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Emilios Avgouleas

University of Piraeus

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Dr. Emilios Avgouleas*

TABLE OF CONTENTS

I. INTRODUCTION ............................................................................................................... 180

II. THE EVOLUTION OF EC SECURITIES REGULATION.................................................. 182
    A. The ECJ’s Jurisprudence and the Single European Act ........................................... 182
    B. The Adoption of FSAP ............................................................................................. 184
    C. The Committee of the Wise Men and the “Lamfalussy Process” ......................... 185

III. THE IMPACT OF MiFID ON MARKET INTEGRATION............................................... 188
    A. Rationales for the Enactment of MiFID ................................................................. 188
    B. Reforming the ISD ................................................................................................... 190
    C. The Principal Features and Objectives of the MiFID .............................................. 191
        1. The New “Constitution” of EU Financial Markets ............................................. 191
        2. The Regulation of Financial Exchanges ........................................................... 192
        3. The Regulation of Multilateral Trading Facilities ............................................. 193
        4. Trade Execution by Investment Firms .................................................................. 195
    D. The Expanded Scope of MiFID ................................................................................ 197
        1. The Provision of Investment Advice and Investment Research ....................... 197
        2. Dealing in Commodity Derivatives and Other Derivative Instruments ......... 198

IV. THE MARKET ABUSE DIRECTIVE.............................................................................. 199
    A. Introduction .............................................................................................................. 199
    B. The Prohibition of Insider Dealing ......................................................................... 201
        1. The Offense ........................................................................................................ 201
        2. Inside Information ............................................................................................. 203
        3. Defenses and Safe Harbors ............................................................................... 205
    C. The Prohibition of Market Manipulation ............................................................... 206
        1. The Offense of Market Manipulation ................................................................. 206
        2. Defenses and Safe Harbors for Market Manipulation ........................................ 207
    D. Complementary Features of the EC Market Abuse Regime ................................ 210
        1. Issuer Continuous Disclosure Obligations, Selective Disclosure, Notifications by Insiders ........................................................ 210
        2. Investment Recommendations and Disclosure of Interests ......................... 213

* Department of International and European Studies, University of Piraeus.
ABSTRACT

The implementation of the European Union’s Action Plan for Financial Services (“FSAP”) is largely complete, though the transposition of relevant legislation into the Member States’ legal orders is still pending. The new legislation has significantly revamped the EU’s legal and regulatory framework governing financial markets. The Lamfalussy process has been successfully utilized in debating and enacting the most important pieces of the new EC securities legislation. This article provides a critical analysis of the securities Directives passed under FSAP and critically evaluates their impact on EU capital markets and the EU financial services industry. Furthermore, this article sheds light on the evolution of EC financial market regulation and on the most important and intricate points of the new legislation. It explains the reasons that make the new legislation an agent of profound change for EU financial markets in terms of structure, business planning and trading processes. Finally, the article debates the cost of compliance with and enforcement of the new framework and the supervisory and enforcement loopholes created due to the absence of a single regulator for EU financial markets.

I. INTRODUCTION

EC securities regulation1 has been, along with the introduction of the euro, the cornerstone of all efforts aiming at the integration of EU financial markets. Yet, developing this body of EC law has been a very lengthy process frequently
marred by controversy. In addition, a marked lack of direction has been its most distinctive characteristic for almost two decades. This was caused by three factors. The first factor was the existence of conflicting national agendas motivated by a desire to protect and preserve domestic investment firms, national securities markets and local business customs. The second factor was the unwillingness of the global financial services industry to engage in a constructive dialogue and find a common language with EC legislators. This unwillingness was attributable to the inability of the industry to recognize the varied and important ways through which EC securities law was able to influence the evolution of its business processes, development of new products, and ultimately the competitiveness and profitability of its members. The third factor was the inability of EC officials and legislators to fully understand the intricacies of modern financial markets; in particular, their globalized nature and the fast pace of innovation within them. This resulted in the production of legislation that often reflected the reserve, awe, and prejudice with which EC bodies used to view the workings of global finance.

The majority of these dysfunctions have been addressed by FSAP and the introduction of the Lamfalussy process. The latter has accelerated the speed of debating and enacting relevant laws in the EU and has widened the scope for constructive industry consultation.\(^2\)

EC legislation passed in the context of FSAP departs radically from the principle of minimum harmonization and creates self-standing regulatory regimes in a number of areas; most notably in the regulation of market abuse and of licensed financial exchanges and Alternative Trading Systems. It also upgrades the EC legal framework that governs the public offer of securities, and their admission to trading on securities exchanges. The transposition of the new legislation into the legal orders of the Member States will be followed by seismic changes in the way investment firms and other investment professionals conduct business in the EU. The new legislation will also have a profound impact on the structure of the Union’s financial markets and financial services industry.

Broadly, EC Directives enacted under FSAP may be distinguished into integrative legislation (measures that promote the aim of integrated financial markets in the EU) and protective legislation (measures that deal with the effects of market integration). Predominantly integrative in their objectives are the following: the Directive on Markets in Financial Instruments ("MiFID"),\(^4\) the

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Public Offers and Admissions Prospectus Directive ("POPD II"), and the Directive on Takeover Bids. The core of protective legislation comprises the Market Abuse Directive and the Transparency Directive. These deal with the effects of market integration by ensuring the availability of information to investors in the single market and a uniform prohibition of market abuse.

The article is divided in seven sections. The first is the present introduction. Section II discusses the evolution of EC securities regulation. Section III describes the rationales for the enactment of MiFID and its main features. Section IV provides a critical discussion of the EC’s emerging market abuse regime mainly comprising the Market Abuse Directive and its Level 2 implementing measures. Section V discusses the new regime for the public offer of securities and their admission to trading on a regulated market in the EU and the periodic disclosure obligations imposed by the Transparency Directive. Section VI attempts an evaluation of the emerging regulatory regime for primary and secondary capital markets in the EU. Finally, the present discussion is brought to a comprehensive conclusion in Section VII.

II. THE EVOLUTION OF EC SECURITIES REGULATION

A. The ECJ’s Jurisprudence and the Single European Act

The existence of a common legal and regulatory framework is often viewed as a *sine qua non* for the establishment and effective operation of integrated markets. Nonetheless, it has not always been possible for the Community to enact harmonization legislation. Until the mid-1980s the decisions of the European Court of Justice ("ECJ") were the most important factor in the approximation of national laws in what was, at the time, the European Economic Community ("EEC"). However, the ECJ’s jurisprudence could not have been an effective alternative to harmonization legislation with regard to market integration.


One of the reasons for this was that rules based on the concept of “general
good” gradually became a very important obstacle in the achievement of the goal
of the single market in many areas, including financial services.\(^{10}\) Under the
ECJ’s jurisprudence, the concept of the “general good” referred to imperative
public interest requirements, which extended, *inter alia*, to the protection of
consumers-investors, regardless of whether the regulations restricting cross-
border trade were imposed by the home or the host state.\(^{11}\) Therefore, the
attainment of the aim of market integration could not be achieved in the absence
of harmonization of Member States’ laws in a variety of areas, including those
covered by “general good” legislation.

In 1985, the Delors’ Commission published its “White Paper” on the internal
market. The goal was to remove all obstacles to market integration.\(^{12}\) To effectively
achieve this aim and facilitate the enactment of harmonization legislation, the
White Paper declared a shift of focus for EC statutory law. This shift moved the
focus away from detailed mandatory rules towards a more flexible framework
within which harmonization legislation would utilize the principles of “mutual
recognition” and “minimum harmonization.” The White Paper’s objectives with
regard to financial services were the complete liberalization of capital movements;
the integration of national markets for financial services; and the establishment of a
harmonized regulatory framework for the licensing, operation, and on-going
supervision of financial institutions. The White Paper was adopted by the Council
of Ministers and constituted the basis for the Single European Act (“SEA”) 1986,
an amendment of the Treaty of Rome.

Financial services legislation produced in the context of SEA dealt with the
issue of prudential regulation of credit institutions and investment firms by
creating a common regulatory framework through the enactment of the Banking
Directives,\(^{13}\) the Investment Services Directive (“ISD”),\(^{14}\) and the Capital

\(^{10}\) Case 15/78, Societe Generale Alsacienne de Banque v. Koestler, 1 C.M.L.R. 89 (1979).
\(^{11}\) Case C-384/93, Alpine Investments BV v. Minister van Financien, 1995 E.C.R. I-1141; Case C-
101/94, EC Commission v. Italy (Re Restrictions on Foreign Securities Dealers), 1996 E.C.R. I-2691; Case C-
\(^{12}\) EC Commission, Completing the Internal Market, White Paper from the Commission to the
\(^{13}\) The term ‘Banking Directives’ encompasses the Second Banking Directive (89/646/EEC, 1989 O.J.
(L 386) 1), the Own Funds (89/299/EEC, 1989 O.J. (L124) 16), the Large Exposures (92/121/EEC, 1992 O.J.
(L 29) 1 and the Solvency Ratio Directives [89/647/EEC, 1989 O.J. (L 386) 14] now all consolidated in
(L 126) 1.
O.J. (L 141) 27.

Adequacy Directive.\(^\text{15}\) It also provided for a harmonized regime to draw up and publish disclosure documents in the context of the public offer of securities\(^\text{16}\) and the prohibition of insider dealing.\(^\text{17}\)

However, harmonization legislation under the SEA did not extend to a number of areas, resulting in a reduction of the pace of market integration.\(^\text{18}\) In fact, even following the implementation of the ISD, wide differences could be observed throughout the EU in: (a) the way financial services contracts were formed; (b) the way national conduct of business rules regulated the relationship between financial services intermediaries and their clients; (c) the way exemptions from the public offer rules were provided or administered in various Member States; (d) the application of marketing and investment advertisement rules; and (e) the way regulators understood and interpreted the harmonized legislation.

B. The Adoption of FSAP

Having considered the aforementioned gaps in EC financial market legislation, the Commission issued a Communication on building a framework for action on financial services in the Autumn of 1998.\(^\text{19}\) This was followed by the Commission Communication on the implementation of the Financial Services Action Plan issued in May 1999.\(^\text{20}\) In these Communications, the Commission recognized the deficiencies of the existing EC financial market legislation in: (a) achieving the goal of market integration; and (b) dealing effectively with the regulatory challenges that an integrated market and modern market developments brought about, such as cross-border market abuse. Thus, the Commission set out in the second Communication a framework for the reform of existing legislation, and the enactment of new legislation in the areas which had not been included in the preceding harmonization attempts.\(^\text{21}\) The legislative program and objectives of this Communication constitute the FSAP.

It is instructive of the extensive scope and volume of the new EC financial services legislation to note that this legislation brings substantial amendments to


\(^{16}\) 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 O.J. (L 124) 8.


\(^{20}\) Supra note 2.

pre-existing EC regulation dealing with: (a) the drawing of disclosure documents in the context of public offers and listing of securities; (b) the provision of investment services in the EU and the conduct of cross-border business by investment firms; (c) the prohibition of insider dealing; and (d) the regime governing regulated collective investment funds and the ability of their management companies to use the common passport. The same legislative measures have introduced new EU-wide regimes for: (a) the regulation of Alternative Trading Systems (“ATS”); (b) the management of conflicts of interests and the handling and execution of client orders by investment intermediaries; (c) the conduct of periodic and continuous disclosures by issuers of listed securities; (d) the prohibition of market manipulation; (e) the production and dissemination of investment recommendations; and (f) the conduct of stabilizations of new issues and share buy backs.

C. The Committee of Wise Men and the “Lamfalussy Process”

The implementation of the FSAP is inextricably bound with the adoption of the so-called Lamfalussy process. Acknowledging the validity of complaints about the speed and efficiency with which EC bodies, national legislatures, and regulators enacted and implemented financial services legislation, the Commission set up in 2000 the so-called “Committee of the Wise Men.” The mandate given to this Committee was to identify and recommend the most efficient and timely (“fast track”) procedure to debate and enact legislation for EU securities markets, taking also into account the fast pace of change and innovation that financial markets have experienced on a continuous basis since the mid-1980’s. The recommendations of the Committee of the Wise Men had also to be acceptable to the European Parliament. The Committee of the Wise Men published its Final Report in February 2001.22

The Final Report of the Committee of the Wise Men shared the view of the financial services industry that keeping pace with emerging market norms and practices should be of paramount concern for EC bodies in drafting new financial market legislation. It suggested a new four-level regulatory approach and the establishment of two committees, which would be involved with the process of drafting and implementing relevant legislation. First, an EC securities committee (“ESC”). Second, an EU securities regulators’ committee with advisory functions, a role that has been taken by the Committee of European Securities Regulators (“CESR”).

