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Integration of European securities markets

Introduction

It is generally recognised that integration of European securities markets is economically beneficial to the Member States of the European Union and the European Economic Area. It promotes competition between securities service providers, enhances efficiency of financial systems and contributes to efficient allocation of resources. Integration can enable businesses to procure cheaper finance through securities market financing as an alternative to bank-based financing. Lower financing costs support growth and employment within the EU and the EEA.

Securities markets constitute an integral part of the single market and the EEA. EC regulation of securities markets, which is primarily based on the objective of market integration, represents an important part of the single market regulation and significantly supports its objectives and functioning. These rules have been incorporated into the EEA Agreement.

This paper discusses the development of EC securities market regulation with regard to its impact on the single market. Assessment will be made of the current scope and level of integration brought about by that regulation. The need for further integration will be considered, with reflections on the role of regulatory measures in delivering it.

The development of EC securities regulation

Objectives

The conventional objective of securities regulation is to correct market failures, i.e. failures in the market's self-regulatory mechanisms which obstruct the efficient allocation of resources by an otherwise perfect market. A number of factors dictate the intensity of such regulation, e.g. market structures, investor profiles and cultural attitudes.[2]

The construction of EC securities regulation began at a time when great differences existed between the scope and substance of Member States' regulation in this field. This presented barriers to cross-border access to national securities markets. The primary objective of EC securities regulation is to abolish such regulatory barriers and thereby to promote integration. The objective of regulating market failures has thus been pursued through the lens of consolidation rather than some clearly defined regulatory philosophy. EC securities regulation has therefore at times been unclear about the objectives it serves beyond market integration.

Treaty provisions and secondary legislation

The task of integrating securities markets follows from Articles 2 and 14 of the EC Treaty. The provision of securities and investment services falls under Chapter 3 EC on the freedom to provide services, and the operation of securities markets and trading is subject to Chapter 4 EC on the free movement of capital.

Articles 43, 49 and 56 EC on establishment, services and capital movements provide the basis for the removal of regulatory barriers to the convergence of securities markets. The Court of Justice has declared that Articles 43 and 49 have direct effect and may therefore be relied upon before national courts.[3] Discriminatory national measures restricting the free-

1. The author is Deputy Director of the Central Bank of Iceland's Financial Stability Department.

2. Moloney, N., *EC Securities Regulation*, OUP, 2002, at 6-10.

3. Case 2/74, *Reyners* v *Belgium* [1974] ECR 631 (establishment), and Case 33/74, *Van Binsbergen* v *Bestuur van de Bedrijfsvereniging voor de Metaalnijverheid* [1974] ECR 1299 (services).

dom to establish or to provide securities or investment services can only be justified under Articles 46 and 55, respectively. A strict proportionality test would, however, be applied for the justification of such discriminatory rules.[4]

The Court has played a key role in the establishment of the single market. However, due to the technical nature of financial services and the need for consumer protection, the free movement provisions have not been considered sufficient to abolish national regulatory barriers to the provision of financial services. In 1986 the Court ruled in the 'insurance cases'[5] that in view of the particular nature of insurance services, a certain degree of coordination and harmonisation was necessary in order to exercise the freedom to provide services in the insurance sector. The lack of harmonisation and coordination in secondary legislation was therefore seen to justify restrictions on the freedom to provide insurance services.

It follows from Articles 3(h) and 5 EC that EC securities regulation must be based on the single market legislative competences. The regulation therefore does not enjoy an existence independent of the single market. Securities regulation has mainly been based on the competences provided for in Articles 44(2)(g), 47(2) and 55 EC, relating to free movement and removal of hindrances, and the general single market competences set out in Articles 94 and 95.

Harmonisation and mutual recognition

The development of EC securities regulation started slowly. The 1966 Segré Report[6] identified obstacles to the integration of capital and securities markets and proposed corrective measures. In 1977 the Commission issued a Recommendation for a European Code of Conduct Relating to Transactions in Transferable Securities[7] which became the first attempt to develop a common set of EC rules for securities and investment services.

