessments had to be produced.

The Commission acknowledges that there are currently a few statistical indicators on domestic capital markets, which could be further extended.

62. The European Semester framework is used to identify reform and investment needs in each Member State. Its recommendations focus on deficiencies that deserve the most attention to support growth and jobs in given Member State. Its role is thus not to focus on every area in which a Member State underperforms the EU average, but prioritise a limited number of policy recommendations that will benefit a given economy, in the light of overall priorities set each year in an Annual Sustainable Growth Strategy. Such streamlined approach has been welcomed by Member States, as focusing on a well-defined limited number of priorities helps better targeting the government’s action and increases ownership of the process by the Member States.

63. At the beginning of each Semester cycle, the Annual Sustainable Growth Strategy clearly sets the priorities of the upcoming policy coordination cycle. In addition, the Euro Area Recommendation adopted each year prior to the adoption of CSRs sets the priority policy recommendations for Euro Area Member States, providing guidance for their CSRs. With regard to the prioritisation of reforms, the recommendations proposed by the Commission reflect its assessment of the priority actions to be undertaken.

64. The fact that a CSR contains various issues reflects the reality that tackling a specific socio-economic challenge requires policy action in different areas. Prescribing a timeframe is also not considered practical, as the Commission is aware that reforms may need to be carried out in different stages over time. What could be envisaged is a more detailed qualitative assessment of the implementation efforts of a Member State. This is already recognised when the Commission assesses implementation and applies different assessment categories e.g. limited progress, some progress, etc.

65. The Commission notes that not every recommendation can be fully or substantially implemented within its lifespan (13 to 16 months). Moreover, it takes time before the result of undertaken reform steps manifests in real economy.

The Commission agrees that the level of implementation of CSRs could be higher. To this end, the Commission proposed the Technical Support Instrument, a stand-alone regulation, which is the continuation of the existing Structural Reform Support Programme (SRSP) in the upcoming Multiannual Financial Framework.
In addition, the Commission proposed a new Recovery and Resilience Facility (RRF). The RRF incentivises Member States’ reform and investment efforts, in line with the priorities identified in Country-Specific Recommendations and green and digital goals by offering substantial financial support.

70. Common Commission reply to paragraphs 70-71 and Figure 7.

The Commission points out that divergences in the number of projects approved and implemented for the countries with less developed capital markets is the result of the technical support that can only be provided based on the demand from Member States, and a competitive selection based on the project quality, expected impact and available budget.10

77. Common Commission reply to paragraphs 77 and 78.

The Commission points out that in the assessment of the technical support, due consideration should be given to the fact that the Commission provides the expertise to the Member States and that the latter is a condition necessary, but not sufficient for Member States to implement a reform, particularly in the case of strategic and political reforms. For this reason, a strong ownership of the support measures and the reform agenda by the Member States is of key importance during the whole reform process.

Such ownership is evidenced when Member States adapt technical recommendations to the specific administrative and political context.

It is important to remind that the outcomes of the technical support projects are to be understood as the changes induced, such as adoption of a strategy, adoption of a new law /act or modification of an existing one, adoption of (new) procedures and actions to enhance the implementation of reforms in the beneficiary structures or organisations.

In practice, technical support projects focusing on implementation of reforms may be much easier to be ‘fully’ implemented by the Member States, as compared to projects focusing on the design of reforms. For such projects, the implementation time may also be much longer and possibly proceed in stages, as evidenced by some of the projects in the scope of this audit.


Fostering financial integration has been and will be a main objective of the CMU. The Commission proposed six legislative measures to introduce new EU wide rules for products, labels and passport. Five of them11 are in the process of implementation after adoption by co-legislators and adoption of the sixth is forthcoming12. Moreover, the new rules on restructuring13 lead to more legal certainty for cross-border investors and the good progress on European financial supervision fosters further supervisory convergence. While it is still too early to assess their effectiveness and their contribution to financial integration in the EU, the Commission acknowledges that further progress is needed.

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With the 2020 CMU Action Plan\textsuperscript{14}, the Commission aims to continue to tackle the key obstacles to market integration. Some of these measures extend beyond the EU financial legislation and seek to address barriers related to a broader legal setting or barriers driven by long-established national preferences or practices. This is in particular the case in the area of taxation and non-bank insolvency. In these areas, the Commission proposes targeted actions, focusing on the most important barriers that cause market fragmentation and deter cross-border investment.

