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WORKING DOCUMENT

From:	Croatian delegation
To:	Working Party on Financial Services and the Banking Union (ESAP)
Subject:	Croatian Non-Paper on the ESAP implementation

Croatian Non-Paper on the ESAP implementation

A quick browse on the Internet will reveal that anything between two thirds and 90% of all IT projects fail. These statistics are concerning. And the more concerning once one realises that **ESAP is first and foremost a complex, ambitious, mission-critical IT project within the wider objectives of CMU**, which therefore has a very high ex-ante probability of failure.

This non-paper looks at the ESAP proposal from an IT project perspective, asking whether the risks of failure common to all IT projects have been duly considered and mitigated. This non-paper suggests that changes can be made to improve significantly both the chances of success, the time to market, and the overall cost.

Modern project management best practice acknowledges that projects are risky, and builds into them both contingencies and a governance system to adapt the project execution to the objectives as the development unfolds. In other words, a successful project is one that has been both flexible in execution and consistent in delivering the initial objectives.

The discussions so far have indicated that a significant number of Member States favour a **bucketing approach** where the information proposed by the Commission to be centralised in ESAP would be categorised as: high priority, medium priority, low priority, and not relevant to be centralized in ESAP.

Croatia fully supports this approach.

However, to ensure the smooth functioning of ESAP, **we believe that more elements that allow for a successful project should be built into the proposal, such as**:

- flexibility,
- room for contingency,
- scope for learning and improving as the project develops or making necessary changes.

More critically, the proposal requires a more adaptable governance structure to make decisions and a stop-button if we were to ever discover that – for some currently unforeseen reason – the project is no longer viable or that its core assumptions have changed.

This non-paper proposes to introduce these features in the legislative proposal by:

1. **Adapting the sequence of the deliverables**. The deliverables would still be categorised as high, medium and low priority. However, an additional prototyping Phase ("*Phase 0.5*") would be introduced. This Phase would include two high priority information sets (one set from a register already available at the level of ESMA, and one set that has been highly prioritised by the Member States), in order to allow for problem-solving early in the process, to facilitate testing and know-how-building, and avoid "big-bang" rollouts. The prototyping Phase would be followed by two more Phases of other high-priority deliverables (Phase 1 and 2), and an additional Phase for medium-priority deliverables (Phase 3). Progressing between Phases would be conditional on the successful implementation of the Phase preceding it. A "lessons learned" ESMA report approved by the Commission would be a precondition to moving forward to the next Phase.

2. **Introducing flexibility** in terms of when to roll out the deliverables, by putting ESMA, backed by the expertise of an outside commercial provider, firmly in charge of the

project management and execution, including in terms of technical choices and functionality.

3. **Placing ESMA and the Commission in charge of the project governance**. The Commission would approve ESMA's implementation plans and suggested execution timelines (ESMA inception reports). The "go live" deadlines of the **high priority** items (Phase 0,5, Phases 1 and 2) would:
   - **Option 1**: be set at Level 1 as a fixed deadline that starts running out from the moment that the Commission approves ESMA's inception report (i.e. 6 months from "X"). The downside of this approach is still a possible lack of flexibility, as this does not provide a way to take into account possible production issues.
   - **Option 2**: bet set at Level 1 as a fixed deadline that starts running out from the moment that the Commission approves ESMA's inception report, but with the option to prolong the deadline, subject to the approval of the Commission (i.e. 6 months from "x", with the option to prolong the deadline up to additional 6 months)
   - **Option 3**: be set at Level 2 in the ESMA inception report(s) (as part of the draft ITS that ESMA will submit to the Commission), to provide the most flexibility.

   The deadline for "go live" of the **medium priority** items which would be listed in Level 1 (Phase 3) could:

   - **Option 1**: be placed in scope via a Commission implementing act (the comitology examination procedure would provide a **safeguard of MS full involvement in approving the scope** of the deliverables beyond the high-priority items), or
   - **Option 2**: be subject to a review clause.

4. All **low-priority items** (Phase 4) would be re-examined in a **review clause** and would be **contingent** on the prior successful implementation of the high and medium priority items.

