

THE PROGRESS REPORT ON THE FINANCIAL SERVICES ACTION PLAN

Summary: The 8th progress report on the Financial Services Action Plan (FSAP) contains a clear message for all European institutions and individual Member States; there are only nine months left to complete the legislative aspects of the FSAP. Some tricky and long-term dossiers have yet to be completed, including: the Takeover Directive; the Prospectus Directive; the revision of the Investment Services Directive; and the third Capital Adequacy Directive. As we look at what needs to be done in the agreed timeframe we can at least conclude that the European institutions are faced with a real challenge. The completion of the FSAP is not a goal in itself - a single European market for financial services is the objective. Assuming that everybody involved will act responsibly and complete the FSAP on time, the question is whether we will then have reached the goal of a single European market for financial services or whether additional efforts are needed. Since the start of the FSAP the Commission has reacted to market developments by introducing new measures, which will not be implemented before the original deadline of the FSAP. Besides these newly introduced measures one can argue that, especially in retail financial markets, a lot of work still needs to be done before we have a truly integrated single financial services market.

1. Financial Services Action Plan: Background

The Financial Services Action Plan (FSAP) of May 1999 identified a significant number of actions that were needed to create a single market for financial services. The Lisbon European Council of April 2000 reaffirmed the implementation of that action plan by 2005 and set a new date for the integration of EU securities markets of end-2003. In early 2001, the Lamfalussy report confirmed that the FSAP priorities were largely the right ones.

2. Eighth Progress Report

On 2nd June 2003 the Commission published its eighth progress report on the FSAP. Of the original 42 measures, 34 have been completed including important measures such as market abuse, pension funds and international accounting standards.

General observations

Recent market developments have put pressure on financial markets; between mid-2000 and early 2003, stock markets consistently trended downwards, economic growth slowed dramatically and corporate scandals and bankruptcies arose around the world. Since late 2002, the prospect of and subsequent conflict in the Gulf dampened investor confidence and continues to strain international relations with inevitable impact on investor sentiment. The slowdown in global economic activity has led to an increasing incidence of bad loans, and a fall in equity and debt market activity. The Commission has noted that, although the financial system remained relatively stable, with limited systemic disruption, these developments have reinforced the need for timely completion of the FSAP. The action plan is designed to:

- bolster financial stability and market integrity
- enhance European regulatory co-operation, which should offer a good starting-point for reaping the full benefits of an integrated market
- create a stable framework for the smooth financial integration of the 10 accession countries

- encourage a long-term restructuring of the European financial sector, which research has shown will generate structural economic benefits

What still needs to be done

A great deal of substantive work needs to be done over the coming nine months in order to deliver the Action Plan by the April '04 deadline. The message accompanying the publication of the latest progress report is therefore one of urgency.

Box 1: Legislative work-programme 2nd half 2003 and Q1 2004

Proposals scheduled for adoption by EP/Council

- Prospectus Directive
- Takeovers Directive
- Transparency Directive
- Investment Services Directive

Prospects for the immediate legislative programme are mixed. While the Prospectus Directive, currently at 2nd Reading, looks to be on schedule, swift adoption of the Takeovers Directive will be extremely challenging. This issue already has a long history, dating back to 1989. For its part the Transparency Directive has only recently been published. It is clear that strong differences exist over some of its contents, such as the obligation to publish quarterly figures. The revision of the Investment Services Directive has also proved to be a delicate exercise. The number of amendments offered on the text illustrates this: over 50 amendments were tabled on Article 25 alone.

