

**SUMMARY RECORD OF THE 66TH MEETING OF THE EUROPEAN SECURITIES COMMITTEE
(ALTERNATES)
19 OCTOBER 2009**

Working document ESC-11-2009

The meeting of the European Securities Committee was chaired by Mr. Emil Paulis, Director of Financial Markets, DG Internal Market and Services. The Chairperson welcomed the members and expressed his wish to have a good meeting and take full advantage of this cooperation opportunity.

1. ADOPTION OF THE DRAFT AGENDA

The agenda was adopted.

2. FINANCIAL SUPERVISION

Commission summarised the state of play following first Council reading of the proposed ESA Regulations, and explained the rationale of the Commission's proposals as regards technical standards, individual decisions, and consistent application of community law.

The representative of CESR emphasised that ESAs must be allowed to continue to carry out all activities of the level 3 committees, and it is not clear if this will be possible based on the current draft Regulations (e.g. in the accounting and auditing fields); stressed the importance of ESMA having supervisory competence for Credit Rating Agencies from the moment of its creation; emphasised the need for a smooth transition from the level 3 committees to ESAs and the need to start preparatory work as soon as possible.

Member States made the following comments: urged early amendment to Credit Rating Agency regulation to prevent Member States taking CRA supervision for a short time only before handing it over to ESMA; some were disappointed with scope of omnibus directive as seen in the Commission Staff Working Paper; some expressed doubts about the usefulness of the Board of Appeal. It was mentioned that voting modalities were an issue, with some MS wanting systematic use of QMV. There was some concern about transitional rules and arrangements from the level 3 committees.

Commission took note of these points, and pointed out that a draft amendment to the CRA Regulation would have to wait for the new Commission, as it is not possible in October 2009 and is not classified as "affaires courantes".

3. FISCO

The Commission services circulated a copy (in all Community languages) of the Recommendation on withholding tax relief procedures, that the Commission had adopted earlier on the day. They also announced that the Recommendation, the Economic Business Case, FAQs and the Press Release would be made available on DG MARKT's website.

The Commission services referred to the earlier discussions in the ESC and/or Working Party IV on Direct Taxation of February/April 2009. They indicated that the Recommendation reflects best practices of EU Member States and contains the Commission's assessment on how withholding tax relief procedures should be simplified and improved. One of the key recommendations is that tax relief should be offered at source, which already is good practice in a growing number of Member States, combined with quick and standardised refund procedures. The Recommendation lists several elements of such refund procedures and also addresses the role of foreign financial intermediaries. Three Member States said that they were surprised that the Commission had already adopted the Recommendation without further discussion with Member States nor sending the document to them before the meeting. They expressed their discontent with this procedure. They recalled that during the ESC meeting in February 2009, many Member States were strongly opposed to the Commission's project, as those Member States considered that the Commission was not competent for writing a recommendation on direct taxation which is an exclusive States' competence and expressed mainly concerns about the proposed obligation to allow foreign financial intermediaries as withholding agencies. The Commission disagreed and noted its institutional competence to issue a Recommendation with the very specific scope and objective as covered in the recently adopted measure. They wondered how the Commission had addressed the control issue and the risk of fraud. In response, the Commission services stressed that the Recommendation has been drafted very carefully, taking into account the concerns expressed previously by Member States, including the issue of control. Further, the Economic Business Case now includes a chapter on the fraud issue. The Recommendation does not aim to provide all answers nor does it solve "Giovannini Barrier 11" completely; it should be seen as part of a process and that it is meant to stimulate the debate further, to share information on best practices and to provide a forum for further discussion. The Commission believes that there is a common interest to pursue these discussions strongly and it is open to comments on both the Recommendation and the economic analysis.

4. UNIDROIT CONVENTION ON INTERMEDIATED SECURITIES

The Commission representative presented to the Committee the outcome of the negotiations on the UNIDROIT Convention on substantive rules regarding intermediated securities. He was glad to report that the Diplomatic Conference, which took place in Geneva between the 5th and 9th of October, was successful, the negotiations were finalised and the Convention text has been adopted. The new Convention will now be called the "Geneva Securities Convention".