The initial objective of secondary securities regulation was to establish a liquid securities market for capital raising, accessible for issuers within the whole Community.[8] The regulatory approach during the late 1970s and early 1980s was to introduce detailed harmonised rules in order to make national standards equivalent.[9] This was the approach taken in the preparation of the Admission Directive,[10] the Listing Particulars Directive[11] and the Interim Reports Directive.[12]

This approach changed as a result of the *Cassis de Dijon* judgment[13] on mutual recognition and mandatory requirements in the context of the free movement of goods. In the field of financial services the *Cassis* jurisprudence developed the concept of mutual recognition of Member States' rules on the right to provide financial services. The core elements of this approach are the 'single passport' and 'home state supervision' concepts. The *Cassis* jurisprudence also introduced the right for Member States to impose non-discriminatory regulation, in the interest of the general good, on cross-border financial services in order to safeguard market stability and consumer protection, even where this hindered the exercise of the Treaty freedoms. The regulatory measure, however, had to be non-discriminatory, objectively justified by imperative requirements in the general interest, and proportionate.[14]

4. Case C-101/94, *Commission* v *Italy* [1996] ECR I-2691.
5. Case 205/84, *Commission* v *Germany* [1986] ECR 3755, Case 220/83, *Commission* v *France* [1986] ECR 3663, Case 252/83, *Commission* v *Denmark* [1986] ECR 3713, and Case 206/84, *Commission* v *Ireland* [1986] ECR 3817.
6. Report by a Group of Experts Appointed by the EEC Commission, *The Development of a European Capital Market* (1966).
7. Recommendation 77/534/EEC [1977] OJ L212/37.
8. See Wouters, J., 'EC Harmonisation of National Rules Concerning Securities Offerings, Stock Exchange Listing and Investment Services: An Overview' (1993) 4 *EBLRev* 199.
9. Edwards, V., *EC Company Law*, OUP, 1999, at 231-233.
10. Council Directive 79/279/EEC of 5 March 1979 coordinating the conditions for the admission of securities to official stock exchange listing [1979] OJ L66/21.
11. Council Directive 80/390/EEC of 17 March 1980 coordinating the requirements for the drawing up, scrutiny and distribution of the listing particulars to be published for the admission of securities to official stock exchange listing [1980] OJ L100/1.
12. Council Directive 82/121/EEC of 15 February 1982 on information to be published on a regular basis by companies the shares of which have been admitted to official stock-exchange listing [1982] OJ L48/26.
13. Case 120/78, *Rewe-Zentral AG* v *Bundesmonopolverwaltung für Branntwein (Cassis de Dijon)* [1979] ECR 649.
14. Case 33/74, *Van Binsbergen* v *Bestuur van de Bedrijfsvereniging voor de Metaalnijverheid* [1974] ECR 1299, Case C-55/94, *Gebhard* v *Consiglio dell'Ordine degli Avvocati e Procuratori di Milano* [1995] ECR I-4165, and Case C-384/93, *Alpine Investments* v *Minister van Financiën* [1995] ECR I-1141.

It was clearly not a desirable situation to have different Member States pleading divergent restrictive national rules by reference to the general good. Furthermore, in its 1985 White Paper, 'Completing the Internal Market', the Commission noted that the harmonisation strategy had presented difficulties relating to over-regulation, cumbersome implementation and inflexibility.[15] Not surprisingly, the focus of regulation now shifted from general harmonisation to a minimum harmonisation of public interest rules.

The White Paper, the ensuing 1986 Single European Act and the 1992 Single Market Programme recognised the importance of securities and capital market regulation for the establishment of the single market. They introduced a new era in EC regulation of investment services and securities markets, based on the model of mutual recognition and minimum harmonisation. They also called for greater liberalisation of capital movements in order to enhance integration of financial services markets.

The UCITS Directive, adopted in 1985, introduced the passport regime whereby home Member States authorise undertakings for collective investment to provide services across the Community in accordance with common standards.[16] The 1988 Capital Movements Directive[17] enabled the adoption of a range of liberalising securities and investment services measures. In 1988 the Major Holdings Directive[18] was adopted and in 1989 the Prospectus Directive[19] and the Insider Dealing Directive,[20] all of which were intended to enhance the integrity of securities markets.

