



9<sup>th</sup> September, 2009

The Committee of European Securities Regulators

**Reply of the Israel Securities Authority to the CESR call for evidence on mutual recognition with non-EU jurisdictions (CESR/09-406b) dated 8<sup>th</sup> June 2009.**

## **1. Preliminary Comments**

The Israel Securities Authority (ISA) is very supportive of CESR's forward looking and progressive work in launching this call for evidence on mutual recognition with non-EU jurisdictions.

The trend towards greater international diversification of investments, together with the huge development in the telecommunication infrastructures that support this activity, mean that cross-border movement of capital is now a permanent feature of all markets.

All regulators have recognized the international dimension of the recent financial crisis and the impact that globalised markets have had on domestic financial stability. Many EU regulators are currently focused on these issues. The ISA believes it is important to bring the current spirit of regulatory reform to bear also on the question of mutual recognition.

The ISA believes that a response to the crisis which treats cross-border activity as a threat will be counter-productive and tend to increase the fragility and potential instability of domestic markets. Regulators need to use the current momentum of reform to embrace and harness cross-border activity.

Such an approach will benefit investors, capital markets, and financial service providers. By focusing on the question of mutual recognition, CESR is demonstrating its own confidence in the future and by doing so encouraging confidence in EU markets.

## **2. The ISA Response**

The call for evidence is directed primarily at market participants and not all the issues raised may be answered by the ISA. However the ISA would like to take this opportunity to supply a response of how a relatively sophisticated market and geographically close neighbour of the EU, views mutual recognition and closer integration with EU financial markets.

In addition to the ISA's response, the Tel Aviv Stock Exchange (TASE) has also prepared its response to the issues relating to trading venues raised in the call for evidence. The TASE response is attached below as an Annex with the question of mutual recognition addressed on page 17.

### **3. Three Options – Standardisation, Exemptions and Recognition**

One of the central issues raised by CESR in the call for evidence is the question of which of the three paths (standardization, exemptions or recognition) offer the best way forward.

The ISA's position is that mutual recognition and standardization should be pursued in parallel. This two track approach would be more effective than pursuing either track alone. Each track will promote and inform developments in the other.

The ISA does not believe that the option of exemptions is itself a goal to be pursued. Exemptions (or a "no-action" response) will usually only be relevant in relation to specific requests from individual entities seeking specific exemptions.

The single most important factor in determining whether an exemption may be granted will, in nearly all cases, be the question of whether the entity is subject to regulation in its own jurisdiction which is considered by the host regulator to provide a sufficient level of investor protection (and perhaps also a satisfactory prudential framework). In other words, the basis and key questions in relation to nearly all exemptions is recognition of the foreign regulation.<sup>1</sup>

In this sense, the ISA views exemptions as being a derivative of recognition. Granting exemptions is a useful tool for regulators, allows greater flexibility in individual cases and indeed may have a role to play for a long time to come. However, exemptions differ importantly from standardisation and mutual recognition in that they are not part of a long term strategy to harmonise regulation between different countries.

This goal of greater harmonization of regulation in EU and non-EU countries is the key feature that standardization and mutual recognition share. Indeed the ISA sees them as two sides of the same coin.

Standardisation is essentially the early, theoretical stage of full harmonization of written regulation. Mutual recognition on the other hand is more directly concerned with the practical integration of markets. Standardisation could be seen as the macro architecture of the process of harmonization whilst mutual recognition is more relevant to the micro day to day cross-border integration of markets, service providers and investors.

Mutual recognition promotes harmonization and integration in a number of ways:

- It facilitates cross-border investment activity – increasing activity of non-Europeans in the EU markets and EU investors outside EU – thus spreading

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<sup>1</sup> Other factors, such as the financial strength of the entity or the expertise of its personnel, may also be considered but generally if the entity is not subject to adequate regulation in its home country, an exemption will not be possible.

knowledge of how other markets work and increases practical day to day integration.

- It provides economic benefits to investors, market participants, trading venues and issuers - primarily through the benefits to investors that flow from deeper liquidity and greater diversification of exposure.
- It encourages detailed cooperation and interaction between regulators. Some examples may be given:
  - It causes regulators to develop the methodology of the administrative process of integrating regulation of different jurisdictions. The very close interaction and cooperation that is required for both sides to be able to reach a point where they are able to accept each other's regulation as being of a standard to permit mutual recognition is a crucial element of a harmonised regulatory environment.
  - Integration of market activity has a ripple out effect – it throws up other questions and issues which regulators must find solutions to. A key example is the field of enforcement. Cross-border activity will often raise enforcement issues that are best solved by consultation and cooperation between regulators.
  - Similarly, cross-border activity will throw the spotlight on general legal issues. A good example is the question of sanctions. Where significantly different sanctions exist between EU and non-EU jurisdictions (or even between different EU countries) the resulting tension will feed back into the debate on standardization.

This last point concerning sanctions is a good example of the strength of the two track approach. The experience of mutual recognition should lead regulators back into discussion of standardization in new regulatory areas and push regulators to set out new global recommendations and standards. In this way mutual recognition and standardization actively promote and develop each other and in so doing are the engine driving greater harmonization of regulation.

