

**DRAFT SUMMARY RECORD OF THE 42ND MEETING OF THE EUROPEAN SECURITIES  
COMMITTEE/ALTERNATES  
8-9 JUNE 2006**

**Working document ESC/32/2006**

The meeting was chaired by David Wright, Director of Financial Markets.

**1. ADOPTION OF THE DRAFT AGENDA**

**2. ADOPTION OF THE SUMMARY RECORD OF THE MEETING OF 26-27 APRIL 2006**

Adoption of the summary record was postponed. The Chairman explained that it would be sent to delegations after the meeting for written approval.

**Comitology Issues**

**3. MiFID – IMPLEMENTING LEGISLATION**

The Commission presented Rev3 of ESC/7/2006 and ESC 8/2006. Further modifications were introduced during this 2 day meeting. The revised working documents incorporate most of the modifications proposed by the European Parliament.

The delegations informally agreed on these documents, provided that some changes were included. The changes agreed upon by the delegations were the following.

**Draft Directive (Working document ESC/8/2006-rev3)**

- Recital 26: substitute "undesirable" by "not permitted".
- Include the following phrase at the end of Recital 43: "Where such information requests are reasonable and proportionate, investment firms should provide additional information". No changes to Article 29.8 (remains deleted).
- Include Recital 44 of the Market Abuse Directive (MAD) as Recital 70a.
- Clarify that Recital 69 is without prejudice to the MAD.
- Apply the last indent of Article 40.1 to a) and b) - to cover Danish bond mortgages.

- Include the following phrase at the beginning of Article 15.3: "Without prejudice to paragraph 2" – to clarify that the policy on outsourcing remains the same.
- Delete the last sentence of Recital 61 – it was repetitive
- Include the phrase "Nothing in this Directive obliges" in the last sentence of Recital 47 – this was necessary to ensure the internal coherence of the recital.
- Include the following paragraph in Article 12.2: "In the case of outsourcing arrangements, the investment firm must ensure that the firm to which the activity is outsourced maintains a record of personal transactions entered into by any relevant person and provides that information to the investment firm promptly on request".
- On Article 45:
  - Replace the words "execution policy" in paragraph 5, third sentence with the words "execution arrangements".
  - Include the following phrase at the end of the first sentence of paragraph 6: "and, where appropriate correct any deficiencies". Delete the second sentence of this paragraph "If such....Article".
  - Delete paragraph 7 and make a reference to paragraph 19.1 in Articles 47, 48 and 49.
- One observer asked for deletion of the last sentence in Recital 62 and the second sentence of Recital 63

#### **Regulation (Working document ESC/7/2006-rev3)**

- Article 40.3: Block trades revision to be carried out in two years from the date of application of the regulation, instead of one
- Delete Recital 15 (iceberg orders) – in order to avoid any misinterpretation of Article 16.2.
- Article 28: the text goes back to its original version - internalisers are therefore obliged to publish the trades they execute during their normal trading hours. This change was included in order to enhance transparency.
- One observer asked that the work "details" be replaced by "items" in Article 26(1)(a).

#### **4. EQUIVALENCE OF US, JAPANESE AND CANADIAN GAAPs WITH IFRS**

The Commission services presented a revised version of the draft amendment to Article 35 of the Prospectus Regulation, and of the Decision under the Transparency Directive ('TD'), extending, in each case, transitional exemptions allowing third country issuers to use certain third country GAAPs until the end of 2008. The principal changes consist of a new recital dealing with the ongoing monitoring of convergence between third country GAAPs and IFRS and the work on the elimination of reconciliation requirements for EU issuers; and a new transitional exemption which would apply to third country issuers using third country GAAPs which are demonstrably converging with IFRS. In addition, the Commission Services outlined the expected timetable for adoption of the measures: the European Parliament was unlikely to be in a position to report until September, and the ESC vote should be scheduled for after the EP reports.

Delegations responded to the revisions.