The Investment Services Directive,[21] adopted in 1993, was a major step in regulating investment services. It sets out minimum authorisation and operating requirements for investment firms, grants them a passport and addresses access to regulated markets across the Community. The Capital Adequacy Directive,[22] also adopted in 1993, provides for harmonised capital requirements for investment firms and credit institutions. The Investor-Compensation Schemes Directive,[23] adopted in 1997, provides for a redress when prudential rules fail and losses are sustained by investors.

By the mid 1990s the harmonisation of some of the basic elements of securities and investment services regulation had been accomplished, supported by a network of national authorities collaborating on the supervision of common standards. Although large areas of market conduct and conduct of business remained outside the scope of harmonisation, the fundamental preconditions for the functioning of a mutual recognition regime had been established. Secondary regulation, relevant to securities markets and services, had removed pertinent obstacles to the freedom of establishment and the free movement of services and capital. EC securities regulation had thereby contributed significantly to the establishment and functioning of the single market.

Mutual recognition as an integration device

Mutual recognition of regulatory standards is based on the acceptance, to a certain degree, of regulatory differences, flexibility and competition between Member States while the minimum harmonisation of prudential regulation, together with supervisory cooperation, ensures basic protection of the public interest. In theory, mutual recognition and minimum harmonisation of public interest rules represent an effective way of removing market and regulatory barriers in the field of securities services within the Community. EC securities regulation is meant to be a coherent framework regulation, existing and func-

15. European Commission, *Completing the Internal Market*, COM (85)310, para 64.
16. Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) [1985] OJ L375/3.
17. Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty [1988] OJ L178/5.
18. Council Directive 88/627/EEC of 12 December 1988 on the information to be published when a major holding in a listed company is acquired or disposed of [1988] OJ L348/62.
19. Council Directive 89/298/EEC of 17 April 1989 coordinating the requirements for the drawing up, scrutiny and distribution of the prospectus to be published when transferable securities are offered to the public [1989] OJ L124/8.
20. Council Directive 89/592/EEC of 13 November 1989 coordinating regulations on insider dealing [1989] OJ L334/30.
21. Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field [1993] OJ L141/27.
22. Council Directive 93/6/EEC of 15 March 1993 on the capital adequacy of investment firms and credit institutions [1993] OJ L141/1.
23. Council Directive 97/9/EC of 3 March 1997 on investor-compensation schemes [1997] OJ L84/22.

tioning in harmony with different national securities regimes. This is based on the premisses that public interest rules have been harmonised and that Member States are willing to apply in full the principle of mutual recognition.

The principle of mutual recognition has proved to be an important lever in opening up national securities markets. Nevertheless, EC securities regulation does not fit altogether the different national securities regimes and fragmented market structures and practices. Consequently, EC regulation and the different national regimes co-exist and function in a complex and inconsistent manner where the latter continue to impose obstacles to the integration of securities markets.

Different national legal traditions and market practices have obstructed the exact and complete definition of the subject matter of the necessary public interest rules for all the national securities markets. It has therefore been difficult to determine whether, how and to what extent public interest rules should be harmonised. Important areas of securities market conduct, conduct of securities business, disclosure and market manipulation have not been harmonised at all, or at an insufficient level.[24] Member States are allowed to impose regulatory, non-discriminatory requirements in the interest of the general good in circumstances not accounted for in the harmonised EC regulation. Furthermore, the implementation and application of the harmonised public interest rules differ widely between Member States. The legislative form of EC securities regulation is predominantly the directive which leaves the choice of form and method of implementation to the national authorities. Incomplete and inconsistent transposition of directives harms their effectiveness as an integration mechanism.[25] Consequently, the scope and level of harmonisation has inadequately supported integration through mutual recognition.

Meanwhile, structural changes have introduced new challenges for securities markets and regulation. The most important ones are the full liberalisation of capital movements, the single currency, Community-wide investment patterns, developments in technology and infrastructures, enhanced competition and market restructuring. These changes have promoted the integration of European securities markets and practices. However, EC securities regulation has failed to respond to challenges posed by these developments and to support their ability to integrate markets.

The Action Plan

At the end of the 1990s the fragmentation of securities markets became an important subject of EC integration policy. The full integration of securities and investment markets was considered to play a key role for the completion of the single market, for the success of the monetary union, and for the enhancement of growth and employment.

