

**DRAFT SUMMARY RECORD OF THE 59TH MEETING OF THE EUROPEAN SECURITIES
COMMITTEE (ALTERNATES)
21 MAY 2008**

Working document ESC-7-2008

The meeting was chaired by Ms Maria Velentza, Head of the Securities Markets Unit.

1. ADOPTION OF THE DRAFT AGENDA

The agenda was adopted.

**2. ADOPTION OF THE SUMMARY RECORD OF THE MEETING OF 14 FEBRUARY 2008
(Working Document ESC-3-2008)**

The summary record of the meeting of 14 February 2008 was approved with no amendments.

3. DETERMINATION OF EQUIVALENCE OF ACCOUNTING STANDARDS (Working Document ESC-4-2008)

At a first stage, the Commission Services introduced the issue of equivalence of third country GAAPs in a more general context (e.g. convergence of third Country GAAPs with IFRS; the reform of the governance of the IASB; strengthening the EFRAG proactive input to the IASB's agenda-setting process, etc).

With particular regard to the determination of equivalence of accounting standards in the Prospectus implementing Regulation and the Transparency Directive, the Commission services are going to table by beginning of June two draft comitology measures to be discussed in the ESC: a new level 2 Regulation implementing the Transparency Directive and a Regulation amending the level 2 Prospectus Regulation. Taking into consideration the advice delivered by CESR on this subject earlier this year, the Commission services intend to include the following in these draft measures:

- Recognise equivalence between IFRS as issued by the IASB, US GAAP and Japanese GAAP.
- Accept the use of Chinese GAAP, South Korean GAAP and Canadian GAAP within the EU for a transitory period, ending no later than on 31 December 2011.

As regards India, the issue still remains open and the Commission services are waiting for CESR to deliver its advice.

As for the timeline, the Commission will formally present the two draft comitology measures at the beginning of June. A vote on these draft measures is expected to take place in the ESC in autumn. This would allow adoption by the Commission and publication in the Official Journal of the EU before the end of 2008.

The delegations which took the floor acknowledged the work done by the Commission services and the CESR and expressed their satisfaction with the progress made on these difficult issues. One delegation stressed the importance of reaching an agreement on the determination of equivalence in time, in order to ensure continuity in the acceptance of third country GAAPs within the EU. Three delegations raised the issue of the necessity to monitor compliance of the financial statements presented by third country issuers within the EU with the respective equivalent or accepted third country GAAPs. Two delegations stressed the issue of reciprocity which is not explicitly included in the working document. According to these delegations, the issue of reciprocity concerns especially the US; this relates to the fact that the US will accept reconciliation towards IFRS of accounts using this carve out only for a period of two years.

The Commission services informed that efforts are being made to resolve the whole issue of the carve out in IAS-39. Furthermore, it will not be possible to exclude entirely possible differences between IFRS as issued by the IASB and IFRS as endorsed in the EU. For the same reason, it is also very important to preserve the political assessment of the Member States and the European Parliament through the endorsement process. As far as the advice by CESR is concerned, the Commission services stressed that it will be taken into account as much as possible. In the near future, CESR is going to provide a technical assessment of Indian GAAP; the timing for this assessment depends on cooperation from the Indian side. As regards China, CESR will closely follow and monitor their application of their standards as their new accounting standards have been applied for the first time in 2007.

The Commission Services assured that they will pay due attention to the several issues raised by Member States and in particular take proper note of the requests to carefully monitor the application of third country GAAPs. The Commission services will also take into consideration similar work taking place with respect to audit equivalence. The Commission Services once again stressed the importance that IASB together with the European Banking Federation identify as soon as possible a technically sound solution on the issue of the IAS 39 carve-out.

4. CREDIT RATING AGENCIES

The Commission services gave a presentation highlighting the issues surrounding Credit Rating Agencies (CRAs) in the context of the current financial turmoil. The presentation covered the current major initiatives in this field launched by various international forces, like the Financial Stability Forum Report (approved on 7 April 2008), the CESR Report (approved on 13 May 2008), the revision of the International Organization of Securities Commission (IOSCO) code of conduct for CRAs

(approved on 26 May 2008) and an ESME Report (to be approved on 4 June 2008). The Commission services noted that these initiatives share concerns in relation to three areas of the activities of CRAs:

- management of conflicts of interest (provision of consulting services, involvement of the analysts in the structuring of the product to be rated, remuneration and career prospects of the analysts, "shopping for ratings" practice, etc.);
- quality of the ratings and the methodology used by CRAs (periodical review of methodologies and assumptions, care on the quality of the information about the underlying assets, adequate staff for all parts of the rating process, inclusion of stress testing and "what if" scenarios in the rating opinion, etc.);
- transparency of the processes used by the CRAs (disclosure of methodologies, differentiation of ratings scales for structured and for traditional corporate products, disclosure of comparable data on the agencies' performance, increase in availability of information via websites, etc.).

