

Set up in 1960, the European Banking Federation is the voice of the European banking sector (European Union & European Free Trade Association countries). The EBF represents the interests of some 5000 European banks: large and small, wholesale and retail, local and cross-border financial institutions.

The EBF is committed to supporting EU policies to promote the single market in financial services in general and in banking activities in particular. It advocates free and fair competition in the EU and world markets and supports the banks' efforts to increase their efficiency and competitiveness.

EBF's response to CESR's call for evidence on mutual recognition with non-EU jurisdictions (Ref.: CESR/09-406b)

Key Points

- 1. The EBF is a strong defender of global financial markets integration. Mutual recognition, rule exemptions and targeted rules convergence are all adequate gateways to achieving that objective.**
- 2. Mutual recognition initiatives should be prioritised with those countries where the potential efficiency gains are to be the highest (e.g. the US). That said, the EBF is supportive of exploring agreements with other countries where political predisposition towards mutual recognition is higher.**
- 3. Mutual recognition initiatives should concentrate, first and foremost, on secondary securities markets and - within this segment - on wholesale business.**
- 4. Parties involved in mutual recognition process should adhere to applying a “top down” approach based on an approximation in regulatory outcomes, principles and objectives.**
- 5. Delivering improved third country market access and regulatory simplification of cross-border business is an EBF priority. CESR is invited to interest the SEC in the release of a final ruling on the reform of Rule 15a-6.**
- 6. On the basis of a mutual recognition agreement, “recognised” European intermediaries should be able to provide cross-border services to foreign wholesale investors without complying with the third-country’s conduct of business rules.**
- 7. Progress on mutual recognition will very much depend on the respective enforcement authorities’ ability to find comfort with regard to the comparability of their enforcement structures, powers, processes and cultures.**

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General comments

1. The European Banking Federation (EBF)¹ welcomes the opportunity to comment on CESR's call for evidence on mutual recognition with non-EU jurisdictions. The EBF is a **strong defender of global financial markets integration**. Integration can potentially eliminate barriers to business that currently cause additional costs associated with compliance with different rules. It has been estimated that only the integration of transatlantic financial markets would produce \$48 billion worth of savings in transaction costs per year from securities trading alone leading to an approximate 50% increase in transaction volumes².
2. As CESR rightly identifies in its paper, mutual recognition is one of the main means to facilitate cross-border activities in financial services. Recognition has the benefit of not necessarily requiring regulatory changes and is most effective when regimes are sufficiently comparable. In line with CESR's statement that the three approaches are not mutually exclusive, European banks will also welcome **rule exemptions** offered unilaterally by third countries and opportunities for **targeted rules convergence** (i.e. standardisation) notably as these may pave the way for taking forward an agreement on mutual recognition.
3. EBF agrees that CESR should prioritise efforts on mutual recognition with those countries and in those areas where the potential efficiency gains are to be the highest. In this respect, the **U.S. remains the most attractive market**. Having said that, a degree of realism is necessary to manage expectations as to the precise results that can be achieved in the current scenario. Whilst the initial steps with the US last year have been encouraging - as CESR recognises in its paper - the next arguably more problematic steps would have to be taken against an uncertain regulatory, economic (and to an extent, political) outlook in that country.
4. The EBF is, therefore, supportive of **enlarging the scope of possible candidates** with whom the EU could eventually negotiate a mutual recognition agreement. In this regard, the EBF wishes to recall that other, smaller jurisdictions have expressed a keener interest for mutual recognition initiatives³. The EBF recommends CESR to concentrate its effort in jurisdictions where political predisposition towards mutual recognition is higher. The idea of a **pilot exercise with one selected jurisdiction** should merit high consideration.
5. At the same time, the EBF recognises and underlines the great importance of the February 2008 Statement by the European Commission and the U.S. Securities and

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² See Deutsche Bank Research (June 2008) *EU-US Financial Market Integration – a Work in Progress* http://www.dbresearch.com/PROD/DBR_INTERNET_EN-PROD/PROD000000000225963.PDF

³ For example, in the South-Pacific area, Australia and New Zealand have agreed a Mutual Recognition Arrangement that will allow an issuer to offer securities or interests in collective or managed investment schemes in those two countries using one disclosure document prepared under regulation in its home country. Another example is the Australia - Hong Kong Declaration of Mutual Recognition that facilitates cross-border offers of managed funds to retail investors in both countries.