These concerns were addressed at the 1998 Cardiff European Council. At its request the Commission issued a Communication later that year on 'Financial Services: Building a Framework for Action'.[26] The Communication acknowledged that securities markets were segmented, and pointed out several areas where reform was needed: (1) a revision of the legislative process in order to respond better to market developments and challenges; (2) modernisation of wholesale financial markets; (3) completion of the single market for retail financial products; (4) review of supervisory mechanisms and regulatory collaboration; and (5) other measures such as integration of infrastructures, effective application of competition and state aid rules, and tax harmonisation.

Subsequently, the Commission translated these objectives into a work programme, 'Implementing the Financial Services Action Plan' (FSAP), adopted in May 1999.[27] It recognised that shortcomings in harmonisation were impeding integration and that market developments had posed new regulatory challenges. It set out a programme of 42 measures aimed at significantly strengthening financial services and securities regulation.

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24. Avgouleas, E., 'The Harmonisation of Rules of Conduct in EU Financial Markets: Economic Analysis, Subsidiarity and Investor Protection' (2000) 6 *ELJ* 72, at 73-77.
25. Moloney, N., *EC Securities Regulation*, OUP, 2002, at 11-16.
26. European Commission, *Financial Services: Building a Framework for Action*, COM(1998)625.
27. European Commission, *Implementing the Financial Services Action Plan*, COM(1999)232.

In the field of investment and securities services the FSAP proposed a revision of the Investment Services Directive in order to clarify the conduct of business regime and remove obstacles to market access for brokers/dealers,[28] a revision of the disclosure framework to foster transparency, an upgrade of the directives on prospectuses in order to enable the use of a single prospectus in cross-border capital raising, a revision of the collective investment regime, an improvement of investor protection and supervisory collaboration, and adoption of a takeover regime. It proposed new directives or regulations on, *inter alia*, insider dealing and market manipulation, a European company statute, financial collateral arrangements, distance marketing of financial services, a new capital framework for banks and investment firms, supplementary supervision of financial conglomerates, taxation of savings income, application of international accounting standards and fair-value accounting.

The 2000 Lisbon European Council took an important political step towards the integration of financial services and capital markets. It recognised the central role of securities markets in generating growth and employment and stressed the importance of convergence, efficiency and stability of securities markets. It set a target date of 2005 for the completion of all the FSAP measures.

The Member States, the Council, the Parliament and the financial industry have generally been supportive of the objectives and the adoption of the FSAP measures.

The Lamfalussy recommendations

In 2000 the Council set up a Committee of Wise Men in order to assess how the regulatory mechanism could better respond to market developments in order to ensure greater convergence of market practices. The Committee delivered its report (the Lamfalussy Report) in 2001.[29] It criticised the inability of the regulatory regime to respond timely and effectively to market developments and new challenges. A revision of the law-making process was called for in order to enhance integration, growth and employment and to strengthen the competitiveness of the EU. It proposed that regulatory measures would consist of four levels. The first level would correspond to the conventional law-making procedure set out in the Treaty whereas the other levels would deal with technical details, supervisory cooperation and enforcement.

By increasing sensitivity to market developments and enabling the adoption of detailed technical measures in a speedy manner on the basis of wide consultation with market participants, such a law-making process would have a fundamental impact on EC securities regulation. The core emphasis would no longer be integration through mutual recognition of national regimes but convergence through effective, regulatory intervention in national regulation and practices.

The 2001 Stockholm European Council endorsed the final Lamfalussy report. However, the European Parliament expressed reservations about the levels of transparency and consultation under the new approach. It sought, in particular, assurances that its powers would be equivalent to those of the Council. These reservations were finally overcome in 2002.

The new legislative process is to work in the following manner:

- Level 1 consists of legislative acts, i.e. directives or regulations, proposed by the Commission following consultation with interested parties, and adopted by the Council and the Parliament under the co-decision procedure in accordance with the Treaty. On the basis of a Commission proposal the Council and the Parliament agree on the nature and extent of detailed technical implementing measures for each legislative act.
- At Level 2, the European Securities Committee (the regulatory committee) assists the Commission in adopting the relevant implementing measures. This is to ensure that technical provisions can be kept up to date with market developments.
- Level 3 measures have the objective of improving the uniform implementation of Level 1 and 2 measures in the Member States. The Committee of European Securities Regulators (CESR) has particular responsibility for this.