The first two levels of the Committee’s proposal are concerned with the “fast track” production of financial markets legislation by EC bodies, and the

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remaining two levels facilitate its implementation and consistent application within EU Member States. The Committee of Wise Men advised that the EC Commission, the Council, and the European Parliament should produce only general principle—framework directives, the so-called Level 1 legislation. Level 1 legislation is followed by Level 2 legislation (implementing measures), which is adopted by the Commission with the assistance of ESC, following consultation with CESR. Thus, the Committee of the Wise Men recommended adopting the "comitology" procedure in the production of Level 2 rules to the exclusion from the drafting (but not the consultation process) of the European Parliament. Level 3 rules are imposed by national regulators through coordinated EU action, following consultation with CESR, and should be applied consistently across the EU in order to ensure common and uniform implementation of Level 1 and 2 legislation into the legal orders of the Member States. The final stage in the new regulatory approach, Level 4, is concerned with the consistent implementation and enforcement of enacted legislation.

The Stockholm European Council of March 2001 endorsed the final report of the Committee of Wise Men. The Lamfalussy process has so far been utilized in the drafting of the Market Abuse Directive, the Transparency Directive, the POPD II, and the MiFID.

A further legislative package of seven measures (a Directive and six Commission Decisions) to extend the Lamfalussy process to banking, insurance and occupational pensions, and to asset management was first released on November 6, 2003. The aim of the extension of the Lamfalussy process is to achieve greater and deeper co-operation between banking, insurance and UCITS supervisors and much greater convergence in day-to-day regulation and supervision. Six Commission Decisions have established the new regulatory Committees: the European Banking Committee know as EBC and the European Insurance and Occupational Pensions Committee known as EIOPC. The EIOPC, like ESC, will assist the Commission in adopting implementing measures at Level 2 for Level 1 legislation in their respective areas. The other committees are the Committee of European Banking Supervisors ("CEBS") and the Committee of European Insurance and Occupational Pensions Supervisors ("CEIOPS") which will perform in their respective sectors duties similar to those discharged

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by CESR. Finally, responsibility for overseeing the implementation of EC law on collective investment funds has been transferred from the UCITS Contact Committee to the ESC and CESR.26

The Commission has appointed an expert group, the Inter-Institutional Monitoring Group (“IIMG”), to evaluate the progress and practical usefulness of the Lamfalussy process.27 From the reports of the IIMG emerges the clear impression that there is strong support within the financial services industry for the use of the Lamfalussy process and the results from its utilization have proved positive, although a number of important issues remain to be addressed. On November 15, 2004 the Commission released an internal report that set out its views on the effectiveness of the Lamfalussy process and its perceived weaknesses in the production and implementation of EC Securities Markets legislation.28 According to the Commission, the most distinct strengths of the Lamfalussy process are the “three Ts”—transparency, trust, and teamwork. The first “has resulted in an improvement in the quality of legislation and an acceleration of the legislative process, and it has encouraged regulatory and supervisory convergence within Europe.”29 Furthermore, “the cooperative working framework that has been developed between all the Institutions, working with regulators, market participants and other stakeholders,”30 has likewise contributed to the creation of procedures that enjoy the trust of all parties involved.31

Endorsing the conclusions of the IIMG reports,32 the Commission sets out in the same document the main areas of the Lamfalussy process that need further improvement. These include recommendations for:33

- Focusing Level 1 Directives on, above all, general rules and principles;
- Careful calibration of Level 2 technical measures so as to avoid over-prescriptive regulation and/or duplicative requirements at the EU level;
- Articulating more clearly the role of Level 3 in the Lamfalussy process;


29. Id. at 14.

30. Id.

31. Id. at 9, ¶ 23.


Critical Evaluation of the New EC Financial-Market Regulation

- Strengthening Level 4 through clear, practical arrangements, whereby the Commission, working with the Member States and national regulators, should lead a major effort to implement and enforce effectively the set of existing rules;
- Taking steps to obtain better input from consumers in consultation processes; and
- Making sufficient resources available to carry out the required consultations.

From all of the above the most important is the clear delineation of the role of national regulators at Level 3 of the Lamfalussy process and the creation of appropriate supervisory tools for the proper implementation of legislation passed at Levels 1 and 2. In addition, there is an urgent need for the creation of a framework for Level 4, the "big unknown" of the Lamfalussy process, especially with respect to the Commission's powers and responsibilities. Finally, the impact of the EU Constitutional Treaty, signed on October 29, 2004, which provides specific rules on the use of delegated powers, remains unclear given the uncertainty that surrounds the ratification of this Treaty by EU Member States.

III. THE IMPACT OF MiFID ON MARKET INTEGRATION

A. Rationales for the Enactment of MiFID

The implementation of the ISD has brought about clear benefits in respect to the integration of the internal market in financial services. Its most important achievement was that it led to the creation of a level playing field between credit institutions and investment firms and prevented national regulatory regimes from discriminating against cross-border competition. However, the ISD regime had a number of weaknesses which prevented it from becoming the steam engine of market integration. In addition, market developments such as the technological revolution and the emergence of alternative trading venues, as well as the very

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35. Acts that will be adopted under Article 1-36 of the Constitutional Treaty, should the Treaty be ratified by the EU Member States, will afford the Council and the European Parliament equal control rights over the Commission's exercise of its delegated powers. To secure its continuing role in the drafting of financial services legislation under the Lamfalussy process, the Commission has added the following Declaration on Article 1-36 of the Constitutional Treaty, which has been annexed to the Final Act: "The Conference takes note of the Commission's intention to continue to consult experts appointed by the Member States in the preparation of draft delegated European regulations in the financial services area, in accordance with its established practice." See also EC Commission, The Application of the Lamfalussy Process, supra note 3, at 13. The text of the Constitutional Treaty can be found at http://ue.eu.int/igcpdf/en/04/cg00/cg00387-re01.en04.pdf.

36. IIMG Third Report, supra note 27, at 39, 43.
significant increase in cross-border trade, made the ISD look rather outdated. The main shortcomings of the ISD regime are summarized below:

(1) Technological revolution: In the 1990s, the EU witnessed significant growth in cross-border trade (both retail and institutional) facilitated by technology and the proliferation of electronic trading venues, which were not licensed exchanges. At the time of the adoption of the ISD, competition between securities exchanges and alternative trading venues was limited to U.S. markets and relatively unknown in Europe. As a result, the ISD did not address the regulatory issues arising by virtue of competition for trading volume between regulated markets, such as securities exchanges and ATSs, and it did not provide a comprehensive regulatory framework within which markets and systems could compete for business.

(2) Internalization: The ISD did not provide a framework for the execution of client orders internally ("off exchange") by investment firms and banks, by either matching them "in house" with another client order, or executing them against a proprietary position. The traditional regulatory model, on which the ISD was based, made a clear distinction between the functions of a market intermediary and those of a marketplace. This structural and institutional dichotomy allowed a clear distinction to be made between conduct of business rules, which applied only to intermediaries, and rules governing the organization and operation of trading venues, mostly applicable to licensed exchanges. This distinction may not be made anymore in light of today's competition between different methods of trade-execution: exchanges, new trading systems, and in-house order execution by investment firms.

(3) The change in the status of EU securities exchanges: the majority of EU securities exchanges have gradually become profit driven corporations the securities of which are often listed, moving away from the old organizational model of state ownership or mutual ownership (i.e., ownership by the members of the exchange). As a result, today, licensed exchanges perform a reduced portfolio of regulatory duties. In addition, privatized (or demutualized) EU securities exchanges faced with the challenges of the single market and of the single currency have sought to expand their activities beyond national borders and take advantage of new business opportunities.

(4) Insufficient harmonization of national prudential regulation and conduct of business regimes: The absence of a clear "country of origin" regime and the ability of the host state to impose additional requirements invoking the concept of the "general good" seriously
inhibited the effectiveness of the ISD passport. In addition, the lack of comprehensive harmonization of national conduct of business rules led to continuing compliance with from fifteen to twenty-five different sets of national conduct of business rules.

(5) Limited scope: The ISD did not cover the full range of services offered to investors such as the provision of investment advice, dealing in commodity derivatives, and the production and dissemination of investment research. The latter was classified as “ancillary service” under the ISD.\(^3\) Thus, the provider of this service could not enjoy the ISD passport, unless it was also licensed to offer a “core investment service.”

(6) Regulatory cooperation: The ISD provisions for supervisory cooperation were designed for an era in which linkages between national financial markets were not intensively employed. As a result, the ISD did not provide a clear allocation of supervisory and enforcement responsibilities between national regulatory authorities within the EU. However, a fully integrated financial market requires that abusive behavior and other market distortions are pursued, deterred, and punished on a consistent basis throughout the Union. Effective cooperation and information exchange between national authorities is imperative for a well supervised integrated market.

B. Reforming the ISD

MiFID is attempting a giant leap forward in the creation of self-standing regimes for the regulation of the operation of capital markets, investment firms, and the provision of investment services in the EU. The formal discussion on the revised ISD opened with the publication by the Commission of its Communication (“Green Paper”) in November 2000.\(^3\) The Green Paper discussed a number of issues relating to the operation and application of the ISD and the Commission received a very large number of responses. These responses obliged the Commission to admit that a wide-ranging review of the ISD was required. The response to the Commission orientations by industry bodies was less than enthusiastic in a number of areas. For instance, the Commission’s suggestions for the regulation of ATSs were found to be anticompetitive. Following industry criticism of its proposals, the Commission published a substantially revised set of recommendations in March 2002. The revised recommendations were also subjected to open consultation. Relevant responses were taken into account before

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37. ISD, supra note 14, at Annex, Schedule C.
the submission of the Commission’s Proposal in November 2002. 39 Both the European Parliament in its first reading and the Council in its Common Position, 40 introduced a large number of changes to the Commission’s Proposal. Following a compromise with Council, 41 further changes were introduced by the European Parliament in its second reading which adopted several of the recommendations of the relevant Parliamentary Committee. In the aftermath of Parliament’s favorable vote, the Directive was formally adopted by the Council of Ministers on April 27, 2004. 42 The next section will describe the main characteristics of MiFID.

C. The Principal Features and Objectives of the MiFID

1. A New “Constitution” for EU Financial Markets

As mentioned above, the most important objective of the MiFID is the modernization of the EU legal and regulatory regimes governing financial markets in order to facilitate market integration and enhance investor protection. The first tool used by the MiFID to achieve the objective of market integration is the detailed harmonization of national supervisory rules. 43 This allows investment firms to utilize more effectively the “single passport” in order to conduct investment business throughout the EU on the basis of their home state authorization. The second tool used is the inclusion in the MiFID of new rules on access to national clearing and settlement systems and on supervisory cooperation.

Furthermore, market integration is facilitated through the introduction of a new core investment service relating to the operation and provision of multilateral trading facilities (“MTF”), which brings under a common EU regulatory umbrella the most important ATSs. In the same manner, the MiFID extends the scope of the new regulatory regime for the carrying out of investment business in the EU to the provision of investment advice and dealing in commodity derivatives, which were not covered by the ISD. This allows cross-

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43. MiFID, supra note 4, arts. 5-13, 16-17.
border trade in the provision of investment advice and commodity derivatives dealing to flourish, having been freed from the burden of compliance with multiple national regimes.

The objective of investor protection is safeguarded by the MiFID through the establishment of a new regulatory framework for the execution of investor transactions on exchange, through ATSs, or internally by investment firms. The MiFID intends to protect investors and the integrity of the market by containing extensive obligations on both pre-trade and post-trade transparency in equity transactions and on transaction reporting. In addition, the MiFID lays the foundations of an EU-wide conduct of business regime.

It should be noted here that although MiFID’s organizational and constitutional requirements for “regulated markets,” MTFs and investment firms do not distinguish between equity and debt markets, the MiFID creates a much less restrictive regime in the case of debt trading. This is largely due to two reasons: (a) the wholesale nature of this market, where most active players are professional traders acting either on own account or on behalf of institutional clients; and (b) fears of migration of trading volume, which would inhibit the liquidity of EU debt markets. Furthermore, although MiFID’s regime for the prudential regulation of investment firms is much wider and more detailed than that of the ISD, an analytical examination of this regime is, because of its volume, outside the ambit of this article.

2. The Regulation of Financial Exchanges

The MiFID introduces new standards for regulated markets and their operators. The MiFID provides a definition of “regulated markets” which extends to all licensed financial exchanges. Accordingly, MiFID provides the framework for the authorization, regulation, and supervision of financial exchanges in the EU, which shall be further specified at Level 2. MiFID requires that operators of “regulated markets” be “of sufficiently good repute and sufficiently experienced as to ensure the sound and prudent management of the regulated market.” The competent authority must ensure, “at the time of authorisation and on an ongoing basis,” that the operator of the market is

44. Id. art. 27-28.
45. Id. art. 18-19.
46. “Regulated market” means a multilateral system operated and/or managed by a market operator, which brings together or facilitates the bringing together of multiple third-party buying and selling interests in financial instruments—in the system and in accordance with its nondiscretionary rules—in a way that results in a contract, in respect of the financial instruments admitted to trading under its rules and/or systems, and which is authorized and functions regularly and in accordance with the provisions of Title III. Id. art. 4 (1) (14).
47. Id. art. 36(1).
48. Id. art. 37-39.
49. Id. art. 4(2).
50. Id. art. 37(1).
endowed with the financial resources needed to secure its orderly functioning.\textsuperscript{51} Furthermore, the MiFID establishes pre- and post-trade transparency obligations applicable to orders and quotes in shares displayed in the market and details of completed equity transactions. “Regulated markets” are required to make public, on reasonable commercial terms and on a continuous basis, “current bid and offer prices which are advertised through their systems for shares admitted to trading” (pre-trade transparency).\textsuperscript{52} The display of large size orders and quotes, or of orders and quotes in illiquid securities, may be exempted.\textsuperscript{53} For completed trades, “regulated markets” will have to publish the price, volume, and time for all trades in equity instruments “concluded under the rules and systems of the market on a reasonable commercial basis and as close to real time as possible” (post-trade transparency).\textsuperscript{54} The reporting of the details of large trades and trades in illiquid securities could be deferred. The range of orders and quotes to be disclosed will also be defined by Level 2 implementing measures.