86. The Enterprise Europe Network’s financial literacy services support SMEs with international growth and innovation by making them aware of:

- Suitable types of finance and EU funding, advantages and pitfalls, and what SMEs need to do to prepare,
- Financial rights (in particular, late payment).

The volume of financial literacy services that Enterprise Europe Network members can provide is constrained by their contractual obligation to deliver all types of EEN services in a balanced way (advice on access to finance and a wide range of other topics).

93. The Commission would like to point out that burdensome WHT refund procedures are a barrier for the free movement of capital constituting a hurdle for cross-border investments.

The Commission remains committed to address this issue, see also Commission reply to paragraph 95.

94. The Commission would like to clarify that the Code of Conduct on WHT is a non-binding instrument. It calls for voluntary commitment of the Member States in aligning their practices to the recommendations included in the Code in the direction of simplifying the WHT procedures. Its main goal is to make WHT refund procedures more efficient (digitalized, swift payments and procedures, etc.), although it also covers the possibility of implementing a standardised and harmonised system for providing tax relief at source.

95. The Commission has been active in promoting simpler withholding tax procedures within the EU for a long time. In this sense, it is also worthy to highlight the Recommendation on WHT relief procedures published in 2009\textsuperscript{15}. The work conducted for example through the Code of Conduct has been a way to address the problem while also getting additional feedback and input on the impact of this problem on the internal market. The Commission has also recently committed to put forward an initiative to introduce a common, standardized, EU-wide relief at source system.

96. The President of the European Commission has made clear that the Commission is willing to explore the application of qualified majority voting principle to tax matters. See also the Commission reply to paragraph 95.

98. The Commission would like to clarify the following: the May 2020 Tadeus Deputies meeting concluded indeed that to prevent tax procedures-related barriers from hampering cross-border investment, the Commission will organise a dedicated work stream to explore legislative and non-legislative initiatives on how to address the current challenges on WHT procedures (such as a potential relief at source system). It highlighted that further work should build in any case on previous work done at EU and international level (Code of Conduct, etc.).

\textsuperscript{14} COM(2020) 590.

\textsuperscript{15} https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32009H0784&from=EN
The Commission is committed to apply the Better Regulation Agenda in order to enable an effective delivery of the next phase of CMU. Since the CMU is about enabling activity that either does not exist or is at a nascent stage, data quality and data availability tends to be limited and does neither allow predictions on how market participants would adjust nor to estimate how markets would develop with reasonable accuracy. The policy approach has been therefore to identify the reasons why an activity has not taken place or has remained underdeveloped, to relate those reasons to market failures or obstacles, and then to design policy measures that are apt to address those failures and obstacles, whilst preserving other important objectives such as financial stability or market integrity.

The Commission acknowledges that some policy objectives were formulated in rather broad terms and that it is therefore difficult to determine with precision to what extent some of those objectives were accomplished. It considers that a more specific or even a quantified objective would neither have made a difference for the design of policies towards CMU nor that a different sequencing or prioritisation of measures would have allowed more significant progress than was actually achieved. CMU is a project for the long-term, which requires continuous and determined efforts on many fronts. This is why the Commission preferred flagging urgencies and structural challenges instead of emphasising priorities.

Building a Capital Markets Union has been a key priority for the Juncker Commission. Five years later, the need for more integrated and deeper capital markets is undisputed. In her opening statement to the European Parliament, Commission President Ursula Von Der Leyen said: “Let’s finally complete the Capital Markets Union”. The President of the Commission requested to speed up the work towards a Capital Markets Union to diversify sources of finance for companies and tackle the barriers to the flow of capital. The second CMU action plan sets out key measures to deliver on that commitment.

The Commission reported the progress with legislative proposals and other measures in its Communications dated 2016, 2017, 2018 and 2019. Staff working document with more details accompanied all these Communications, except that of 2019. The Commission created a monitoring framework that applied economic indicators capable to measure progress with the CMU objectives already in 2016, but it acknowledges that this framework was not applied and maintained in the following years. It turned out as premature because of the substantial time lag with which statistics cover changes in financial structures. For example, most structural indicators available at the time of the mid-term review covered the time when the initial action plan was set up; data available today does not yet indicate whether the CMU initiatives enacted over the last years have had an effect. For this reason the Commission only reported statistical indicators that inform about progress with CMU in condensed form. Monitoring the actual impact of the measures under the CMU Action Plan was premature since most measures were adopted only recently and are still in the phase of being implemented.