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28. Ilmonen, K.R., 'Changing the Investment Services Directive: Brokers-Dealers and Institutional Investors' (2002) *Company Lawyer* 135, at 136-138.

29. Final Report of the Committee of Wise Men on the Regulation of European Securities Markets, February 2001.

- Level 4 addresses the effective enforcement of EC law by the Commission.

Implementation and enforcement

A study, prepared at the request of the Commission and published in November 2002,[30] highlighted the powerful role that efficient and liquid financial markets can play in complementing bank-based finance to support growth and employment in the EU. The study predicted that the integration of EU financial markets would bring significant benefits to businesses, investors and consumers. It indicated that EU-wide real GDP would increase by 1.1% over a decade, and that total employment would increase by 0.5%. Businesses would be able to procure cheaper finance as integration of equity markets would reduce the cost of equity capital by 0.5%. A 0.4% decrease in the cost of corporate bond finance was expected to follow. Investors would also reap benefits from integration in the form of higher risk-adjusted returns on savings. The study called for the completion of the FSAP by 2005 and stressed the need for adoption of legislative proposals on investment services, prospectuses, market abuse and pension funds.

The Commission monitors the progress of the FSAP and has submitted reports on the adoption of the proposed measures. In November 2003 it issued its Ninth Progress Report[31] in which it concluded that the FSAP had been one of the driving forces behind the development of the European capital market, and had improved prospects for sustainable, investment-driven growth and employment. The legislative timetable for the adoption of FSAP measures had continued to be respected and 36 of the 42 original measures been finalised.[32] In the report the Commission stated that the FSAP was now drawing to its close and that the focus would shift from intensive legislative drafting and negotiation to the delivery of the FSAP through consistent transposition and enforcement of the adopted measures.

Furthermore, the Commission stated in the report that it would launch a wide-ranging, transparent and bottom-up assessment of the state of integration of European financial markets following the completion of the FSAP. The purpose of the assessment would be to understand the extent of any remaining gaps in the regulatory, supervisory, administrative and public policy framework. The assessment would be a key input in developing a consensus on policy challenges at the European level. However, the process should not be viewed as the prelude to an ambitious new legislative programme, although legislative action should not be ruled out. Sectoral expert groups would be constituted in the areas of banking, insurance, securities and asset management. Their task would be to identify impediments to the effective integration of financial markets and assess which market failures give rise to the biggest opportunity cost for Europe.[33] The work of the sectoral group is expected to serve as a basis for a high-level forum in the summer of 2004.[34]

The way forward

The need for further integration

The FSAP measures will abolish many of the existing regulatory barriers to securities market integration. It is therefore important to ensure effective and coordinated implementation and application of these measures. However, it would be premature to expect that they will complete the picture and deliver a fully coordinated single securities market. Regulatory impediments, in some form or another, will exist as long as there are different national securities regimes and supervisory practices. Therefore, in due course, the Community will have to take stock again of the need to adopt further corrective measures.

This is in fact an ongoing process. New measures will be needed in order to coordinate regulatory standards and supervisory practices. This will continue to enhance the level and scope of convergence of securities markets and could, eventually, lead to the establishment of a truly single securities market.

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30. London Economics, *Quantification of the Macro-Economic Impact of Integration of EU Financial Markets*, November 2002.
31. European Commission, *Financial Services: The FSAP enters the Home Straight, Ninth Report*, November 2003.
32. ibid, at 1-2.
33. ibid, at 10-12.
34. In addition to the work of the Commission in this respect, the ECOFIN Council in July 2003 provided the Financial Services Committee with a mandate to prepare a report on the benefits of financial integration, the state of integration and the areas where progress needs to be made in order to create a truly integrated financial market in the EU.

The extent and pace of that process is, however, a highly political matter. It concerns the level of overall economic integration in Europe, and the sensitive issue of further relinquishment of national sovereignty in this field. This relates, for example, to the extent to which securities regulation should be centralised, and whether securities supervision should be transferred from the Member States to a central securities supervisor.

