

EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 22 November 2001

at the request of the Council of the European Union concerning a proposal for a Directive of the European Parliament and of the Council on insider dealing and market manipulation (market abuse)

(CON/2001/38)

(2002/C 24/09)

1. On 10 July 2001 the European Central Bank (ECB) received a request from the Council of the European Union for an opinion on a proposal for a directive of the European Parliament and of the Council on insider dealing and market manipulation (market abuse) (COM(2001) 281 final) (hereinafter referred to as the 'proposed directive')⁽¹⁾.
2. The ECB's competence to deliver an opinion is based on the first indent of Article 105(4) of the Treaty establishing the European Community (hereinafter referred to as the 'Treaty'), since the objective of the proposed directive is to ensure the integrity of Community financial markets and to enhance public confidence in securities and derivatives. In accordance with the first sentence of Article 17(5) of the Rules of Procedure of the European Central Bank, this opinion has been adopted by the Governing Council of the ECB.
3. The objective of the proposed directive is to ensure the integrity of European financial markets, enhance investor confidence in these markets and establish and implement common standards against market abuse throughout Europe. Currently, there are no common provisions against market manipulation at the level of the European Union and the Insider Dealing Directive⁽²⁾ is limited to the prevention of misuse of privileged information whereas, at the level of the Member States, there is a great deal of variation in the rules dealing with market abuse. The proposed directive intends to complete the existing Community legal framework in order to protect market integrity. It also provides that a single competent authority of an administrative nature should be designated in each Member State to deal with market abuse. Increasing cross-border activities require improved cooperation and a set of provisions for the exchange of information between competent national authorities. The proposed directive also provides that Member States shall ensure that the prohibition on engaging in market manipulation or taking advantage of inside information shall be applicable to any natural or legal person and that any infringement of the prohibitions or requirements laid down by the proposed directive should be promptly and effectively sanctioned. Finally, the comitology procedure is envisaged by the proposed directive, following the resolution of the Stockholm European Council of 23 March 2001 (which endorses the recommendations of the Committee of Wise Men).
4. The ECB considers that the proposed directive constitutes an important step towards the harmonisation of the currently divergent national rules addressing market manipulation and insider dealing. Consequently, the ECB welcomes this contribution to the establishment of sound and consistent standards, which should further promote the integrity of European financial markets, enhance investor confidence and ensure smooth functioning of the market. The ECB also welcomes the proposed directive as it implements the conclusions of the Lisbon European Council of March 2000, which stressed that steps should be taken to accelerate the completion of the internal market for financial services and those of the Stockholm European Council of March 2001, which stated that the creation of a dynamic and efficient European securities market is an essential element thereof. Furthermore, the proposed directive responds to one of the objectives of the financial services action plan, i.e. the setting of common rules to prevent market players from rigging the market. In the view of the ECB, the proposed directive would contribute positively to the achievement of these objectives.
5. In accordance with the recommendations of the Committee of Wise Men endorsed by the Stockholm European Council, the ECB welcomes the use of the comitology procedure as envisaged by the proposed directive, with the involvement of the Committee of European Securities Regulators and of the European Securities Committee. The ECB considers that the use of the comitology procedure provides the necessary flexibility, enabling the response in an adequate and timely manner to dynamic market developments. Generally, the ECB holds the view that the application of the comitology procedure to securities market regulation should take account of the advisory role that the Treaty confers upon the ECB, by allowing for the incorporation of the views of the ECB in the regulatory process. More specifically, and for the sake of the clarity and efficiency of this procedure, there may be a need for a clear identification of the implementing measures that should be adopted in accordance with the procedure referred to in Article 17(2) of the proposed directive (i.e. the comitology procedure). It may therefore be advisable either to expressly enumerate the articles which envisage the use of the comitology procedure in Article 17(2) or, as a minimum, to assemble all categories of implementing measures to be adopted according to the comitology procedure in one single article.

⁽¹⁾ OJ C 240 E, 28.8.2001, p. 265 (adopted by the European Commission on 30.5.2001).