Most of the Member States and the EU were present at the negotiations and initialled the Convention's Final Act. The Convention adopts a functional approach and avoids characterisations. In that respect, it leaves national laws to continue with their characterisations and it thus facilitates the integration of the Convention's provisions into the relevant national rules.

Schematically, the Convention deals with four interrelated issues. The first one concerns the "proprietary aspects" of intermediated securities. These cover, inter alia, the methods of acquisition, disposition etc., of intermediated securities and interests in intermediated securities, the (minimum) rights deriving from a credit of a security to a securities account, good faith acquisition rules, rules on shortfalls, etc.

The second issue is the relationship of the Convention with national insolvency laws. The Convention approach is that rights that have become effective under the Convention should be recognised by national insolvency rules. Having said that, the Convention does not affect

national insolvency provisions on preferences, avoidances etc., unless specifically mentioned in the Convention. The Convention also preserves the Settlement Finality Directive and contains an optional Chapter which replicates almost entirely the Financial Collateral Directive.

The third issue is the role of intermediaries. The Convention recognises the important role of intermediaries, it introduces certain duties that they need to comply with and prevents them from waiving their liability for gross negligence and wilful misconduct. Finally, the Convention allows Contracting States to limit the implementation of the Convention to securities held through regulated entities only.

Finally, the Convention addresses the issuer/final account holder relationship. The position adopted is the one of neutrality. In other words the Convention tries not to interfere with this relationship and to leave assessments and procedures subject to national, non-Convention, law.

The Commission representative closed its presentation with a brief comment on future developments that the Commission and the EU Member States need to take into account when deciding the way forward. The Official Report (commentary) of the Convention should be amended in order to take into account the discussions and the amendments made during the Diplomatic Conference. This should happen within a period of 14 months. Delegations will have the time and the opportunity to comment formally on the text before its finalisation. The Commission is also preparing its proposal for a Securities Law Directive which will cover, to a large extent, the same ground as the Geneva Securities Convention. The Commission timeline is for the proposal to be formally adopted mid 2010. One Member State thanked the Swedish presidency and the Commission for their strong commitment in reaching a European compromise during the negotiation which was helpful to improve the quality of the Convention. Nevertheless, it underlined that despite some progresses, the Convention did not offer sufficient guarantees for the final investor nor for the protection of the market integrity. Therefore, the future directive on securities law should not be a copy of the Unidroit convention but should promote higher standards, in particular concerning the regulation of intermediaries. This Member State asked the Commission for a consultation on the project of directives, considering that the technical questionnaire on its principles launched in June 2009 was not equivalent to a consultation on a text. The Commission agreed and committed to apply this approach.

5. COMMODITIES MARKETS

The Commission services provided a brief summary of the note "Commodities and commodity derivatives – Interaction with securities markets legislation" distributed to the ESC members and gave an overview of the six written answers received up to now. The Commission invited the other delegations to submit written answers as soon as possible.

Emission allowance markets (EUAs)

Two delegations asked for further analysis before deciding whether emission allowances should be classified as financial instruments. Further consideration should be given to the consequences of such a classification. As an example it might bring firms which are usually not regulated under the supervision of financial regulators. Various delegations also pointed out the difficulty of gathering relevant information on these markets as responsibilities are shared with other Ministries (i.e. in many Member States, spot markets fall under the authority of the Ministry of Environment). It might be interesting to know whether responsibilities are shared with other Ministries in other Member States too. A third

delegation stressed the need of having a regulation at the EU level for both spot and derivatives markets. They are currently analysing internally whether specific / tailor made regulation would be needed for emission allowances. Another delegation asked for further information on the auctioning regulation of EUAs to be finalised by the Commission by June 2010, as auctioning is very similar to any financial market.

Energy and agricultural markets

Delegations were generally supportive of the initiatives of the Commission. There was a clear consensus about the need to improve the oversight and transparency in the commodity derivatives markets. Several delegations explained that these work streams should be placed in a more general context, that is to say the work on the derivative markets. In addition several delegations underlined the importance to coordinate the work on the three work streams (emission allowances, energy and agriculture), and to move in parallel on the issues of commodities markets and derivatives markets in order to avoid any inconsistency or loopholes. In addition CESR also stressed the importance of international coordination.