Full integration of securities markets would contribute significantly to the completion of the single market project and provide important economic benefits. However, various factors, other than conventional EC regulatory measures, need to be considered as means of achieving that objective. Some of these are discussed below.

Regulatory competences

National securities markets tend to be characterised by different rules, practices and preferences relevant to market conduct and conduct of business, many of which have not been subject to EC regulation. Corrective measures need to be taken where such inconsistencies unduly impinge on securities market integration. It is questionable, however, whether and to what extent this should be done through national regulation, supervisory cooperation or harmonisation at EC level. Although the subsidiarity principle provided for in Article 5 EC is generally not seen as impeding the coordination of securities regulation it could affect the extent to which the EC legislator is willing to harmonise such local practices and preferences.

It is generally recognised that securities market integration is economically beneficial. It provides a larger securities market, enhances freedom to provide and receive cross-borders securities services and contributes to efficient allocation of resources. However, a well functioning securities market is characterised by more than size and accessibility. Stability, security and efficiency are key characteristics of such a market. Abolishing regulatory barriers to the interaction of national securities markets is therefore not enough. They need to function as a single, coherent unit in a secure and efficient manner.[35] It is therefore necessary to ensure that overall stability, security and efficiency are appropriately provided for in regulation and supervisory practice. This requires coordination of national securities regulation beyond the conventional objective of abolishing regulatory obstacles to cross-border market access.

In this respect, however, it needs to be considered that although the Court has shown a tendency to respect the competences of the EC legislator to regulate complex economic situations,[36] it held in the *Tobacco Advertising* ruling[37] that, in principle, the internal market competences do not confer a general power to regulate the internal market. This may in certain circumstances obstruct the development of EC securities regulation aiming at fine-tuning practices and techniques relevant to the operation of integrated securities markets.

In situations where there is a need for regulatory measures, but where the single market regulatory mandate is not sufficient, fit or appropriate to provide for the necessary coordination, national authorities need to cooperate in order to achieve convergence of national standards and practices. The network of national regulators and supervisors needs to be strengthened for this purpose. The first steps in this direction have already been taken under the Lamfalussy law-making model and the new securities committee framework.[38]

Regulatory competition

At the current stage of the development of EC securities regulation it is worth considering whether regulatory competition represents an alternative or an addition to the existing tools for securities regulation. This question is particularly pertinent with regard to the effect of the principle of subsidiarity and the limits of the single market regulatory mandate.

35. Ferrarini, G., 'The European Regulation of Stock Exchanges: New Perspectives' (1999) 36 *CMLRev* 569, at 590-597.

36. Case C-233/94, *Germany* v *European Parliament and Council* [1997] ECR I-2405.

37. Case C-376/98, *Germany* v *European Parliament and Council* [2000] ECR I-8419.

38. See Commission Decision 2001/527/EC of 6 June 2001 establishing the Committee of European Securities Regulators [2001] OJ L191/43, as amended by Commission Decision 2004/7/EC of 5 November 2003 [2004] OJ L3/32, and Commission Decision 2001/528/EC of 6 June 2001 establishing the European Securities Committee [2001] OJ L191/45, as amended by Commission Decision 2004/8/EC of 5 November 2003 [2004] OJ L3/33.

In connection with the principle of mutual recognition, the Member States have been able to adapt their securities regulation to the preferences of market players in order to strengthen domestic markets. Regulatory competition has been regarded in this context as a positive phenomenon as it removes the regulatory focus from the EC to the Member States and improves market access and efficiency.

Regulatory competition can put pressure on national regulators to take measures to adjust domestic standards to market demands and preferences. Based on regulatory arbitrage, such competition encourages market participants to choose the market which best fits their preferences, be it low cost, information, speed or other efficiency parameters. It also enables market players to select the most suitable home state for establishment, i.e. where the regulatory regime and supervisory practices best fit their business objectives.

The extent to which this view still applies may be doubtful, however, given that the trend seems to be in the direction of greater coordination of national securities regulation. Regulatory competition can contribute to divergence of securities regimes and trading practices. Moreover, despite the notion that investors and market players generally prefer a balanced approach between market efficiency and security, regulatory competition may entail the danger of a 'race to the bottom' with respect to prudential regulation and supervision. Furthermore, asymmetric regulation and divergent market practices increase the risk that disruptions or failures in one market will spill over to other markets and affect financial stability.