Finally, Article 40 (1) of the MiFID requires financial exchanges to have “clear and transparent rules regarding the admission of financial instruments to trading.” The requirements of Article 40(1) are only very “high level” principles and the drafting of detailed rules for the admission of instruments to trading on “regulated markets” is left to Level 2 implementing measures.\textsuperscript{55}

3. The Regulation of Multilateral Trading Facilities

As mentioned above, the functionality of the operation of Alternative Trading Systems did not correspond directly to any of the existing ISD services. Thus, the MiFID introduces a new “investment service” relating to the operation of Multilateral Trading Facilities (“MTFs”).\textsuperscript{56} This allows the operators of such systems to be authorized as investment firms, subject to a customized regulatory regime. Following the implementation of MiFID by Member States, MTF operators shall be able to benefit from the Directive’s “common passport,” and make their trading facilities and services available to users throughout the EU, on the basis of home country authorization.\textsuperscript{57} This means that MTF operators, like all authorized investment firms, will be required to hold initial capital and an

\textsuperscript{51} Id. art. 37(3).
\textsuperscript{52} Id. art. 44 (1).
\textsuperscript{53} Id. art. 44(2).
\textsuperscript{54} Id. art. 45(1).
\textsuperscript{56} MiFID, supra note 4, Annex I – List of Services and Financial Instruments, Section A-Investment services and activities.
\textsuperscript{57} Id. art. 31(5).
additional amount of their own funds in accordance with the Capital Adequacy Directive (93/6/EEC).\textsuperscript{58}

The definition of MTFs in MiFID\textsuperscript{59} captures systems, which support the multilateral disclosure of firm orders/indications of interest between the users of the system and the execution of orders resulting from the interaction of buy/sell interests expressed through the system. It also includes “auction-crossing” systems, where user orders are executed against a reference price imported from outside the system. The common feature of auction-crossing systems is that they support autonomous trading decisions by the users of the system, without any participation of the system operator (against a proprietary trading book) in the transactions concluded on the system, or any intervention to facilitate trades. The system supports and facilitates direct user (third-party) interface in a way that results in a contract.

As mentioned earlier, the MiFID sets out a framework of obligations applicable to investment firms operating MTFs in order to ensure the objective, fair, orderly, and efficient handling of trading interests expressed through the MTF and the efficient execution of orders, which should be based on objective criteria.\textsuperscript{60} In addition, MTF rules regarding the criteria for determining the admission of financial instruments that can be traded under the system must be transparent\textsuperscript{61} in order to facilitate traders’ access to the systems. Moreover, MTF operators are required “to provide, or ensure” that users have access to “sufficient publicly available information” enabling them to form an informed judgment.\textsuperscript{62}

Other rules governing the operation of MTFs require compliance with pre-trade and post-trade transparency obligations with respect to equity transactions concluded on MTFs.\textsuperscript{63} Investment firms operating MTFs do not have post trade transparency obligations (namely, the obligation to publish data on concluded trades), where such information is made public under the system of a “regulated market.”\textsuperscript{64} Possibilities for deferral of trade reporting, and the range/depth of pre-trade disclosure are quite similar to those applicable to regulated markets.\textsuperscript{65}

MiFID gives the right to MTFs to finalize, clear, and settle transactions concluded on them through access to central counterparty and clearing and settlement facilities operated in another Member State.\textsuperscript{66} Such connectivity is
necessary to facilitate the finalization of transactions concluded on MTFs and safeguard traders' legal rights.

4. Trade Execution by Investment Firms

MiFID has introduced strict "best execution" and "client order handling" requirements. MiFID also provided a very comprehensive set of rules mandating the new EU regime for the "best execution" of client orders by investment firms. This is yet another step towards maximum harmonization, since the ambit and nature of "best execution" rules had traditionally been determined by Member States. Accordingly, investment firms acting on behalf of clients may show that they have provided their clients with "best execution", if they can prove that:

(a) they have exercised due diligence to ensure that the order is executed in the manner most favorable for client conditions, unless the client has given specific instructions otherwise;

(b) they have developed suitable procedures that enable them to demonstrate that they have tried to obtain the best deal for the client; firms must be able to demonstrate to their clients, at the client's request, that they have executed their orders in accordance with the firm's execution policy;

(c) they have informed investors of the different channels through which their orders may be executed; and

(d) they have taken measures for the earliest possible execution of clients' limit orders, and have made public client limit orders with respect to shares admitted to trading on a regulated market, which are not immediately executed on the wider marketplace (unless the client has instructed the firm otherwise). Firms are deemed to have complied with this obligation if they have transmitted the orders to a "regulated market" or an MTF.

67. Id. art. 21(1).
68. Id. art. 21(5).
69. Id. art. 22(2).
Furthermore, MiFID requires investment firms called "systematic internalisers" to make their quotes public regularly and continuously, during normal trading hours. On the basis of MiFID's definition of "systematic internalisers," an investment firm is subject to this obligation only if it deals on its own account client orders on an "organized, frequent and systematic basis," and in sizes up to standard market size, subject to the qualification that there is a liquid market for the shares in question. In addition, the MiFID imposes post-trade transparency obligations to investment firms, which conclude internally or through any other OTC facility, and outside of a "regulated market" or an MTF, transactions in shares admitted to trading on a "regulated market." They must make public details of such transactions "as close to real time as possible." MiFID requires investment firms to "take reasonable steps" to identify and manage, through the establishment of appropriate organizational structures, conflicts of interest that may arise between themselves and their clients in the course of providing "investment services" and "ancillary services" to their clients, as defined in the Annex I of the MiFID. Relevant interests include the identifiable interests of investment firms' managers, employees, tied agents, and of any other person "directly or indirectly linked to them by control" or to the 

71. "Systematic internaliser" means an investment firm which, on an organized, frequent, and systematic basis, deals on own account by executing client orders outside a regulated market or an MTF. MiFID, supra note 4, art. 4(1)-(7).
72. Id. art. 27(1)-(3).
73. For CESR's views on the content of this qualification see CESR, Second Consultation Paper on MiFID, supra note 70, at 38-41.
74. According to the Directive the "standard market size" for each share traded by a "systematic internaliser" is derived by grouping shares "in classes on the basis of the arithmetic average value of the orders executed in the market for that share." The market for each share comprises "all orders executed in the European Union in respect of that share excluding those large in scale compared to normal market size for that share." It follows that "the standard market size for each class of shares shall be a size representative of the arithmetic average value of the orders executed in the market for the shares included in each class of shares." MiFID, supra note 4, art. 27(1). Furthermore, the regulator of the most relevant market, in terms of liquidity, on which the biggest number of transactions for each share is taking place "shall determine at least annually, on the basis of the arithmetic average value of the orders executed in the market in respect of that share, the class of shares to which it belongs" and shall make relevant information "public to all market participants." Id. art. 27(2). Under Art. 25(7) of the MiFID the specific content of the criterion of liquidity, i.e. number and/or value of transactions remains to be determined at Level 2. CESR has suggested that a share should be deemed to have a liquid market for the purpose of Article 27 if it satisfies the following criteria: (a) Trading activity: The share is traded daily; and (b) The free float of the share is at least 1 billion euro. The free float should be calculated by excluding those holdings exceeding 5% of the voting rights, as defined in the Transparency Obligations directive. See CESR, Second Consultation Paper on MiFID, supra note 70, at 43. If CESR's definition of "liquidity" is adopted by the Commission in Level 2 legislation, then "systematic internalisers" will have to fulfill the requirements of Article 27 in all relevant shares, even if these are not liquid in their home state markets.
76. MiFID, supra note 4, art. 28(1).
77. Id.
78. Id. art. 18.
interests of different clients of the firm. Where the proper management of conflicts of interest through the firm’s internal mechanisms is not possible and there remains a reasonable risk that the clients’ interests may be damaged, MiFID requires investment firms to clearly disclose “the general nature and/or sources of conflicts of interest to the client before undertaking business on its behalf.”

Moreover, MiFID attempts to harmonize, to the extent that it is possible, the body of conduct of business rules, other than those governing conflict of interests and best execution, which commonly apply to investment firms in the EU. Member States will, of course, remain free in all areas to impose additional and possibly stricter national rules. Level 2 detailed rules will differentiate in their application between different forms of investment services and between professional and retail clients, who require different forms and intensity of investor protection. Annex II of the MiFID sets out criteria and procedures for determining when a client can be categorized as a “professional client” for the purposes of applying the relevant less restrictive conduct of business rules.

D. The Expanded Scope of MiFID

1. The Provision of Investment Advice and Investment Research

The MiFID extends the list of “investment services” that firms may offer on the basis of the “common passport,” on a stand-alone basis, to the provision of investment advice, which was listed as an “ancillary service” under the ISD. The principal implications of the inclusion of investment advice to the list of “investment services” are the following: (a) investment advisors become subject to MiFID’s initial authorization and ongoing supervision obligations, including initial capital and continuing adequate resources; (b) entities (including natural persons) providing investment advice as their principal activity will be required to be licensed as an “investment firm,” as opposed to being subject to a variety of specialized national regimes as at present; and (c) even firms which provide investment advice on a “stand-alone” basis and not in conjunction with any other investment business will be able to utilize the common passport and set up a branch in another Member State or conduct business, on a cross-border basis.

MiFID defines as investment advice: “the provision of personal recommendations to a client, either upon its request or at the initiative of the investment firm, in respect of one or more transactions relating to financial instruments.” Therefore, it would seem that the provision of general investment recommendations to clients or the public at large, in the form of financial

79. Id. art. 18(1).
80. Id. art. 18(2).
81. Id. art. 19.
82. Id. art. 19(10).
83. Id. art. 4(1)(4).
analysis or research, does not constitute "investment advice" under MiFID. However, in a recent Consultation Paper, CESR has sought to expand the ambit of MiFID's definition in order to bring under the "investment advice" regime "implicit advice" and "generic recommendations."^84 CESR's chief arguments pertain to the scope of suitability rules for the provision of investment advice and the ability of investment firms offering advisory services to utilize MiFID's passport. Accordingly, in CESR's view it would not be possible for investment firms to use the exclusion of generic advice from the definition of investment advice to circumvent the suitability requirement.^85 Furthermore, the "exclusion of generic advice from the definition of investment advice" would mean that investment firms would not be able to offer full advisory services under MiFID's passport,^86 since the production and dissemination of investment research and analysis is classified as an "ancillary service."^87 As the results of the consultation are pending, no definite view may be offered on this subject.

Arguably, advisory firms, which do not provide any other investment service or hold client money or assets, do not pose any financial risk to investors. Thus, initial capital requirements are relaxed for such firms. Sole providers of investment advice may substitute the initial capital requirement with the much cheaper and cost efficient professional indemnity insurance.

2. Dealing in Commodity Derivatives and Other Derivative Instruments

Commodity derivatives have been included in the list of financial instruments covered by the MiFID.^88 Thus, both trading and intermediation services concerning these instruments fall within the scope of MiFID. The exclusion of commodity derivatives from the ISD's definition of financial instruments had prevented investment firms from using the ISD passport for the cross-border provision of investment services in commodity derivatives. MiFID plausibly exempts from its scope firms dealing on their own account,^89 which do not need a regulatory license in order to continue conducting business. As such, entities do not purport to provide investment services outside a very limited circle of customers, which usually include affiliated and parent companies. It would have been very restrictive and unfair to force them to obtain authorization to operate as investment firms.^90

^84. See CESR, Second Consultation Paper on MiFID, supra note 70, at 10-12.
^85. Id. at 11.
^86. Id. at 12.
^87. MiFID, supra note 4, Annex I, §B.5.
^88. Id. at §C.
^89. Id. art. 2(1)(i),(k).
The definition of commodity derivatives includes (beyond straightforward commodity derivatives), futures contracts traded on regulated markets (or MTFs), which are physically settled, provided that such contracts possess the characteristics of financial instruments.9

Furthermore, the list of financial instruments covered by MiFID extends to a number of innovative contracts. These contracts include credit derivatives,9 contracts for differences,9 and derivatives settled in cash or capable to be settled in cash at the option of one of the parties. The class of derivatives capable of being settled in cash includes contracts whose subject matter refers to freight rates, emission allowances, economic statistics, and climatic variables9 such as “weather derivatives.” In addition, MiFID covers any other derivative contracts: relating to assets, rights, obligations, and indices, which the Directive does not mention by name and which have the “characteristics of other derivative financial instruments,” because they are traded on a regulated market or an MTF, or “are cleared and settled through recognised clearing houses or are subject to regular margin calls.”9

IV. THE MARKET ABUSE DIRECTIVE

A. Introduction

At the heart of FSAP sat a proposal for the enactment of a Directive that would prohibit both insider dealing and market manipulation, replacing the Insider Dealing Directive.96 In an integrated financial market, investors may access a multiplicity of trading venues across the EU. The volume of cross-border investment business, including cross-border trading, has significantly increased in recent years. Investors (retail or institutional) have taken advantage of opportunities offered by the advent of e-commerce to access for trading purposes, either directly by using the Internet, or through an intermediary (regulated markets or Alternative Trading Systems) based in another Member State. Investor’s transactions, as well as the provision of investment services to them, had to be governed by uniform market conduct rules prohibiting price manipulation, dissemination of false information, and insider dealing. A uniform regime protects symmetrically financial markets from abusive practices, which undermine investor confidence, as shown by the severe “bear market” that followed the eruption of a series of financial scandals, such as the cases of Enron,

91. MiFID, supra note 4, Annex I, § C.
92. Id. § C(8).
93. Id. § C(9).
94. Id. § C(10).
95. Id.
WorldCom and Adelphia and the Wall Street analysts’ scandals. This allows regulatory authorities to cooperate more effectively where necessary to prevent cross-border abuse from harming investors.