#### **4. Modular approach to mutual recognition**

The decision of CESR to highlight three different areas of investment activity (trading venues, intermediaries and products) suggests that CESR expects mutual recognition to be introduced on a modular basis, i.e. in relation to different areas of activity as and when they reach a sufficient level of equivalency. The ISA supports this idea. There is no reason for mutual recognition of, for example, mutual fund offerings to be held up because regulation of portfolio managers is not yet equivalent.

Many jurisdictions outside the EU have particular areas of regulation that follow the same basic lines as EU regulation.<sup>2</sup> Once such a position is reached, mutual

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<sup>2</sup> The comparative level of each country's wider economic development is also of course a key issue here as well.

recognition is also a crucial catalyst to increased market integration and closer regulatory harmonization.

To try to reach harmonization on the basis of theoretical standardization alone is the less efficient approach. Regulation must remain close to the market and connected to it. Theory is important but the day to day lessons of actual market integration which follow mutual recognition are the safest guide of how best to further harmonise regulation.

Once a sufficient equivalency of regulation appears to be in place in a particular area of investment activity, mutual recognition should be actively pursued as a crucial step towards the safe integration of different markets.

## **5. Competition**

The Introduction to the CESR call for evidence contains the following important comment: "Mutual recognition presumably does not create a level playing field across borders since rules already established continue to exist and are simply mutually accepted. Differences in these rules may cause competitive distortions between the market participants of the participating jurisdictions."

This statement arises out of the conception of mutual recognition as a goal in itself at the expense of standardisation. The need to embrace mutual recognition, not as a goal in itself, but as a productive stage in a process of cross-border regulatory harmonization and market integration must always take into account the important role that standardization plays in this process.

It is certainly the case that mutual recognition may cause some competitive distortions between local and foreign firms. However, by the time regulation can be pronounced close enough to support mutual recognition the scope for these regulatory gaps (which may impose greater costs on one or the other of the participants) should have been narrowed significantly. Rather, the 'competitive distortion' is more likely to be found in the fact that suddenly very large multi-national financial institutions will gain access to markets that have been somewhat insulated from them by strict and detailed local regulation.

From the perspective of the Israel market looking at closer integration with the EU, this is a very real concern of many Israeli investment firms. Whilst the primary goal of the ISA is investor protection it will listen carefully to the concerns of local providers.

The question of the long term benefit to local investors is difficult to gauge in these circumstances. Regarding reductions in prices paid to service providers and trading venues as a result of the increased competition that cross-border activity creates, the evidence is still very limited and hard to draw conclusions from. CESR's own recent report on the Impact of MiFID on equity secondary markets functioning (Ref. CESR/09-355) clearly shows that even a massive increase in competition does not necessarily lead to meaningful reduction of costs although the reasons for this may stem from many different factors.

## **6. The basis of mutual recognition - what is equivalency?**

Of the four FSAP Directives which make up the group of "Lamfalussy Directives", only two, the Prospectus Directive (2003/71/EC) and the Transparency Directive (2004/109/EC), contain provisions that permit the recognition by EU regulators of parallel third country regulation. This term "equivalency" is the basis of the threshold for recognition required by the Directives.

The absence of any reference to the concept of equivalency in the Markets in Financial Instruments Directive (2004/39/EC) means that in its current form member states do not appear to have the option of recognizing foreign regulation as equivalent to their own in any of the many business areas covered by MiFID.

This is an important omission from MiFID. Currently any non-EU investment firm or exchange wishing to do business within the EU must apply to a member state of its choice for the necessary local license. If one accepts the principle of mutual recognition as a positive and effective way to promote and achieve harmonization of international regulation, then this omission is negative in its effect and may act as a barrier to recognition of EU regulation outside the EU.

The protection afforded to EU investment firms by this omission may act to dampen enthusiasm for recognition of EU regulation outside the EU. Despite this the ISA has recently taken some important steps towards unilateral recognition of foreign regulation (see section 7 below). However, the situation would be far healthier if mutual recognition, based on a thorough investigation of equivalency by the EU regulator, was at least permitted.

The current situation undoubtedly has a negative effect on the international profile that EU markets could otherwise achieve outside the EU. Mutual recognition is after all an important tool for both EU and non-EU regulators to improve access to their markets. Ironically, such an improvement in profile and market access would be likely to benefit EU investment firms since it would be they that would facilitate a significant proportion of the growth in capital movement to the EU that mutual recognition within MiFID would almost certainly promote.

## **7. Unilateral recognition of foreign regulation by the ISA**

The ISA has already taken some important steps towards unilateral recognition of foreign regulation in a number of areas.

These steps are clear evidence of the ISA's commitment to opening up the Israeli market to foreign products and service providers in order to offer a greater range of investment options to the Israeli market and improve the already generally high standard of investment services in Israel.

### Investment advisors and portfolio managers

Regarding unilateral recognition of foreign intermediaries, the ISA is currently introducing legislation that takes a first step in this direction. Amendment 11 to the Regulation of Investment Advice, Investment Marketing and Investment Portfolio

Management Law, 1995 ("the Investment Law") will for the first time open up the Israeli institutional and retail market to foreign investment advisors and portfolio managers.