The subprime debacle demonstrated that the existing framework for the operation of CRAs in the EU has to be significantly reinforced. Taking into account all these inputs, the Commission services are concluding its assessment of the conduct and practices of the CRAs and are expected to come up with policy responses before the summer break. The Commission services invited delegations to express their initial views on the subject.

The CESR observer presented the main elements and recommendations of CESR's report in detail. A number of delegations welcomed CESR's report. During the discussion one delegation recalled that it is not the first time that the ESC has discussed about CRAs (Enron, Parmalat, Asiatic crisis, etc.), as this is a recurrent issue. Some delegations considered that any policy response should be proportional; excessive rules might hamper access to the market for newcomers (and therefore jeopardise competition in a *per se* oligopolistic market). A number of delegations pointed out that the revision of the IOSCO code is a good starting point. Concerning the question of oversight, the majority of the delegations which took the floor expressed a preference for a self-regulatory solution; the Code of Conduct for Clearing and Settlement was put forward as the example to follow. Finally, some delegations stressed the need for an international solution with the lead coming from the EU institutions.

5. MiFID REPORTS (Working Document ESC-5-2008)

The Chairperson presented the approach suggested in Working Document ESC-5-2008, regarding MiFID reports, and asked delegations to express their views on the following:

- The suggested approach, i.e. combining all remaining reporting obligations in one report to be finalised by mid-2010.

- Whether a deferred deadline beyond mid 2010 should be considered for tied agents and telephone recording.

The CESR observer informed the delegations that CESR would produce a follow-up to its Non-Equity Market Transparency report in the light of recent developments in financial markets. The observer also agreed with the idea of a single report; he also said that so far he had not seen any evidence of problems in relation to tied agents and telephone recording. However, this is not an adequate justification for postponing the reports for these issues after mid 2010.

Five delegations agreed on the suggested approach and expressed a preference to also include telephone recording and tied agents in the same report. Three other delegations also agreed on the suggested approach; nevertheless they would be open to the possibility of postponing the reports on telephone recording and tied agents. One delegation agreed on the suggested approach, but expressed concerns about postponing the report on tied agents in 2010, as they had seen some problems in this regard.

The Chairperson concluded that the majority was in favour of producing a single report by 2010 including the issues on tied agents and telephone recording. It should be investigated whether the issues that one delegation had encountered with respect to tied agents could be solved in the meantime by other means, such as interpretation.

6. LAMFALUSSY REVIEW

The Commission services briefly presented its consultation paper on amendments to Commission Decisions establishing CESR, CEBS & CEIOPS and invited the delegations to comment on the ideas presented. The Commission services informed that neither a radical overhaul of the Decisions nor a full harmonisation between them is foreseen. The aim of the exercise is to ensure greater coherence and consistency between the three Decisions and to establish a clearer framework for the activities of the Level 3 Committees in the area of supervisory cooperation and convergence. To this end, the Commission services are going to propose to refer in the Decisions, in an explicit manner, to the main tasks that the Level 3 Committees are expected to perform. These include *inter alia*, developing common practices concerning mediation, information exchange, reporting requirements, delegation of tasks and responsibilities, colleges of supervisors, ensuring effective cross-sector cooperation and the development of a common supervisory culture. The Commission services also encouraged comments on the proposed role of the Level 3 Committees with regard to financial stability monitoring and reporting. The consultation paper will be open for public consultation until 18 July.

One delegation inquired about the references to the Level 3 Committees in 2010 forthcoming legislation. The Commission services replied that once the Decisions setting out the responsibilities of the Level 3 committees become more specific as to what level 3 committees are expected to do to foster supervisory cooperation and convergence, it would become easier for the co-legislators to refer to these tasks, where necessary, in the relevant Directives. Certain tasks are already granted to

CEIOPS and CEBS, respectively, in the Solvency II proposal and the upcoming review of the CRD.

