

ZENTRALER KREDITAUSSCHUSS

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Comments of the Zentraler Kreditausschuss¹ on CESR's revised draft Technical Advice on Possible Implementing Measures of the Transparency Directive

Ref.: CESR/05-267

27 May 2005

¹ The ZKA is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public-sector banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks financial group, and the Verband deutscher Hypothekenbanken (VdH), for the mortgage banks. Collectively, they represent more than 2,300 banks.

I. General remarks

The Zentraler Kreditausschuss (ZKA) thanks CESR for the opportunity to comment on the revised draft Technical Advice of Possible Implementing Measures of the Transparency Directive and welcomes the fact that, in many areas, responses to the preceding consultation papers have been taken into account and the draft technical advice for Level 2 measures has been revised accordingly. We take a positive view, for example, of the clarification that market makers wishing to make use of the exemption under Article 9(5) of the Transparency Directive are not required to create Chinese walls to be deemed independent when engaging in market making activity (cf. paras. 108 and 109). We also support CESR's position that no indirect disclosure requirement should be introduced for holdings below the 5% threshold set in Article 9 (cf. para. 370). Furthermore, we believe that the revised advice for implementing measures affecting investment firms marks a step in the right direction. Before going into these and some of the other questions raised in the consultation paper in detail, we should like to draw attention to three major concerns from our point of view.

Who should make the notification under Article 10 (paras. 174-181)

In our comments on the December consultation paper² concerning CESR's approaches to the issue of who should make the notification required under Article 10 of the directive, we favoured approach A. We argued that this was the only approach covered by the wording of the directive and that there was therefore no legal basis for more extensive regulation along the lines of approach B, which, moreover, would trigger a not inconsiderable number of additional, virtually meaningless notifications.

This consultation paper does not revisit these two approaches, but instead explains CESR's "new thinking" on Articles 9 and 10. The result of this new thinking, the revised draft technical advice on pp. 43-44, essentially reflects approach B of the December paper and is to be rejected for the reasons referred to above. We should like to set out our rationale once again in more detail.

Market practitioners assume that CESR's new approach would result in a doubling of notifications³, a large proportion of which would be virtually meaningless or even misleading. A good illustration is provided in paragraph 181, which describes the diverging view of one CESR member. Under CESR's proposed interpretation of Article 9, a shareholder giving a proxy over his voting rights would be treated as if he were disposing of his shares. This would de facto introduce a notification requirement for changes in voting instructions (Article 10(h)

² In our comments, the October consultation paper refers to document CESR/04-511 on dissemination and storage, while the December consultation paper refers to document CESR/04-512 c on notifications of major holdings of voting rights, half-yearly financial reports, equivalence of third countries information requirements and procedural arrangements whereby issuers may elect their home member state.

³ In Germany, from around 4,000 at present to an estimated 8,000.

in conjunction with Article 9(1)), which could trigger numerous notifications ahead of shareholders' meetings with the potential to distort the market. In any event, more notifications will not in themselves create more transparency. Furthermore, it should be borne in mind that a notification requirement of this kind could make proxy voting unattractive since legal uncertainty would sometimes arise as to whether a specific instruction had been issued within the meaning of Article 10(h) or whether a notification was required.

Legal considerations also argue against the interpretation in paragraphs 174-178. The wording of Articles 9 and 10 is unequivocal; there is no scope for interpretation. Article 10 focuses on the exercise of voting rights. The only persons therefore required to make notifications are those entitled to acquire, dispose of, or exercise voting rights. Under Article 9, on the other hand, the only persons required to make notifications are those who reach, exceed, or fall below one of the article's thresholds by acquiring or selling shares. CESR's interpretation of Article 9 in paragraph 178 as requiring persons to notify the acquisition or disposal of voting rights even if they do not acquire or dispose of any shares clearly conflicts with the wording of Article 9(1). The same applies to Article 9(2). The phrase "events changing the breakdown of voting rights" refers merely to circumstances such as a capital increase. These are the only "events" that change the voting rights per share and thus the "breakdown of voting rights".