One delegation made the following points:

- The powers of the Commission to extend the transitional exemptions for third country issuers under Article 23(4) of the TD were dependent on a decision that the third country accounting standards in question were not equivalent. That delegation requested clear wording to eliminate the current ambiguity in this regard.
- Without clear measures indicating how equivalence is going to be determined during the transitional period, there is a real risk that the ESC and the Commission will find themselves in the same position in 2009, and no closer to a resolution of which third country GAAPs are equivalent to IFRS for the purposes of the financial reporting requirements under the Prospectus regime and the TD. It suggested that - with respect to the US GAAP - the decision on equivalence should mirror the decision of the SEC whether to remove the current reconciliation requirements for EU issuers: that requirement will be lifted only if the US authorities consider that IFRS is equivalent to US GAAP, and accordingly the EU should not accept US GAAP as equivalent in any other circumstances.
- The texts should deal expressly with the question of interpretation. It is not sufficient to ensure that standards are applied: they must also be understood and interpreted. In particular, there is a need to examine the application of IFRS in third countries.

Four delegations agreed that the text should contain express provision designed to maintain pressure on the US to respect its commitments on convergence:

- One recommended that, from the beginning of 2007, the EU should also put in place the remedies recommended by CESR in its report of July 2005 on the equivalence of Canadian, Japanese and US GAAPs. Furthermore, CESR should be asked to report before the end of 2008 on the ongoing convergence of third country GAAPs with IFRS.

- One also noted that CESR could play a role in ensuring that convergence progressed. However, this delegation disagreed that the determination of the equivalence of US GAAP should mirror the SEC approach to its own reconciliation requirements. This delegation also emphasised the political nature of the equivalence issue, and argued that it needed to be discussed at some point at the political level - something which was not envisaged in the comitology process.

Another delegation supported the view that any transitional arrangement must be able to maintain pressure on the EU-US convergence process - a political project. However, it disagreed that changes to the legal text were necessary for that purpose. Instead, the Commission should establish a 'road map' analogous to that of the SEC. This State expressed the view that the new Commission text was a huge improvement. However, the last sentence of Recital 6 was unnecessary.

Three further delegations expressed support for the Commission's approach:

- One expressly supported the Commission's revision as a pragmatic and workable solution that would ensure a fair outcome and which took account of the range of views expressed at the ESC meeting in April. This approach was more likely to deliver the goal of convergence between EU and US accounting standards, and to ensure that the US reconciliation requirement is removed by 2009, than an approach which attempted to put pressure on the US by restricting the use of US GAAP in the EU at this stage.
- Another considered that the condition that the issuer should demonstrate the existence of an appropriate convergence programme is too restrictive.

However, two delegations opposed the extension of the transitional period for third country GAAPs other than Canada, Japan and the US. One noted that there was no guarantee that they will be found to be equivalent by 2009.

Two delegations expressed concern that the necessary equivalence decisions should be taken in 2009:

- One of these delegations requested express provision in the measures obliging the Commission to determine the equivalence of third country GAAPs other than those already assessed by CESR (Canada, Japan and the US) by 2009, while the other wanted the reference to the equivalence mechanism to be restored to Article 35 of the Prospectus Regulation.
- One also emphasised that issuers need to know as soon as possible which third country GAAPs, if any, will be subject to transitional exemptions after the end of 2006, since an issuer will start preparing a prospectus many months in advance of its approval and publication.
- The other warned that convergence and equivalence were different issues, and should not be confused. The EU should not allow the use of third country standards simply because the relevant authority had a work programme for convergence. This would discriminate against the Canadian, Japanese and US

GAAPs, which had had to undergo an assessment by CESR. However, this point was disputed by a delegation that supported the Commission revision: if there is discrimination, it would be against other third country GAAPs that had not had the opportunity of an equivalence assessment. Both delegations agreed that those other GAAPs should be subject to a proper equivalence assessment, and one pointed out the proposed two year extension of transitional exemptions was necessary precisely to enable such an assessment to be made.

