



Ref: CESR/04-349

**THE ROLE OF CESR AT “LEVEL 3”
UNDER THE LAMFALUSSY PROCESS**

SUMMARY OF RESPONSES

October 2004



1. Background

As the European Union reaches the final stages of an ambitious programme to modernise Europe's Financial Services Legislation, the ability of regulators to fulfil their part in working towards the realisation of this objective becomes more critical. Particularly, as investors will need to be sure that they receive equivalent levels of protection across Europe and market players will need to know what they can expect in terms of regulation and that there is a level playing field across Europe.

The role of securities regulators in working towards the realisation of this objective was recognised by a Group of "Wise Men", chaired by Baron Alexandre Lamfalussy, which proposed a new legislative approach for the revision of Europe's securities legislation in June 2001, at the request of the Council and which following approval by the European Parliament was introduced into the European Union's decision making processes, commonly known as the "Lamfalussy Process".

On 3 May 2004, the Committee of European Securities Regulators (CESR) published the consultation paper *"The Role of CESR at 'Level 3' under the Lamfalussy Process"* (Ref. CESR/04-104b) seeking to engage market participants, consumers and end-users in a discussion to establish how securities regulators can fully play their part at level 3 in ensuring firstly, that there is greater consistency across Europe in the process of implementation (where CESR members contribute towards the local transposition of European financial services legislation in their Member States) and secondly, to establish greater EU-wide convergence through the application of this legislation (that is undertaken on a day-to-day basis through the exercise of their supervisory tasks).

The consultation paper aimed at presenting the views of CESR on how it should organize its role at level 3 under the "Lamfalussy Process" and how CESR members might fully exercise their responsibilities within the four level framework of the "Lamfalussy Process". These proposals on how CESR can further develop its role at level 3 recognise the need for CESR to co-ordinate with other key players, such as the Member States, responsible for transposition of EU law into national legislation, and the European Commission as "Guardian of the Treaties", whose function includes enforcing any failure to implement legislation under level 4 of the legislative framework (Article 226 of the Treaty).

The consultation paper was structured in two parts. The first section provided an introduction and description of the current general principles governing the way in which the Lamfalussy approach and in particular Level 3 should work. The second section set out in a more detailed manner the organization of CESR's role at Level 3 which can be subdivided into the following three different categories: i) coordinated implementation of EU law, ii) regulatory convergence, and iii) supervisory convergence.

Some 35 responses to the consultation were received. These came from a variety of sources including national and EU trade associations, issuers, analysts, auditors, asset managers, exchanges, individual banks and investment services. The complete list of respondents is given in Annex 1. All public responses can be viewed on the CESR website.

This feedback statement focuses on the substantive points and key issues which were raised in general terms and as to the three different categories identified. These will be followed by a combination of subsidiary points and answers to the questions posed in the consultation paper.

2. General Comments

All responses welcomed the initiative taken by CESR to consult on how it should organise its role at level 3 under the Lamfalussy procedure and expressed strong support for the described role of CESR at level 3. The general tenor of responses was that the consultation paper had correctly identified the role of CESR at level 3 and there was considerable agreement that the role described in the consultation paper was indeed the role CESR should play.

Respondents encouraged CESR to continue and strengthen its communication with market participants in the context of Level 3, in order to enable regulators to draw on the expertise in the field of securities markets within the private sector.



Some respondents commented that CESR should be wary not to give up the flexibility of level 3. CESR was also requested to conduct thorough cost-benefit and impact analyses and fact-finding exercises before starting work at level 3, though the difficulty and costs of such analyses were acknowledged. In a number of comments received, it was suggested that consultation practice at level 3 should be aligned with those at level 2, so that all interested parties could give their input in this work, as well. In this respect, one respondent felt that CESR should ensure that CESR Members also consult their industry in an open and transparent manner. A proposal was made that CESR should establish sub-groups of market practitioners for particular issues, topics and sectors as part of the consultative process.

As regards the consultation process, CESR follows the same consultation practices at level 2 and level 3. Therefore, the CESR Charter and CESR's Public Statement of Consultation Practices (Ref. CESR/01-007c) do not distinguish between level 2 and level 3 in CESR's approach to consultation (e.g. publication of consultation papers, setting-up of Consultative Working Groups).

3. Coordinated implementation of EU law by CESR members

Network of CESR experts

The responses also reflected strong support for CESR's proposal to keep 'alive' the network of CESR experts advising on application of EU law, as it guarantees that industry is involved effectively at Levels 2 and 3 of the process. These Expert Groups could represent a channel through which developing an open dialogue with the interested parties or just continue the dialogue started at the former levels legislation. One of the respondents added that this network of experts should not be confined only to the legal specialists, and proposes that market practitioners as well as legal specialists participate in the network of experts. Another respondent suggested that it would be useful to give practitioners the chance to directly highlight to CESR concrete problems as to coordinated implementation of EU law and regulatory and supervisory convergence.