But even an interpretation of Articles 9 and 10 would only confirm their wording. The predecessor Directive 2001/34/EC talks in Article 89(1), which regulates notification requirements associated with significant holdings, about the acquisition or disposal of a "holding", not a "holding of voting rights". It is therefore not "clear", as CESR claims, that Article 9 of the Transparency Directive refers to the acquisition or disposal not only of shares, but also of voting rights. Member states have interpreted the term "holding" differently when implementing the directive in national law. The European legislators had the opportunity to put an end to this practice – the corresponding national law in Germany, for example, requires notification only of the acquisition and disposal of shares – with clear wording in Article 9(1) at Level 1. They opted not to do so, but confirmed the above implementation alternative by using the term "shares" in Article 9(1).

In consequence, even an interpretation of Article 9(1) could only confirm the already unequivocal wording of Article 9. CESR's revised draft Technical Advice on pages 43 and 44 thus goes beyond the authority granted it at Level 1.

The circumstances under which the shareholder, or the natural person or legal entity referred to in Article 10 should have learnt of the acquisition or disposal of shares to which voting rights are attached (Sec. 5)

We continue to be unconvinced by the advice in para. 269 proposing that a person should be deemed to have knowledge of the acquisition or disposal of shares or voting rights one day after the transaction. We entirely share the diverging view of the CESR member outlined in paras. 258-260. To avoid repetition, we should like to refer you to the arguments in our reply to question 14 of the December consultation paper⁴. In a nutshell: a period cannot start running until the event triggering the period has occurred.

Furthermore, we believe it is open to question whether CESR's proposed definitions of the execution of a transaction will always provide sufficient legal certainty. Focussing on the matching of orders for transactions taking place on an exchange is unlikely to pose any problems. It is doubtful, however, whether the term "meeting of the minds" selected for off-exchange trades will really enable those required to make notifications to pinpoint the time of execution. The term is vague and gives those involved considerable room for interpretation with the result that the desired harmonisation might ultimately not be achieved. It would therefore be in the interests of legal certainty if, for off-exchange trades at least, a transaction were considered executed when the acquirer actually became the owner of the share.

Information disclosable under the Prospectus Directive

If the intention is to retain CESR's original proposal (cf. para. 652) whereby issuers would be required to make available to the central storage systems the information that has to be disclosed under the Prospectus Directive, we reiterate our categorical rejection of such a rule. Neither the Transparency Directive nor the Prospectus Directive establish a requirement for issuers to make available the information that has to be disclosed under the Prospectus Directive to the central storage mechanisms. On the contrary, Articles 21 and 22 of the Transparency Directive show that there is in fact no such requirement: Whilst Article 22 of

⁴ The notification requirement and the commencement of the notification period are geared to the acquisition or disposal of voting rights. The acquisition or disposal is, however, only completed once the shareholder has acquired or (in the case of disposal) lost title to the shares. This is the case on the value date. Only once the shareholder has or should have obtained knowledge thereof does the notification period commence under Article 12 (2) (a) of the Transparency Directive. Otherwise the notification period would commence before the notification requirement is triggered. An approach geared to the date of execution of the transaction would therefore also shorten the notification period. We thus suggest gearing commencement of the notification period to the value date. This is unlikely to lead to an excessive lack of homogeneity within the EU because a settlement cycle of T+2 to T+3 is the standard throughout Europe. Compared with the approach proposed by CESR, the delay for market participants would probably be one trading day here. This appears quite reasonable, particularly as, according to its wording and purpose (notification of an **existing** proportion of voting rights), Article 12 (1) (a) of the Transparency Directive is geared to acquisition/disposal under property law. At any rate, knowledge of the acquisition or disposal should not be assumed to have been obtained any earlier than one day after the execution of the transaction.

the Transparency Directive, which deals with the creation of an electronic information network, expressly includes for this purpose the information that has to be disclosed under the Prospectus Directive, Article 21(1), sentence 1, of the Transparency Directive refers only to so-called “regulated” information, and not to Prospectus Directive information. This legislative decision at Level 1 of the Lamfalussy process for the Transparency Directive, which incidentally is in line with the Commission’s proposal, cannot now be negated by the Commission at Level 2 or by guidelines within the meaning of Article 22 of the Transparency Directive. We therefore firmly reject requiring issuers to make available, at considerable expense, the Prospectus Directive information to the central storage mechanisms although they are not required to do so at Level 1. This applies all the more given that the one-stop shop for investors can also be created by other means.