Currently any non-Israeli intermediary wishing to offer investment advice and/or management services must comply with all the licensing conditions applying to Israeli providers, including even the requirement that the provider be an Israeli corporation (which includes a foreign corporation that has registered itself as such with the Israeli Registrar of Companies) or person (which includes a foreign national resident in Israel). Amendment 11 will introduce changes in the law designed to facilitate the entry of foreign advisors and managers into the Israeli market. Following enactment of the amendment, certain foreign providers of advice, marketing and management services will be entitled to be active in Israel without the need to receive a license as currently described in the law. Amendment 11 creates two new ways that this may occur:

1. The foreign intermediary will be able to enter into an arrangement with an Israeli licensed intermediary, whereby the local intermediary will bear full regulatory liability for the activities in Israel of the foreign intermediary. Since this route to the Israeli market allows Israeli investors recourse to a local provider, it is intended that this arrangement will be open to all foreign intermediaries without any additional conditions such as the quality of its home regulation or its capital
2. In relation to portfolio management for sophisticated investors, there will be a second option however it will only be available to intermediaries with significant equity levels that are licensed in jurisdictions where the ISA has found the regulation to be equivalent to the parallel Israeli regulation i.e. based on unilateral recognition. Broadly, it appears that full transposition of MiFID into local regulation will permit recognition by the ISA of the EU member state's regulation on portfolio management. However, more work on this is required and there may be specific issues that the ISA will need to examine on a state by state basis within the EU to see how transposition has been achieved.

A strong example of this would be implementation of the requirement in the implementing directive to "to employ personnel with the skills, knowledge and expertise necessary for the discharge of the responsibilities allocated to them"<sup>3</sup>. ISA regulation contains an extensive study curriculum for up to six examinations and a period of in-house training before a license may be granted.

As stated, foreign intermediaries that are licensed by their local EU regulator, would be permitted to solicit for new business and provide services directly to sophisticated clients in Israel.

### Collective Investment Schemes

Another area in which Israel is currently moving towards unilateral recognition of foreign regulation is in the area of collective investment schemes (CIS). The ISA has formulated an important amendment to the Joint Investment Trust Law, 1994, known

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<sup>3</sup> Article 5(1)(d) of Commission Directive 2006/73/EC

as Amendment 13. This has been drafted and is currently in the early stages of the legislative process.

Under Amendment 13, regulation will be created that stipulates the conditions under which a foreign CIS manager will be entitled to offer its fund units in Israel based on the scheme's home regulation without the need to comply with Israeli regulation. The said regulation has not been finalized however, the key element will certainly be the question of the equivalence of the applicable foreign regulation. It is likely that investment policy and the characteristics of a fund's manager will also be relevant, but only once the basic equivalency of regulation is established.

### Duel Listing

This important example of ISA unilateral recognition of foreign regulation has been in force since 2000 and currently there are around 50 duel listed companies on the Tel Aviv Stock Exchange (TASE).

This regime allows equity and debt issuers on certain recognized stock exchanges outside Israel to complete a secondary listing on the TASE using the prospectus and ongoing reports that it files in the foreign jurisdiction. Duel listing is of direct benefit to the Israeli market in bringing these listings to Israel, however it also played an important role in directing ISA thinking towards the ides of recognition of foreign regulation.

These examples of unilateral recognition demonstrate the ISA's willingness to open the Israeli market to international products and services so long as they comply with acceptable regulatory standards.

However, it should be stated that the ISA's experience of unilateral recognition has been that it does little to push forward the process of harmonization. Whilst it does bring benefits for investors and market participants, its impact on harmonization of regulation is very limited. In particular, since the process is unilateral, it does not lead to discourse and cooperation between regulators.

## **8. Mutual recognition – steps already taken**

Unlike with unilateral recognition, the ISA's experience of working with some EU regulators and CESR itself on mutual recognition of prospectus regulation has been extremely positive. The process of cooperation and consultation with a number of EU regulators that resulted in mutual recognition was extremely positive and beneficial and had a very real impact on the future direction of the development of Israeli regulation towards closer harmonization with the EU.

## **9. Overview of the Israeli Market**

The market in financial instruments in Israel is generally of a sophisticated level, both in terms of the products available and the investment services offered. The information in this section seeks to describe that market in the context of EU markets.

Israel has recently been classified as a developed market by both the leading index firms, FTSE and MSCI.<sup>4</sup> The EU countries included in the MSCI Developed Market Index are Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Netherlands, Portugal, Spain, Sweden and the United Kingdom

The main stock exchange in Israel is the Tel Aviv Stock Exchange (TASE). The tables below offer a comparison of TASE activity with regulated markets in the Europe.

The first three tables relate to activity in equities. As the data indicates, the characteristics of the TASE are those of a fairly typical EU exchange in terms of market capitalization, the number of companies listed and turnover.<sup>5</sup>

### **Equity Trading on TASE**

| Market Capitalization - Equity |                     |
|--------------------------------|---------------------|
| Exchange                       | Total Value (EuroM) |
| Euronext                       | 1,566,237.00        |
| London Stock Exchange          | 1,565,993.50        |
| Spanish Exchanges (BME)        | 776,184.41          |
| Deutsche Börse                 | 772,138.00          |
| SIX Swiss Exchange             | 601,207.23          |
| NASDAQ OMX Nordic              | 465,135.44          |
| Borsa Italiana                 | 379,165.21          |
| Oslo Børs                      | 113,528.13          |
| <b>Tel Aviv Stock Exchange</b> | <b>94,856.00</b>    |
| Athens Exchange                | 78,177.69           |
| Warsaw Stock Exchange          | 65,940.23           |
| Wiener Börse                   | 64,578.66           |
| Luxembourg Stock Exchange      | 58,112.27           |
| Irish Stock Exchange           | 37,751.07           |
| Prague Stock Exchange          | 28,932.90           |
| Budapest Stock Exchange        | 15,209.40           |
| Ljubljana Stock Exchange       | 9,215.75            |
| Bucharest Stock Exchange       | 6,793.34            |
| Cyprus Stock Exchange          | 6,574.65            |
| Bulgarian Stock Exchange       | 5,539.60            |
| Bratislava Stock Exchange      | 3,858.43            |
| Malta Stock Exchange           | 2,356.81            |

