

CREATING A SINGLE EUROPEAN MARKET FOR FINANCIAL SERVICES

- A DISCUSSION PAPER

**Produced by a working group in the City of London drawn from a broad
range of international financial services interests**

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EXECUTIVE SUMMARY

CREATING THE SINGLE EUROPEAN MARKET FOR FINANCIAL SERVICES

This note:

- **Recalls the Lisbon Council Conclusions calling for the completion of the single market in financial services, which is one where buyers and sellers of financial services and products may deal with one another throughout the EU, wherever they, their systems or infrastructures may be located;**
- **Emphasises the benefits, in terms of greater choice and better value for customers, prosperity, jobs and growth, which a single financial services market can bring;**
- **Describes what the single financial market should look like, including the need to be responsive to users;**
- **Reminds that financial markets usually work with “other people’s money” and that investors expect markets to operate in a stable, responsible and ethical manner and to be subject to high standards of governance and accountability;**
- **Explains why such a market does not yet exist;**
- **Sets out eight Principles and Practices to underpin policy, legislation, consultation, regulation, surveillance, implementation, enforcement, corporate governance and external review which are needed to achieve the objective of a competitive, innovative fully functioning single market.**

On the basis of the reasoning in this paper, it is suggested for discussion that the following Principles and Practices should be formally enshrined in the most authoritative manner in Community law and practice:-

- 1. Markets are created and developed by market participants not by rules and regulations (paragraph 36)**
- 2. Policy instruments other than legislation should always be considered in preference to the legislative route. If legislation is necessary it should be proportionate, cost effective and address clear market failure (paragraphs 37-38)**
- 3. Consultation with participants is required at all stages, and in a timely manner, and with a reasoned response to practitioner input (paragraphs 39-41)**
- 4. Regulation must be risk based, taking account of the different nature of the risks facing the different types of firms, customers, investors and counterparties (paragraphs 42-43)**
- 5. Surveillance, implementation and enforcement must be effective both at the national level and by the Commission (paragraphs 44-45)**
- 6. Regulation and behaviour of market participants must help build fair and honest markets, while not frustrating or stultifying their innovation and development (paragraph 46)**
- 7. Representatives of market practitioners should provide regular reports to the European Council, ECOFIN, Parliament and Commission on progress towards creating a fully functioning single market (paragraph 47)**
- 8. A European Financial Market Forum should be established to help develop a coherent approach and philosophy for the creation of the Single Market (paragraphs 48-50)**

I INTRODUCTION

“Efficient and transparent financial markets foster growth and employment by better allocation of capital and reducing its cost. They therefore play an essential role in fuelling new ideas, supporting entrepreneurial culture and promoting access to and use of new technologies. It is essential to exploit the potential of the euro to push forward the integration of EU financial markets. Furthermore, efficient risk capital markets play a major role in innovative high-growth SMEs and the creation of new and sustainable jobs.”

1. This was the agreement of the Heads of State or Government at the Lisbon European Council in March 2000. In effect this acknowledged the progress made since the launch of the single market vision in the 1985 Internal Market White Paper but recognised that more remains to be done. Since 2000 further progress has been made towards the Lisbon goal of integrated EU financial markets. For example,
 - Passage of the legislation in the Financial Services Action Plan (FSAP) is well under way. The latest report from the Commission (2 October 2002) notes that 30 measures have been completed and that progress is being made on 15;
 - The creation of a Monitoring Group to review progress in implementing the Lamfalussy process, which will report in Spring 2003;

- **The Community's legislative institutions have agreed on the procedures that were recommended in the Lamfalussy report to speed up and make more efficient the legislative process to improve co-operation among regulators;**
- **The enhancement of the policy role of the Financial Services Policy Group;**
- **The extension of the multi-level Lamfalussy process to banking and insurance.**

2. Despite the adoption or proposal of legislation since Lisbon and progress at the institutional level most market participants would agree that a great deal of work is still needed to create a functioning Single European Market for Financial Services (hereafter referred to as the "Single Market"). The procedural and institutional improvements described above, though necessary, do not of themselves deliver the integrated market which requires market-driven changes by the participants, including new entrants. It is therefore timely to reflect on what further needs to be done to accomplish the goal set out at the Lisbon Council. Of course, such reflection should not impede any constructive work now in hand. It is in this spirit that this note has been written. It should be treated as a draft and as representing "work in progress", on which comments would be warmly welcomed.