Furthermore, financial institutions, regulated markets and other investment intermediaries that offered cross-border investment services were required to comply with the market conduct rules of multiple jurisdictions, subject to the qualifications of the Court’s rule of reason, since the EU lacked harmonized rules on market manipulation. This, of course, entailed increased costs of compliance. In addition, the fact that a plural number of legal orders regulated the same transaction raised the possibility of rule conflicts.

Faced with these challenges, the Commission correctly perceived a pressing need to enact harmonized rules for the detection and punishment of market manipulation and insider dealing. These harmonized rules would remove the possibility of national rule conflict and of a regulatory “race to the bottom” in the integrated EU market for financial products. Another advantage of a harmonized regime was that it would ensure “throughout the Community the same framework for allocation of regulatory responsibilities, enforcement and cooperation.”

The Market Abuse Directive was formally endorsed in December 2002 following a great deal of consultation. It aims “to ensure the integrity of Community financial markets and to enhance investor confidence in those markets.” It provides an EC wide prohibition of insider dealing and market manipulation and prohibits selective disclosure. Furthermore, it upgrades the EU regimes for disclosure of inside information by issuers of financial instruments, and creates a harmonized regime for, inter alia, the disclosure of analysts’ (and other producers and disseminators of financial information) conflicts of interests. The respective regimes have been further specified through the enactment of three Commission Directives, which constitute Level 2 implementing measures. These


98. Market Abuse Directive, supra note 7, rec. 11.

99. Id. rec. 12.


101. Id. rec. 11.

have been supplemented by an EC Regulation,\textsuperscript{103} which has established a detailed EU-wide regime for the carrying out of share buybacks and stabilizations.

B. The Prohibition of Insider Dealing

1. The Offense

The combined reading of Articles 2, 3, and 4 shows that the Directive dispenses, in most cases, with the requirement of intent and sets out insider dealing as an objective, three-pronged offense committed through:

(a) dealing in ("acquiring or disposing or attempting to acquire or dispose of")\textsuperscript{104} financial instruments,\textsuperscript{105} on the basis of inside information, by the persons listed in Article 2(1), the so-called primary insiders, or any other person, who possesses inside information,\textsuperscript{106} if that person knows, or ought to have known that it is inside information;\textsuperscript{107}

(b) the disclosure of inside information by "primary insiders" to third persons, unless such disclosure is made in the normal course of its employment or profession, or by secondary insiders;\textsuperscript{108} and

(c) a recommendation or inducement made by primary insiders, or by secondary insiders,\textsuperscript{109} to another person, on the basis of inside information, to deal in ("acquire or dispose of") financial instruments to which the information relates.\textsuperscript{110}


\textsuperscript{104} "Member states shall prohibit any person referred to in the second subparagraph who possesses inside information from using that information by acquiring or disposing of, or by trying to acquire or dispose of, for his own account or for the account of a third party, either directly or indirectly, financial instruments to which that information relates." \textit{Market Abuse Directive, supra} note 7, art. 2(1).

\textsuperscript{105} Dealing on the basis of inside information is usually called the "primary offence" of insider dealing.

\textsuperscript{106} Usually such persons are called "secondary insiders" or "tippees."

\textsuperscript{107} \textit{Market Abuse Directive, supra} note 7, arts. 2(1) & 4.

\textsuperscript{108} \textit{Id.} arts. 3(a) & 4.

\textsuperscript{109} \textit{Id.} arts. 3(b) & 4.

\textsuperscript{110} Disclosing inside information, and recommending or inducing, on the basis of inside information, constitute the so-called secondary offence of insider dealing, although the Directive does not make such distinctions.
The list of "primary insiders" under Article 2(1) includes persons who possess inside information:

(a) by virtue of their membership of the administrative, management, or supervisory bodies of the issuer;

(b) by virtue of their holding in the capital of the issuer;

(c) by virtue of their having access to the information through the exercise of their employment, profession or duties; or

(d) by virtue of their criminal activities.

Therefore, judicial and regulatory authorities do not have to prove that persons under investigation had an intention to use inside information to obtain a gain. As intent is usually the hardest element to prove, prosecutors of insider dealing and similar regulatory actions in the EU have a lesser burden than those in the U.S. prosecuting cases under section 10(b) of SEA 1934 and SEC Rule 10b-5.

Furthermore, if a "primary insider" is a legal person, then the prohibition extends to the natural persons, "who take part in the decision to carry out the transaction" on behalf of the legal person in question. The list of "primary insiders" is almost the same as that provided under Article 2(1) of the Insider Dealing Directive, with the addition of the new element of access to inside information by virtue of criminal activities. This addition was necessitated by the alleged involvement of organized crime and terrorist groups in securities markets as a means to profiteer or finance their illegal activities, including instances of theft of inside information, or of running of extortion rackets aiming at the acquisition of inside information.

"Secondary insiders" may be acquitted if they prove that they did not know or did not have to know that they were in possession of inside information. The determining criterion is what "a normal or reasonable person would know or should have known in the circumstances." The defense of lack of "actual knowledge," or of lack of a reasonable obligation to know that the relevant information was inside information is not available to "primary insiders." In

111. Market Abuse Directive, supra note 7, art. 2(2).
114. Id. art. 4.
115. "Use of inside information can consist in the acquisition or disposal of financial instruments by a person who knows, or ought to have known, that the information possessed is inside information. In this respect, the competent authorities should consider what a normal and reasonable person would know or should have known in the circumstances." Id. rec. 18.
116. Article 4 of the Directive grants the "knowledge" defense only to secondary insiders, whereas Articles 2 and 3 make no mention of such qualification/defense for primary insiders.
addition, obtaining a financial benefit, as a result of the actions described in Articles 2-4, does not seem to be part of the constitutive elements of the offense.

A discussion of the mechanics of insider dealing, its effect on economic efficiency, and of the rationales for its prohibition are outside the ambit of this Article. Thus, the next step in the analysis of the offense of insider dealing under the Directive, is to define what constitutes “inside information.”

2. Inside Information

The Market Abuse Directive offers a definition of inside information that is much more complex than that included in the Insider Dealing Directive. In this respect, the Market Abuse Directive provides a general definition of “inside information” and two special (complementary) definitions. Under Article 1(1) “inside information” means information, which:

(a) is of a precise nature;
(b) has not been made public;
(c) relates directly or indirectly to one or more issuers of financial instruments or to one or more financial instruments; and
(d) if such information was made public, it would be likely to have a significant impact on the prices of relevant “financial instruments or on the price of related derivative financial instruments.”

This general definition of inside information seems to be applicable to all persons in possession of inside information and to all financial instruments, other than commodity derivatives, which fall within the scope of the Directive. The two special (complementary) definitions of inside information are respectively used in relation to trading in derivatives on commodities, and in relation to persons “charged with the execution of orders.”

Thus, in relation to derivatives on commodities, inside information means information of a precise nature, which has not been made public, and which relates directly or indirectly to one or more derivatives on commodities, provided that users of markets, on which such derivatives are traded, would expect to receive such information, in accordance with “accepted market practices” on

117. See EMILIOS AVGOULEAS, THE MECHANICS AND REGULATION OF MARKETS ABUSE, A LEGAL AND ECONOMIC ANALYSIS 75-101, 156-234 (Oxford University Press 2005); chapters 3 and 5 of the same book provide extensive analysis of the mechanics of insider dealing, its effect on economic efficiency, and of the rationales for its prohibition.

118. “Inside information’ shall mean information which has not been made public of a precise nature relating to one or several issuers of transferable securities or to one or several transferable securities, which, if it were made public, would be likely to have a significant effect on the price of the transferable security or securities in question.” Council Directive 89/592/EEC of 13 November 1989 Coordinating Regulations on Insider Dealing, art. 1(1), O.J. (L 334) 30.
those markets. Article 4 of the Commission Directive on Accepted Market Practices clarifies that users of markets on which derivatives on commodities are traded, are deemed to expect to receive such information, when this relates directly or indirectly to one or more derivatives on commodities, and is:

(a) routinely made available to the users of those markets; or

(b) is required to be disclosed in accordance with legal or regulatory provisions, market rules, contracts or customs on the relevant underlying commodity market or commodity derivatives market.

Furthermore, in relation to “persons charged with the execution of orders concerning financial instruments” inside information means information conveyed by a client, which relates “to the client’s pending orders,” provided that it is of a precise nature and relates directly or indirectly to one or more issuers of financial instruments, or to one or more financial instruments, and which, if it were made public, would be likely to have a significant impact on the prices of those financial instruments, or on the price of related derivative financial instruments.

As mentioned above, the first of the special definitions of Article 1(1) applies only to derivatives on commodities and is inapplicable to all other classes of financial instruments. Within the ambit of the second special definition falls intermediate or executing brokers (or any other person “charged with the execution of orders concerning financial instruments”), who are in possession of client information regarding their pending orders. The clear target of the second special definition is the elimination of “front-running.”

A careful reading of the general definition of inside information, and of the two special definitions, leads to the identification of a number of constitutive elements, which are shared by all of them. First, inside information is information that: (a) is not public; (b) is of a precise nature; and (c) directly or indirectly refers to relevant financial instruments (including derivatives on commodities), or the issuers of financial instruments (excluding derivatives on commodities) where the issuer is deemed to be of no material importance.

The general definition of inside information and the second of the special definitions incorporate an element of price sensitivity; namely, that the relevant information must also have a significant effect on “the prices of financial instruments, or on the price of related derivative financial instruments.” The first of the special definitions dispenses with this criterion. It replaces the element of price sensitivity with “information” that users of commodity derivatives markets would expect to receive in accordance with “accepted practices” on those markets.

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119. See also Market Abuse Directive, supra note 7, rec. 19.
120. Id. art. 1(1).
3. Defenses and Safe Harbours

Under Article 8 and Recital 33 of the Market Abuse Directive, trading in one's own shares in the context of buy-back programs and the stabilization of financial instruments are exempted from the prohibitions of the Directive, if they comply with the requirements of the Regulation on share-buy backs and stabilizations. Furthermore, Article 2(3) of the Directive creates a "safe harbour" from the prohibition of transactions conducted in the discharge of an obligation (contractual or legal) to acquire or dispose of financial instruments. This safe harbour exists provided that the relevant obligation has arisen in the context of an agreement that was concluded before the person concerned possessed inside information and before the parties' obligations have become due. In this manner, the Directive protects the certainty of contracts and allows for the proper performance of pre-existing contractual obligations, which, in the absence of the "safe harbour" could have been exposed to the threat of voidability as a result of supervening illegality, creating unnecessary risks in the conclusion of financial transactions.

In addition, market makers, bodies authorized to act as counterparties (as for instance, exchanges and related organizations that act as "central counterparties"), settlement and payment systems, custodians, and persons authorized to execute orders on behalf of third parties who possess inside information, will not be found in violation of the prohibition, provided that: (a) market makers, central counterparties, or settlement and payment systems restrict themselves to activities that involve the mere buying or selling of financial instruments; and (b) brokers, who act for third parties, simply carry out "an order dutifully." Assuming compliance with the above conditions, market makers and brokers are afforded a "safe harbour" and their trading activities are not deemed as constituting use of inside information.

Another "safe harbour" is granted by Recital 29, which provides that the mere fact of having access to inside information relating to another company and using it in the context of a public takeover bid for the purpose of gaining control of that company, or proposing a merger with that company, should not in itself be deemed to constitute insider dealing. This provision should be read and interpreted in conjunction with Article 6 of the Directive on Takeover Bids. Article 6 requires bidders to disclose without delay their decision to make a bid, and pre-notify the supervisory authority of their decision, being also obliged to draw in a timely fashion an offer document addressed to the shareholders of the offeree company.