| Companies with Listed Shares   |                                     |
|--------------------------------|-------------------------------------|
| Exchange                       | No. of Companies with Listed Shares |
| Spanish Exchanges (BME)        | 3,517                               |
| London Stock Exchange          | 2,926                               |
| Euronext                       | 1,169                               |
| Deutsche Börse                 | 815                                 |
| NASDAQ OMX Nordic              | 806                                 |
| <b>Tel Aviv Stock Exchange</b> | <b>633</b>                          |
| Warsaw Stock Exchange          | 467                                 |
| Bulgarian Stock Exchange       | 399                                 |
| SIX Swiss Exchange             | 350                                 |
| Borsa Italiana                 | 295                                 |
| Athens Exchange                | 288                                 |
| Luxembourg Stock Exchange      | 259                                 |
| Oslo Børs                      | 243                                 |
| Bratislava Stock Exchange      | 187                                 |
| Wiener Börse                   | 118                                 |
| Cyprus Stock Exchange          | 117                                 |
| Ljubljana Stock Exchange       | 80                                  |
| Irish Stock Exchange           | 66                                  |
| Bucharest Stock Exchange       | 65                                  |
| Budapest Stock Exchange        | 44                                  |
| Prague Stock Exchange          | 25                                  |
| Malta Stock Exchange           | 19                                  |

PT<sup>4</sup> TP FTSE – decision published 20th September 2007, reclassification took effect June 2008.

MSCI - decision published 15th June 2009, reclassification will take effect from May 2010.

PT<sup>5</sup> TP Unless stated otherwise all data in the tables below is taken from the following sources:

EU exchanges data: The Federation of European Securities Exchanges, Statistics – available at <http://www.fese.be/en/>

TASE data: The Tel Aviv Stock Exchange, Statistics – available at <http://www.tase.co.il/TASEEng/Homepage.htm>.

Unless stated otherwise, all data is shown as of 30<sup>th</sup> June 2009.

| Value of Equity Trading, Year to Date |                                                     |                                                           |                 |
|---------------------------------------|-----------------------------------------------------|-----------------------------------------------------------|-----------------|
| Exchange                              | Electronic Order Book Transactions Turnover (EuroM) | Off - Electronic Order Book Transactions Turnover (EuroM) | Total Turnover  |
| London Stock Exchange                 | 664,444.8                                           | 673,731.1                                                 | 1,338,175.9     |
| Deutsche Börse                        | 531,931.6                                           | 418,696.7                                                 | 950,628.3       |
| Euronext                              | 669,803.0                                           | 0.0                                                       | 669,803.0       |
| Spanish Exchanges (BME)               | 421,350.2                                           | 122,725.8                                                 | 544,076.0       |
| Borsa Italiana                        | 310,690.2                                           | 0.0                                                       | 310,690.2       |
| SIX Swiss Exchange                    | 271,503.4                                           | 28,400.6                                                  | 299,904.0       |
| NASDAQ OMX Nordic                     | 252,919.2                                           | 30,098.5                                                  | 283,017.7       |
| Oslo Børs                             | 77,986.8                                            | 5,968.7                                                   | 83,955.5        |
| <b>Tel Aviv Stock Exchange</b>        | <b>30,075.0</b>                                     | <b>2,192.2</b>                                            | <b>32,267.2</b> |
| Athens Exchange                       | 19,008.2                                            | 1,403.8                                                   | 20,412.0        |
| Warsaw Stock Exchange                 | 16,296.6                                            | 444.8                                                     | 16,741.4        |
| Wiener Börse                          | 15,999.9                                            | //                                                        | 15,999.9        |
| Irish Stock Exchange                  | 3,242.9                                             | 8,999.9                                                   | 12,242.8        |
| Prague Stock Exchange                 | 8,444.8                                             | 39.5                                                      | 8,484.3         |
| Budapest Stock Exchange               | 8,048.9                                             | 6.2                                                       | 8,055.1         |
| Cyprus Stock Exchange                 | 627.0                                               | 43.5                                                      | 670.5           |
| Bulgarian Stock Exchange              | 196.9                                               | 216.7                                                     | 413.6           |
| Ljubljana Stock Exchange              | 211.8                                               | 162.4                                                     | 374.2           |
| Bucharest Stock Exchange              | 278.9                                               | 13.7                                                      | 292.6           |
| Luxembourg Stock Exchange             | 131.6                                               | //                                                        | 131.6           |
| Malta Stock Exchange                  | 13.9                                                | 0.0                                                       | 13.9            |
| Bratislava Stock Exchange             | 1.7                                                 | 8.3                                                       | 10.0            |

