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Assessment of the integration of the Single Market for financial services by the Commission

CESR (Committee of European Securities Regulations) Conference

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Chairman, Ladies and Gentlemen,

I am delighted to have been invited to address you today. Given the pioneering work CESR is carrying out and the excellent reputation you have established, it is fully appropriate that I am making my first speech here in Paris, at CESR's first major conference. Indeed I understand that CESR does not want to be only a pioneer – but you also want to scale the Himalayas as well. I applaud your ambition!

I join the new Barroso European Commission, as Commissioner for the Internal Market and Services, at an exciting time in the development of the internal market in financial services. Although the legislative phase of the Financial Services Action Plan is drawing to a close, there is still much to do to build a real European integrated capital market.

Such an integrated capital market will be a major asset for what is the first priority of the Barroso Commission: meeting the objectives set out in the Lisbon strategy. A more efficient and liquid market will facilitate the financing of the economy and thus be good for competitiveness, growth and jobs. This will allow the European Union to preserve its social and environmental models. What we will discuss here today, therefore, matters for financial markets, for the users of financial markets but also for the European economy at large.

Implementation of the Financial Services Action Plan (FSAP)

Let me pay tribute to what has been achieved over the past five years, while my predecessor Frits Bolkestein was at the helm in the Commission. In terms of agreement on the legislative measures, the Financial Services Action Plan has been largely delivered on time.

But those agreements are only the first step. Now the measures must be properly implemented and enforced to ensure a level playing field across Europe. That is essential for the credibility and legitimacy of the whole project.

As for the impact of the Action Plan itself, it is of course too early to draw any firm conclusions. Its effect will manifest itself only over the medium-to-longer term.

But there is incontrovertible evidence, particularly in the wholesale business, that European markets are beginning to integrate and costs are falling – trading costs, the cost of capital, spreads in the bond market and so forth.

Cross border investments are accelerating. The number of foreign market participants has increased in equities markets. The proportion of shares held by non-residents is estimated by the Federation of European Stock Exchanges to be at least 20% in almost all European stock exchanges. In Helsinki, well over 70%. And in Madrid Stock Exchange, non-resident investors account for over 60% of the total value of trading. This is much higher than in the US.

Collective investment funds are already traded extensively cross-border. And common trading platforms, stock exchanges and post-trading infrastructures are being reshaped on a pan-European cross border basis. Increased competition is resulting in what you would expect – greater innovation, product choice and reduced costs for investors, issuers and consumers.

In short, a European reflex in financial markets is emerging. This is positive.

The Action Plan is certainly one of the catalysts of this change – along with the extraordinary success of the euro.

And there is no doubt that the success of the Lamfalussy process so far, which has improved legislative quality, and speed, has convinced market participants that the European Union is on the right track towards developing an appropriate regulatory framework for fast moving financial markets.

Post-FSAP agenda

One of my key priorities over the next six to twelve months will be to present and gain support for a forward strategy on financial services.

First of all, I should emphasise that I will be listening hard to all sides in this debate. To market participants, the banking, securities and insurance sectors, issuers, institutional investors, consumers and other end-users. To the European Parliament. To the Member States. To regulators and supervisors.

I hear clearly the message from the financial services industry. I understand the strain that the Action Plan has put on the resources of all actors. I recognise there is some "regulatory fatigue".

The importance of good implementation and enforcement

As I already mentioned, timely implementation of the FSAP measures will play a crucial role in securing the benefits of integrating financial markets.

The Commission takes its responsibilities in this area very seriously. I regret that there have been delays in the implementation of the Market Abuse Directive. But I should also emphasise that the Commission will continue to work closely with the Member States, particularly at the technical level, in order to achieve correct, consistent and, indeed, more timely implementation of all the Lamfalussy measures across Europe.

I fully intend, therefore, that implementation and enforcement shall be a key priority throughout my mandate as Commissioner. We will develop a coherent strategy, supported with a full range of tools, to ensure that tangible results are delivered by Member States. Companies that want to undertake cross-border business must be able to do so.

I want to build a constructive partnership with the Member States, whom I am sure will take seriously their own responsibilities in this area under the Treaty. In an EU of 25 or more Member States, there is an increased risk that late or incorrect transposition of legislative measures will result in fragmentation of the internal market. And a consequent dwindling of the economic benefits.

My staff will continue to monitor carefully progress on implementation:

- through regular discussion and monitoring in the European Securities Committee;
- through what we call "transposition workshops", that is to say meetings of the Commission, the Member States with the regulators. The aim of these workshops is to converge views on how to implement technical provisions and so promote even implementation; and
- through encouraging the production of so-called "transposition tables" by the Member States in order to increase the transparency of implementation.