In practical terms, **the changes to the draft would look as follows**:

A. Rearrange the delivery into **5 Phases**:
   a. Phase 0.5. or the prototype basket → choose two high priority deliverables that would be used in the prototyping Phase (we would suggest the prospectus register from the Prospectus Regulation and either all of a subset of the information from the Transparency Directive).
   b. Phase 1 or High priority basket 1 → first bucket of high priority items (Accounting Directive, Non-Financial Reporting, Market Abuse Regulation).
   c. Phase 2 or High priority basket 2 → second bucket of high priority items (Sustainable finance disclosure Regulation, Taxonomy regulation, Corporate Sustainability Reporting Directive, Audit Regulation).
   d. Phase 3 or Medium priority basket → medium priority items (Credit Rating Agencies Regulation, Short Selling Regulation, Benchmark Regulation, MiFIR, PEPP, Takeover bids Directive, Shareholders' rights Directive, Covered bonds Directive, (possibly) UCITS).
   e. Phase 4 or the Low priority basket → everything else would be covered by a review clause.

B. The **first and immediate delivery bucket (Phase 0.5) would function as the prototype** and would include a subset of data that is currently already hosted by ESMA

(the prospectus register[1]) and published on ESMA's website, and the set of regulated data from the Transparency Directive that is collected by OAMs today (the scope of information from the Transparency Directive that would be the most suitable for this prototype Phase could be discussed further).

C. Partition the next Phases into **high priority (Phase 1 and 2), medium priority (Phase 3) and low priority reports/information sets (Phase 4)**.

D. The **high priority items** would in any case be transparency[2], financial and non-financial reporting data, market abuse, sustainability reporting and ESG. These high-priority items would also be structured into two buckets of delivery (Phase 1 and 2), **to enable more focused troubleshooting, thus reducing the overall "time to market" if corrections need to be made**. The current proposed structure of the two Phases should be subject to further debate, as we are aware that a number of Member States favour providing data on sustainability in ESAP as a priority. While we understand and agree with the intent, there are a number of advantages in starting with established data sets first and allowing for more time for outstanding issues in sustainability reporting to be resolved, before we centralise this information in ESAP to make it more widely available.

E. For high-priority items, provide deadlines for their inception and a review process between the Phases (see points H and I below).

F. For medium priority items, provide that a pre-determined list (specified in Level 1) can be brought in scope **via a Commission implementing act (the examination procedure),** but **only after the successful implementation of the high priority items, and the reception of technical advice by ESMA on whether and when to implement this Phase.** An **alternative to Commission implementing act** could be a **ESMA report and review clause for <u>any</u> scope expansion, possibly through a fast-track procedure, and in any case, only after the successful implementation of the high priority items.**

G. For **low priority** items, an **ESMA report and a review clause** would be used, subject to the successful implementation of the high and medium priority items.

H. Structure the delivery of each Phase for high priority items in such a way that **ESMA must present an inception report to the Commission** on how it intends to deliver the task for each Phase, which the Commission can **approve**, thus initiating the implementation sequence. The inception report will also include updated estimates of costing, resources, and pricings. The estimated costs would be benchmarked against the actual costs of implementation before any expansion of the scope can be triggered (for medium and low priority items).

I. Provide a deadline for ESMA to deliver its inception report to the Commission, but make its application **conditional** on the Commission's approval and phrase entry into force/delivery dates for the ESAP "go live" date in the following way: *"within x months from the approval of the inception report"* (or one of the other options listed above)

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[1] This means that implementation of the information from the Prospectus Regulation would be divided between Phases 0.5 and 1.

[2] If only a subset of transparency information is chosen for Phase 0.5.

to introduce flexibility, and enable ESMA to problem-solve without it requiring changes to the Level 1 text;

J. **Technical specifications would be provided in level 2** (the ITS – please note that a separate discussion should be had on if the Joins Committee of the ESAs should still be the body to adopt the ITS, if the scope is reduced to items best suited for ESMA), the drafts of which will **form part of the inception report** described above;

K. Close all deliveries within a Phase with an implementation report by ESMA (a "lessons learned report"), which may introduce changes and amendments to the project, for the Commission to approve, before a new phase can be initiated.