### **Bond trading on TASE**

| Exchange                       | Total No. of Bonds Listed |
|--------------------------------|---------------------------|
| Luxembourg Stock Exchange      | 31,401                    |
| Irish Stock Exchange           | 24,357                    |
| Deutsche Börse                 | 24,050                    |
| London Stock Exchange          | 15,444                    |
| NASDAQ OMX Nordic              | 5,215                     |
| Spanish Exchanges (BME)        | 4,829                     |
| Euronext                       | 4,037                     |
| Wiener Börse                   | 3,566                     |
| SIX Swiss Exchange             | 1,386                     |
| Oslo Børs                      | 972                       |
| Borsa Italiana                 | 620                       |
| <b>Tel Aviv Stock Exchange</b> | <b>554</b>                |
| Bratislava Stock Exchange      | 134                       |
| Athens Exchange                | 122                       |
| Budapest Stock Exchange        | 119                       |
| Prague Stock Exchange          | 117                       |
| Bulgarian Stock Exchange       | 94                        |
| Malta Stock Exchange           | 94                        |
| Ljubljana Stock Exchange       | 86                        |
| Bucharest Stock Exchange       | 56                        |
| Cyprus Stock Exchange          | 55                        |
| Warsaw Stock Exchange          | 49                        |

| Value of Bond Trading, Year to Date |                                                     |                                                           |                        |
|-------------------------------------|-----------------------------------------------------|-----------------------------------------------------------|------------------------|
| Exchange                            | Electronic Order Book Transactions Turnover (EuroM) | Off - Electronic Order Book Transactions Turnover (EuroM) | Total Turnover (EuroM) |
| London Stock Exchange               | 0.0                                                 | 3,299,624.0                                               | 3,299,624.0            |
| Spanish Exchanges (BME)             | 67,444.0                                            | 3,181,065.0                                               | 3,248,509.0            |
| NASDAQ OMX Nordic                   | 6,417.5                                             | 662,777.6                                                 | 669,195.1              |
| <b>Tel Aviv Stock Exchange</b>      | <b>478,594.3</b>                                    | <b>54,363.4</b>                                           | <b>532,957.7</b>       |
| Borsa Italiana                      | 125,557.7                                           | 0.0                                                       | 125,557.7              |
| Oslo Børs                           | 2,759.0                                             | 74,206.0                                                  | 76,965.0               |
| Deutsche Börse                      | 10,377.9                                            | 50,601.4                                                  | 60,979.3               |
| SIX Swiss Exchange                  | 16,023.0                                            | 44,347.8                                                  | 60,370.8               |
| Irish Stock Exchange                | //                                                  | 31,538.9                                                  | 31,538.9               |
| Euronext                            | 5,953.0                                             | 5,665.0                                                   | 11,618.0               |
| Prague Stock Exchange               | 0.4                                                 | 11,016.1                                                  | 11,016.5               |
| Bratislava Stock Exchange           | 463.7                                               | 5,292.8                                                   | 5,756.5                |
| Budapest Stock Exchange             | 610.8                                               | 26.2                                                      | 637.0                  |
| Wiener Börse                        | 419.1                                               | //                                                        | 419.1                  |
| Malta Stock Exchange                | 219.0                                               | 0.0                                                       | 219.0                  |
| Warsaw Stock Exchange               | 172.3                                               | 4.0                                                       | 176.3                  |
| Ljubljana Stock Exchange            | 97.7                                                | 0.0                                                       | 97.7                   |
| Bucharest Stock Exchange            | 53.5                                                | 8.1                                                       | 61.6                   |
| Bulgarian Stock Exchange            | 42.4                                                | 4.1                                                       | 46.5                   |
| Luxembourg Stock Exchange           | 18.6                                                | //                                                        | 18.6                   |
| Cyprus Stock Exchange               | 3.0                                                 | 2.7                                                       | 5.7                    |
| Athens Exchange                     | 2.5                                                 | 0.0                                                       | 2.5                    |

### Derivatives on TASE

A range of derivatives are traded on TASE including options on the TA25 index, the TA Banking Index, individual companies (currently four such options are available), FX options on the Euro and US Dollar, and futures on the three month interest rate.

The figures for Israel in following table relate to trading in options on the TA25 only. The details are listed in order of notional turnover, however in terms of the number of contracts traded TASE is the second most active exchange on the list.

| Stock Index Options            |                                            |                  |                           |
|--------------------------------|--------------------------------------------|------------------|---------------------------|
| Derivative Exchange            | Country                                    | Contracts Traded | Notional Turnover (EUROm) |
| EUREX                          | Germany, Switzerland                       | 33,046,841       | 794,423.70                |
| Euronext.Liffe                 | UK, France, Netherlands, Belgium, Portugal | 4,962,840        | 191,210.00                |
| Borsa Italiana                 | Italy                                      | 215,346          | 10,506.90                 |
| OMX Nordic Exchange            | Denmark, Sweden, Finland, Iceland          | 1,041,062        | 7,234.90                  |
| <b>Tel Aviv Stock Exchange</b> | <b>Israel</b>                              | <b>5,317,800</b> | <b>6,190.30</b>           |
| Spanish Exchanges (BME)        | Spain                                      | 469,119          | 4,591.60                  |
| ATHEX Derivatives Market       | Greece                                     | 37,514           | 212.2                     |
| Warsaw Stock Exchange          | Poland                                     | 49,688           | 207.5                     |
| Austrian Derivates Market      | Austria                                    | 1,255            | 47.4                      |
| Oslo Børs                      | Norway                                     | 94,279           | 41.1                      |