Following the publication of the first interim report by the CESR Review Panel (Ref. CESR/03-414b), all interested parties were invited to comment on the work on the Review Panel. In addition, CESR will develop the role of the CESR Market Participants Consultative Panel in this area.

Review Panel

Regarding the comments on the Review Panel, respondents expressed their support for the recent creation of the Review Panel, with its specific role to evaluate the coherent implementation of European legislation at the level of Member States. Respondents also felt that CESR – through the Review Panel – should analyse existing national rules and practices when developing new initiatives. It was also stressed that market participants should have a role in the Review Panel process.

The Review Panel will continue to assess implementation of CESR Standards and Recommendations in the future, with the next step being the review of CESR's Standard No. 1 on Financial Information (Ref. CESR/03-073).

Rule-making powers of CESR members

Some of the respondents stressed that transposing EU legislation through rules of national regulators might have benefits by allowing rules to be adopted or amended more quickly and to be drafted by those with technical expertise, but, if this is to be the case, these rule-making powers should be accompanied by rigorous transparency arrangements and should be subject to a proper consultation process. In this respect the issue of national accountability of securities regulators was raised. Another respondent argued that there was a compelling need for an urgent review of the legal situation in various Member States and a publication of these findings.



As regards the idea expressed in the paper that the distinction established between level 1 and level 2 should be an indication of what could be transposed in national laws and what could be transposed by delegation in rules of national regulators, concerns were raised that in a number of cases it would not be appropriate that level 2 provisions were transposed by regulators or level 1 provisions were transposed by national legislators.

With respect to CESR members being given equivalent rule-making power, a majority of the responses was in favour of this concept. It was suggested that this concept had already – at least implicitly – been foreseen in the Lamfalussy Report as an important requirement for the effectiveness of the Lamfalussy Process in general, and level 3 in particular. Respondents indicated that any follow-up to CESR's recommendation must respect the national legislative process and the divisions of legislative and executive powers. Nevertheless, the granting of rulemaking powers to CESR members by way of delegation was considered by some to be part of the broader general need for convergence of goals and functioning of supervisors. One of the respondents added that this proposal was fully in line with the conclusions of the Committee of Wise Men: it stressed in its report that level 3 depends above all on closer cooperation between member states, regulators and the European Commission, and this cooperation would be much more productive once regulators have identical resources for transposing and enforcing level 1 and 2 measures.

Additional role of CESR as to co-ordinated implementation of EU law

One respondent added that CESR and its members should press for changing the level 2 legislation from the type “directive” to the type “regulation” which applies directly in all Member States. Such a change could give CESR the role of issuing guidelines interpreting level 1 directives and level 2 regulations at a European level and monitoring the application of the regulation in the Member States. One respondent saw an additional role of CESR in highlighting the importance of mutual recognition between supervisors. Another one felt that there was a role for CESR at level 3 in facilitating shared knowledge of each country's rules and practices to help ensure consistent implementation.

It was suggested that CESR should play a role in alerting the Commission of the failure of a Member State in transposing a specific level 1 or level 2 provision.

Ad-hoc transposition meetings

Responses were generally in favour of CESR's current efforts in the transposition process, such as ad-hoc transposition meetings. Some respondents stressed the importance at this stage of both the coordination among regulators and the coordination among Member States and national regulators. Respondents were also of the view that CESR should urge the Commission to make more extensive and early use of such meetings during the transposition process where Member States and national regulators could discuss transposition problems and examine preliminary drafts of transposition measures.

4. Regulatory convergence

Other aspects of regulatory convergence

Some of the respondents did not see any other aspects of regulatory convergence where CESR could play a role, instead level 3 should be exclusively concerned with the co-ordination and convergence of supervisory practices among the competent authorities rather than the creation of new legislation or jurisprudence. Rather, they were of the view that coordinated implementation and regulatory convergence could be sufficiently achieved through non-binding guidelines, recommendations and standards issued by CESR.

One aspect identified in a comment was that CESR could play a role at level 3 in streamlining or simplifying national rules where those rules impede, rather than foster, EU integration. An example given was the UCITS registration requirements.



It was further suggested that CESR could establish standards for training and competence throughout the industry, in particular in the field of financial advisers, so that mutual recognition of national professional qualifications could be considered.

CESR work in non-harmonised areas

In this respect, some respondents reflected the belief that whenever legislation was not yet in force at level 1 or level 2, CESR should not be entitled to create new norms with binding effect, in particular as this could bring CESR into potential conflict with the EU Institutions (mentioning the work on the clearing and settlement standards as example). The normative function of CESR should therefore be limited to indicative guidance and only in instances when legislation was in place at level 1 and level 2, could CESR be granted authority, under a specific mandate of the Commission, to create binding rules.