⁽²⁾ Council Directive 89/592/EEC of 13 November 1989 coordinating regulations on insider dealing (OJ L 334, 18.11.1989, p. 30).

6. The ECB supports the wide scope of application of the proposed directive in terms of the financial instruments and markets covered (Article 9), as well as its wide geographical application (Article 10), which should contribute to creating a level playing field within the European financial markets.
7. The ECB notes the exemption from the scope of the proposed directive of 'transactions carried out in pursuit of monetary, exchange-rate or public debt-management policy by a Member State, by the European System of Central Banks, a national central bank or any other officially designated body, or by any person acting on their behalf, as stated in Article 7. According to Article 105(2) of the Treaty, the basic tasks to be carried out by the European System of Central Banks ('Eurosystem') shall be, *inter alia*, to define and implement the monetary policy of the Community, to conduct foreign exchange operations and to hold and manage the official foreign reserves of the Member States. In these areas, the Governing Council of the ECB has sole competence and as such always has inside information at its disposal that should not prevent it from carrying out the necessary transactions to implement its policies and this should be reflected in the provisions on this exemption. In addition, as long as there are Member States with a derogation, their NCBs retain competence in these areas pursuant to Article 122(3) of the Treaty. It should be noted, regarding Article 7 of the proposed directive, that a similar exemption is included in Article 2(4) of the Insider Dealing Directive.
8. The ECB understands that the proposed directive is intended to cover market abuse both in the form of insider dealing and in the form of market manipulation (recital 9 of the proposed directive). The ECB recommends in this respect that the core definitions related to the purpose of the protection of market integrity be clarified in the proposed directive itself, so as to avoid any discrepancy between the various national laws of Member States. As stated in the explanatory memorandum, the ECB shares the view that the updating of the list of financial instruments defined in Section A of the Annex to the proposed directive should take into account new developments in financial markets.
9. The ECB notes that the European Commission envisages, in its preliminary suggestions regarding the future review of the Investment Services Directive (ISD)⁽¹⁾, the possible incorporation in the revised ISD of some provisions which would supplement the obligations and prohibitions currently enshrined in the proposed directive. Such provisions might address, in particular, individual responsibilities attributed to competent authorities within the meaning of the proposed directive, to market operators and to investment firms. Without prejudging any future Commission proposal for a directive revising the ISD, it might be recommended at this stage that consistency be ensured between the proposed directive and the revised ISD, in particular in respect of the legal concepts used in these different legal texts and of the allocation of responsibilities between the different parties concerned with regard to the aim of safeguarding the integrity of the financial markets. In this respect, the ECB would like to submit the following comments. First, Article 6(5) of the proposed directive requires that 'a natural person, or an entity, professionally arranging transactions in financial instruments shall refrain from entering into transactions, and reject orders on behalf of its clients, if it reasonably suspects that a transaction would be based on inside information or would constitute market manipulation'. It may be helpful to clarify whether this provision also covers back office activities such as order matching. Furthermore, the desirability for market operators to have mechanisms in place which promptly detect abusive or anomalous activities may also be highlighted in the proposed directive. Secondly, it may be helpful to specify in the proposed directive whether and under which conditions competent authorities within the meaning of its Article 11 may have the possibility to delegate parts of their supervisory responsibilities to market operators in terms of monitoring and surveillance activities. Such clarification might be desirable as the current wording of the proposed directive only provides for collaboration of competent authorities with 'other authorities, including judicial authorities'. Thirdly, for the sake of consistency, it is recommended that the list of financial instruments included in the proposed directive be identical to the list annexed to the ISD, once formally upgraded, and that the latter be as exhaustive as possible.
10. The ECB also notes that the proposed directive provides for specific cooperation (such as mutual assistance and sharing of information) between the competent 'single administrative authorit[ies]' in order to ensure the application of the provisions of the proposed directive (hereinafter referred to as the 'administrative authorities'). In the view of the ECB, this cross-border cooperation is certainly valuable and the ECB welcomes the relevant provisions in the proposed directive. In addition, the ECB suggests that broadening the scope of cooperation should be considered, by including a possibility, or even an obligation, of cooperation and sharing of information that goes beyond mere cooperation between administrative authorities. This is of particular relevance in the light of Articles 9 and 10 of the proposed directive which recall the increasing cross-border dimension of abusive practices in financial markets. The ECB sees potential benefits in a closer cooperation between the administrative authorities and the competent authorities in charge of supervising credit institutions, investment firms, insurance undertakings and, perhaps, collective investment undertakings (regulated entities), to the extent that they are distinct from the designated administrative authorities. These regulated entities participate actively in regulated markets and their staff often possess inside information. As part of the operational risk, these regulated entities are exposed to the risk that their staff or management may breach the provisions of the proposed directive. Such breaches may have a significant negative impact on investors and also mean significant reputational risk for the regulated entity involved. The ECB therefore believes that close cooperation between the administrative authorities and the 'competent