Furthermore, Article 3(a) creates a clear "safe harbour" from the secondary offense of disclosure of inside information, where such disclosure is made by a

121. Supra note 103.
122. Market Abuse Directive, supra note 7, art. 2(3).
123. Id. rec. 18.
person in the normal course of the exercise of his/her employment, profession or duties. Within the “safe harbour” fall directors that discuss the unpublished results of an issuer with their auditors and bankers, the regulatory and tax authorities, and the company’s lawyers or accountants who share “inside information” with their co-workers for the purposes of work carried out for the issuer.

Arguably, the obfuscating way that the Directive’s “safe harbours” have been drafted could prejudice their successful application in real market conditions. Accordingly, the onus falls on national regulators to endeavor to draft properly calibrated “safe harbours” which are clear in their application, during the implementation stage.

C. The Prohibition of Market Manipulation

1. The Offense of Market Manipulation

The second offense proscribed by the Market Abuse Directive is that of market manipulation. As in the case of insider dealing, the Directive has dispensed, to the extent possible, with any requirement of intent in the definition of market manipulation, in order to increase the rate of successful prosecutions and of similar regulatory actions. Accordingly, under the Directive, market manipulation is an objective, effect-based offense, at least in the majority of its manifestations. Under Article 1(2) of the Directive, market manipulation is a three pronged offense committed through:

(a) transactions or orders to trade:
   — which give, or are likely to give, false or misleading signals as to the supply of, demand for or price of financial instruments, or
   — which secure, by a person, or persons acting in collaboration, the price of one or several financial instruments at an abnormal or artificial level, unless the person who entered into the transactions or issued the orders to trade establishes that his reasons for so doing are legitimate and that these transactions or orders to trade conform to accepted market practices on the regulated market concerned;

(b) transactions or orders to trade which employ fictitious devices or any other form of deception or contrivance; [and],

(c) dissemination of information through the media, including the internet, or by any other means, which gives, or is likely to give, false or misleading signals as to financial instruments, including the dissemination of rumors and false or misleading news, where the person who made the dissemination knew, or ought to have known, that the information was false or misleading.
The Directive indicates a number of market practices and instances of market behavior which are likely to amount to market manipulation under the above definition:  

- conduct by a person, or persons acting in collaboration, to secure a dominant position over the supply of, or demand for, a financial instrument which has the effect of fixing, directly or indirectly, purchase or sale prices or creating other unfair trading conditions;
- the buying or selling of financial instruments at the close of the market with the effect of misleading investors acting on the basis of closing prices; and
- taking advantage of occasional or regular access to the traditional or electronic media by voicing an opinion about a financial instrument (or indirectly about its issuer), while having previously taken positions on that financial instrument and profiting subsequently from the impact of the opinions voiced on the price of that instrument, without having simultaneously disclosed that conflict of interest to the public in a proper and effective way.

Therefore, the Directive prohibits most known forms of market manipulation including: (a) trade-based manipulations or misleading trades; (b) artificial transactions and “wash sales;” and (c) information-based manipulations effected through the dissemination of false and misleading information.

The Commission Directive on the Definition of Public Disclosure of Inside Information and Market Manipulation describes a number of objective (market) events and perspectives. The Directive suggests that Member States’ competent authorities and market participants must regard these events and perspectives as “signals” of market manipulation and they should be examined when considering whether particular behavior constitutes, or may lead to, the first form of market manipulation: “misleading trades” under Art. 1(2)(a).

2. Defenses and Safe Harbours for Market Manipulation

In addition to the defenses discussed in section IV.B.3 above, Article 8 and Recital 33 of the Market Abuse Directive provide that trading in one’s own shares in the context of buy-back programs and the stabilization of financial instruments are exempted from the prohibitions of the Directive, if they are

125. See AVGOULEAS, THE MECHANICS AND REGULATION OF MARKETS ABUSE, A LEGAL AND ECONOMIC ANALYSIS, supra note 117, at 103-154 (providing extensive analysis on these types of market manipulations).
carried out in accordance with the requirements of the EC Regulation on share-
buy-backs and stabilizations. It appears that, by choosing to enact a Regulation
instead of a Directive, the Commission aimed at the maximum harmonization of
Member State legal and regulatory regimes governing share buy-backs and
stabilizations.126 The use of a Regulation leads to greater legal certainty in the
implementation and application of the relevant rules. This does not, however,
mean that share buy-back schemes and stabilizations that do not comply with the
provisions of the Commission Regulation “should not in themselves be deemed
to constitute market abuse.”127 They should be examined by the Member States’
competent authorities on an ad hoc basis for the purposes of enforcing the
prohibition of market manipulation in the Directive and applying requisite
sanctions.128

The Commission Regulation on share buy-backs and stabilizations defines
buy-back programs as trading (by an issuer) in one’s own shares in accordance
with Articles 19 to 24 of Council Directive 77/91 EEC.129 Under Article 3 of the
Regulation the exemption of the Market Abuse Directive extends only to “buy
back” schemes which lead to reduction of the issuer’s share capital, satisfy
obligations arising from debt financial instruments exchangeable into equity
instruments, obligations arising from allocations of shares to employees of the
issuer of an associate company, or by virtue of “employee share option
programmes.” In addition, in order to benefit from the share buy-back programs
exemption, issuers must comply with disclosure and trading obligations imposed
by Articles 4, 5, and 6 of the Regulation, and with the conditions on share capital
maintenance130 laid down by Article 19(1) of Directive 77/91/EEC (the Second
Company Law Directive),131 requiring the approval of the program by the
competent (company law) authorities.

126. The Regulation has, to large degree, endorsed CESR recommendations following a very extensive
round of consultations on the subject undertaken by CESR and its predecessor FESCO. See Stabilisation and
Allotment, A European Supervisory Approach, Consultative Paper, FESCO (Sept. 15, 2000), Ref. Fesco/00099b,
available at http://www.kredittilsynet.no/archive/stab_word/01/01/20003002.doc; Second Consultation Paper:
Stabilisation and Allotment—an European Supervisory Approach, FESCO, (June 2001), Ref. Fesco/01-085,
untopyynnot/L05920011pmLiite.pdf+fesco+01-085&hl=en.

127. Regulation on Share Buy-Backs and Stabilisations, supra note 103, rec. 2.

128. Id. rec. 3.

129. Id. art. 3.

130. Id. art. 4(1).

which, for the Protection of the Interests of Members and Others, are Required by Member States of Companies
within the Meaning of the Second Paragraph of Article 58 of the Treaty, with Respect to the Formation of
Public Limited Liability Companies and the Maintenance and Alteration of their Capital, with a View to
Making Such Safeguards Equivalent, 1977 O.J. (L 26) 1.
Furthermore, under the Commission Regulation, stabilization may only be undertaken in connection with "transferable securities" (as defined in the ISD and now in the MiFID), which are admitted to trading on a regulated market or for which a request for such admission has been made, provided that they are subject to a "significant distribution," and the stabilization is undertaken exclusively for the purpose of supporting the market price of securities "due to a selling pressure in such securities." Furthermore, a number of disclosure, reporting, time, and price conditions must be fulfilled. Accordingly, the permitted forms of stabilization comprise:

(a) purchases of transferable securities and transactions in "associated instruments" undertaken "in the context of significant distribution" of such securities and exclusively for the purpose of supporting the market price of these securities (for a predetermined period of time); all transactions must be conducted by investment firms or credit institutions, which act for the issuer or the offeror; and

(b) the use of ancillary stabilization devices such as the use of the "overallotment facility" and of "greenshoe options."

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132. MiFID, supra note 4, art. 4(1)(18).
133. Regulation on Share Buy-Backs and Stabilisations, supra note 103, art. 2(6).
134. "Stabilisation" is "any purchase or offer to purchase relevant securities, or any transaction in associated instruments equivalent thereto, by investment firms or credit institutions, which is undertaken in the context of a significant distribution of relevant securities exclusively for supporting their market price for a predetermined period of time, due to a selling pressure in such securities." Regulation on Share Buy-Backs and Stabilisations, supra note 103, art. 2(7).
135. Id. art. 7-11.
136. Id. art. 2(6), (7).
137. "Associated instruments" means the following financial instruments (including those which are not admitted to trading on a regulated market, or for which a request for admission to trading on such a market has not been made, provided that the relevant competent authorities have agreed to standards of transparency for transactions in such financial instruments): (a) contracts or rights to subscribe for, acquire or dispose of relevant securities; (b) financial derivatives on relevant securities; (c) where the relevant securities are convertible or exchangeable debt instruments, the securities into which such convertible or exchangeable debt instruments may be converted or exchanged; (d) instruments which are issued or guaranteed by the issuer or guarantor of the relevant securities and whose market price is likely to materially influence the price of the relevant securities, or vice versa; (e) where the relevant securities are securities equivalent to shares, the shares represented by those securities (and any other securities equivalent to those shares). Id. art. 2(8).
138. Id. art. 2(7).
139. "Offeror" means the prior holders of, or the entity issuing, the relevant securities. Id. art. 2(10).
140. "Overallotment facility" means a clause in the underwriting agreement or lead management agreement which permits acceptance of subscriptions or offers to purchase a greater number of relevant securities than originally offered. Id. art. 2(13).
141. "Greenshoe option" means an option granted by the offeror in favour of the investment firm(s) or credit institution(s) involved in the offer for the purpose of covering overallotments, under the terms of which such firm(s) or institution(s) may purchase up to a certain amount of relevant securities at the offer price for a certain period of time after the offer of the relevant securities. Id. art. 2(14).
D. Complementary Features of the EC Market Abuse Regime

1. Issuer Continuous Disclosure Obligations, Selective Disclosure, Notifications by Insiders

Article 6(1) of the Market Abuse Directive imposes on financial instruments issuers that have “requested or approved admission of their financial instruments to trading on a regulated market in a Member State,” a duty to disclose inside information as soon as possible. The manner that such disclosure must be effected is clarified by Article 2 of the Commission Directive on the Definition of Public Disclosure of Inside Information. The relevant disclosure must be made in such a mode as to allow “fast access and complete, correct and timely assessment of the information by the public.” The same provision requires prompt disclosure of the occurrence of an event or of a set of circumstances, even if there is no formal assurance about their occurrence. It also requests that publicly disclosed inside information is continuously updated. The regulatory authorities of Member States shall ensure that issuers of financial instruments, for an appropriate period, post on their Internet sites all inside information that they are required to disclose publicly. The adoption by the Commission of CESR’s recommendation that issuers should not disseminate inside information through other channels before it is disclosed through an officially appointed mechanism has created additional legal certainty. Disclosure by the issuer of non-public information through a channel that is not one of the “officially appointed mechanisms” would not, therefore, constitute proof of timely disclosure.

Article 6(2) of the Market Abuse Directive allows an issuer of financial instruments to delay the public disclosure of inside information, if such disclosure would prejudice his legitimate interests. Any such delay must satisfy two requirements: (a) the omission would not be likely to mislead the public; and (b) the issuer is able to ensure the confidentiality of the inside information whose disclosure has been delayed, in order to prevent insider dealing. An issuer...
who has decided to delay the disclosure of inside information for the aforementioned reasons must inform the competent authority of this decision without delay.  

Furthermore, the Market Abuse Directive expressly prohibits selective disclosure by issuers of financial instruments, regardless of whether the disclosure is made by the issuer itself, or a person acting for the issuer. Selective disclosure usually takes the form of disclosure by issuers of non-public information to a selected group of analysts (selective briefing), and has been the subject of considerable debate over recent years.

In contrast, the practice seems to encourage favoritism and insider dealing. Namely, one group of analysts is granted access to price-sensitive issuer data to the exclusion of other analysts and investors, helping those analysts to publish more accurate research in exchange for granting the company's management a favorable review. In addition, it allows the analysts' employer institution, in breach of any Chinese walls, to trade on the basis of this selectively disclosed non-public information, profiting at the expense of uninformed investors. Yet the practice of selective disclosure is thought to be an effective mechanism for the "discreet leaking" of good or bad news, which filters into the price of the specific issuer's securities, without the issuer having to disclose detailed information that could be exploited by its competitors. Selective disclosure acting in this manner does, arguably, enhance the information and pricing efficiency of financial markets.

In the United States, selective disclosure by issuers was finally prohibited, following a long debate, with the adoption of SEC Regulation FD (Fair Disclosure). The Directive has also opted for a complete prohibition, perceiving it as a practice that harms investor confidence in the integrity of the market. Arguably, academic opinion does not take such a dim view of selective disclosure. However, given investor sentiment in the post-Enron era and the serious shift of regulatory attitudes towards investment analysts, it would have been very difficult to avoid the resulting blanket prohibition.

misuse or improper circulation of such information; (c) the issuer has in place measures which allow immediate public disclosure in case the issuer was not able to ensure the confidentiality of the relevant inside information, without prejudice to the second subparagraph of Article 6(3) of Directive 2003/6/EC.” Relevant “effective arrangements” include the establishment of Chinese walls.