L. Introduce the possibility for ESMA to recommend terminating parts of the project under a specified set of conditions if for unforeseen reasons it is discovered that it is no longer viable (e.g. cost overrun or miscalculation in terms of costs of maintenance)

We would also propose to involve **a commercial third-party provider** for the technical solution itself and the day-to-day management of the ESAP, to increase efficiency and to reduce the risk that ESMA will lack the capacity to run the project and to run ESAP itself after it becomes functional. This does not mean that ESMA would not be in charge of the project, especially the governance. It would also be crucial to retain ownership of the system with ESMA. However, using commercial IT and user management expertise from the onset of the project would reduce the time to market and provide much-needed additional capacity to ESMA. We note that a separate dedicated discussion will be necessary on the budget of the project, and if a public tender would postpone the process and for how long. However, considering the scope and the complexity of the project, we have doubts if it would even be possible to implement the project without also engaging a private actor.

An **illustrative example** of the process is shown in the **Annex**.

Please note that the deadlines and the items chosen in the high/medium buckets are not our final position and are only used to showcase the possible project flow. The high/medium/low priority information sets (both the legal acts and the specific information sets within those legal acts) warrant a separate dedicated discussion.

Croatia firmly believes that it is necessary to have a review after each phase of the project in order to assess if the process and system have performed as planned, and to adjust them accordingly. This will prevent replicating errors due to inexperience or wrong assumptions based on incomplete data into the next stages, thus, improving the system overall and perhaps lowering the costs of implementation.

Annex – An illustrative example of the ESAP implementation process and governance

ESAP

Phase 0.5 Prototype

0-12M | 12+2=14M | 14+6=20M | 20+3=23M | 23+2=25M | 25+1=26M

ESMA submits the Inception Report to the COM

Prospectus Regulation
Transparency Directive

- COM approves Inception report
- Implementation period
- Go Live / The system operates for 3M before the review
- ESMA submits an implementation report based on the first 3M to the COM
- COM approves Implementation report

COM approval process for the inception report (applies to all Phases)
If the report cannot be approved; troubleshooting between ESMA and the Commission - up to 2 additional months. If there are conceptual/material faults with the inception of the project that cannot be resolved within that 2 month period, the Commission can send ESMA "back to the drawing board" with specific instructions and deadlines. ESMA may, in its inception report, propose to postpone the implementation of a specific data set, if there are compelling reasons to do so.

The inception report
An **external stakeholder group** is consulted, providing feedback to ESMA's inception report. ESMA includes in its inception report a sumary how the stakeholder feedback has been taken into account

Phase 1 High Priority first batch

0-26M | 26+2=28M | 28+6=34M | 34+3=37M | 37+2=39M | 39+1=40M

ESMA submits the Inception Report to the Commission
Non Financial Reporting
Market Abuse Regulation
Accounting Directive

- COM approves Inception report
- Implementation period
- Go Live / The system operates for 3M before the review
- ESMA submits an implementation report based on the first 3M to the COM
- COM approves Implementation report

Phase 2 High Priority second batch

0-40M | 40+2=42M | 42+6=48M | 48+3=51M | 51+2=53M | 53+1=54M

ESMA submits the Inception Report to the Commission
Sustainable finance disclosure Regulation
Taxonomy regulation
Audit Regulation
Corporate Sustainability Reporting Directive

- COM approves Inception report
- Implementation period
- Go Live / The system operates for 3M before the review
- ESMA submits an implementation report based on the first 3M to the COM
- COM approves Implementation report

Phase 3 Medium priority batch

0-54M | 54+6=60M | 60+10=70M | 70+2=72M | 72+6=78M | 78+3=81M | 81+2=83M | 83+1=84M

ESMA submits technical advice to the COM on the feasibility and the neccesity of implementing Phase 3
Credit Rating Agencies Regulation
Short Selling Regulation
Takeover bids Directive
Shareholders' rights Directive
Covered bonds Directive
Benchmark Regulation
MiFIR
PEPP & PRIIPs

COM adopts an implementing act (comitology procedure) expanding the scope of ESAP, and providing deadline(s) for an ESMA inception report

ESMA submits the Inception Report to the Commission
Credit Rating Agencies Regulation?
Short Selling Regulation?
Takeover bids Directive?
Shareholders' rights Directive?
Covered bonds Directive?
Benchmark Regulation?
MiFIR?
PEPP & PRIIPs?

- COM approves Inception report
- Implementation period
- Go Live / The system operates for 3M before the review
- ESMA submits an implementation report based on the first 3M to the COM
- COM approves Implementation report