International
Capital
Market
Association Ltd

ICMA

European Commission
DG Internal Market Services

13th January 2006

Dear Sir/Madam

Working Document ESC/34/2005 Rev. 2

The International Capital Market Association (ICMA) is pleased to respond to DG Internal Market Services' Working Document on implementing measures for the Transparency Directive (2004/109/EC). ICMA is the self-regulatory organisation and trade association representing the investment banks and securities firms issuing and trading in the international capital market worldwide.

We attach our response as an Annex to this letter. DG Internal Market Services has drawn particular attention to a number of topics in its Introduction to the Working Document. We have focussed on certain areas of the Working Document in preparing our response. We respond in Part 1 of the Annex to the topics raised in the Introduction. Our specific comments on the text that relates to those areas on which we have concentrated appear in Part 2 of the Annex.

We apologise for submitting our response late, and hope that you will nevertheless be able to consider it. We would be pleased to discuss it with you at your convenience.

Yours faithfully

Mary Hustings

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PART 1

a) The use of recitals and recommendations for some issues

We agree with DG Internal Market Services that formal Commission implementing measures may not be necessary to address all issues, and that alternative approaches to the issue of harmonised implementation should be considered. We welcome the proposal that other ways of clarifying definitions and principles may be more appropriate for some issues. The implementing measures address many technical and administrative matters that by their nature are likely to be subject to change as market practices and regulatory priorities evolve and technological advances occur. Overly-detailed legislation that restricts unnecessarily the ability of regulators and markets to respond to such changes in a proportionate, timely and sensible way risks harming the capital markets and impeding their natural development. Appropriate flexibility to address necessary or desirable change is therefore essential. CESR and its work at Level 3 have a key role to play in achieving this.

When such flexibility is required, we agree that recommendations can be an effective way of achieving it. On the other hand, recitals are generally understood as interpretation tools. Usage of recitals not reflected in the actual text of the legislation may create legal uncertainty. Where the proposed recitals are intended to provide guidance while maintaining a degree of flexibility for the future, we recommend that they be replaced with corresponding recommendations. Conversely, where they are intended to provide for binding rules of conduct, they should form part of the text of the legislation.

We suggest that administrative requirements relevant to the cross-border activities of investors and financial intermediaries must be standardised as far as possible if the goal of achieving a single, efficient, cost-effective pan-European market is to be achieved. For this reason, we recommend strongly that there should be one standard form across the EEA for notifying the acquisition or disposal of major holdings of voting rights and financial instruments of EEA issuers, and that this should be binding (subject to our comments below on the content of the form). For holdings in non-EEA issuers, the standard form should not be mandatory. There should be an equivalence provision, with the expectation that the notification required in the issuer's home country will be acceptable, at a minimum if the notification requirements of the issuer's home country reflect at least the requirements of Article 12(1) of the Transparency Directive. If this were not the case, shareholders would have to supply two different forms of notification for the same holding. This would be inefficient, confuse shareholders and issuers and increase the chance of administrative errors. Shareholders and other market participants that invest globally would also incur significant costs changing their systems and procedures to deal with any duplicate reporting requirements.

For the avoidance of doubt, we do not support maximum harmonisation for other aspects of the Directive, as it is essential that flexibility in relation to issuers' reporting requirements is retained in order to reflect differences between markets.

b) Mandatory notification of major holdings electronically

We agree that notification of major holdings by electronic means is preferable. We suggest, however, that it should not be mandatory as it may not always be practical. Other methods should therefore remain open to investors, at least for the time being.

c) The relation between the proposed text in connection to half yearly financial reports and the current legislative framework on accounting rules (including the proposal for the modification of the 4th and 7th Company Law Directives), as well as Article 5(3) 2nd paragraph of the Transparency Directive