More specifically concerning energy markets, there was general support for the CESR-ERGEG conclusions. Several delegations expressed the need to put in place adequate coordination between energy and financial regulators. We will have to clearly define who is responsible for oversight and who is responsible for enforcement. CESR added that we should look at what kind of administrative arrangements could be put in place to facilitate the cooperation between energy and financial regulators. One of the delegations was of the view that it would make sense to extend the tailor made market abuse regime to be developed for energy spot markets to spot emission allowances.

One delegation asked why metals are not included in the energy markets work stream. Another delegation raised the question whether further consideration should be given to oil and coal markets, in addition to metal markets.

6. DERIVATIVES

The Commission gave a short update on its work on derivatives, in particular a brief outline of the contents of the upcoming second Communication on derivatives markets. The floor was then given to Member States to express their views on this issue.

Some Member States took the floor to ask for additional clarifications on the treatment of non-financial companies under the upcoming Commission proposals. In this context, one Member State noted that the Commission's approach would seem to differ from the one contemplated in the US, where legislators appeared to be contemplating the possibility of exempting non-financial companies from legislation.

A second issue that was raised was that of supervision of central counterparties (CCPs). One Member State pointed out that CCPs could probably be considered as natural monopolies that have important implications (i.e. externalities) for Member States other than the one in which they are located. Therefore, the Member State argued, coordinated supervision of this entity is essential; from this point of view, the European Securities Markets Authority (ESMA) could have an important role. Another Member State pointed out that, in line with the discussions on the future structure of supervision in the EU, supervisory powers should remain with national authorities, because fiscal responsibility would remain with the Member State where the CCP is located.

One Member State also highlighted the importance of having more over-the-counter (OTC) derivatives traded on organised venues. Another one indicated that it would like to see the

Commission promote the use of CCPs and trade repositories located in the EU, both for prudential and data protection reasons. Finally, a Member State expressed its doubts about the possibility of mandating the use of CCPs and organised trading venues, stating that, in line with G20 declarations, such solutions should be mandated only where appropriate.

On the treatment of non-financial companies the Commission replied that as beneficiaries of the use of derivatives markets they would probably need to bear their share of the burden of upcoming regulation. This share would probably be smaller than the one that financial companies would need to bear, as non-financial companies are usually not of systemic importance. The Commission also pointed out that granting blanket exemptions could create loopholes which could be exploited to circumvent regulation.

On the issue of the location of infrastructures, the Commission pointed out that, in case of credit default swaps, it did ask the industry for a commitment to clear these products on EU-based CCPs. For what concerned trade repositories, the Commission stated that whether or not the same type of approach would be used would largely depend on whether EU authorities would have full and unencumbered access to information stored in repositories located outside the EU.

On the issue of mandating the use of CCPs and organised trading venues for standardised OTC derivatives, the Commission stressed that the reference to "where appropriate" in the G20 statement applied only to the latter, but not the former.

7. PROSPECTUS DIRECTIVE

The Commission services presented the proposal adopted by the Commission for the review of the Prospectus Directive.

The delegations of the Member States who took the floor generally expressed their support for the proposal, in particular in relation to the provisions on SME. Some feared that the relation between cost reduction and consumer protection could appear unbalanced. Some delegations expressed their concerns in relation to the €50,000 threshold in the exemption of Art. 3(2) of the Directive by requesting an increase of such thresholds. Also some delegations suggested boosting the €1,000 threshold of Art. 2(m)(ii) of the Directive to avoid forum shopping. In addition, in relation to the proposed extension of the validity of the prospectus, some concerns were raised on the readability of a prospectus with multiple supplements.

8. A.O.B

One delegation requested to have on the next agendas of the ESC meetings more points requiring contributions and an active participation from the Member States and less points for information. The same delegation with the support of another Member State requested to be updated at the ESC meetings on the work undertaken at the G20 level.