## Collective Investment Schemes

CIS are not listed on TASE, although they are cleared through the TASE Clearing House. The figures for European funds in the following table include both UCITS and non-UCITS funds.<sup>6</sup>

| Fund Industry  |                              |                                       |
|----------------|------------------------------|---------------------------------------|
| Country        | Number of Funds <sup>7</sup> | Total Net Assets (EuroM) <sup>8</sup> |
| Luxembourg     | 12,325                       | 1,526,563                             |
| France         | 12,232                       | 1,301,438                             |
| Germany        | 6,052                        | 902,518                               |
| Ireland        | 5,025                        | 632,384                               |
| United Kingdom | 3,062                        | 468,778                               |
| Italy          | 1,132                        | 238,317                               |
| Spain          | 3,014                        | 194,945                               |
| Switzerland    | 777                          | 130,569                               |
| Austria        | 2,307                        | 122,970                               |
| Denmark        | 789                          | 93,728                                |
| Belgium        | 1,924                        | 89,388                                |
| Sweden         | 565                          | 83,062                                |
| Netherlands    | 522                          | 64,400                                |
| Finland        | 522                          | 40,417                                |
| Norway         | 530                          | 31,930                                |
| Portugal       | 523                          | 24,111                                |
| <b>Israel</b>  | <b>1,078</b>                 | <b>19,694</b>                         |
| Liechtenstein  | 508                          | 19,183                                |
| Turkey         | 357                          | 15,081                                |
| Poland         | 436                          | 14,562                                |
| Greece         | 279                          | 9,172                                 |
| Hungary        | 412                          | 8,084                                 |
| Czech Republic | 107                          | 3,849                                 |
| Slovakia       | 124                          | 3,038                                 |
| Slovenia       | 132                          | 1,759                                 |
| Romania        | 68                           | 1,427                                 |
| Bulgaria       | 82                           | 146                                   |

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PT<sup>6</sup> TP The sources of data in the table on funds are:

European figures: European Fund and Asset Management Association, Statistics – available at <http://www.efama.org/index.php>

Israel figures: Israel Securities Authority – available in Hebrew only at <http://www.isa.gov.il/>

PT<sup>7</sup> TP Figures as at 31<sup>st</sup> December 2008.

PT<sup>8</sup> TP Figures as at 31<sup>st</sup> March, 2009.

## **Annex**

The following material has been prepared by the **Tel Aviv Stock Exchange** in response to the CESR call for evidence on mutual recognition with non-EU jurisdictions (CESR/09-406b). The TASE feedback relating specifically to recognition of trading venues begins on page 17.

### **Mutual Recognition with Non-EU Jurisdictions**

#### **Description of the Tel-Aviv Stock Exchange Market (the "TASE")**

##### **About TASE**

The Tel Aviv Stock Exchange Ltd., the only stock exchange in Israel, was established in 1953 as a limited liability company. Following the enactment of the Israel Securities Law, 1968 (the "**Securities Law**"), the TASE obtained a license from the Minister of Finance to operate a stock exchange, and became subject to the supervision of the Israel Securities Authority (the "**ISA**").

The TASE provides a highly advanced platform for trading in shares, corporate bonds, treasury bills, derivatives, index-tracking notes and some other products. It offers a "one stop shop" which includes a full range of market services, including clearing and settlement, data vending services and the calculation of indices.

The TASE operates an order driven fully computerized system, and is a "designated offshore securities market" for purposes of Regulation S, promulgated by the United States Securities and Exchange Commission under the Securities Act of 1933.

##### **The Equity Market**

There are 633 equity listed companies, Thereof:

- 48 dual listed in the U.S., 3 dual listed in London, 3 dual listed in continental Europe.
- 100 High-Tech and Bio-Med companies.

We estimate that international investors comprise 20%-25% of the turnover in equities.

As of January 2008, all companies traded on the TASE have been required to report according to International Financial Reporting Standards (IFRS).

The average daily turnover of TASE for the first quarter of 2009 came to US\$ 300 million, and in the second quarter it rose to US\$ 430 million- some 20% lower than last year's average.

| <b><u>The Equity Market</u></b>        | <b><u>2006</u></b> | <b><u>2007</u></b> | <b><u>2008</u></b> | <b><u>1-6/2009</u></b> |
|----------------------------------------|--------------------|--------------------|--------------------|------------------------|
| Average Daily Turnover (US \$ million) | 326                | 505                | 547                | 366                    |
| Market Capitalization (US \$ billion)  | 161                | 235                | 134                | 176                    |
| Capital Raised (US \$ billion)         | 2.7                | 5.2                | 1.8                | 0.2                    |
| TA-25 Index (US \$ terms)              | 23%                | 44%                | (46%)              | 28%                    |
| Price/Earnings                         | 16.4               | 11.8               | 12.1               | NA                     |
| Price/Book                             | 2.4                | 2.1                | 1.0                | 1.4                    |

## **The Derivatives Market**

Trading in options on the TA-25 index is active, liquid and characterized by high turnovers. The lively action in the options market attests to the vast interest investors have in the flagship index of the Tel Aviv Stock Exchange. During the first half of 2009, activity on the derivatives market slowed in comparison to 2008, with the average daily turnover coming to 250 thousand contracts as opposed to 330 thousand last year. This year TASE launched trading in options on individual shares: Israel Chemicals, Bank Hapoalim, Bank Leumi and Teva Pharmaceutical Industries.