147. Id. rec. 4.
148. Market Abuse Directive, supra note 102, art. 6(2).
149. Id. art. 6(3).
152. See Zohar Goshen & Gideon Parchomovsky, On Insider Trading, Markets, and “Negative” Property Rights in Information, 87 VA. L. REV. 1229 (2001), who are firmly in favor of selective disclosure, favoring analysts over insiders. For a more balanced approach, see Donald C. Langevoort, Taming the Animal Spirits of the Stock Markets: A Behavioral Approach to Securities Regulation, 97 NW. U. L. REV. 135, 164-176 (2002). As Professor Langevoort observes: “The strongest claim against Reg FD is that it removes a useful predicate to the efficiency of the stock market, leaving it less well calibrated and more volatile.” Id. at 170.
Article 6(3) of the Market Abuse Directive provides that “whenever an issuer, or a person acting on his behalf or for his account, discloses any inside information to any third party in the normal exercise of his employment, profession or duties . . . he must make complete and effective public disclosure of that information.” Effective public disclosure of the information in question must be made through officially appointed mechanisms. The disclosure of relevant information should take place either simultaneously with any selective briefing to a third party, in the case of intentional disclosure, or “promptly in the case of a non-intentional disclosure.” There is no obligation to effect simultaneous disclosure, where the person receiving the information owes a regulatory, contractual or otherwise imposed duty of confidentiality. This is, of course, a “safe harbour” covering disclosure of inside information to the issuer’s non-executive directors, its lawyers, auditors and other professional consultants for the purpose of facilitation of the issuer’s business, the auditing of its financial statements or the carrying out of due diligence surveys for the purpose of a merger or an acquisition.

Finally, issuers and “persons acting on their behalf or for their account,” are required to draw up lists of persons “working for them, under a contract of employment or otherwise, who have access to inside information.” The relevant lists shall be regularly updated, and capable of being transmitted “to the competent authority whenever the latter requests it.”

Article 6(4) of the Market Abuse Directive requires from “[p]ersons discharging managerial responsibilities within an issuer of financial instruments and, where applicable, persons closely associated with them” to notify the relevant competent authority of any transactions conducted on their own account relating to shares of the issuer in question, “or to derivatives or other financial instruments linked to them.” This form of information is particularly relevant in order to monitor the compliance of such persons with the prohibition of insider dealing. It also constitutes very important market information and its disclosure significantly enhances both the transparency and the information efficiency of the marketplace. For this reason, the Market Abuse Directive requires Member States to ensure that “public access to information concerning such transactions, on at least an individual basis, is readily available as soon as possible.”

153. Market Abuse Directive, supra note 7, art. 6(3).
154. “Greater transparency of transactions conducted by persons discharging managerial responsibilities within issuers and, where applicable, persons closely associated with them, constitutes a preventive measure against market abuse. The publication of those transactions on at least an individual basis can also be a highly valuable source of information to investors.” Id. rec. 26; Commission Directive on Accepted Market Practices, supra note 102, rec. 7.
155. Market Abuse Directive, supra note 7, art. 6(4).
2. Investment Recommendations and Disclosure of Interests

Article 6(5) of the Market Abuse Directive requests Member States to implement regulations which will oblige producers and disseminators of investment research and investment recommendations to fairly present "research concerning financial instruments or issuers of financial instruments" and information "recommending or suggesting investment strategy," where such research or investment recommendation is intended for submission to distribution channels or for dissemination to the public and not for internal use. The same persons are assigned the duty to disclose relevant interests and conflicts of interests "concerning the financial instruments to which that information relates."

The Directive addresses through the introduction of the dual duty of "fair presentation" and disclosure of interests and conflicts of interests, the very serious issue of production and dissemination of tainted investment research. The purpose of such research is usually to serve the interests of the producer (or of the disseminator), even if this is proved to be to the detriment of investors, who will rely on its findings or recommendations. The best-known examples of published investment analysis guided by colossal conflicts of interests are the investment reports and recommendations produced by "star analysts" within major U.S. investment banks during the 1990s. Analysts' reports were intentionally partial as they were consistently utilized by the analysts' employer institutions in order to obtain investment banking business. Their over-optimism had an appreciable impact on the creation of the stock market bubble of the 1990s.

The revelation of the extent to which such reports were tainted, created a serious crisis of confidence for U.S. investment banks and the global financial markets. It also led to the imposition of very significant sanctions on both the analysts concerned and their employers. The U.S. reforms included, with respect

156. The Attorney General for the State of New York opened his statement on the so-called "Wall Street Settlement" (with most of the major U.S. investment banks involved in the misleading research scandal) with the following words: "When my office began investigating conflicts of interest at Wall Street investment firms nearly two years ago, there was a prevailing sense that if problems existed they were the result of actions by a few rogue individuals. However, it soon became clear that firms routinely disseminated tainted investment advice that was designed to help investment banking clients but which harmed individual investors. It was also clear that systemic reform was imperative." Office of New York State Attorney General Eliot Spitzer, Statement by Attorney General Eliot Spitzer Regarding the "Global Resolution" of Wall Street Investigations' (Apr. 28, 2003), available at http://www.oag.state.ny.us/press/statements/global_resolution.html.

157. As reported by the Financial Times, the final settlement "included findings of fraud against three banks—Citigroup's Salomon Smith Barney unit, Credit Suisse First Boston and Merrill Lynch. The regulators also released evidence showing alleged conflicts of interest at other leading banks including Goldman Sachs and Morgan Stanley." See Joshua Chaffin et al., Tougher Action Urged against Wall St Banks, FIN. TIMES, Apr. 28, 2003.

158. "Regulators are turning up the heat on those who let abuses of investor trust occur during the bull market of the late 1990s, those whom investors were told would be pursued after Wall Street reached the research settlement in April. Last Friday, the banks found out just how high regulators would look. So far, the only individuals punished have been analysts such as Merrill Lynch's Henry Blodget and Citigroup's Jack Grubman. Both have been fined and barred from the industry." Regulators Turn up the Heat on Wall Street, FIN. TIMES, June 3, 2003.
to production and dissemination of investment research:\textsuperscript{159} (a) clear separation of the research and investment banking divisions at firms;\textsuperscript{160} (b) new mechanisms for providing independent research to investors at no cost to help them make more informed decisions;\textsuperscript{161} and (c) transparency of rating information.

There is hope that the utilization of the Market Abuse Directive's dual duty of "fair presentation" of research and disclosure of interests\textsuperscript{162} will similarly minimize the risk of dissemination of false or misleading information through the production and dissemination of investment research and recommendations enabling investors to rely on the accuracy, objectivity, and reliability of analysts' reports.

The Commission Directive defines investment "recommendations" as "research or other information recommending or suggesting an investment strategy, explicitly or implicitly, concerning one or several financial instruments or the issuers of financial instruments, including any opinion as to the present or future value or price of such instruments, intended for distribution channels or for the public."\textsuperscript{163} Furthermore, Article 1(4) of the Commission Directive on Fair Presentation and Disclosure of Interests defines the term (of Article 6(5) of the Market Abuse Directive) "[r]esearch or other information recommending or suggesting investment strategy," as:

(a) information produced by an independent analyst, an investment firm, a credit institution, any other person whose main business is to produce recommendations or a natural person working for them under a contract of employment or otherwise, that, directly or indirectly, expresses a particular investment recommendation in respect of a financial instrument or an issuer of financial instruments;

(b) information produced by persons other than the persons referred to in (a) which directly recommends a particular investment decision with respect to a financial instrument.

\textsuperscript{159} Other measures included: (a) a ban on IPO spinning—investment firms will no longer be allowed to allocate to officers or directors of public companies preferential access to valuable IPO shares of corporations from which they have sought or obtained investment banking business; (b) the appointment of independent monitors for each firm—a monitor would report to regulators on the firm's compliance with the terms of the agreement; (c) investor education—programs would be established to help investors protect themselves against securities fraud; and (d) the largest overall monetary payments in Wall Street history—$1.4 billion. See Joint SEC/NYAG/NASAA/NASD/NYSE Press Release, available at http://www.sec.gov/news/press/2003-54.htm.

\textsuperscript{160} Analysts would be insulated, and they would no longer be allowed to solicit business or accompany investment bankers on pitches and road-shows, or identify investment banking prospects. Investment banking would not be allowed input into analyst evaluation and compensation.

\textsuperscript{161} The rationale for the adoption of this measure was that independent research would guarantee that alternative views are made available to the retail customer, and also make the analyst aware that he or she is being judged on the basis of comparative independent analysis.

\textsuperscript{162} Market Abuse Directive, supra note 7, art. 6(5).

\textsuperscript{163} Commission Directive on Fair Presentation and Disclosure, supra note 102, art. 1(3).
Accordingly, securities research reports produced by investment firms and credit institutions, and securities research reports produced by independent research institutions, which fulfill the above criteria, fall within the ambit of Article 6 (5) of the Market Abuse Directive. Nevertheless, the production and dissemination of macro-economic analysis, general market commentary, and research concerning broad markets, which do not carry investment recommendations, need not comply with the above duties. Also, credit rating agencies’ reports on the creditworthiness of specific issuers fall outside the above definition of investment “recommendations.”

Articles published in the press that disseminate the findings of investment research or recommend investment strategy could be seen as falling within the scope of Article 6(5), and they must incorporate disclosure of relevant interests or conflicts of interest. However, the Commission leaves it to the discretion of Member States to determine the form of applicable regulation, including self-regulation in this area. This unsatisfactory solution was reached because the Commission was particularly intent on avoiding any conflicts between the Directive and the constitutional protection of the rights of free expression in Member States’ legal orders, and the European Convention for the Protection of Human Rights and Fundamental Freedoms.

V. POPD II AND THE TRANSPARENCY DIRECTIVE

A. Introduction

POPD II has replaced the Listing Particulars Directive of 1980 and the Public Offer Prospectus Directive of 1989; both codified by the Securities Consolidation Directive of 2001. It provides a harmonized regime for drawing up and scrutinizing the disclosure documents used for the public offer of equity and non-equity securities, or the admission of such securities to trading on regulated markets in the EU. The Directive provides a definition of what constitutes an “offer of securities to the public,” which it extends to the placement of securities though financial intermediaries. It grants the issuer of the securities a “single passport,” which, on the basis of the country of origin principle, enables the

164. Id. rec. 10. The Commission has recently consulted on possible new legislation governing the operation of credit rating agencies and the production of their ratings. See EC COMMISSION, CALL TO CESR FOR TECHNICAL ADVICE ON POSSIBLE MEASURES CONCERNING CREDIT RATING AGENCIES (July 27, 2004), available at http://www.europa.eu.int/comm/internal_market/securities/docs/agencies/2004-07-27-advice_en.pdf. The core issues that the Commission thinks that should be tackled by EC regulation are: “(i) potential conflicts of interests within rating agencies; (ii) transparency of rating agencies’ methodologies; (iii) legal treatment of rating agencies’ access to inside information; and (iv) concerns about possible lack of competition in the market for provision of credit ratings.” Supra note 102, at 2.

165. Id. art. 2(4).

166. Id. rec. 11.

167. Id.

168. POPD II, supra note 5.
issuer or offeror to offer the securities in any EU Member State, or have them
admitted to trading on any regulated market located within the EU without
having to comply with any regulatory requirements, other than those imposed by
the country, where the offer was first made or the securities were first admitted to
trading.

One of the main concerns of the legislature was to avoid creating a rigid, one-
size-fits-all disclosure regime that would place overly burdensome compliance
costs on SME’s, prejudice the development of the London Eurobonds market,
and/or stifle market innovation. The draft directive became the subject of fierce
debate and disagreement during the consultation process, and this led to a
hesitant political compromise. As a result, it is doubtful whether the multi-
document format of the passported prospectus, one of the most important
innovations in this context, will ever be utilized by the critical mass of EU or
third country issuers. Furthermore, POPD II has not been successful at creating a
“lighter touch regime” for SME’s. It is also puzzling why EU policymakers
have not addressed, with the degree of seriousness required, the necessity and
desirability of such an extensive, detailed and inflexible regime for mandatory
disclosure and its costs. Nor has there been any debate (with the exception of a
limited number of academic voices) about the possible interplay between
mandatory regulation and self-regulation in the area of issuer disclosure rules.

B. The Main Features of POPD II

1. The POPD II Prospectus

A prospectus drawn under the Directive must contain all the information
which, according to the particular nature of the issuer and of the securities
offered to the public or admitted to trading, is necessary to enable investors to
make an informed assessment of the assets and liabilities, financial position,
profit and losses, and prospects of the issuer and any guarantor of the rights
attaching to such securities. This information must be presented in an easily
analyzable and comprehensible form. The Directive’s disclosure requirements, as

169. See FERRAN, supra note 22, at 179-180. For a perceptive critical assessment of POPD II, see
FERRAN, at 201-205.

170. See, e.g., Eddy Wymeersch, Regulating European Markets: The Harmonisation of Securities
Regulation in Europe in the New Trading Environment, in REGULATING FINANCIAL SERVICES IN THE TWENTY
FIRST CENTURY 189, 196-200, 204-206 (Ellis Ferran & Charles Goodhart eds., 2001).