II THE BENEFITS OF A SINGLE MARKET

3. The benefits of a Single Market should accrue to all the users of the market as well as to the European economy at large. They were clearly set out in the Interim Report from the group of “Wise Men” chaired by Alexandre Lamfalussy in November 2000, in particular:

- **Improved allocation of capital, through, for example**
 - ♦ **More efficient, deeper and broader security markets enabling savings to flow more efficiently to investment;**
 - ♦ **Lower transaction costs and improved market liquidity;**
 - ♦ **More diversified and innovative financial systems;**
 - ♦ **More opportunities to pool risk;**

- **More efficient intermediation between savers and investors, through**
 - ♦ **Intensified competition among financial intermediaries across Europe, leading to fewer inefficiencies;**
 - ♦ **Giving users greater freedom of choice;**
 - ♦ **The opportunity to reap economies of scale and scope across a larger market;**

- **A stronger, faster growing European economy resulting from the above.**

In short, the benefit is improved customer value and choice together with greater economic prosperity and efficiency.

4. Of all the elements in the process of economic reform set out at the Lisbon European Council, the achievement of the single European financial market is perhaps the most crucial one in creating

“the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion” (Lisbon Council Conclusions, March 2000)

This is because the financial market is the mechanism for allocating the savings of the Community’s citizens to their most productive uses – to creating growth, prosperity and jobs. Such a market can only be created by responding to the needs of users – savers, borrowers, issuers, intermediaries, traders, infrastructure and information suppliers - and by innovation and competition among participants. Europe faces global competition for capital and the world will not wait for Europe.

5. There has been a number of useful studies that have attempted to quantify the benefits, in terms of potential higher returns to savers, lower transaction costs or higher GDP. But none of these studies has had the public impact of the Cecchini Report, which publicised the benefits of the 1992 Single Market programme. But an important study for the Commission by independent consultants (November 2002) has just quantified some of the potential economic benefits of financial market integration. On the other hand there have been studies, such as the Gyllenhammer report (2001), which demonstrate how much more needs to be done to remove obstacles to an open, competitive single market.
6. The creation of a single market will allow the wider European market to compete on an equal basis with international rivals that are already

free of the constraints under which Europe labours. Finance is a global industry, and global players will seek to meet their financial needs in the marketplaces that offer them the greatest advantages in terms of cost, flexibility and liquidity. Beyond the potentially huge advantage offered to European retail investors by a single European market, there is another, potentially even greater prize to be won by ensuring that Europe is the wholesale financial marketplace of first choice for global investors.

III WHAT WOULD A SINGLE MARKET LOOK LIKE?

- 7. The objective is to achieve an integrated, fully functioning market where buyers and sellers of financial assets and services can deal with one another throughout the EU, wherever they, their systems or infrastructures may be located.**

- 8. Today, although there are some parts of the capital market which function well on a pan-EU basis, the systems of market participants, the processes of financial intermediation, the functions offered and the range of products available still largely reflect the old national markets. There is still some way to go to create the competitive, innovative, fully functioning, single financial market across the EU that is envisaged in the Lisbon Presidency conclusions.**

Such a market would involve:

- The freedom of market participants – intermediaries and end users – to invest and raise funds in all Member States;**

- Financial institutions authorised by their home state authorities to be able to compete whether by a branch or on a cross-border**

service basis within all national systems, with access to all essential infrastructures, on a remote basis if necessary;

- Intermediaries able to offer whatever functions, products, services and instruments they are licensed to provide by their home state authority across the EU;**
- Infrastructure providers to be free to offer services across the EU;**
- Market structures, intermediation processes, products/services/instruments, and infrastructures to evolve in response to market forces, competition and innovation;**
- An EU wide market for corporate ownership within a framework of sound corporate governance which safeguards shareholders interests;**

Simply to list such characteristics of an integrated market is sufficient to demonstrate how much still needs to be done.