We suggest it is inconsistent to require companies that are not otherwise required under the Accounts Regulation EC/1606/2002 to adopt IAS, to re-organise their reporting systems and practices to comply with IAS principles for their half yearly accounts. We also note that the proposal is not consistent with Article 5(3) 2nd paragraph of the Transparency Directive which requires issuers preparing their half-yearly financial reports to follow 'the same principles for recognising and measuring as when preparing annual financial reports'.

d) The requirements for third country issuers for equivalence purposes as regards the contents of financial reports

Third country issuers play a significant part in the international market in Europe. It is important that the competitiveness and attractiveness of the EU's markets are not reduced through over-prescriptive requirements. We therefore strongly support the concepts in possible recital 16 that equivalence should be assessed on the general disclosure rules of third countries; and that equivalence does not mean 'identical'. We do not support any requirement for an item-by-item assessment. This is unnecessary if the sum of the relevant third country requirements provides investors with comprehensive and adequate disclosure of relevant information. An item-by-item assessment would also require costly and complex analysis, without proportionate benefit to issuers or investors. A declaration of equivalence should also be a permanent decision, except in very exceptional circumstances. It should also be a presumption that if a third country GAAP has been deemed equivalent, the contents of financial reports should also be considered equivalent. Third country issuers will require certainty about their continuing financial reporting obligations when they access the EU's capital markets.

Different timing between decisions on the parameters for equivalence of financial reporting at Level 2 (and any subsequent determinations by national competent authorities) and decisions about GAAP equivalence which are currently being considered by the Commission will cause uncertainty for issuers and confusion for market participants. We suggest that the Commission should clarify the timing and aim to co-ordinate the timing of both.

We give some more detailed comments on Article 14 below, and refer also to our comments below on Article 4. Article 4 should also be subject to an equivalence provision for third country issuers, but does not appear to be.

e) The use of the 'execution of the transaction' as the triggering event for the purposes of clarifying when the notifying person should have learned of the acquisition, disposal or of the possibility to exercise voting rights.

We suggest that 'execution of transaction' provides better transparency than 'settlement date', as settlement dates may occur some time after execution. In principle we do not see why an off-exchange transaction should be subject to a different requirement from an on-exchange transaction.

We suggest that the Transparency Directive should not regulate when transactions should be executed. The second sentence of possible recital 10 should therefore be deleted.

f) The notification to the Competent Authority of the issuer to be made by market makers, knowing that the Competent Authority of the market maker might be different. In particular whether an appropriate system of co-operation among Competent Authorities would allow for market makers to notify only their own Competent Authority.

We have seen the response of the London Investment Banking Association (LIBA) on Article 7. We support LIBA's response. As a general principle, market makers should be regulated as market makers by their competent authority under MiFID. If the Transparency Directive introduces a different approach, MiFID's aim to facilitate cross-border activity by regulating market makers through their home Member State is compromised. We therefore agree with the proposal that a market maker should notify its home competent authority, which would then notify the issuer's competent authority promptly in accordance with an appropriate system of co-operation among competent authorities.

PART 2

We have the following detailed comments on the proposed text, presented in chronological order.

Article 4 (Minimum content of half-yearly non-consolidated financial statements)

Article 5 of the Transparency Directive is subject to an equivalence provision for third country issuers. But Article 14 of the Working Document (Equivalence for third country issuers) does not contain an equivalence provision in respect of Article 4 of the Working Document. We suggest that it should. It is essential that the principle of equivalence for third country issuers is respected for all aspects of financial reporting.

We also note that the proposals are very detailed and may lead to unnecessary inflexibility. For example, any future changes in relevant accounting principles for the content of half yearly reports could not apply to Transparency Directive Level 2 reporting requirements without changes to the Level 2 Directive and Member States' implementing legislation.

Article 4.1 line 4: We suggest that this should refer to the 'condensed' balance sheet, profit and loss account etc to in accordance with Article 5 (3) 2nd paragraph of the Transparency Directive. This applies throughout Article 4.