A number of respondents were of the view that CESR's initiative in areas not already covered by EU legislation should be limited to well-justified cases, and should be the exception, not the rule avoiding CESR initiatives in areas where EU legislation is up-coming. Indeed, some respondents went further to suggest that CESR should wait for the implementation of its recommendations until there is a specific political mandate at level 1 and level 2 of the Lamfalussy procedure in place. In particular, the need for a mandate from the Commission becomes more critical, in their opinion, if the measures are to have a binding effect.

Other consultees supported the example given of CESR's work in adopting standards on clearing and settlement, though they underline that it was essential that CESR should first consult extensively with the industry on any aspects of regulatory convergence in order to assess whether additional standards would be useful and needed. One respondent felt that where CESR proposed to develop standards, CESR would need to explain clearly to market participants what it was planning by way of developing guidance.

In general, respondents mentioned that CESR should be as transparent as possible and conducting consultations as far as possible, aligning the procedures in the non-harmonised areas to those successfully used at level 2.

It was also mentioned that, when defining CESR's tasks at level 3, the report of the Committee of Wise Men had explicitly referred to the formulation of joint interpretative recommendations as well as common standards in fields not covered by EU legislation.

CESR alerting the Commission

A majority of respondents supported CESR's proposal to alert the Commission to practical difficulties or unworkable level 1 or level 2 legislation, as it would have expertise and contact with the industry that could generate useful feedback for the Commission. However, this should not prevent national regulators from approaching the Commission directly.

One respondent also stated that it was normal that CESR should have the power to alert national regulators to the questionability of implementing a particular point, however, it was not normal that the committee should also have coercive powers.

Coordinated opinion on new services or products with pan-European scope

Many respondents agreed that CESR could play a role in providing coordinated opinion on new services with pan-European scope as long as CESR would keep its original nature as international forum. To the extent that such new services or products would require consistent and harmonised interpretation of existing EU law, CESR could play a role in providing a coordinated opinion. One respondent was of the opinion that there might be occasions where a firm wished its national regulator would seek a broader range of regulatory opinion through CESR. One respondent mentioned that any role for CESR in providing coordinated opinion on new services or products should have its emphasis on mutual recognition and the removal of barriers to cross-border service provision, and not the imposing of new restrictions on innovation.



It was a recurring comment, that any such procedure should be neutral vis-à-vis market development and encourage, and not stifle, competition. There were also some comments that such a procedure should not amount to any form of product approval directly by CESR, since this would be solely within the powers of the national regulators. It was suggested by one respondent that CESR could play the role of a coordinator among CESR members for new non-passport services or products.

Some of the respondents hesitated as to whether CESR should play a role in providing a coordinated opinion on new services or products unless these would have a clearly stated pan-European scope and the areas were identified and developed in response to industry concerns and in cooperation with market participants, giving CESR a retrospective, but not proactive role. It was suggested that in the case of products or services not covered by European legislation, Level 1 legislation should be required.

Endorsement by the European Commission

A majority of the respondents was not supportive of the possibility of giving more authority to CESR guidelines, recommendations and standards through a possible endorsement by the Commission, in particular as this could reduce the flexibility and adaptability of level 3 measures. There was concern that this would in effect bring about a third layer of European legislation, in addition to level 1 and level 2. It was also suggested that endorsement by the Commission could diminish the scope of action for the Commission in any later infringement proceedings.

Other respondents took the view that this approach could be used and were of the view that this would give additional authority to such guidance, though there should be caution that it would be used under exceptional circumstances and subject to rigorous procedural principles, and only for issues where there was genuine lack of clarity, lack of powers of national regulators to implement level 3 instruments or need for enforcement of level 3 instruments in national courts.

One issue raised was that binding interpretation of level 1 and level 2 measures can ultimately only be given by the European Court of Justice, notwithstanding the fact that CESR and the Commission have a role to play in clarifying certain issues.

Another respondent suggested that in order to ensure consistent application of EU directives/regulations, a procedure identical and parallel to the level 2 procedure should be implemented at level 3.

5. Supervisory convergence

Most of the respondents stated that convergence of supervisory practices was an important element for ensuring the proper functioning of the single market in securities and also part of the recommendations in the “Lamfalussy Report”. A regular and intensive exchange of information among supervisory authorities was seen as a prerequisite for establishing uniform supervisory practices and consistent enforcement.

It was commented that CESR should concentrate on the supervisory issues presented in the consultation paper and prioritise them, rather than seeking new areas of activity. In one response IFR Standards, enforcement and implementation of Market Abuse and Prospectus Directive, and the issue of transaction reporting were considered as priorities for CESR.

Databases

Many respondents welcomed CESR’s objective of using databases to facilitate regulators’ access to other regulators’ decisions and national judicial decisions (including pending cases). It was suggested that CESR would be the appropriate body to establish and manage a database of enforcement cases and an appeal mechanism, and that the database envisaged as to the application of IFRS could serve as a model for other domains.