IV AN ETHICAL AND STABLE FINANCIAL MARKET

- 9. Money and securities are the materials which financial markets handle. The sums involved account for a very large part of the wealth of the personal sector in the Member States. The relevant markets intermediate, reallocate and mitigate most of the biggest risks faced by private households and businesses, particularly (though not only) through insurance and pension provision. No other part of the economy apart from government itself has so much of people's wealth, welfare and wellbeing in its hands. So whenever financial service businesses or their employees fail to observe proper standards, they have it in their power to do great damage to**

individuals as well as to society at large. It is therefore natural that government authority should intervene through a variety of laws and regulations, to a greater degree than elsewhere in the economy, to protect people and institutions from such potential behaviour. In this regard we acknowledge the aims of the Competitiveness Council concerning corporate governance, the need for rigorous accounting standards, and of the Commission's concern for fair treatment of consumers.

- 10. It is also natural that the authorities should take a keen interest in maintaining the stability and continuity of financial markets and business, and their services and products. The economic and social costs of failure can be very serious. Hence the authorities' very proper interest in maintaining defences against the domino-effects of systemic failure. So, clearly regulators have a duty to act to promote and safeguard ethical and stable markets. But it is important too to recognise that inappropriate regulation can stunt innovation and product development and reduce customer choice. Misguided or heavy handed official action can damage or even destroy markets, as the initial development of the eurobond market in Belgium and Luxembourg following the adoption of measures by the USA illustrates.**

V DIFFERENT APPROACHES TO POLICY TOWARDS FINANCIAL SERVICES REGULATION

- 11. There are different approaches to policy towards financial services, reflecting the legal and political history and culture of different Member States and, in many cases, the nature of their financial markets. Whichever approach is followed, effective regulation requires the authorities to work with market participants to avoid mere lip service compliance with rules. One approach is characterised by detailed, highly prescriptive, hard-edged rules, as in the case of much of American securities regulation, but experience demonstrates the need to focus on substance rather than form. Another legislative approach is based more on overarching principles, trusting competition among firms and markets to deliver financial services efficiently and discourage non-compliance by a minority of participants.**

- 12. Moreover there can be a role for non-legislative solutions to single market problems as the first answer to difficulties, with legislation only used as a fall back. In many cases self-regulation by industry bodies, reinforced by the need of participants to avoid damage to their reputation, may provide the best results, particularly in sectors which are rapidly changing; legislation and regulation will be hard pressed to keep up with important new developments. Ombudsmen too may provide non-judicial redress, but this does not rule out judicial redress should the aggrieved individual wish to take the matter further. Ombudsmen are, however, invariably quicker than the judicial process.**

- 13. There is a place too for private sector and market driven solutions and of joint working between governmental and private sector**

bodies. But it should be emphasised that such non-legislative solutions can only play a role if they enjoy the confidence of the public and there is a high degree of assurance that they will deliver outcomes in a more effective way than legislation.

14. It can be difficult to lay down hard and fast rules to determine which of the different approaches to regulation is preferable for a particular market, product or industry and the judgement should be made on a case by case basis. It is a mistake to think that one approach is always the better one and the legislative framework should contain sufficient flexibility to accommodate a range of options, some being more appropriate for particular markets, participants or risks than others.
15. However, while healthy and productive financial markets will need intervention by the authorities, the well being of markets depends to an unusual degree on other factors. The intimate and intricate web of relationships in healthy markets is permeated and promoted to a remarkable degree by values, conventions, confidence, trust, incentives and expectations. The values these promote embrace honesty, openness, putting the customer first, avoiding conflicts, maintaining confidentiality, behaving in a professional way and with social as well as commercial responsibility. Where this value framework flourishes, financial markets generally flourish too; and where it is weak (for whatever reason), however good the laws and regulations may be themselves, the economy will perform less well, and citizens and consumers will suffer - all too often very directly.
16. Creating and maintaining these values is, primarily, a matter of self-regulation, active social responsibility, training and education in promoting good standards in corporate governance, the ethics of the professions and the proficiency levels of market operators in other

areas. However, marking and policing the frontier between official regulation, private sector self-regulation and social responsibility of many other kinds which one encounters requires a subtle, active and considered partnership between all parties involved.