7. PROSPECTUS DIRECTIVE (Working Document ESC-6-2008)

The Commission services presented the issue of the equivalence of third country prospectuses. They recalled the equivalence decisions released by three competent authorities in October 2007, followed by the memorandum of understanding agreed on in January 2008 by the French and Israeli competent authorities on the same issue. The Commission services confirmed the right for Member States to issue such decisions; they nevertheless expressed their concerns regarding the transparency and fairness of the process followed in order to establish the equivalence of third country prospectuses. The Commission services also pointed out that this right cannot be exercised without taking into account the practical consequences of the approval of prospectuses for other jurisdictions. Third country issuers having their prospectuses recognised by one EU Member State are entitled to use the same prospectus in all other Member States in the EU. Third country prospectuses can be thus "passported" throughout the EU, without the possibility for the host Member States to further scrutinise them. The Commission services' concern is that -in response to unilateral equivalence decisions followed by a passport- some host competent authorities may consider that the home jurisdiction has not used appropriate criteria to assess the equivalence and thus refuse the use of those passports on their territory. Therefore, it is fundamental to enhance cooperation among regulators to avoid possible disruptions to the functioning of the passport mechanism set up by the Prospectus Directive.

The Commission services suggested the way forward: on the basis of the duty of cooperation laid down in Art. 22 par. 2 of the Prospectus Directive, EU competent authorities should agree to a solution consisting of common transparent criteria for establishing equivalence. In case of failure, the Commission can make use of the comitology power conferred by the Prospectus Directive to ensure uniform application of the Directive in this regard (Art. 20 par. 3)

The CESR observer agreed with the legal analysis of the Commission services and pointed out that the issue is relevant for the Transparency Directive as well. The observer recognised the need for further convergence of supervisory practices, but noted that this discussion cannot undermine the legality of the actions and decisions taken by the relevant supervisory authorities. Two CESR expert groups have been working on this issue. This issue was also discussed in the CESR Plenary meeting held in Ljubljana on 13 May 2008, where the Chairman proposed to follow a process to facilitate coordination of decisions consisting in the following: when a competent authority is taking a position on equivalence of third countries prospectuses, it has to inform the CESR secretariat, which will subsequently inform the other competent authorities. If it is necessary, the position will be firstly discussed in the relevant CESR working groups and referred to the Commission should the CESR working groups fail to reach an agreement.

One delegation suggested that the Commission should use its comitology power in this instance, regardless of the length of the process.

Another delegation recognised the legality of any equivalence decisions, but nevertheless stressed the current fragmentation on the issue. It supported the idea of defining a common approach within CESR, leaving the comitology measure as a last resort. It also recalled the question of reciprocity with the US, and asked whether this element was considered when issuing the equivalence decisions.

One delegation explained its approach in assessing the equivalence of US prospectuses. It reminded that there are a lot of similarities between an EU and US prospectus; however, the EU rules on financial history are more stringent than the US ones; therefore, all US prospectuses need to be checked. It also supported the idea of facilitating the dialogue within CESR on the matter.

Another delegation suggested to carefully monitor the work within CESR, but not to renounce the possibility of using the comitology powers.

One delegation recalled the need for a transparent and consistent approach in the determination of equivalence of third country prospectuses; it also affirmed that any determination of equivalence is premature at this stage, since no proper assessment of third countries legislation has been carried out.

One delegation affirmed that competent authorities are acting individually on this issue, without taking into account the question of "passportability" of third country prospectuses. The current fragmentation should be removed by coordinated actions.

Two delegations contested the legal terminology used by the Commission services in the working document ESC-6-2008. They specified that the competent authorities concerned had declared the equivalence of the standards between the EU and the US, not the equivalence of the US prospectuses *tout court*. Moreover, this does not imply an automatic and general recognition of equivalence; it just refers to individual US prospectuses to be approved by the relevant competent authority. They requested that the Commission services amend the working document ESC-6-2008 accordingly.

The Commission services replied that this document was not a document for adoption or publication; its only purpose was to trigger a discussion among delegations and to receive comments and explanations on the facts described in this document. It was also stated that no revised version would be circulated since no further discussion has been planned on this issue. Finally, the Commission services drew the attention of delegations to the fact this has always been the practice followed in the ESC. They said that, of course, they would record all comments and objections in the summary record of the ESC meeting. In this context, and at the request of one delegation the following statement is included in this summary record:

The Belgian Delegation asks the European Commission to replace, in point 3 of the document on Equivalence of 3rd Countries' prospectuses, the words "recognition of 3rd country prospectuses" with the words "concerning 3rd country issuers" and to replace the words "equivalence of US prospectus on their respective regulated markets" with the words "equivalence of US standards for the purpose of the filing of a prospectus by an issuer seeking admission to trading on their respective regulated markets". Given the refusal of the European Commission, the Belgian Delegation has maintained a general reservation on the document.