CESR also took this view in its Progress Report⁵, at least as far as the dissemination of information is concerned. On the issue of storage, it suggested that how Prospectus Directive data is fed into the electronic network should depend on the situation in individual member states (cf. paras. 138 to 143 of the report). Even if the proposal in para. 660 is not part of the final advice, we strongly advocate that CESR should refrain from including a corresponding proposal in the explanatory text to the final advice or should at least make it consistent with the Progress Report.

II. Specific comments

Chapter I: Dissemination of regulated information by issuers

Q1: Do consultees agree with the above proposal?

No. The decisive criterion is pan-European dissemination of the prescribed information. Provided that this is ensured, it does not matter which media are used to transmit the information. We do not believe there is any justification for restricting the flexibility of issuers and service providers as long as pan-European dissemination is ensured.

Q2: What distribution channels do consultees consider should be mandated? Please provide reasons for the answer.

CESR should not make any specific distribution channels mandatory (see reply to question 1).

⁵ Ref. 05 – 150b of March 2005.

Q3: Do consultees consider that CESR should mandate that the connections between issuers (either directly or through a service provider) and media be based on electronic systems, such as dedicated lines?

No. In particular, CESR should not make it mandatory to maintain dedicated lines between issuers and the media. Such a costly solution is not necessary given that information can now be transmitted swiftly and securely over the internet. It should merely be ensured that price-sensitive information, in particular, is always sent over the internet in a secure manner. Concrete details should be left to the parties involved and will be regulated by market forces. We nevertheless support the possibility of disseminating the data to the media and operators electronically.

Q4: Do consultees consider that a specific method should be mandated? Which one? Please provide reasons for your answers.

No. See our reply to question 3.

Q5: Do consultees agree with the approach of redrafting the required field of information, as proposed above?

Yes.

Q6: Do consultees consider that a specific method of issuer identification should, in addition, be mandated (such as the identification number in the companies registrar or the ISIN)? Which of these? Please provide reasons for the answer.

No.

Q12: Do consultees agree that media should not be charged by service providers to receive regulated information to be disseminated by them? Please provide reasons for the answer.

CESR should refrain from proposing any rules concerning which costs should be borne by whom. It should be left to the parties involved, i.e. the issuers, service providers and media, to negotiate such issues.

Q13: Do consultees consider that it is possible, on a commercial basis, to mandate that media receive regulated information for free from service providers? Please provide reasons for the answer.

See our reply to question 12.

Q14: Do consultees consider it useful and practicable to require a document from service providers showing how they meet the dissemination standards and requirements? Please provide reasons for the answer.

A document of this kind would be useful to issuers if it enabled them to exempt themselves from liability at least in the event of administrative proceedings and demonstrate that they had taken all necessary steps to ensure that the regulated information was disseminated to the media. Otherwise, the matter should be left to the parties involved.

Q15: Do consultees consider that CESR should undertake, at level 3, future work on how to address the concerns raised on how approval of operators is to work, even if approval is not mandatory? Please provide reasons for your answer.

Yes, we consider it would be useful for CESR members to reach an understanding at Level 3 that a service provider which has been approved in one member state will also be recognised in others. This will improve legal certainty both for the service provider and for the issuer using its services.

Chapter II: Notifications of major holdings of voting rights

Section 1: The maximum length of the short settlement cycle for shares and financial instruments if traded on a regulated market or outside a regulated market and the appropriateness of the T+3 principle in the field of clearing and settlement

The advice in para. 91, which would make T+3 mandatory also for shares traded outside regulated markets, still fails to convince in our opinion. The parties involved in transactions outside a regulated market normally agree on settlement cycles on an individual basis under existing freedom of contract rules. The exemption under Article 9(4) should therefore be applicable in this area for the length of the settlement cycle agreed by the parties or at least for a longer period, such as ten days. Otherwise, misleading notifications would be triggered since the person acquiring the shares for the purpose of clearing and settlement has no interest whatsoever in exercising any influence on the management of the issuer. We hope that our proposal will be reflected in CESR's final advice. A lack of consistency in the suggested alternatives to the T+3 timeframe for shares traded outside a regulated market should not be the decisive factor in advocating the extension of the T+3 principle to such trades (cf. para. 78).