VI HOW DO WE CREATE A FULLY FUNCTIONING INTEGRATED SINGLE MARKET?

- 17. Most, if not all, developed markets require some sort of “rules of the game”, if only to define the responsibilities of the various market participants and the means to enforce those responsibilities. Such rules can be informal but normally have the force of law. What should be the “rules of the game” for the single European financial market described above? What should be the legislative/ supervisory/ regulatory framework?**
- 18. In broad conceptual terms, two approaches have been suggested for providing the framework for the creation of the Single Market.**
- 19. The first approach is the complete harmonisation of legislative/ supervisory/regulatory objectives, instruments and structures; “harmonisation” in this context often being taken to mean complete uniformity of detailed rules rather than a harmony of outcomes. Thus, since the law in each Member State is the same any institution, process, product or financial instrument permitted in one Member State is permitted in all. Conversely, any process, product etc disallowed in one Member State is disallowed in all. Such an approach has the benefit of eliminating conflicting or overlapping national rules.**
- 20. The complete harmonisation approach was rejected by the European Community for the reasons set out in the 1985 White Paper on the**

Internal Market. It would take years to achieve, even if it could ever be achieved. In the meantime innovation would be delayed. Furthermore, as experience has unfortunately shown, national authorities would be effectively lobbied, for legitimate commercial reasons, by domestic firms to oppose the harmonisation measures which threaten to expose them to greater competition.

21. The second broad approach is mutual recognition. This “new” approach was incorporated, in theory at least, in the 1985 White Paper for the “1992” programme for the single market.

22. This approach involves in broad terms:

- Minimum harmonisation of essential prudential rules incorporated in Directives concerning e.g. solvency, own funds, accounts;**
- Home country supervision on the basis of such harmonised rules;**
- Mutual recognition of each national competent authority of the others;**
- Thereby enabling an institution authorised in one Member state to operate in all, offering whatever products it was authorised to supply at home in all without the need for complete harmonisation.**

23. The two approaches summarised above are not mutually exclusive. Some standardisation is essential in some areas for an efficiently functioning Single Market, for example accounting standards. Furthermore, participants value standardisation of market practices where it has been market driven and designed by the market itself to meet business needs. An important advantage of market driven standardisation is that it can include participants world wide and

provide an important step to harmonisation at the global level. There are important examples:

- ISDA¹ and ISMA² conventions represent industry forms of contractual netting, although the risk that such contracts might not be recognised in some jurisdictions created a need for the collateral directive to underpin them;
- ISO 15022 message standards introduced and implemented by most share and settlement companies have, for the first time, begun to provide their customers with the opportunity of using standard interfaces and standard message protocols to communicate with their chosen settlement service provider.

24. Yet despite market practitioners' recognition that harmonisation has a role in creating the framework of the European single financial market, most practitioners have favoured mutual recognition of conduct of business and any product regulation as the normal basis for cross border transactions between professionals. This is to enable transactions to be based on one set of regulations without needing to wait for standardisation across Member States, given that professionals can be expected to understand and have confidence in such an approach.

25. In the case of retail customers, who have both less market power and less familiarity with the regulatory framework within which a supplier in another Member state operates, greater harmonisation or host state regulation is often favoured by authorities on grounds of consumer protection rather than mutual recognition; however there is no mechanism to test whether or not restrictions on the ability of

¹ International Securities and Derivatives Association

² International Securities Market Association

non-domestic suppliers to offer products or services is proportionate to the problem and consistent with EU competition law or is simply protecting domestic suppliers under the guise of consumer protection.

VII WHY IS THERE NO SINGLE MARKET?