(¹) Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field (OJ L 141, 11.6.1993, p. 27).

authorities' will be beneficial to the pursuit of the respective objectives of these authorities. In fact, national legislation in this field already provides, in certain instances, for such cooperation. Consequently, it may be worthwhile to introduce such a framework of mutual cooperation for the entire single market. However, in order to achieve this result, a re-examination not only of the provisions of the proposed directive (in particular Articles 12 and 16) but also of the relevant provisions of the sectoral directives on professional secrecy and supervisory cooperation (see Article 30 of the Consolidated Banking Directive ⁽¹⁾ and the corresponding provisions in the other sectoral Directives) is warranted. Such a re-examination would have to investigate, in accordance with the abovementioned comitology procedure, whether the respective provisions of these directives allow such cooperation ⁽²⁾. For the sake of clarity, the ECB also recommends that the single administrative authorities designated by Member States in accordance with Article 11 of the proposed directive (i.e. the 'coordinating authorities') be notified to the European Commission and their names published in the *Official Journal of the European Communities*.

11. As stated in the explanatory memorandum (see section 1(d)), the 'new disciplinary framework set out by this Directive is not intended to replace the national provisions by directly applicable Community provisions, but contribute towards helping some convergence among the different national regimes through compliance with the requirements of the Directive'. In this respect, the ECB suggests that it should be further considered how the

pursuit of the desirable convergence of supervisory practices could be best fostered to ensure a level playing field. In the view of the ECB, a committee of representatives of the administrative authorities in charge of promoting the convergence of supervisory practices might be valuable in this respect. Moreover, a provision calling for a report by the Commission on the progress regarding harmonisation and Member States' experience with the application of the proposed directive might be considered.

12. The ECB notes the priority given by the Council to the proposed directive and its firm objective of ensuring that the fight against financial crime linked to terrorist activities will be covered by the Community's proposed legal framework on market abuse. In line with its public statement of 1 October 2001 on its support for measures to prevent the use of the financial system in the funding of terrorist activities, the ECB wishes to reiterate the commitment of the Eurosystem, within its field of competence, to contribute to the adoption, implementation and execution of measures against the use of the financial system for terrorist activities.
13. This opinion shall be published in the *Official Journal of the European Communities*.

Done at Frankfurt am Main on 22 November 2001.

The President of the ECB

Willem F. DUISENBERG

⁽¹⁾ Directive 2000/12/EC of the European Parliament and of the Council of 20 March 2000 relating to the taking up and pursuit of business of credit institutions (OJ L 126, 26.5.2000, p. 1).

⁽²⁾ For the banking sector, the question at issue would be, for instance, whether 'authorities responsible for the supervision of financial markets' within the meaning of the first indent of Article 30(5) of the Consolidated Banking Directive, are identical with 'administrative authorities' within the meaning of the proposed directive. As regards the proposed directive, for instance, the question at issue would be whether for such cooperation to take place, the scope of powers laid down in Article 12 of the proposed directive should be amended in order to allow sharing of information with 'competent authorities'.