CESR expressed the view that further transitional exemptions should be available only for Canadian, Japanese and US GAAPs. In respect of other third country GAAPs, it pointed out that an assessment of equivalence for the purposes of the TD and the Prospectus Regulation can be made at any time, including after 2009. GAAPs that wish to be considered equivalent should simply request an assessment. Any other solution would constitute a disincentive for third countries to adopt IFRS. CESR also supported the adoption of a 'road map' by the EU which should, among other things, indicate the contents of the proposed Commission report. CESR should also be asked to report on the progress of remedies.

## **5. TRANSPARENCY DIRECTIVE – IMPLEMENTING LEGISLATION**

Member States generally welcomed the Commission draft proposal for a directive implementing the Transparency Directive.

Articles 6 and 8, and Recital 10 gave rise to most of the comments. On Article 6 (market makers) of the draft proposal, a delegation questioned the compatibility with the Transparency Directive of the notification by the market maker to its own competent authority, rather than that of the issuer. This was echoed by two others who considered that the market maker should notify to the competent authority of the relevant issuer.

On Article 8 (notifications of major holdings), two delegations expressed the view that a list of the various notification situations referred to in Article 10 of the Transparency Directive would be clearer than the proposed drafting.

On Recital 10, two delegations expressed concern with regard to the proposal that the execution of off-exchange transactions should be deemed as having taken place upon completion, rather than upon entering into the agreement.

Member States were requested to send to the Commission their comments in writing for discussion at the ESC meeting of 13 July.

### **Other Issues**

## **6. MiFID REVIEWS – REPORT ON NON-EQUITY TRANSPARENCY**

The Commission services presented their plans for the review of transparency in non-equities markets required under Article 65(1) of MiFID. They explained that the Commission is required to report to the Council and the European Parliament by the

end of October 2007. At this stage, they said, the Commission has a completely open mind on the outcome of the review.

They went on to explain that Article 65 (1) requires the Commission to investigate the extent to which pre- and post-trade transparency obligations should be imposed on transactions in financial instruments other than shares. It does not cover shares that are not admitted to trading on regulated markets. It also does not require a binary choice between making all markets transparent or none. It also permits consideration of a range of options for each instrument market in order to ensure tailored regulation.

They said that the Commission is required to consult the public and discuss the matter with competent authorities. Two public consultations are planned - one on the basis of a call for evidence, to be discussed below, and one on a draft report. It is also intended to seek expert technical assistance from CESR. The Commission services said that they also intended to involve the European Securities Markets Expert Group (ESME) in the work. This is a 20-member expert group set up to advise the Commission on the functioning of securities legislation.

The Commission services said that they planned to issue a Call for Evidence shortly, consulting industry and other stakeholders on a series of questions relating to the scope and conduct of the review.

The Call for Evidence would set out the legal framework for the report, the methodology (including the reliance on impact assessment), the proposed scope of the report in terms of instrument classes to be prioritised, and the possible policy rationales for transparency. The Call for Evidence would seek feedback on these and other issues, in particular whether there are demonstrable problems with respect to the rationales for transparency in instrument markets, whether there is evidence that mandatory pre- or post-trade transparency would solve any of those problems, whether EU-level action would be called for in view of the principle of subsidiarity, and whether any problems identified would disappear as the natural result of short-to-medium term market evolution. The Call for Evidence would also consult on the options to be considered if indeed problems are made out. Those options at this stage in respect of each of pre- and post-trade transparency include no change, a self-regulatory option, a MiFID-style transparency option, and (for post-trade transparency) a TRACE-style transparency option.

Delegations generally welcomed the Commission services' statement and said that the Call for Evidence would be carefully evaluated. One delegation in particular welcomed the Commission services' emphasis on seeking evidence of whether there were any problems that required mandatory transparency to be solved. One observer requested sufficient time to conduct proper consultation of market participants.

The Commission services said the Call for Evidence would be released shortly after the meeting and would be open for consultation under mid-September.

## **7. MARKET INFRASTRUCTURE**

### **7.1 Clearing and Settlement**

This point began with a presentation by the Commission services (DG Competition) of the Commission's recent Competition Issues Paper on Securities Trading and Post-trading, on which the consultation period was open until 30 June. The Commission services said that they hoped to receive feedback within that period.