- 26. The hopes expressed in the 1985 White Paper have not been borne out in practice. There are a number of reasons for this disappointing state of affairs.**
- 27. Some are associated with the fact that market practices, structures, cultures and ways of doing business differ across Member States. This can make penetration by foreign newcomers difficult and costly, whatever their preferred business model. Other reasons are that domestic suppliers and perhaps the authorities arrange matters so as to impede competition and innovation.**
- 28. Then there are issues associated with the EU legislative process and outcomes or which raise matters of competition policy :**
 - Clauses in Directives concerning the general good, monetary policy and consumer protection have enabled Member States to introduce national rules which have created barriers to foreign competition, whether by a local branch or cross-border. Examples include clauses in passporting directives concerning banking, insurance, UCITS and distance marketing; clauses in the original ISD which allow different national definitions of professional investors, or which require retail business to be concentrated on regulated markets, or which enable restrictions to be imposed or maintained on cross-border access to trading**

systems such as a stock exchange, on provision of trading facilities and on access to clearing and settlement services;

- Such rules have been introduced into EU law without testing whether such national measures are proportionate to the problem that it is asserted they need to address and without checking that they are compatible with competition law;**
- There have been flaws in implementation, sometimes arising from ambiguities in Directives which are themselves the result of compromises reached in the Council of Ministers and the difficulty of effectively enforcing these imperfect texts;**
- National tax regimes can have the effect of discriminating in favour of domestic products/institutions, such as investment funds; of course non-discrimination between domestic and non-domestic products is compatible with differences between different national tax structures.**

29. Moreover:

- Treaty and ECJ requirements concerning non-discrimination against foreign EU suppliers have been used by Member States without legal challenge to ban products offered by foreign institutions on the grounds that the ban also applies to national institutions – which may be unwilling or unable to provide such products. Whatever the legal complexities, the effect is certainly discriminatory and also reduces choice, competition and innovation;**
- Enforcement measures against discrimination are usually not initiated without a formal complaint; but some financial institutions are often unwilling to lodge one, for understandable reasons. In**

these circumstances there is a case for the Commission taking a more proactive role. If this requires more resources the Commission should have them.

30. The practical result of these various factors is that:

- Products authorised in one Member state cannot always be sold in another, such as interest bearing current accounts;
- Even where funds are so authorised (e.g. UCITS) the cost of local registration and compliance with marketing requirements is prohibitive;
- The tax system may discriminate against non-domestic products, such as mutual funds;
- Authorisation for innovative products authorised elsewhere in the EU may be delayed until local firms can compete;
- Cross border transactions between professional counterparties can be subject to overlapping or contradictory rules;
- Transactions between professionals may be subject to regulation more appropriate to transactions with retail customers and small savers;
- Access to essential national infrastructures may be denied or the use of non-domestic infrastructures for transactions involving a domestic counterparty may be impossible;

These examples, taken together with many others throughout the European Union present users with higher costs and restricted choice, and make the financial sector less competitive and innovative than it could be. Capital is allocated inefficiently and the end result is that the European economy is worse off.

- 31. It is not surprising that the thicket of obstacles described above have frustrated the creation of a fully functioning single financial market in Europe. Brave words and good intentions pronounced by the European Council have not been followed through in the detail of legislation or in national implementation or enforcement. The new "Lamfalussy process" will help, but it is clear therefore that there needs to be a high profile political push if a Single Market is to be completed and fully implemented.**

VIII THE CHAMPION FOR THE SINGLE MARKET

- 32. One key element in the completion of the Single Market should be a visible, ongoing commitment by the most senior political body in the Union.**
- 33. It is the Conclusions of the European Council which have set out the ambitious programme for creating a more efficient and productive European economy. It is right that this body, which comprises not only the elected Heads of State or Government of the Member States of the European Union but also the President of the European Commission, should champion the completion of the Single Market. The European Council needs to equip itself to monitor and to promote the implementation of its Conclusions.**
- 34. But the European Council cannot itself supervise the detailed work which is required. This must rest with the Commission, with ECOFIN Council, and with the European Parliament. And to carry out these responsibilities, those bodies must be properly supported by a strong yet supple advisory and decision-making process.**

IX EIGHT PRINCIPLES AND PRACTICES FOR THE SINGLE MARKET

- 35. Agreement on structures to take the work forward is not sufficient. There also needs to be agreement on the fundamental principles that should underlie their creation, regulation and operation of such structures. Eight Principles and Practices are suggested below. They need to be formally embedded in the most authoritative manner in Community legislation and practice so that they underpin the action necessary.**

i Markets are created and developed by market participants not by rules and regulations