Exchange Commission on Mutual Recognition in Securities Markets⁴. As the most important trading partner in financial services, the EU has a strong interest in making decisive progress towards a barrier-free US-EU financial market. The Statement marks an important step, and both sides can greatly benefit from intensifying their work on that basis.

6. In this connection, however, the Federation considers that **ongoing regulatory reform legislation in the US and the EU could benefit from more coordination**. Any regulatory fragmentation resulting from the current regulatory reform process would not only reduce efficiency and distort competition in transatlantic and global financial markets, but also create very significant barriers to future efforts of mutual recognition, convergence of rules or unilateral rule exemptions in the field of securities rules and elsewhere.
7. In terms of material scope, the EBF recommends:
 - To fold the three areas identified in the consultation paper (i.e. trading venues, intermediaries and products) into two: primary and secondary markets – i.e. the issuance and trading of securities. The existing distinction in the consultation paper between trading venues and intermediaries is at odds in the European space with MiFID as the latter allows investment firms across the EU to internalise flows as trading venues in their own right.
 - To concentrate first and foremost, as priority areas for action, on the potential for mutual recognition in respect of **secondary securities markets and - within this segment - on wholesale business**.
 - In addition, it might be useful to examine which other areas of the securities business can be improved in that way. Such examination should, however, not stand in the way of advancing the priority areas identified above.
8. The EBF believes that in order to mitigate possible prejudices around the establishment of a mutual recognition system in securities trading in the wholesale business space, the parties concerned should adhere to applying a **“top down” approach based on an approximation in regulatory outcomes, principles and objectives**. In this regard, the EBF advises CESR not to concentrate on a rule-by-rule comparison between the EU framework and any given particular jurisdiction but on whether those rules are consistent with a globally agreed framework such as on a *revised* set of IOSCO Principles.⁵ Furthermore, the Federation encourages CESR to do some exploratory work of what might be possible metrics for comparing regulatory outcomes.

⁴ Statement by the European Commission and the U.S. Securities and Exchange Commission on Mutual Recognition in Securities Markets. Securities and Exchange Commission and EU Commission. Washington. February 2008.

⁵ In 1998 IOSCO published its report *Objectives and Principles of Securities Regulation*. The Report established 30 principles for securities regulation with the specific purpose of protecting investors, ensuring market integrity and transparency and reducing systemic risk. On the basis of the principles establishing well regulated jurisdictions that have been endorsed by 100 IOSCO member jurisdictions and therefore apply to 90% of the world's securities and other financial markets, the IOSCO Principles provide a sound and internationally acceptable framework within which to deliver regulatory recognition over the coming years. However, it is generally considered that IOSCO's Principles require significant further work to serve as a benchmark for mutual recognition frameworks in the future.

9. IOSCO could also be instrumental in managing **potential issues of extraterritoriality** of rules (for example, in the area of investor protection) and financial stability. The EBF welcomes, in particular, the establishment by IOSCO of a Task Force on Supervisory Cooperation that will consider the manner in which regulators cooperate in the supervision and oversight of market participants whose operations cross borders⁶.
10. Additionally, the EBF believes that mutual recognition should be underpinned by a set of **globally standardised definitions**. The lack of a common understanding of what is meant by the concept of mutual recognition or terms such as wholesale business, for example, makes a principles-based assessment of the different regulatory frameworks less straightforward.