Box 2: Work-programme 2nd half 2003 and Q1 2004

Expected Commission Proposals

- Follow-up Action Plan on Company Law and corporate governance*
- Modernisation of the 8th Company Law Directive (statutory audit) *
- 10th and 14th Company Law Directive
- Endorsement of the International Accounting Standards
- Commission Communication on Clearing and Settlement*
- 3rd Money Laundering Directive*
- Review capital requirements financial institutions (CAD3)
- Insurance Solvency II*
- Reinsurance Supervision*
- EU Legal Framework for Payments in the Internal Market*

* not in the original FSAP, added as result of market developments

As for proposals, which have yet to be tabled, it is also clear that here, too, some difficult issues remain. Clearing and Settlement, the Legal Framework for Payments and most notably Capital Adequacy are all complicated dossiers which raise specific operational and structural issues. Legislative work on these dossiers will have to be adopted by end 2005.

Looking at boxes 1 and 2 it is clear that there are some very important measures still on the table. The sense of urgency from the Commission is therefore understandable: the crux of the FSAP and the single market for financial services will be tackled over the coming two years.

Beyond the nine months of legislative action

Following its mid-term review of the FSAP, in February 2002, the Commission identified where the focal point should be after the period of intensive legislative drafting. In its Progress Report three primary policy objectives are identified:

1. Common implementation and enforcement

In order to take full advantage of the framework that is taking shape, focus should be on effective implementation and enforcement. As the 12th Internal Market Scoreboard shows, Member States are, in general, late in implementing legislation. To improve common implementation, a mechanism for solving individual cases has been established (SOLVIT). In the near future the Commission will examine these mechanisms to optimise the implementation of the FSAP. The proposal to extend the Lamfalussy process to banking and insurance and consequently, establish Level 2 and Level 3 Committees will also encourage common implementation and enforcement by national financial regulators and supervisors.

2. Optimising the FSAP – identifying and resolving new challenges

Technological developments and other structural changes have an impact on the financial markets. This requires an objective method of determining where the focus of the legislative authorities should be. The Commission has developed a set of financial indicators which could act as policy guidance tools. Furthermore the initial Financial Services Policy Group (FSPG) has been reconfigured into the Financial Services Committee (FSC). The tasks of the FSC will be to give political oversight and advice to ECOFIN and the Commission on issues related to the regulatory framework for financial markets.

The introduction of more rigorous cost-benefit analysis - something the Parliament has requested for some time - will be part of developing regulatory proposals.

3. Handling the Global Dimension

It is clear that regulation and supervision of financial markets can no longer ignore the global dimension. In particular, the relationship with the US is of the utmost importance. The Commission has underlined the importance of cooperation and continuous dialogue between Europe and the US and it is with this in mind that the EU has entered into the ‘EU-US financial markets regulatory dialogue’. This process should be politically endorsed and remain high on the agenda.

3. What does the post-FSAP world hold?

Beyond 2005, the focus is expected to be on implementation and enforcement. Ideally, implementation progress reports would continue, in order to sustain momentum and to bring peer pressure to bear on Member States to apply legislation appropriately. This could be achieved through, for example, a Financial Services Scoreboard similar to that already in place for Internal Market measures.

However, there will undoubtedly be more issues in the financial services sector that require EU action. In the area of retail financial services, for example, coordinated action will be needed to facilitate the cross-border selling of financial products and ensure a level playing field with limited national discretion. New market developments, global developments (e.g. relationship with the US) and the accession of the ten new countries will likely require additional initiatives by the European institutions, though not necessarily of a legislative nature.

Conclusion

The creation of a truly single European market for financial services will require continued effort from all of the Union's institutions and the individual Member States.

Whatever the format of the post-FSAP approach, the essential message must be that progress should remain on track. Once necessary measures to enhance investor protection and investor confidence such as Market Abuse Directive have been adopted and implemented, industry will look to the EU Institutions to re-focus on efforts to remove the many barriers to cross border activity that will remain despite the FSAP's enactment. For its part, industry will have to be more effective in identifying such barriers and notifying them to the appropriate EU bodies.

Briefing notes are prepared by the Industry Advisory Committee to the European Parliamentary Financial Services Forum. For further information on the subjects raised in the briefs please contact the Chairman, Members or Secretariat of the Advisory Committee.

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