- 36. However well legislation is drafted and however speedily and accurately it is transposed into national legislation, it cannot of itself guarantee a thriving single market. This, in the end, rests with “economic agents”, the investors and issuers of capital and the myriad of market intermediaries which link them together using the facilities provided by the operators of the market infrastructure. In short, the development of the Single Market needs to take full account of the legitimate needs of market participants, who in the end create and develop the market, provided that the obstacles are removed.**

ii Policy instruments other than legislation should always be considered in preference to the legislative route. If legislation is necessary it should be proportionate, cost effective and address clear market failure

37. Non-legislative solutions to single market problems should be seen as the first answer to difficulties, with legislation used as a last resort. Legislation can, and sometimes does, hinder the development of markets or can drive them abroad. Legislation is often not the solution to dismantling barriers in the way of the creation of the Single Market. Private sector and market driven solutions and joint working between governmental and private sector bodies should always be considered before resorting to legislation. Sometimes implementing and enforcing existing legislation or using competition policy more vigorously would provide a better route forward.
38. If legislation has to be proposed, its emphasis must be on the creation of a genuine competitive and innovative Single Market, which avoids creating new obstacles or legitimising obstacles created by national legislation. It is important to avoid legislation which imposes burdens on market participants which are disproportionate to the problem it is said to address. Likewise, legislation needs to take account of the variety of participants and products, so that as well as being proportionate it needs to be differentiated; in this context it should also be borne in mind that some participants, particularly in the retail sector, have no cross-border business ambitions and are sufficiently regulated under their home country national law. All proposed legislation should be judged by the following tests-

- Does it provide for authorised service providers in one Member State to have the right to offer services licenced by their national competent authority throughout the EU?
- Does it give authorised service providers right of access, on a remote basis if they have no local establishment, to all necessary infrastructures?
- Is it proportionate to the problem that it claims to address?
- Is it cost-effective?
- Does it address a clear market failure and have a significant probability of producing benefits that demonstrably exceed the cost?
- Are the terms sufficiently clear so as not to create ambiguities of interpretation which could hinder the single market?

iii Consultation with participants is required at all stages, and in a timely manner, and with a reasoned response to practitioner input

39. Legislative and other initiatives agreed at the level of the Community are increasingly affecting all aspects of commercial and economic life in the Community. It is therefore becoming even more important for legislation to reflect the most thorough consultation with those whom it will affect.
40. Such an obligation to consult at all stages of the legislative process should be laid upon the Commission by a suitable amendment to the Treaty. Indeed, this principle of consultation is emphasised in the Conclusions of the European Convention's Working Group 1 on the

Principle of Subsidiarity. The Conclusion states³ “It is for the Commission to consult, as soon as possible, all the players (particularly the Member States, economic operators, local and regional authorities and social partners) who may be affected directly or indirectly by the legislative act being planned or drafted.”

41. Such an obligation to consult should encapsulate principles of good consultation, such as requirements for

- **Timely consultation before proposals are formally adopted as well as during the principal stages of the legislative process which allows sufficient time for those affected to make submissions to the Commission;**
- **Reasoned responses by the Commission to submissions, including reasons for acceptance and non- or partial acceptance;**

iv Regulation must be risk based, taking account of the different nature of the risks facing the different types of firms, customers, investors and counterparties

42. There is one general principle that should shape regulation to protect the interests of customers and savers in the Single Market. Regulation should be risk based. It should take account of the different nature of risks facing different types of participants. This principle of risk based regulation should underpin all legislation dealing with conduct of business rules, permissible products and transactions with differing categories of customer.