Specific comments

a) Market access

11. Delivering **improved third country market access and regulatory simplification** of cross-border business is a priority for the EBF. As CESR acknowledges, the provision of investment services to professional investors in third countries represents a significant activity for major and mid-sized European banks with investment activities. As the provision of investment services in those countries (as in the EU) is a regulated activity, European banks are required to obtain a license. Licensing means submission to the third country's regulatory and supervisory oversight and to the local supervisor's enforcement authority.
12. The EBF recalls that there are two non-mutually exclusive ways to improving third-country market access whilst avoiding burdensome local licensing:
 - a) Recognising the authorisation of appropriately regulated foreign (say European) intermediaries
 - b) Exempting intermediaries from local licensing requirements. Exemptions usually cover only certain transactions and investor types. Foreign (say European) firms may still be subject to certain local requirements that preserve a local regulator's ability to intervene.
13. Importantly, in the US context, an exemption already exist (i.e. SEC Rule 15a-6) that permits non-US persons (say European) to make securities-related contacts with certain types of institutional investors without registering under the Exchange Act, provided some conditions are met. In March 2008, the SEC announced its intention to flexibilise Rule 15a-6 to substantially reduce the more burdensome areas in the existing ruling (e.g. notably the so-called chaperoning and recordkeeping requirements). In its announcement, the SEC said that **reform of Rule 15a-6 is one of the actions that need be taken to further the implementation of the concept of mutual recognition** between the EU and the US. However, reform of rule 15a-6 seems to have stalled. Consequently, the **EBF**

⁶ 34th Annual IOSCO Conference. Final Update. See at <http://www.iosco.org/library/statements/pdf/statements-6.pdf>
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recommends CESR to interest the SEC in the release of a final ruling in this respect. A revised Rule 15a-6 will have an impact on the material scope of any future mutual recognition agreement between the EU and the US.

b) Conduct of business

14. The EBF believes that any “recognised” European intermediary providing cross-border services to foreign wholesale investors should be able to provide its services **without complying with the third-country’s conduct of business rules** and other investor protection rules. In order to achieve that goal, a preliminary comparability assessment of key regulatory areas where divergences normally exist among different jurisdictions is crucial. We again refer to our earlier point (c.f. paragraph 7) that such comparability assessments are based on outcomes, principles and objectives rather than on individual rules. Those regulatory areas are the following:

1. Know Your Customer (KYC) requirements
2. Best execution requirements
3. Requirements to adequately manage conflicts of interest
4. Segregation of assets provisions
5. Information to customers requirements
6. Consumer protection arrangements

c) Enforcement

15. The EBF is convinced that **progress on mutual recognition will very much depend on the respective enforcement authorities’ ability to find comfort** with regard to the following: (i) that breaches of rules are properly investigated and enforced; (ii) the existence and soundness of a due process in reaching enforcement decisions; and (iii) the ability to share information and to co-operate on enforcement actions on a cross-border basis effectively while respecting national rules and practices.
16. The EBF believes that comparability on enforcement structures, powers, processes and cultures is a “red line” that CESR should address simultaneously to the investigation of the microeconomic analysis of potential benefits from market integration and the possible regulatory obstacles that a mutual recognition system could overcome in any given jurisdiction.

Concluding remarks

17. The ongoing financial and economic crisis has shifted the order of priorities with regard to financial markets regulation. The objective of increasing integration to which mutual recognition can be seen as instrumental is giving way to issues such as reinforcing transparency, strengthening investor protection and fortifying market integrity.
18. Financial markets regulatory reform cannot, however, be approached from a silo, national mentality. The financial crisis has demonstrated the interconnectedness of financial

markets and the need, therefore, to regulate and supervise the latter on an increasingly coordinated cross-border basis.

19. The EBF is, consequently, supportive of CESR's initiative to further explore possible ways to put cross-border securities activity on a sounder and more business-friendly footing. In this regard, the EBF is in favour of a pragmatic, long term and principles-based vision approach that combines an emphasis on mutual recognition with taking advantage of regulatory exemptions and standardisation.
20. The EBF looks forward to CESR's ensuing consultation paper on the technical analysis on possible criteria and procedures that could be taken into account for mutual recognition and would appreciate the opportunity to pass on further views on those issues.