Clearly, CESR has an important role to play in the implementation of the Lamfalussy measures. Peer reviews and other joint working, benchmarking and agreement on common standards are likely to prove extremely useful in facilitating more uniform and consistent application of EU legislation.

Good coordination by CESR at Level 3 of the Lamfalussy process is also likely to help convergence and, indeed, financial integration. And it could ease considerably the Commission's enforcement workload at Level 4.

And I also call on the financial services industry to play their role. They should inform the Commission when they know things are going wrong – and be much more pro-active. The Commission cannot know what is happening in every nook and cranny of financial markets. I also expect that this Commission will become more active on the competition aspects of European financial markets – and I look forward to working with my fellow Commissioner, Neelie Kroes, in this vein.

To sum up, my aim will be to ensure adequate implementation of EU law through a close partnership with all interested parties instead of having to initiate infringement procedures. But let me be clear – the Commission will not hesitate to do so if necessary.

Implementation of the Markets in Financial Instruments Directive (MiFID)

In this context, I should make special mention of the Markets in Financial Instruments Directive, often referred to simply as the MiFID. I know and I am very grateful that CESR is currently working – under much pressure – on constructing advice to the Commission in respect of the implementing measures needed to underpin and complete the Level 1 Directive.

This highly complex measure is crucial in our efforts to construct a pan-European capital market. I am extremely conscious of concerns that the timetable for its implementation and application is very tight, particularly in the industry, which will need to make major adjustments to IT systems in respect of certain provisions in the Directive.

I am currently examining the arguments. I understand the complexities of this legislation make it quite an exceptional case: I would like to hear more about the technical difficulties faced by industry before taking a decision. If we were to go down this route, there would need to be maximum cooperation between Member States, regulators and the industry to work as much as possible in parallel to gain time. And there could be absolutely no suggestion of reopening any substantial issue.

Future regulatory and supervisory structures

What else is important for the Post-FSAP agenda?

One important aspect of the Post-FSAP debate will be the future shape of regulation and supervision of financial markets at European level over the medium to long term. CESR's recent "Himalaya report" is therefore a timely contribution to this debate, which the Commission will formally respond to.

Naturally, the Commission intends to listen to arguments from all sides, in the tradition of transparency and consultation that is the hallmark of the Lamfalussy process.

CESR is right to highlight the need for convergence of rule-making and supervisory powers among national regulators. Such alignment could well prove to be the crucial next step in encouraging further pan-European regulatory rationalisation. Convergence should be evolutionary rather than revolutionary, building bottom up, not top down. Bringing markets, regulators, Member States and the European Parliament along in the process.

Lamfalussy review

In the short-term, the recent Lamfalussy review has been a helpful stock-take on progress in implementing the recommendations of the Lamfalussy report.

It is clear that the preparation of EU legislation affecting securities markets is now more open and transparent, with better involvement of external stakeholders. Moreover, there is better political cooperation between the Commission, Council and European Parliament.

All of this has led to an increase in both the speed and quality of EU legislation. The use of implementing measures will make it easier and faster to adapt EU legislation in the future. I think it is also fair to say that the process is beginning to encourage some regulatory and supervisory convergence.

Our overall conclusion is that good progress has been made so far in implementing the four-level Lamfalussy approach, which is now being extended to all financial services sectors, and even wider.

Nevertheless, further improvements can be made. These could include:

- Strengthening even further the democratic accountability of the process;
- Refining our approach to consultation – including better involvement of consumers;
- Looking more critically at timetables for transposition – not least to avoid the problems I have already outlined on the MiFID;
- Strengthening efforts to foster greater understanding of the Lamfalussy process – in particular the roles and tasks of the respective levels. We should be aiming for a greater focus on general rules and principles at Level 1 and to avoid over-prescription at Level 2;
- Level 3 needs to be developed – but there needs to be much more reflection on the issue of political accountability.

The Commission recently published a staff working paper exploring these issues, which is open for public comments until the end of January. The results of this consultation will be fed into the Commission's work on a post-FSAP strategy.

Priorities over the near term

I referred earlier to the "regulatory pause" that industry has often asked for in recent months. I cannot promise you that there will be no proposals from the Commission during my mandate. But I can at least reassure you that I do not envisage bringing forward any major co-decision proposals aimed at securities markets during 2005.

The rules that are needed for an efficient and integrated wholesale market are there. We now have to make them work in practice.