CONCLUSIONS AND RECOMMENDATIONS

Overall, Europe’s capital markets have continued to develop since the first CMU Action Plan was put in place. The Commission tabled all legislative proposals set out and delivered on the non-legislative
measures. While the measures taken have started to have an impact, it will take time for the benefits to fully materialise and effects be felt on the ground. It was always clear that CMU is a project for the long-term, which requires continuous and determined efforts by all stakeholders. The measures announced in the second action plan will further transform the EU financial system and contribute to addressing the political and economic challenges ahead. The Commission agrees that access to some forms of funding, such as public equity, remains limited. The new measures put forward in the 2020 Action Plan aim at striking the balance between enhancing the information available to investors and rendering the reporting obligations for SMEs more proportionate. The Commission shares the ECA’s view that measures to support securitisation have not yet led to the expected effects. Securitisation will be relevant in recovery when banks come under pressure to extend credit to, in particular, SMEs and to expand their balance sheets. To this aim, the Commission already proposed targeted changes to the securitisation framework in the capital markets recovery package in July 2020\(^\text{16}\).

**Recommendation 1 – Propose well-targeted actions to further facilitate SME access to capital markets**

The Commission accepts recommendation 1 a). It will seek simplifications of the existing listing rules to reduce compliance costs for SMEs and review the legislative framework for European long-term investment funds as well as seek to provide for an appropriate treatment of long-term SME equity investment for banks. The Commission will also assess the merits and feasibility of introducing a requirement for banks to direct SMEs whose credit application they have turned down to providers of alternative financing.

The Commission accepts recommendation 1 b). In addition to the measure described under 1 a) that aims to improve the balance between interests of firms and investors, the Commission will propose to set up an EU wide platform (European Single Access Point) that provides investors with seamless access to financial and sustainability related company information.

The Commission accepts recommendation 1 c). In order to scale-up the securitisation market in the EU, the Commission will review the current regulatory framework for securitisation to enhance credit provision by banks to EU companies, and in particular SMEs. The Commission however cautions that the review of the EU securitisation framework would not necessarily make SME securitisation significantly more attractive given the riskiness of SME loans and potential lack of investor interest in SME securitisation.

130. See Commission reply to paragraphs 57 and 58.

131. See Commission reply to paragraphs 59-65.

132. The Commission points out that the demand-driven technical support cannot be ensured to all Member States in need.

**Recommendation 2 – Foster deeper and better integrated local capital markets**

The Commission does not accept recommendation 2 a). It already reviewed best practices and outlined the directions that actors at different levels could take (SWD(2019) 99). The next step would be for Member States to build on this. Several Member States have worked on national capital market strategies. The Commission will closely follow and support progress in building an interconnected ecosystem of strong, transparent and accessible capital markets in the EU, including through

\[^{16}\text{COM(2020) 282 final.}\]
continued technical support. The Commission aims to reinforce its monitoring and dialogue with the Member States, and to continue its efforts to address the needs of local markets.

The Commission partially accepts recommendation 2 b). Country-specific recommendations can play an instrumental role in fostering structural reform and therewith in stimulating policy measures at Member State level that foster market-based financing. The need to progress in market funding needs to be evaluated against other structural shortcomings that Member States face, the urgency to address these and the means available to successfully address them. The Commission can therefore not accept the underdevelopment of capital markets as stand-alone criterion to issue country-specific recommendations.

The Commission partially accepts the recommendation 2 c). The Commission points out that the enhancement of the demand-driven model of the technical support will be continued via the reach out activities with Member States organised as part of the annual calls for Member States’ requests in the area of capital market development. However, the Commission cannot ensure that Member States with highest needs in a given policy area will ultimately make requests for technical support in the future, and that all of them will receive the Commission’s technical support in that policy area.

In fact, the technical support provided by the Commission remains an instrument on demand – as prescribed by the SRSP (futue TSI) Regulation – and it is also subject to a competitive selection based on the criteria set in the regulation, including the assessment of the quality of all the requests received, their expected impact and the Commission’s available budget.

133. The Commission did not see the list of actions proposed as exhaustive, and invited Member States in the expert group to identify other barriers in CMU-relevant areas.

See also Commission replies to paragraphs 79 and 81.

134. See Commission reply to paragraph 86.

136. The Commission would like to point out that the Code of Conduct has allowed to make some progress towards improving the efficiency of the WHT procedures. In addition, as explained in paragraph 99, it will put forward a legislative initiative to introduce a common, standardized, EU-wide relief at source system.