Section 2: Control mechanisms to be used by competent authorities with regard to market maker and appropriate measures to be taken against a market maker when these are not respected.

Q16: Do you agree with this change? Please provide reasons for your answer.

Yes. The expression “any of the rights attached to the shares” could refer to many rights that have nothing to do with the possibility of exerting influence on the issuer. The reference to “voting rights” therefore makes good sense in our view. Methods of influencing the issuer other than by exercising voting rights are covered by the phrase “to use the shares to influence the management of the issuer concerned”.

Q17: Do you agree with this change? Please explain.

Yes, we welcome the clarification that market makers wishing to make use of the exemption under Article 9(5) are not required to create Chinese walls. It is now proposed in para. 110 that firms should prove that there is no conflict of interests by identifying the other activities they are conducting in relation to the issuer. Since, in practical terms, this proof will be provided during an inspection by, or at the request of, the competent authorities, we suggest replacing the word “identified” with “identifiable” or “identified on request”. This would describe the requirement to be met by market makers more precisely.

Q18: Do you agree with the proposed changes to this advice? Please explain.

Yes.

Section 6: The conditions of independence to be complied with by management companies, or by investment firms, and their parent undertakings to benefit from the exemptions in Articles 12(4) and 12(5).

The proposed test of independence

According to para. 309, CESR considers it necessary for the persons who decide how the voting rights are to be exercised not to be the same for the parent undertaking and a subsidiary. To satisfy this requirement, however, it should be sufficient if the persons are different at the level actually involved in deciding how the rights will be exercised. The intention should not be to prescribe an arms-length relationship between staff at parent undertakings and subsidiaries right up to senior management level. Close links between the subsidiary and the parent undertaking are needed at management level to enable the parent to exercise effective oversight of its subsidiaries.

Q20: Do you consider there to be any benefit by CESR retaining its original proposals and requiring a subsequent notification from the parent undertaking when it ceases to meet the test of independence?

No. We totally agree with CESR's conclusions in para. 331 and therefore support the proposal in para. 332. The competent authority learns anyway from the parent company's notifications that the exemption is no longer being made use of. An additional specific notification would therefore only create more red tape.

Q21: What are your views on this new definition of indirect instruction?

We believe the narrower definition is a step in the right direction, but is not yet sufficiently unequivocal. The expression "specific interests" could also cover group-wide corporate governance principles, for example, thus making their application impossible. It would therefore be better to use the term "specific business interests".

Section 7: Standard form to be used by an investor throughout the Community when notifying the required information

Q22: Do you agree with this approach in relation to Article 12(1)(d)? Please give reasons.

Yes, we expressly welcome CESR's proposal since a notification requirement is triggered under the Transparency Directive only when the 5% threshold is reached, fallen below or exceeded.

Q23: What do you think the resulting situation information disclosure should be when the notification is of a holding below that of the minimum threshold?

In these cases, too, it should only be necessary to report that the holding has fallen below the 5% threshold. A requirement to indicate what percentage is still held would introduce a notification requirement for holdings below 5%. The directive envisages no such requirement. It assumes that holdings below the 5% threshold are not relevant for the market. Such notifications are therefore not necessary.

Section 8: Financial instruments

We should like to clarify that the notification requirements under Articles 9 and 10 and those under Article 13 are to be considered separately. This applies above all when calculating whether or not thresholds have been exceeded. Aggregation of the circumstances triggering the various notification requirements would mislead the market since ownership patterns would be suggested that did not in fact exist. The separate form for notifications under Article 13 on pp. 78 ff. indicates that CESR also seems to assume this distinction.

Chapter IV: Equivalence of third countries' information requirements

Q26: Do you agree with these principles?

Under the approach selected by CESR the key criterion for evaluating the equivalence of financial information is the needs of the investor. To be recognised as equivalent, information under the law of a third country must offer the investor a basis on which to make an investment decision comparable to that provided by EU transparency requirements. We consider this approach appropriate and agree with the principles. They are consistent with those forming the basis of the “Draft Technical Advice on Equivalence of Certain Third Country GAAP”⁶.

⁶ Cf. document CESR/05-230.