That is not the case yet as regards retail financial services. I will therefore have to reflect on what can be done to ensure that the vision of an integrated financial market also becomes a reality for all EU citizens. A legislative programme similar to what has been proposed for the securities markets will certainly not be on the agenda. However, if there is convincing economic evidence that targeted legislative action is needed in some areas of the retail market, then I will consult on the options available.

Coming back to securities markets, over the near term – that is to say from 2006 onwards – I can see three priority areas where progress may be needed.

First, the need for a more efficient and secure post-trading environment for cross-border securities transactions – clearing and settlement. My staff have already established or are in the process of establishing a number of groups of mainly private sector market participants to discuss the very technical and complex issues involved and ensure continuous dialogue. For clearing and settlement, 2005 will be a year of preparation, analysis, economic impact assessment and building consensus.

As to whether there should be a new Directive or not, many of you will know that I am a firm believer in better regulation – and that I do not favour overregulation. Preparing a thorough economic impact assessment is now standard practice for all major Commission proposals and it will be a vital element in our decision on whether to propose a Directive and, if so, its content.

Second, we need to take fresh look at asset management. The FSAP stock-taking exercise has revealed that the current single market framework for investment funds is in need of considerable improvement. To be honest, it's a bit of an old banger.

We are already working hard to get the most out of our current rules. But more needs to be done to broaden the single market freedoms available to fund managers. To give investors access to best of breed savings products. To embrace financial innovation. To give investors relevant regulatory protection.

In the second half of 2005, we will publish the Commission's assessment of priorities. We will present options for tackling them. Stakeholders will have the opportunity to comment on this assessment and on the proposed options.

This will therefore be the first step in a potentially significant project – promoting an integrated, modern and competitive fund industry which can play a large part in defusing Europe's pension timebomb.

Third, I have already mentioned implementation of the MiFID. Clearly, producing the Level 2 implementing measures required to underpin and complete the MiFID will be a major part of the Commission's work programme during 2005.

I should perhaps also mention a few other important issues that affect capital markets.

First, the Basel II capital requirements directive is currently being negotiated and political agreement should be reached on it in ECOFIN tomorrow. This measure aims at modernising the existing capital requirements framework; making it more comprehensive and risk-sensitive; and fostering enhanced risk management amongst financial institutions. This will strengthen financial stability and help maintain confidence in financial institutions.

Second, CESR has just published a consultation paper on credit rating agencies. I look forward to receiving CESR's advice on this issue in April. The Commission will then come forward with a policy view in the second half of next year. Whatever solution we propose must take into account the global context in which credit rating agencies operate.

Third, common International Accounting Standards (IAS) are essential for the integration of EU capital markets. Investors need to be able to compare company results across borders. And IAS are also crucial as a first step towards global convergence of accounting standards.

On IAS 39, I want to underline that the two carve-outs the Commission decided on are of a temporary nature. The Commission made perfectly clear in its declaration of 19 November that we expect the International Accounting Standards Board to come forward with a solution on the fair value option later this month – and on the hedge accounting provisions in autumn 2005. We should at all costs avoid letting these outstanding issues drag on.

I should note that CESR-FIN is also undertaking important work on advising the Commission on the equivalence of US, Canadian and Japanese GAAPs with IAS. This is a very difficult exercise but I hope we can come to sensible technical judgements by the end of 2005. I stress that our approach will be technical, not political.

Fourth, I underline the importance I attach to raising corporate governance standards throughout the EU. This is vital for raising confidence and belief in capital markets.

Finally, the external aspects of financial integration. We all know that financial markets are increasingly global and interconnected. The potential for problematic regulatory overspill is a very real one and one we should seek to avoid. So another top priority for my tenure as Commissioner will be regulatory dialogue with the US and other major financial markets: China, Japan, India and no doubt others in the future.

We must work to achieve "friction-free" relations. Our common objective should be to promote growing capital markets that supply the widest possible range of products at the lowest possible cost – to bring increased growth, prosperity and employment on a global basis. Here there is a real opportunity for the EU's regulatory system to become a model for the rest of the world.

Conclusion

To conclude, I should underline all that has been achieved so far. The FSAP has been largely agreed. But it still has to be properly implemented and applied – this will be the top priority.

Looking forward towards our Post-FSAP strategy – I will come forward with a policy view in the late spring. The watchword will be consolidation. I don't envisage another sweeping regulatory programme. The Commission's approach will be evolutionary – not revolutionary; practical not theoretical; and carefully calibrated.

I also want to see a vibrant risk capital market in the EU so we provide the best conditions for the development of our best small firms.

Throughout our work, we will check and make sure that our measures contribute positively to the Lisbon economic reform agenda and continue to boost growth and employment.

And that is the acid test for all of us.

Will the measures strengthen the European economy?

Thank you.