43. The principle of risk based regulation provides a rationale for regulation to distinguish between

³ WD19 REV1 - WG1 page 5

- professional clients/counterparties, such as financial institutions, corporate treasuries, and SMEs/individuals that provide financial services; and
- retail clients, such as personal customers and SMEs (except those that provide financial services)

It can reflect the different experience and expertise of those concerned so that the more experienced and expert ("transactions between equals") are subject to lighter regulation than the retail customer. Moreover, where demonstrable risks are minimal legislation is not needed.

v Surveillance, implementation and enforcement must be effective both at the national level and by the Commission

44. The Commission is the guardian of the Community treaties and of the legislation made under them. That role requires the Commission to ensure
- Proper implementation of Community legislation at the national level;
 - The implementation and enforcement of legislation by Member States, taking into account the specific legislation itself and the Treaty more widely;
 - The vigorous pursuit of competition policy in the financial services area, to avoid anti-competitive behaviour by market participants;
 - The systematic evaluation, in a transparent manner, of national laws and regulations. Measures alleged to be justified on

grounds of the general good, monetary or consumer policy, should be tested to ensure that they are proportionate, non-discriminatory in their economic effect and consistent with competition policy;

- The instigation of proactive, annual monitoring of how national financial markets are evolving and the extent to which impediments to competition of any type persist, along the lines of the reviews of Unfair Tax Competition by Member States, or the multilateral surveillance of economic/fiscal developments.

45. This is a massive task that will increase significantly as the Single Market deepens and the Community enlarges. Moreover, the Commission needs to take every opportunity to move its role as Treaty guardian to a more proactive level, actively pushing forward the three tasks referred to above and without waiting for complaints to be put before it. Indeed, such a proactive obligation of the Commission should be considered for explicit inclusion in the Treaty, to reinforce Article 226. For such a role, the Commission will undoubtedly require more resources and staff, perhaps grouped within a new Enforcement Unit. It also requires that market participants should ensure that the Commission is supplied with information on anti-competitive behaviour, on a confidential basis if they prefer.

vi Regulation and behaviour of market participants must help build fair and honest markets, while not frustrating or stultifying their innovation and development

46. Earlier in this note it was pointed out that financial markets deal with “other people’s money”. Market participants, whether traders, managers or company directors, exercise therefore a sort of “trustee relationship” in their management of those savings. The regulation and behaviour of market participants, both firms and people, needs to reflect that fact. But this objective needs to be brought about in a way which does not frustrate or stultify the development of the Single Market in a manner which prevents it becoming the facilitator of growth by the methods envisaged in the Lisbon Conclusions.

vii Representatives of market practitioners should provide regular reports to the European Council, ECOFIN, Parliament and Commission on progress towards creating a fully functioning single market

47. It has been emphasised in this note that market participants carrying out their everyday business transactions and initiatives create and develop financial markets. It therefore seems appropriate for a group of representative market participants to provide the European Council, ECOFIN, the European Parliament and the Commission with independent, regular reports of progress towards the creation of a fully functioning Single Market. Such reports, which could be accompanied by ECOFIN/Commission assessments, could be provided for the Spring European Councils. These reports would assess the extent to which obstacles to the completion of the single market remain and advise on the extent to which legislation is compatible with the eight Principles and Practices set out above.

viii A European Financial Market Forum should be established to help develop a coherent approach and philosophy for the creation of the Single European Financial Market

- 48. Both market participants and regulators in the financial markets of the Member States face different challenges and different market structures and practices and to some extent they still operate in different cultures.**
- 49. It is not therefore surprising that there is some lack of a coherent approach and philosophy (which will be exacerbated by the impending enlargement of the Community) among market participants and the authorities involved in the creation of the Single European Financial Market. Without some common understandings on these matters, there is a real risk that its creation may well be inhibited.**
- 50. This risk could be mitigated by the establishment of a European Financial Markets Forum. It might be composed of officials from the national authorities concerned, market participants and their associations having appropriate market share, and academic experts. Its role might be to debate the issues and to develop sound principles and practices, including approaches to global standards, able to command support from the authorities and markets.**

X WHAT NEEDS TO BE DONE?

51. On the basis of the reasoning in this paper, it is suggested for discussion that the following Principles and Practices should be formally enshrined in the most authoritative manner in Community law and practice:-

- 1. Markets are created and developed by market participants not by rules and regulations (paragraph 36)**
- 2. Policy instruments other than legislation should always be considered in preference to the legislative route. If legislation is necessary it should be proportionate, cost effective and address clear market failure (paragraphs 37-38)**
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