**Recommendation 3 – Address key cross-border barriers to investment**

The Commission partially accepts recommendation 3 a). The Commission accepts the objective of recommendation 3 a) to promote financial literacy. The 2020 CMU Action Plan envisages two dedicated measures to promote financial literacy. First, in order to support Member States in their efforts to foster financial literacy, the Commission will conduct a feasibility assessment for the development of an EU dedicated financial competence framework. Secondly, it seeks to require Member States to promote learning measures that support financial education as regards responsible investing in sectoral legislative acts.

The Commission accepts recommendation 3 b). To make outcomes of insolvency proceedings more predictable, the Commission will take a legislative or non-legislative initiative aiming at increased convergence in targeted areas of core non-bank insolvency. This initiative could address a definition


18 COM(2020) 590.
of triggers for insolvency proceedings, the ranking of claims and further core elements such as avoidance actions or asset tracing.

The Commission accepts recommendation 3 c). The Action Plan on Fair and Efficient taxation supporting the recovery strategy, published on 15 July 2020, refers to a legislative initiative with respect to the introduction of a system of WHT relief at source.

137. See Commission reply to paragraphs 101-106.

138. In relation to paragraph 138 and 139, see Commission reply to paragraphs 115-124.

**Recommendation 4 – Develop specific objectives, critical measures and the monitoring of the CMU**

The Commission accepts recommendation 4 a). The 2020 CMU Action Plan will put forward specific measures that are effective for reaching specific objectives that underpin the CMU objectives. The Commission is determined to address critical measures. Advancing on CMU requires overcoming the structures where national differences are shaped by preferences, entrenched habits and legal traditions. The Action Plan flags urgencies and structural challenges.

The Commission accepts recommendation 4 b). Now that the path towards CMU is firmly established and that the impact of the first Action Plan is expected to show up in data, the Commission will complement its regular reporting of progress on legislative action with the monitoring of how the EU capital market evolves in a set of targeted indicators.

The Commission partially accepts recommendation 4 c). The study referred to in the ECA’s analysis presents a good starting point to identify indicators that are suitable and for which data is reliable, have sufficient coverage over time and Member States, and are linked to CMU objectives. Since the study reveals a lack of data for some policy areas and finds the link between input and output indicators is often difficult to establish empirically, the Commission’s monitoring of progress towards the CMU objectives will unavoidably be based on best efforts. It will aim to improve the underlying data basis provided this can be done without increasing un-proportionally the reporting burden for the financial industry. However, if data are to be taken from third parties, the Commission is not in a position to guarantee their reliability.
Audit team

The ECA’s Special Reports set out the results of its audits of EU policies and programmes, or of management-related topics from specific budgetary areas. The ECA selects and designs these audit tasks to be of maximum impact by considering the risks to performance or compliance, the level of income or spending involved, forthcoming developments and political and public interest.

This performance audit was carried out by Audit Chamber IV Regulation of markets and competitive economy, headed by ECA Member Alex Brenninkmeijer. The audit was led by ECA Member Rimantas Šadžius, supported by Mindaugas Pakšty, Head of Private Office and Tomas Mackevičius, Private Office Attaché; Marion Colonerus, Principal Manager; Anna Ludwikowska, Head of Task; Athanasios Koustoulidis, Ezio Guglielmi, Nadiya Sultan and Karolina Beneš, Auditors. Victoria Gilson and Richard Moore provided linguistic support.
## Timeline

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<tr>
<td>Adoption of Audit Planning Memorandum (APM) / Start of audit</td>
<td>16.7.2019</td>
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<tr>
<td>Official sending of draft report to Commission (or other auditee)</td>
<td>5.8.2020</td>
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<tr>
<td>Adoption of the final report after the adversarial procedure</td>
<td>20.10.2020</td>
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<tr>
<td>Commission's (or other auditee's) official replies received in all languages</td>
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The EU has a predominantly loan-based system for financing the real economy and therefore relies strongly on banks. To address this, the Commission launched in 2015 an Action Plan on Building Capital Markets Union (CMU) in order to foster the development of EU capital markets and their integration and to ensure alternative sources of funding for businesses, SMEs amongst others. The Action Plan included a number of measures, many of which require cooperation between market participants, Member States and European institutions. Overall, we found that the Commission made small steps towards its goal of building the CMU, but was so far unable to catalyse substantial progress with the measures it was able to take within its remit. We recommend that the Commission proposes well-targeted actions to further facilitate SME access to capital markets, fosters deeper and better integrated local capital markets, addresses key cross-border barriers to investment, defines specific objectives and critical measures as well as develops a system for monitoring the implementation of CMU.

ECA special report pursuant to Article 287(4), second subparagraph, TFEU.