## **Fixed Income Market**

TASE has a highly developed, fixed income market that includes 40 series of government bonds and 500 series of corporate bonds. Most of the bonds are indexed to the CPI.

Corporate debt was the asset class on the TASE that was hit the hardest by last year's financial crisis. Corporate bonds experienced precipitous price declines in the closing four months of 2008. Prices recover, however, in the first half of 2009. Trading on the bond market continued to be active with the average daily turnover coming to US\$ 1.1 billion – similar to 2008 record volumes.

| <b><u>The Fixed Income Market</u></b>    | <b><u>2006</u></b> | <b><u>2007</u></b> | <b><u>2008</u></b> | <b><u>1-6/2009</u></b> |
|------------------------------------------|--------------------|--------------------|--------------------|------------------------|
| Average Daily Turnover (US \$ million)   | <b>384</b>         | <b>799</b>         | <b>1,120</b>       | <b>1,091</b>           |
| Thereof: Government Bonds                | 323                | 634                | 865                | 878                    |
| Corporate Bonds                          | 61                 | 165                | 255                | 213                    |
| Market Capitalization (US \$ billion)    | <b>99</b>          | <b>151</b>         | <b>170</b>         | <b>181</b>             |
| Thereof: Government Bonds                | 63                 | 71                 | 84                 | 88                     |
| Corporate Bonds                          | 36                 | 80                 | 86                 | 93                     |
| Capital Raised in Bonds* (US \$ billion) | <b>10.8</b>        | <b>21.2</b>        | <b>6.6</b>         | <b>4.0</b>             |
| General Bond Index                       | <b>14.0%</b>       | <b>14.3%</b>       | <b>0.5%</b>        | <b>7.5%</b>            |

\* Including issues to institutional Investors.

## **TA 25 - The TASE's Leading Indices**

TASE calculates many equity and bond indices, in collaboration with the Central Bureau of Statistics.

TA-25 is the TASE's leading index of the 25 leading Israeli listed companies. The combined market capitalization of these companies was \$103 billion as of June

2009. Trading in TA-25 shares comprises about 59% of the total turnover on the TASE, and from the beginning of 2003 until June 2009 the index has risen by about 210%.

Currently there are nine long and short index-linked certificates traded on the TASE, tracking the TA-25. Open End Certificates (OECs), tracking the TA-25 index, are also traded on the Milan, Zurich, Frankfurt and Stuttgart stock markets.

### **Israel Upgraded to Developed Market Status by MSCI**

Recently, MSCI Inc. announced its decision to upgrade Israel's classification from an emerging to a developed market, starting in May 2010. The MSCI Israel index will be included in the MSCI World Index and the MSCI EAFE Index. Only securities of companies domiciled in Israel that have a listing on the Tel-Aviv Stock Exchange will be eligible. FTSE has already taken similar measures, upgrading Israel to a developed market status in June 2008.

### **Supervision of the TASE**

A stock exchange in Israel is required to obtain a license from the Minister of Finance in order to operate, which the TASE has obtained. The requirements for obtaining such a license are that the exchange does not limit the number of its members, that its Memorandum of Association limits its purposes to the operation of a stock exchange, that its Articles of Association assure that any profits be used to further its purposes and not be distributed among its members and that its rules be approved by the Minister of Finance, after consultation with the ISA, and by the Finance Committee of the Israeli Parliament (the “**Knesset**”).

The TASE is managed and administered by a Board of Directors consisting of 15 voting directors and the chief executive officer of the TASE who is a director without a voting right. Seven of the fifteen directors, including the chairman, are not affiliated with members of the TASE (the “**TASE Members**”), and an eighth director is appointed by the Bank of Israel.

Pursuant to the Securities Law, the TASE is required to adopt rules which must be approved by the Minister of Finance, after consultation with the ISA, and by the Finance Committee of the Knesset. Once the rules have been approved, the TASE may issue regulations, subject to the approval of the ISA, for the implementation of the rules. The rules and regulations must be based on the principle of fair and proper conduct of the TASE and include the following:

- Rules pertaining to membership of the TASE;
- Rules for the listing of securities for trading;
- Rules regarding the trading system;
- The post-registration obligations of a listed company;
- Conditions and procedures for suspending the trading of a security and for delisting of a security;
- Rules for the dissemination of data by the TASE; and

- Fees.

In accordance with the Securities Law, if the ISA decides that the TASE's rules should be modified to ensure that the TASE operates in a proper and fair manner, it is empowered to request the TASE to amend its rules. If the TASE does not comply, the Minister of Finance may, in accordance with the ISA's proposal and with the approval of the Finance Committee of the Knesset, promulgate an order modifying the TASE's rules.

If the ISA believes that the TASE is violating its rules or regulations or operates in a way that is prejudicial to its fair and proper operation, then, after giving the Chairman of the TASE's Board of Directors an opportunity to be heard, it may order the TASE to take the proper action to ensure that it operates in a proper and fair manner.

In addition, the ISA operates a market surveillance department to monitor trading on the TASE. The Securities Law provides that in order to facilitate the implementation of the Securities Law, or in case there is suspicion of a violation of the Securities Law, the ISA is empowered to demand from any person any information and documents pertaining to a company which is subject to the Securities Law. The ISA can also apply to the court for a search warrant, to investigate and interrogate any person suspected to be connected with any violation of the Securities Law and to petition for injunctive relief enjoining the commission of the suspected violation.

