Ref: CESR/04-330

European Financial Integration: progress & prospects
Contribution to High Level Panel by Arthur Docters van Leeuwen, Chairman of CESR
22-23 June 2004, Palais d'Egmont, Brussels

Ladies and Gentlemen,

Accompanied by these distinguished fellow panel members and in front of this audience in this "Royal Ambiance", I thank the Commission, and Commissioner Bolkestein in particular, for giving me the opportunity to present to you, in a nutshell, CESRs views on the lessons to be learned from the past and challenges for further integration towards a Single Market for Financial Services. CESR recently has submitted its first contribution to the Commission for this debate and, what follows here, is based on those views.

Let me start by saying that Lamfalussy is a success! This is not in the first place the opinion of CESR, but this is the publicly expressed opinion of quite a few highly regarded, independent sources. Interesting too is that nobody expressed the view that it is a failure. The current FSAP has (almost) been completed at EU-level which is a major achievement as such. Key-part in this process has been the intensified interaction between authorities and market participants. So far the good news! This good news is exactly the reason to carefully think about our future way forward.

Let us be very careful and not drown in our own success! Do we really need a plan for the next phase? I am not there yet. Can we do *without* a plan and base ourselves on a commonly shared vision? Of course, we have to identify areas where regulatory intervention is still needed in order to remove existing barriers. Yes, clearing and settlement, corporate governance and upgrading the UCITS Directives in this respect are obvious candidates for future work.

Beyond this, one can think of a lot of areas where useful work is possible. For instance: items as improvement of cross-sectoral and cross-border investor protection. From the industry I picked up the fascinating proposal to create a cross-industry approach of conflicts of interests. Also our new relations with the SEC will bring new things. However, if we want to prevent drowning, we have to watch out for comprehensiveness of any new vision or plan. In CESR's view, that we seem to share with a quite a few of you, the focus for the next years should be on transposition, implementation and operability. The way from a European rule to a changed, or new, specific national regulatory decision is long, steep and arduous. Creating a comprehensive deep vision now will create an easy escape route away from our mandatory labour.

But optimistic as I am, let us assume that we succeed in this. How then are we going to prepare our decisions about new rules? I agree with everyone that we should pay more attention to impact-analysis and assess possible costs and benefits when considering making new rules. But I would like to go one step further. A key question to decide on the introduction of any new rules should in my view be: do these envisaged new rules add specific value to further integration of the Single Market of Financial Services? In other words: are we sure that these improvements actually make the market participants "jump"? I mean that they jump from jurisdictions in which they already operate to jurisdictions that are now unknown to them. If we expect, on the basis of thorough analysis, that this will <u>not</u> be the case, we should have the courage to amend or refrain from putting these, undoubtedly attractive, ideas into practice.

The question behind this is: do companies and investors have a so-called 'mental picture' how the Market for Financial Services really works in other jurisdictions? In one of my previous speeches, I have used the example of a Portuguese investor who might be hesitant to invest in Finnish or Dutch

shares (because he does not exactly know what rights Dutch shares give to him). What are the reasons for (especially retail) investors to mainly allocate their investments (in listed shares and bonds) in their local jurisdiction only? Why do they hardly invest in other jurisdictions of the EU market? Why do some (small) firms refrain from offering their services in other jurisdictions, even if the opportunities are there? Are the administrative hurdles too high? Is it right for both the buy-and sell-side to use their own jurisdiction as a benchmark to judge the other ones? I have no problem to expand this list of questions, but the message here is that the answers to these questions are vital for making progress in the integration process. I am convinced that this mental picture, is currently lacking. To overcome these bottlenecks, we have to decide what specifically needs to be done by industry and by regulators, respectively.

The second question is the following. Let us assume that the Portuguese investor more or less knows which financial product he is actually buying, if he decides to do this in another jurisdiction. Can he, if he considers doing so, create also a mental picture of how the regulatory, supervisory and financial system will work over there? Would you, for instance, buy a unit linked life insurance policy outside your own jurisdiction if you don't envisage how the regulatory system over there will work?

I think at least four questions are relevant. In the first place can I be sure that the regulator over there has more or less the same power as the regulator I am accustomed to? I was taking this aspect of the regulatory situation in consideration where the Lamfalussy report spoke of *"a remarkable cocktail of Kafkaesque inefficiency".* Since then the situation has improved substantially, but the conclusion is that we still not have reached a level that market participants can believe in.
The second and third questions are about co-operation and the network that CESR is. Considering co-operation we see that all the new directives demand co-operation. Not only between home and host regulator, but also on a horizontal basis on, for instance exchange of information and enforcement. Here is much work to do. Does the market participant know exactly how the home and the host regulator will interact? Is it for regulators possible, as they now for instance do in clearing and settlement, to work on a basis of legally firm equal footing?

Let us assume that we decide for a lead regulator. What exactly can the market participant assume that this lead regulator will do in his interest? Asking our self the same question about the level 3 network, which CESR is. How can we make sure that the reassuring effect (that is the essential purpose of it) becomes reality? Because we co-ordinate our decisions about regulation, supervision and enforcement in an open and transparent manner we enhance predictability and make it more clear for the Portuguese market participant how the Finnish regulator will respond to a given problem. But this effect will diminish if the network becomes too complicated, for instance when it extends his operations in areas that were better to be covered by Level 2 and Level 4 (as might be the case now that we have started level 3 work on the UCITS Directives as they are).

The fourth and last question is: is this enough? Will the European market participants believe that everything can be covered by proper answers on the first three questions? Let us for instance assume that a big transatlantic financial conglomerate is in trouble. The FED and the SEC at the one side and how many of us will be at the other side? Do you think it is efficient and effective to sit together with tens of regulators (securities, banking and insurance) on the EU-side to solve a crisis? The same line of argument should at least be investigated when we Europeans apply IFRS rules.

Although it is tempting to go on, I will, with great difficulty, refrain myself. We, the CESR members, have taken it upon us to create an analytical document that, I hope, we can present in the autumn of this year.

Concluding.
The focus should now uppermost be on transposition, implementation and operability. Concerning rulemaking let us first take stock of what we already have to do. Clearing and Settlement, the 8th Directive, modernisation of UCITS, equivalence of non-European GAAPS etc. That is quite a lot of work to begin with. Second, let us be cautious with new items. Let us take them aboard only if we are sure that they have a specific impact. Third and last: lets make supervision and enforcement believable from the perspective of the European market participants.

Why am I optimistic? It is in my nature! More serious: ff I look back at what the Commission, the Council and the Parliament have achieved I have reason to be optimistic and if I look back at CESR's contribution, I am, to say the least, no less optimistic.

Thank you.