The global dimension

The world's securities markets are increasingly showing signs of interaction, globalisation and convergence. European securities markets co-exist and interact with non-European markets, for example the US market. It is seen as a positive sign that firms and investors can access global markets from their home countries. European securities markets are in many respects subject to comparison to, and competition from, other securities markets. Consequently, European regulators face the challenge of supporting the efficiency, reputation and competitiveness of European securities markets in a global context.

Furthermore, international cooperation has established regulatory standards for enhancement of the stability and efficiency of securities markets at a global level. The International Organisation of Securities Commissions (IOSCO), the Basel Committee on Banking Supervision and the International Accounting Standards Board have cooperated in establishing prudential standards and best practices for financial and securities services and markets. Such internationally recognised standards are likely to be incorporated in some way or another into European securities regulation. Cooperation with international bodies is therefore needed in order to ensure equivalent regulatory standards and to avoid unnecessary regulatory duplication. International developments are thus likely to become an increasingly influential factor in the regulation of EC securities markets.

Market restructuring

EC financial regulation, integration of financial markets and the single currency have encouraged credit institutions and investment firms to expand their activities beyond national boundaries. For them the convergence of financial and securities markets has become a business opportunity in an enlarged market. Consequently, they have been pushing for further coordination of regulatory standards and supervisory practices.

The consolidation of market players through vertical and horizontal mergers, the establishment of financial conglomerates and the emergence of the European Company (Societas Europaea) call for uniform and coherent regulation and supervision. National and EC regulators realise that they have to respond to new regulatory challenges posed by market trends and restructuring in order to enhance integration, and to ensure an adequate level of investor protection, competition and financial stability. Meanwhile, they need to consider regulatory preferences of market players with regard to their international competitive position.

The interaction of different national securities markets is much dependent on the interoperability of the different securities trading systems and securities settlement systems. Consolidation of infrastructures can therefore be an important vehicle for further integration of securities markets. In recent years,

alliances between traditional stock exchanges, pan-European trading platforms and alternative trading systems have contributed to the integration of European securities markets.[39] However, the interoperability of different securities settlement systems has lagged behind, and these systems remain fragmented. The inefficiency, cost, time and risk involved present an important obstacle to the convergence of securities markets operations. The interoperability of settlement systems is a complex technological task which will have to be resolved through market-driven innovation, cooperation and consolidation, rather than regulation.[40] Nevertheless, in this respect, the EC and national regulators, supervisors and overseers have an important role to play in limiting systemic risk and in ensuring a level playing field as regards access to and operation of these systems.

Conclusion

Integrated securities markets form an integral part of the single market. EC securities regulation is an important element in the regulation of the single market and significant for its objectives and development.

EC securities regulation is primarily based on the objective of integrating fragmented national securities markets. Integration has mainly been achieved through mutual recognition of national standards and minimum harmonisation of public interest rules. EC securities regulation and different national securities regimes nevertheless function in a complex and inconsistent manner where the latter continue to impose obstacles to the full integration of securities markets.

The 1999 FSAP addressed the weaknesses of securities regulation and proposed corrective measures. These measures will abolish many of the existing regulatory barriers to securities markets integration. However, it is very likely that new regulatory measures will be needed in order to enhance further the level and scope of integration. Greater coordination of local securities market practices and business conduct rules needs to be promoted. EC securities regulation needs to address increased globalisation of financial systems, securities markets and regulatory standards, and respond to new challenges posed by market trends and developments. This requires enhanced cooperation between EC and national regulators and supervisors, and could promote the centralisation of regulatory and supervisory powers.

Meanwhile, the integration of securities markets affects the way in which national financial markets and systems are exposed to the risk of disruptions and failures. This makes it necessary to turn the focus increasingly towards the overall stability and efficiency of the integrated markets as a whole.

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39. See e.g. Hirsch, S., and Marquette, V., 'EURONEXT: The First Pan-European Exchange, An Overview from Creation to Completion' (2001) 3(3) *Journal of International Financial Markets* 105, at 105-106.

40. The Giovannini Group, *Second Report on EU Clearing and Settlement Arrangements*, April 2003, at 39-40.

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