171. See Paul G. Mahoney, The Exchange as Regulator, 83 VA L. REV. 1453 (1997); Merritt B. Fox,
Holland, Economic incentives for the Self-Regulation of the Release of Price-Sensitive Information, 221 EUR. J.
L.& ECON. 221 (1996); Daniel R. Fischel, Organised Exchanges and the Regulation of Dual Class Common
Stock, 54 CH. L. REV. 119 (1987); Emilios Avgouleas, Financial Market Regulation and the New Market
Landscape: In Search of a New Regulatory Framework for Market Abuse, 2 INT’L COMP. CORP. L. J. 89, 116-
117 (2000).

172. POPD II, supra note 5, art. 5.
specified by a Level 2 Regulation, reflect to a significant extent the standards for cross-border offerings of the International Organisation of Securities Commissions.

A prospectus drawn in accordance with the provisions of the Directive should include a "summary," which is a brief statement, no more than 2,500 words, drafted in non-technical language in order to convey to investors the essential characteristics and risks associated with the issuer, any guarantor and the securities. The prospectus, subject to the updates dictated by Article 16 (filing of supplements) remains valid for twelve months.

The Directive grants the issuer of securities, once the prospectus has been approved by the competent authority, the right (via a "single passport") to offer its securities anywhere in the EU or have them admitted to trading on a regulated market located in any EU Member State.

One of the biggest innovations of the Directive is that it allows issuers to divide the prospectus into a number of documents. Thus, issuers and offerors, at their discretion, may either draw a prospectus as single document or divide the information to be disclosed into the following documents:

(a) "Registration document:" containing the information relating to the issuer;

(b) "Securities note:" containing the information concerning the securities to be offered to the public or be admitted to trading on a regulated market; and

(c) "Summary note."

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173. Commission Regulation (CE) 809/2004 of 29 April 2004 implementing Directive 2003/71/EC of the European Parliament and of the Council with regard to information contained in prospectuses as well as the format, incorporation by reference and publication of such prospectuses and dissemination of advertisements, [2004] OJ L149/1. The Regulation lays down: (1) the format of the prospectus referred to in Article 5 of the Directive; (2) the minimum information requirements to be included in a prospectus provided for in Article 7 of the Directive; (3) the method of publication referred to in Article 10 of the Directive; (4) the modalities according to which information can be incorporated by reference in a prospectus provided for in Article 11 of the Directive; (5) the publication methods of a prospectus in order to ensure that a prospectus is publicly available according to Article 14 of the Directive; and (6) the methods of dissemination of advertisements referred to in Article 15 of Directive.


175. POPD II, supra note 5, art. 5(2), rec. 21.

176. Id. art. 9(1).

177. "A prospectus composed of separate documents shall divide the required information into a registration document, a securities note and a summary note. The registration document shall contain the information relating to the issuer. The securities note shall contain the information concerning the securities offered to the public or to be admitted to trading on a regulated market." Id. art. 5(3).

178. "A prospectus composed of separate documents shall divide the required information into a registration document, a securities note and a summary note. The registration document shall contain the
Another innovation of the Directive is the introduction of a "base prospectus." A base prospectus may be drawn in the case of programs for non-equity securities such as notes and warrants of any form, and for continuous and repeated issues of non-equity securities by credit institutions. The base prospectus remains valid for twelve months.

A number of other innovations introduced by POPD II aim also at fostering market integration by facilitating cross-border offers of financial instruments and multiple admissions to trading (e.g., cross-listings). Accordingly, the Directive:

(a) Allows for the incorporation of documents containing information required to be disclosed in the prospectus by reference to one or more previously or simultaneously published documents that have been approved by the competent authority of the home Member State;

(b) Harmonizes the law on the publication of prospectuses and advertisement of public offers;

(c) Introduces a new concept of "language that is customary in the sphere of international finance" that may be used in prospectuses drawn in relation to cross-border offers or multiple admissions to trading. Thus, issuers' obligation to translate the full prospectus in case of multi-jurisdictional offers is abolished—the home and host state regulators may only require the translation of the summary prospectus into their official language; and

(d) Requires, in the same mode with the Market Abuse Directive, the establishment of a single competent authority for the scrutiny and approval of the public offer and admissions prospectus, which should be an administrative authority "completely independent from all market participants." This provision excludes privatized securities exchanges from discharging the role of the competent authority, unless Member States allow the central competent authority to

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179. Id. art. 5(4).
180. Id. art. 9(2).
181. Id. art. 11.
182. Id. art. 14.
183. Id. art. 15.
184. Id. art. 19.
185. Id.
186. Id. art. 21(1).
delegate to them specified powers with respect to scrutiny and approval of public offers and admissions prospectus. Any such delegation of tasks under the Directive is to be reviewed by 2008 and end in 2011.

Finally, the Directive requests Member States ensure that their laws, regulations, and administrative provisions on civil liability apply to those responsible for the information given in a prospectus. Arguably, issuers or even the offerors do not have much involvement with the drafting of an offer or admission prospectus, as this is a job usually entrusted to professionals such as investment bankers, corporate lawyers, tax specialists, and translators. As a result, the Directive defines “persons responsible for drawing up the prospectus” and for auditing the financial statements as directors, senior management, advisers, and auditors. A possible “safe harbour” is created for the professional advisers who have drafted the summary under Article 5(2)(d) of the Directive, which provides that such persons—frequent litigation targets because of their “deep pockets”—are liable only if the “summary” is misleading, inaccurate or inconsistent when read together with the other parts of the prospectus.

2. Exemptions

The lack of a comprehensive definition of the institutional and professional investors exemption under the previous regime created conditions of market fragmentation and insurmountable problems in the conduct of private placements on a Pan-European basis. For this reason, the Directive introduces a formal private placement and professional investors’ exemption. As a result, there is no obligation to draw a prospectus where the offer of securities is addressed solely to qualified investors and/or where the number of offerees is up to 100 natural or legal persons per Member State, other than qualified investors (private placement). Subsequent resale of the securities by qualified investors or private placees shall be regarded as a separate offer and may be caught by the public offer regime. Under the Directive, the term “qualified investor” means:

(a) “Legal entities which are authorised or regulated to operate in the financial markets, including: credit institutions, investment firms, other authorised or regulated financial institutions, insurance companies, collective investment schemes and their management companies, pension funds and their management companies,

187. Id. art. 21(2).
188. Id.
189. Id. art. 6(2).
190. Id. Annex I & Annex III.
191. Id. art. 3(2).
commodity dealers, as well as entities not so authorised or regulated whose corporate purpose is solely to invest in securities;”

(b) “national and regional governments, central banks, international and supranational institutions such as the International Monetary Fund, the European Central Bank, the European Investment Bank and other similar international organizations;”

(c) other legal entities which are not small or medium-sized enterprises;

(d) natural persons, subject to mutual recognition, if they expressly ask to be considered as qualified investors and meet at least two of the following criteria:

(i) “the investor has carried out transactions of a significant size on securities markets, at an average frequency of, at least, 10 per quarter over the previous four quarters;”

(ii) “the size of the investor’s securities portfolio exceeds 0.5 million euros;”

(iii) “the investor works or has worked for at least one year in the financial sector in a professional position which requires knowledge of securities investment.”

(e) SMEs which have expressly asked to be considered as “qualified investors.” In accordance with Article 2(1)(f) of the Directive, SMEs are companies which, in light of their last annual or consolidated accounts, meet at least two of the following three criteria: the average number of employees during the financial year is less than 250, their balance sheet does not exceed 43,000,000 euros, and their annual turnover does not exceed 50,000,000 euros.

Public offers or admissions to trading of units of collective investment vehicles, government securities, and securities issued or guaranteed by central banks or other defined public bodies are not subjected to the obligation to issue a prospectus, because these instruments fall outside of the scope of the Directive. Securities issued under debt programs established by credit institutions are also exempt, when
the total consideration of the offer is less than 50,000,000 euros, provided that the relevant securities are not exchangeable or convertible, the issued debt is not subordinated, and the securities do not serve as rights warrants nor are linked to derivative instruments.202 Furthermore, certificates of deposit and other money market instruments203 and securities included in an offer where the total consideration for the offer is under 2,500,000 euros also fall outside of the scope of the Directive.204

Finally, POPD II provides exemptions based on numerical thresholds, which are quite similar to those provided by its predecessor, Prospectus Directive 1989. These exemptions may be utilized cumulatively with the “qualified investors” exemption and the “private placement” exemption for offers to fewer than 100 natural or legal persons. Thus, there is no obligation to draw a prospectus where:

(a) the total consideration is at least 50,000 euros per investor for each separate offer;

(b) the denomination of the offered securities is at least 50,000 euros; or

(c) the consideration for the entirety of the offered securities does not exceed 100,000 euros over a period of 12 months.205

C. The Transparency Directive: Objectives and Main Features

The Directive on Transparency Obligations of Traded Companies was adopted by the Council of Ministers, which agreed with Parliament’s amendments effected in the first reading of the Directive on May 11, 2004, yet the formal adoption of the Directive was secured several months later.206 This Directive complements the Market Abuse Directive, the EC Regulation on International Accounting Standards, or Regulation IAS,207 and the POPD II in constructing an all encompassing EU market integrity regime. It introduces new disclosure (transparency) requirements with regard to information on issuers whose securities are admitted to trading on a regulated market in the EU. The main objectives of the Directive are summarized below.

The Directive aims at improving the EU regulatory framework governing the reports that issuers of securities admitted to trading on a regulated market produce on a regular basis. It mandates publishing an annual financial report within four months from the end of the financial year.208 In the case of depositary receipts representing securities, an issuer is regarded as the issuer of the underlying securities.

202. Id. art. 1(2)(j).
203. Id. art. 1(2) (f).
204. Id. art. 1(2) (h).
205. Id. art. 3(2).
208. Transparency Directive, supra note 8, art. 4.
Another improvement the Directive brings about is in the area of issuer periodic disclosure obligations, through the introduction of mandatory periodic disclosure obligations for issuers of debt securities. These must be made public as soon as possible after the end of the relevant six-month period, and at the latest two months thereafter. Exemptions to the above obligations are provided for credit institutions whose shares are not admitted to trading on a regulated market and who have only issued debt securities in the context of a “program,” provided that the total nominal amount of all such debt securities remains below 100 million and that they have not published a POPD II prospectus. An exemption is also granted to issuers of debt securities, who have not issued shares, on the basis of an individual denomination per unit starting at 50,000 euros.

Issuers of shares admitted to trading on a regulated market, who do not publish quarterly reports acting under a national law obligation or on their own initiative, acquire an obligation to publish half-yearly statements by its management, which shall contain information covering the period from the beginning of the relevant six-month period to the date of publication of the statement. The management statement should include at least indication of important events that occurred during the first six months of the financial year and their impact on the condensed set of financial statements, together with a description of the principal risks and uncertainties for the remaining six months of the financial year.

In addition, the Directive acts in a complementary way with Article 6(1) of the Market Abuse Directive on the issuer’s obligation to publish price-sensitive information on a continuous basis. Moreover, the Directive lowers the threshold for the reporting of changes to important shareholdings (5%) and provides procedures for the notification and disclosure of major shareholdings and their acquisition or disposal where the proportion of voting rights of the issuer held by the shareholder as a result of the acquisition or disposal reaches, exceeds, or falls below the thresholds of 5%, 10%, 15%, 20%, 25%, 30%, 50% and 75%. The notification obligation extends to the rights of a natural person or legal entity to acquire, to dispose of, or to exercise voting rights attached to shares held by a third party in various ways, including shares held as collateral or placed in the hands of depositary for safe custody.

209. Id. art. 5(1).
210. Id. art. 8(2).
211. Id. art. 8(1)(b).
212. Id. art. 6.
213. Id. art. 6(1).
214. Id. arts. 16(1), 21(6).
215. Id. arts. 9 and 12.
216. Id. art. 10.
Article 20 of the Directive introduces into annual and periodic reports the concept of language customary in the international sphere of finance. This may be used for ongoing disclosure by issuers of securities with cross-border listings, and also may be chosen by issuers who offer their securities to the wholesale market (e.g., issuers of Eurobonds). 217

Furthermore, the Directive harmonizes EU issuers' reporting obligations with certain provisions of the Sarbanes-Oxley Act 218 on issuer reporting. The most prominent example is the inclusion in the yearly and half-yearly reports of statements made by persons responsible within the issuer to the effect that financial statements and the condensed financial statements have, to the best of their knowledge, been prepared in accordance with the applicable set of accounting standards and give a true and fair view of the assets, liabilities, financial position, and profit or loss of the issuer. 219

Finally, liability, including civil liability, for the accuracy of the aforementioned reports is attached to the issuer or its administrative, management, or supervisory bodies and persons responsible within the issuer for drawing up and making public relevant information. 220

A number of other important features of the Transparency Directive are summarized below.