### **TASE Membership**

Trading on the TASE is carried out by TASE members on behalf of their clients. As of the date of this letter, there are 14 bank members (including the Bank of Israel), 13 non-bank members and 1 remote member. The non-bank members are brokerage firms, whose main activity is handling securities-related business on behalf of their clients. A non-bank member may also engage, directly or through subsidiaries, in other specified activities incidental to its securities-related business.

The TASE supervises its members and monitors their compliance with the rules and regulations of the TASE.

The surveillance of bank members focuses on issues related to fair and proper conduct, including the fairness of the banks' dealings with their clients as they apply to securities transactions on the TASE. The TASE members' compliance is enforced through fines, suspensions and permanent termination of trading rights, as well as termination of TASE membership in extreme cases.

In addition, the TASE surveillance of non-bank members deals with financial stability, including shareholders' equity and working capital criteria, amount of assets and liquid assets free of encumbrances and limitations on credit and guarantees provided to clients.

The Bank of Israel supervises the financial stability of the TASE bank members.

The supervision of the non-bank members' financial stability is supported by two monitoring policies that each non-bank member is required to adopt:

- *Real-time Credit and Collateral Controls Policy* – requires the appointment of a credit controller and implementation of a system that automatically blocks orders that would cause an account's collateral requirements to deviate from its credit ceiling, as well as block non-permissible short sales.
- *Compliance Policy* – requires the appointment of a compliance officer to ensure compliance with the laws and regulations to which it is subject, including the TASE rules and regulations.

TASE members are also subject to Israel's money laundering laws and regulations, which require implementing client identification and "know-your-customer" policies and recording and reporting certain transactions.

Most TASE members are corporations incorporated in Israel. However, the TASE rules also permit a non-Israeli banking corporation that has received a foreign bank license from the Governor of the Bank of Israel and has a branch in Israel to become a member. There are currently two non-Israeli bank members, Citibank, N.A., a U.S. banking corporation, and HSBC Bank PLC, a U.K. banking company. The acceptance criteria are similar to those that apply to Israeli banks, which are listed on the TASE.

In addition, two Israeli TASE non-bank members, Deutsche Securities Israel Ltd. and UBS Securities Israel Ltd., are affiliates of Deutsche Bank AG and UBS AG, respectively.

There is one remote member, Merrill Lynch International.

TASE members serve the community of local and international investors in Israel's growing market. The capital and liquidity requirements of TASE members are stringent, for the sake of protecting the investing community.

## **The Trading Systems**

Trading is conducted on the Tel-Aviv Continuous Trading System ("TACT") which began operating in 1997. TACT is an order driven fully computerized system composed of trading stations and mainframe computers linked to the TASE's trading engine by a comprehensive communications network.

## **Clearing and Settlement Systems**

There are two clearing houses, fully owned by TASE which serves as central counter party (CCP);

1) The **Tel Aviv Stock Exchange Clearing House Ltd.** which clears and settles transactions in securities listed on the TASE, excluding derivatives (options and futures). This clearing house also provides additional clearing services, such as

clearing non-listed securities The Clearing House serves as the only Central Securities Depository in Israel (Including for non listed securities).

2) The Maof Clearing House Ltd. The Maof Clearing House issues derivatives and clears derivatives transactions.

Each Clearing House operates under bylaws established by its board of directors.

The clearing houses are supervised by the ISA, pursuant to the Securities law.

### **Mutual Recognition – response to CESR call for evidence regarding trading venues**

The TASE is very interested in Mutual Recognition between Israel and the E.U. countries, particularly with Great Britain, France, Holland, Belgium, Portugal and Germany.

The TASE feels that enabling TASE members to set up TASE trading screens in E.U. countries will facilitate European investors interested in investing in the Israeli market. This option will most likely increase the number of foreign investors as well as the volume of their investments in the Israeli market. It will also contribute to the liquidity of market and add diversity to the investor community.

European investors' interest in the Israeli market is also expected to increase in light of the recent upgrading of the Israeli market by MSCI and FTSE, from an emerging market to a developed one. Direct access from Europe to the Israeli market will ease investment opportunities and assist investors in diversifying their investment portfolios.

Mutual Recognition will also facilitate Israeli investors interested in investing in European markets and will enable them to broaden and vary the scope of their investments.

Trading on the TASE is restricted to TASE members. Pursuant to the TASE rules, a TASE member should be a corporation, incorporated in Israel. However, a non-Israeli banking corporation is permitted to become a member if it has received a foreign bank license from the Governor of the Bank of Israel and has a branch in Israel. An international investment house that meets the criteria set by the TASE rules but does not have a branch in Israel can become a remote member. A remote member may not become a member of the Tel Aviv Stock Exchange Clearing House Ltd.

Direct Electronic Access to the TASE can be obtained through a TASE member. TASE members supply their clients with trading screens, either locally or outside of Israel, through which the clients gain direct access to the TASE's trading engine. The clients are then able to communicate their orders directly to the TASE. These orders are identified as orders communicated by the TASE member through whom the client acts as the TASE does not "recognize" the client.

TASE members are required to pay fees to the TASE and remote members are equally obliged to pay these same fees. A client, on the other hand, does not pay fees to the TASE, rather to the TASE member through whom he acts, following negotiations between the member and the client.