Mediation

In most of the comments received on this issue the idea that CESR should be entrusted with the tasks of a mediator charged with the role of providing assistance in trying to settle amicably conflicts between national regulators was received favourably. Some respondents felt that a system of mediation between national regulators should be limited to resolve any conflicts that arise as a result of the implementation of level 2 measures, others would see this issue in a more broader context.

It was proposed in one comment that such a mediation mechanism should cover the entirety of securities market law and that a maximum degree of binding force should be given to the conclusions of such a mediation procedure.

Other consultees were of the opinion that the mediation role of CESR between its members should remain limited and that any mediation role would have to be advisory. It was also felt that such a mechanism should not have the result that the increased automaticity of mutual recognition would be systematically questioned, but it should contribute to the strengthening of that principle. It was also mentioned that a mediation mechanism should not limit the right of regulators, investment firms or other entities to bring a case to the Commission or in front of the European Court of Justice.

There were also several comments that interpreted the proposed mediation mechanism more as a complaints mechanism where individual investment firms or trade associations could be set up by CESR in cases where a regulator would apply EU law or CESR Standards in an incorrect way. In this respect, it was proposed that it would be useful that a senior non-CESR figure who could act as an ombudsman or mediator between a firm and a CESR member in circumstances where the firm was unhappy about a decision by its regulator. One respondent also made a proposal to set up a Professionals' Ombudsman for Financial Services, outside CESR, to mediate and solve problems and disputes between market participants and regulators.

In particular, respondents held the view that the mediation role was going to arise where regulators had interpreted a requirement differently, with the result that either a firm would be subject to inconsistent rules or where firms in different countries would continue to be regulated differently. Under such circumstances a specialist mediator could take evidence from the firm or firms involved and the relevant regulators in order to come to a conclusion. The process proposed should be consensual and would be used for bilateral disputes or disputes between a small numbers of CESR members.

Other areas

One respondent stated that for transaction reporting supervisors should share information among them instead of making investment firms report to several regulators the same data.

It was also suggested that regulators should forward their requests for information to the supervisory authorities of other Member States, which already hold the information, rather than to the financial services provider.

The idea of establishing urgent-issues groups within CESR was welcomed.

As to joint supervisory inspections, in one comment received it was argued that this would not be appropriate for CESR to deal with but should be rather dealt with through bilateral agreements between the regulators concerned.

Catalogue of mutual recognition and cooperation obligations

In relation to the catalogue of all mutual recognition and cooperation obligations under the Directives where CESR is active annexed to the consultation paper, respondents appreciated the catalogue and encouraged CESR to complete and update the catalogue on a continuing basis, and to publish it. It was requested that Recital 27 and Article 23 Paragraph 1 of the Commission Regulation (EC) No 809/2004 implementing the Prospectus Directive should be added to the catalogue for completeness.



It was proposed by one respondent that CESR should undertake legal analysis as to whether the legal differences regarding exchange of information obligations would be intentional and what their legal effects would be, and what the interaction in areas such as banking secrecy or admissibility of evidence were.

Annex 1: Consultation Responses

- ~ Association Française des Entreprises d' Investissement
- ~ Association Française des Entreprises Privées
- ~ Association of Insurers in the Netherlands
- ~ Association of Private Client Investment Managers and Stockbrokers
- ~ Assogestioni. Associazione del risparmio gestito
- ~ Associazioni Italiana Intermediari Mobiliari
- ~ Bankenverband
- ~ Barclays
- ~ BNP Paribas
- ~ British Bankers' Association
- ~ Deutsche Bank
- ~ Deutsches Aktieninstitut
- ~ Danish Bankers Association
- ~ Danish Securities Dealers Association
- ~ European Association for Listed Companies
- ~ The European Federation of Financial Analysts Societies
- ~ European Savings Banks Group
- ~ Fédération Bancaire de l'Union Européenne
- ~ Fédération des Experts Comptables Européens
- ~ Fédération Européenne des Fonds et Sociétés d' Investissements
- ~ Federation of European Securities Exchange
- ~ Fortis Bank
- ~ International Primary Market Association
- ~ International Securities Market Association
- ~ International Swaps and Directive Association
- ~ Investment Company Institute
- ~ Investment Management Association
- ~ Irish Association of Investment Managers
- ~ London Investment Banking Association
- ~ London Stock Exchange
- ~ Mouvement des Entreprises de France
- ~ Mediobanca: Banca de Credito Finanziario
- ~ Nederlandse Vereniging Van Banken
- ~ Rabobank Nederland
- ~ Swedish Securities Dealers Association
- ~ UNICE
- ~ Van der Moolen NV
- ~ Zentraler Kreditausschuss