First, the Directive delegates the supervision of issuer compliance with ongoing and period disclosure obligations to the same competent authority that scrutinizes the POPD II prospectus. Therefore, this power is also removed from securities exchanges and other regulated markets and transferred to the relevant capital market commission. 221

Second, the concept of the home Member State used in the Directive refers to the issuer and not to the issued securities. 222 The "annual financial report" constitutes a complete source of financial information and consists of the audited financial statements, the management report and statements made by persons responsible within the issuer. 223

Third, the half-yearly report comprises a condensed set of financial statements and a management report on company activities. 224 In the case of an issuer required to prepare consolidated accounts, the condensed set of financial statements must be prepared in accordance with IAS 34, applicable to the interim financial reporting adopted pursuant to the procedure provided for under Article 6 of Regulation (EC) 1606/2002. Where the issuer is not required to prepare

217. Id. art. 20.
220. Id. art. 7.
221. Id. art. 24(1).
222. Id. art. 2(1)(i).
223. Id. art. 4(2).
224. Id. art. 5(2).
consolidated accounts, the condensed set of financial statements shall at least contain a condensed balance sheet, a condensed profit and loss account, and explanatory notes on these accounts.

Finally, when the registered office of the issuer is in a third country, the competent authority of the home Member State may exempt that issuer from the periodic and continuous disclosure requirements of the Directive, provided that the law of the third country concerned provides equivalent requirements or the issuer in question complies with requirements of the law of a third country that the competent authority of the home Member State considers as equivalent.\footnote{Id. art. 23(1).}

In addition, an issuer whose registered office is in a third country may be exempted from preparing its financial statements (for its annual and half-yearly reports) in accordance with Article 4 or Article 5 prior to the financial year starting on or after January 1, 2007, provided that such issuer prepares its financial statements in accordance with internationally accepted standards referred to in Article 9 of Regulation (EC) 1606/2002.

The Commission shall, inter alia, through the issue of Level 2 implementing measures: (a) determine the technical conditions under which a published half-yearly financial report is to remain available to the public; (b) clarify the nature of the auditors’ review; and (c) specify the minimum content of the condensed balance sheet, profit and loss accounts, and explanatory notes on these accounts where they are not prepared in accordance with the International Accounting Standards, pursuant to the procedure provided for under Article 6 of Regulation (EC) 1606/2002.

The usefulness of the Transparency Obligations Directive has been questioned in many quarters of the European financial services industry. Since most Member States have already enacted legislation that mandates the filing of quarterly reports by listed companies and have set very low thresholds for the reporting of changes in important shareholdings, the Directive does not seem to present any major breakthrough in the reporting regime of EU and third country issuers whose securities are admitted to trading in European markets.

VI. A CRITICAL EVALUATION OF THE NEW EC FINANCIAL MARKETS LEGISLATION

A. General Observations

The new EC financial market legislation comprises a mix of deregulatory and protective rules, which serve the dual purpose of liberalization in order to achieve market integration and investor protection in the integrated market. Thus, FSAP legislation preserves the “synthetic” approach regarding its objectives of liberalization and investor protection, regardless of whether the concurrent
pursuit of both is the most effective means for their achievement.\textsuperscript{226} The objective of liberalization is directly related to the pursuit of market efficiency, and the objective of investor protection is related to the achievement of fairness in the market. However, a number of arguments have been raised in recent years objecting to the concurrent pursuit by lawmakers of the economic efficiency and fairness objectives and pointing to the intrinsic tension, if not outright conflict, between the two.\textsuperscript{227} An example of such tension may prove to be the discussed trade transparency measures in MiFID, which have a distributional objective as they favor investors over investment intermediaries.\textsuperscript{228} However, they could prove detrimental to both market efficiency and investors if they adversely affect liquidity levels in EU capital markets.\textsuperscript{229}

The volume of legislation to be implemented and complied with, especially at Level 2, is phenomenal—placing an enormous strain on the resources of domestic lawmakers and regulators. In addition, Member State lawmakers and regulators might lack the "know how," experience, and sophistication required to properly implement and apply the new legislation. This will create lacunae in the application and enforcement of the new regime, contrary to the aspirations of the Lamfalussy process. Moreover, despite the efforts of the EC securities Directives to establish a comprehensive framework for cross-border regulatory supervision and enforcement, the new regime will again suffer from regulatory fragmentation (multiple regulators). Following FSAP implementation, EU financial markets will present a very paradoxical view. These markets will be governed by harmonized rules in the areas of prudential regulation, public offer, and admission of securities to trading, market integrity, disclosure of information to investors, and conduct of business. Yet relevant rules shall be enforced by at least twenty-five different national authorities, probably much more, due to overlap of regulatory responsibilities within national jurisdictions. As a result, supervisory and enforcement decisions in what is, essentially, a single regime, will be informed by the supervisory and enforcement cultures of at least twenty-five different national regulators and by the conflicting agendas these may pursue. From all of the FSAP implications discussed above, this is clearly the most


important, and possibly the most threatening, to the successful application and enforcement of the new legislation.

The reasonable and cost-effective solution to this problem can only be the establishment of a central regulatory body for the supervision of EU securities markets. This body, which cannot and should not be another Commission outpost or the ECB, should be granted not only lawmaking, but also enforcement powers which should be observed across the EU. Due to the restrictions posed by the current EU legal framework, the establishment of such a body is not yet possible.

**B. The Impact of New Legislation on the Structure of EU Financial Markets**

With the implementation of FSAP related legislation, the institutional aspect of the integration of EU financial markets is almost complete, notwithstanding the lack of a single EU securities regulator. Yet actual market integration has not been achieved. One of the factors inhibiting such integration is the unresolved issue of integration and connectivity of clearing and settlement systems in the EU.

Nonetheless, EC financial services legislation enacted under FSAP seems poised to have a profound impact on the structure of EU financial markets and the European financial services industry. The recent attempt by Deutsche Börse and Euronext to acquire Europe’s oldest and most liquid market, the London

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232. “On the side of market participants a fully fledged pan-European dimension of market activities remains to be achieved. On the side of public authorities the basic components of the institutional framework are already in place, but they need time before fully producing the desirable results.” Jean-Claude Trichet, President of the European Central Bank, The integration of the single market for financial services: The Eurosystem perspective, Address at the CESR Conference (Dec. 6, 2004), at http://www.cesr-eu.org/data/document/Trichet_speech_6_12_04.pdf; Himalaya Report, *supra* note 34, at 6-8 (giving a detailed review of the state of market integration in the fields of market infrastructure, investment firms, primary markets, and retail and wholesale markets for investment products).


234. Euronext constitutes itself an amalgamation of the former Paris, Amsterdam, Brussels, and Lisbon stock exchanges, as well as LIFFE. Euronext N.V., a holding company incorporated under Dutch law that operates through local subsidiaries, was formed on September 22, 2000 when the exchanges of Amsterdam, Brussels and Paris merged. The Euronext group expanded at the beginning of 2002 with the acquisition of LIFFE (London International Financial Futures and Options Exchange) and the merger with the Portuguese
Stock Exchange, is a testament to the competitive pressures faced by regulated markets in the EU and the increasing trends towards consolidation.  

The volume and detail of new legislation means that transaction costs in the form of costs of compliance in EU markets may increase concentration within the European investment services industry. The new regime is, on one hand, in some cases, flexible and disclosure based, but in many others is overly legalistic and bureaucratic. This is justified, to a certain extent, by the demands of an integrated market, which in certain areas such as the rules of conduct, require maximum harmonization. On the other hand, maximum harmonization means that lighter national regulatory regimes will have to raise their standards in order to converge with those of more developed and heavily regulated national ones, which inevitably, in order to consent to the enactment of new legislation, have imported in it the majority of their regulations. Higher regulatory standards translate into increased expenditure on the part of domestic financial services firms. Investment firms from European countries with less developed financial markets face significantly increased costs in order to comply with the new regulatory framework. Firms from countries with more developed financial markets will also face increased compliance costs, although to a lesser extent, as they are better prepared and more sophisticated in terms of regulatory compliance. MiFID’s demands on investment firm resources will be further exacerbated following the implementation of the revised Capital Adequacy Directive, which will introduce into the EU the new (and stricter) Basel capital adequacy standards.

In light of the above, it is arguable that the new regime will threaten the survival of all small and medium size investment firms in the EU; especially those based in smaller countries. It will also encourage bringing together large players through takeovers or mergers, in order to minimize compliance costs and achieve economies of scale in the integrated market. Therefore, the combined result of MiFID and of other FSAP related financial market legislation (such as the new CAD and the Market Abuse Directive) may be less and not more competition between providers of investment services in the EU, as the number of currently operating investment firms, “regulated markets,” and MTFs seems bound to decrease. Reduced competition in an already oligopolistic market exchange BVLP (Bolsa de Valores de Lisboa e Porto), at http://www.euronext.com/editorial/wide/0.5371, 1732_4427342.00.html.

235. Mike Verdin, Euronext Moves to Ease LSE Bid Fears, TIMES ONLINE, Feb. 9, 2005; Martin Waller, Börse’s Bid Plans Ignite LSE Battle, THE TIMES (LONDON), Jan. 28, 2005 at Business 55; Mike Verdin, LSE Rejects Deutsche Börse’s £1.3bn Bid, TIMES ONLINE, Jan. 27, 2005; all available at http://www.timesonline.co.uk.

restricts, instead of enhancing, consumer choice; an outcome that could hardly be found desirable by the architects of FSAP.

Furthermore, Article 40(5) of the FIMD could potentially prove to be a very important catalyst for market integration. It gives the right to “regulated markets” to admit to trading, without the consent of the issuer,\footnote{The issuer must, however, be informed by such regulated market of the fact that its securities are traded on that regulated market. \textit{MiFID}, supra note 4, art. 40(5).} of transferable securities issued in another jurisdiction, provided that it has already been admitted to trading in that jurisdiction. It facilitates, therefore, multiple admissions of securities, which is arguably a strong integrative mechanism. Concurrently, it creates the potential that large exchanges will use this facility to win business from regulated markets in countries on the periphery of the EU, by admitting to trading the most popular securities listed, and admitted to trading on those markets. This will, of course, offer to professional and institutional investors the possibility of “one-stop shop,” allowing them to concentrate on the same trading venue the entirety of their trading volume in the most popular (liquid) European securities, economizing in transaction costs. Thus, liquidity will be diverted from smaller markets to licensed exchanges, MTFs, and “systematic internalizers” that operate in the more developed EU markets. Such a result would diminish the role of smaller securities exchanges as price formation mechanisms for highly sought “blue chip” securities, which maintain a local listing. However, the price discovery function is the principal reason (and possibly the only reason) smaller markets are able to attract trading custom in their most popular securities. If this function is adversely affected to a considerable degree, because liquidity is concentrated on foreign (and more developed) regulated markets, the viability of the smaller EU securities exchanges will be seriously threatened. Today, smaller markets face serious liquidity threats as a result of trading opportunities engineered by, and based on, modern technology. Therefore, the reduction in their number through consolidation, whether the result of a conscious business decision or of the threat posed by Article 40(5), may prove to be a positive development. Yet, because of its seriousness, the pursuit of such a policy agenda should be an explicit and not an implicit objective of EC securities legislation.

VII. CONCLUSION

The implementation of FSAP has been the main driver of reform of EC financial market regulation since 1999. This article has provided a very analytical discussion of the most central parts of the new EU regime for capital markets. This legislation has been a very important step towards the integration of EU financial markets. Yet many obstacles remain. These include discrepancies in the EU tax regime for income from investments and private law rules (especially in the field of contracts) governing investors’ transactions on EU financial markets and
discrepancies in corporate governance standards.\textsuperscript{238} In addition, the implementation of FSAP has made apparent the existence of a deep hole at the heart of the EU regulatory edifice, due to lack of a single regulator of EU securities markets. Therefore, one of the most pressing issues that the implementation of FSAP presents to European lawmakers is the challenge of finding a way to make possible the establishment of such a functionary. It is also the most daunting one, due to the opposition any such move is bound to face from the majority of the Member States.

Furthermore, market integration is mostly a matter of market forces. Market participants will embrace this task only if they identify cost savings and market opportunities in adopting Pan-European business (trading) processes and structures. Until the difficulties mentioned above are overcome the European single securities market will remain “under construction.”\textsuperscript{239}

Finally, the extensive volume of regulation that investment firms will have to comply with, following the implementation of FSAP legislation into the legal orders of the Member States, will trigger a colossal wave of consolidation within the European financial services industry. The creation by FSAP legislation of self-standing Pan-European regimes for the admission and trading of securities on regulated markets and MTFs, frequently without a requirement to obtain the consent of the issuer of the securities concerned, is predicted to lead smaller European securities markets to loss of business and eventual merger with larger exchanges, or even to extinction.

\textsuperscript{238} Commission Communication, Modernising Company Law and Enhancing Corporate Governance in the European Union—A Plan to Move Forward, COM (03) 284 final at 10-22.

\textsuperscript{239} Trichet, \textit{supra} note 233 (using the phrase “under construction” while referring to the European single securities market).