The French Delegation maintains the same general reservation on the document for the same reasons as the Belgian Delegation.

Another delegation expressed support of the view presented by the previous two delegations, noting that the Euronext regulators have been acting in a transparent way.

The Commission services summarised the discussion, expressing satisfaction for the general support of the proposed way forward, which should generate an agreed solution at CESR level. Moreover, the discussion confirmed the need for more transparency and circulation of information on the issue.

8. EXTERNAL RELATIONS IN THE AREA OF FINANCIAL SERVICES

The DG MARKET Services presented the outcomes of the second Transatlantic Economic Council (TEC) meeting which was held in Brussels on 13 May. The discussions on DG MARKET issues on financial markets went well: on accounting equivalence (good progress on the EU side, the US side having done its part of the job), securities trading (both sides have intensified their work on defining a process for carrying out a comparability assessment of EU and US securities regimes which they hope to finalize in the coming months) and reinsurance collateral (the European Commission insisting on more results-oriented cooperation to reform US rules on reinsurance collateral). Both sides stressed the good progress made on transatlantic capital market integration during the past years due to the excellent cooperation in the context of the informal EU-US Financial Markets Regulatory Dialogue (FMRD). With a view to better ensuring continuity of the TEC process beyond this US administration, it was agreed to have a second TEC meeting in October 2008 in Washington.

9. NON-HARMONISED RETAIL INVESTMENT FUNDS

The Commission services presented the state of play and the background of its work regarding non-harmonised retail investment funds. Developments during recent years include the existence of a number of non-harmonised retail investment funds with good track records in some Member States, the continuing strong growth of these types of funds in the EU and the potential risks resulting from 'evasion strategies' through which some providers try to sell strategies or assets which are not eligible under the UCITS Directive in different wrappers like certificates or unit-linked life insurances to retail investors across borders.

The Commission report to the Council and European Parliament, due in autumn 2008, will analyse the need for and possible options for developing a single market framework for non-harmonised investment funds. This report will:

1. demarcate the boundaries of the UCITS universe
2. map the different categories of non-harmonised funds
3. evaluate the case for EU-level action – from both sell-side and investor perspective

4. identify which non-harmonised funds are ripe for the retail market, i.e. determine whether a SM framework for these funds would provide real net benefits
5. present options for EU-level action
6. assess whether particular attention would be required, e.g. in terms of risk-management, disclosure or distribution rules

It will be based on different strands of background work on European markets non-harmonised funds:

Two studies support the analysis of, firstly, differences and similarities between UCITS and non-UCITS. The final report of this study has been published recently and reveals that UCITS investment powers already encompass the vast bulk of the investment strategies that fund managers wish to bring to the retail market. The second study explores the extent to which non-harmonised funds are actually being distributed to retail investors and through which distribution channels. The final report is due in August.

An ad-hoc industry expert group prepared a report on the European market for open-ended real estate funds and its regulatory framework. The group's report provides technical, commercial and market analysis. It presents a case for pan-EU distribution of real estate funds to retail investors and recommends that legislation would be needed in order to overcome existing barriers to the cross border development of this sector. The industry experts express a preference for incorporating OEREF within the existing UCITS Directive.

An open hearing on 8 April 2008 provided the fund industry, investors and supervisors with an opportunity to react to the study findings and the expert group report and to exchange their views on the need for an EU regime for these funds. The Commission will consider the analyses and views presented in the different external inputs in its own analysis in an impact assessment report and in the report.

One delegation expressed its support for the analysis and conclusions of the real estate expert group. Another delegation inquired about the link between the work on non-harmonised funds and other retail investment products. The Commission services clarified that while the subjects will be dealt with in separate reports, it will certainly take linkages between the issues into account.

10. A.O.B

The Chairperson explained to delegations that the next meeting scheduled on 18 June 2008 will most likely have only one point on the agenda, namely the determination of equivalence of accounting standards. She therefore asked whether delegations agree on a written procedure to avoid a mission to Brussels. Two delegations supported the proposal, while another two expressed their preference to hold the meeting.