The Commission services (DG Internal Market) then briefly summarised the contents of the draft working document on post-trading that was published by DG Internal Market and Services on 16 May, stressing the complementarities between the findings of this document and those in the paper published by DG Competition. While welcoming the document, a few delegations expressed their disappointment at the lack of a cost/benefit analysis on the policy options being considered by the Commission. Some questions were raised about the size of the estimates of the potential benefits of dismantling the barriers to post-trading. The Commission services pointed out that the cost/benefit analysis would be published in the forthcoming regulatory impact assessment and that the estimates of the benefits fully incorporate the uncertainties stemming from the estimation process.

## **7.2 Hague Securities Convention**

The Commission services said that internal discussions on the legal assessment were still continuing, but they hoped to be able to present it at the Civil Law Committee on 10 July and at the ESC meeting three days later.

## **7.3 Settlement Finality Directive**

With reference to the implementation report of December and the earlier debates in the ESC, the Commission services indicated that their current thinking was that potentially changes may be needed in four areas of the SFD, and they formulated suggestions to that effect. It concerns: (i) issues concerning the scope of the SFD, (ii) issues concerning 'insolvency proceedings', (iii) issues concerning the governing law, and (iv) two other issues falling outside these categories. The Commission services invited comments on these proposals before the summer.

The areas and proposals outlined at the meeting were not necessarily an exhaustive list of all problem areas in the SFD. Rather, it was stressed that they should be regarded as proposals that have been identified so far as requiring further discussion. Further issues may arise e.g. as a result of the ongoing industry consultation, potential legislative action in the field of clearing and settlement or progress of the Hague Convention and Unidroit. Moreover, action eventually taken by the Commission can take a variety of forms ranging from amendments to the SFD, a focus on ensuring even implementation across Member States, bilateral contacts with Member States concerned etc.

Further, the Commission invited delegates to check the notifications of designated authorities to notify about the opening of insolvency proceedings and of national designated payment and security settlement systems on DG MARKT's website.

[http://ec.europa.eu/internal\\_market/financial-markets/settlement/index\\_en.htm#national](http://ec.europa.eu/internal_market/financial-markets/settlement/index_en.htm#national)

This information may be sent by post to European Commission, DG MARKT, Unit G2 Financial Market Infrastructure, Rue de la Loi 200 (C107), 1049 Brussels or by e-mail to [markt-sfd-notifications@cec.eu.int](mailto:markt-sfd-notifications@cec.eu.int)

#### **7.4 Evaluation of Financial Collateral Directive**

The Commission asked delegates from Germany, Hungary, Italy, Spain, Sweden and UK to check whether their administrations have already sent their replies to the questionnaire for the evaluation of the financial collateral directive.

### **8. LEVEL 4 OF THE LAMFALUSSY PROCESS - Transposition by Member States**

The Commission services reported that the state of play regarding transposition of the Market Abuse Directive (MAD) and the Prospectus Directive was encouraging. The Commission had closed a number of infringement proceedings that were initiated on the grounds of non-transposition of the MAD and the Prospectus Directive. As regards the MAD, only two cases remained which were expected to be finalised soon. As regards the Prospectus Directive, only two Member States had not yet fully notified the transposition.

### **9. A.O.B.**

#### **9.1 Indicative remaining work programme for the ESC in 2006**

The Commission services explained the changes in the revised work programme and said that it would be regularly updated.

#### **9.2 ESC Newsletter**

The Commission services explained that the newsletter would be circulated to delegations shortly.

#### **9.3 ESC Mailing list**

The Commission service explained that they wanted to update the ESC mailing list. The said that the current list was too long and that probably included a number of people who no longer needed to receive ESC documents. It also contained e-mail addresses which were now obsolete. The plan was therefore to draw up an entirely new mailing list. The Commission services asked delegations to send them a definitive list of those people from their Member State who should be on the new list.