Article 4.1 (c): Final indent: We suggest that this overlaps Transparency Directive Article 5(4) and should be deleted. We also suggest that the generality of the formulation and absence of definition of "materiality" might lead to a requirement to expand half yearly reports to the full scope of an annual report because, theoretically, only full scope disclosure ensures that "any events that are material to an understanding of the first six months of the financial year" are caught.

Article 4(2): If an issuer provides additional information in its annual report on a voluntary basis, we suggest it should not be mandatory for the issuer to continue to provide such disclosure in its half yearly statements (although it may decide to do so if the information is material). If retained, the requirement would be more onerous for voluntary information than for information mandatorily disclosed in the annual report, not all of which has to appear in the half yearly statement.

Article 5 (Major related parties' transactions)

Paragraph (e) appears to duplicate (d) and should therefore be deleted.

Article 7 (Control mechanisms by competent authorities as regards market makers)

As noted above, we agree with LIBA's comments about the requirements in Article 7 relating to market makers. We also support LIBA's response on Paragraph 3 (c). The CESR final advice (paragraph 103) requires firms to be able either to identify shares used for market making or for shares to be held in a separate account. It should be sufficient for firms to be able to identify holdings, without the need for a separate account. We suggest that the text should state that the proviso to paragraph 3 (c) is only one way to demonstrate that the shares can be identified.

Article 7 refers only to Article 9 of the Transparency Directive (Notification of the acquisition or disposal of major holdings). Transparency Directive Article 13 (dealing with 'financial instruments that result in entitlement to acquire voting rights') refers to Transparency Directive Article 9. The notification provisions of Article 7 of the Working Document apply only to shares. It would be helpful if the implementing measures clarify that the market maker exemption contained in Transparency Directive Article 9(5) applies also to market makers' activities in financial instruments, and therefore Article 7 applies also to financial instruments.

Article 12: (Types of financial instruments that result in an entitlement to acquire, on the holder's own initiative alone, shares to which voting rights are attached)

Paragraph 1(b) is a list of instruments that are clearly not "financial instruments within the meaning of Article 13(1) of the Transparency Directive", and we suggest it should be deleted. If it is retained, however, the list should be preceded with "in particular" or 'for the avoidance of doubt'. Currently, the list is formulated as it were exhaustive which would give rise to uncertainty as to the status of financial instruments not included in it. If retained, the list should also be further scrutinised for its consistency with the Directive. For example, the effect of the third indent of sub-section (b) is to suggest that derivative contracts on 'currencies, interest rates or yields' are subject to the Transparency Directive, which is clearly not the case.

We suggest that the reference to 'national law' in paragraph 3 should be deleted. Legally binding arrangements may be entered into under a variety of laws, whether of the issuer, the holder or another law.

We do not understand possible recital 13. It appears to mandate the content of the contractual arrangements between the parties. This is beyond the scope of the Directive, and possible recital 13 should be deleted.

Article 13: (Dissemination of regulated information)

Article 13 (1) states that the Transparency Directive requires issuers to ensure that the minimum standards set out in the draft implementing measures are met. This is not correct. Article 21 (1) of the Directive requires the Home Member State to ensure that 'the issuer discloses regulated information…. in a manner ensuring fast access…. on a non-discriminatory basis,…….. and to use such media as may reasonably be relied on for effective dissemination of the information throughout the Community.' Article 13 therefore goes much further than the Transparency Directive and imposes unmanageable and burdensome requirements on issuers to monitor the operations of third parties they appoint and to be legally liable for their actions.

It is common practice for issuers to appoint third parties to disseminate regulated information (for example, the Regulatory News Service in the UK). We agree that it is important that information is disseminated in an orderly manner. An issuer should be entitled, however, to rely on standard contractual arrangements with a third party supplier, and should not be responsible for the negligence or failures of the supplier. We note that Article 13(3) has an exclusion for errors and shortcomings of the media to which the information is sent. We suggest that, at a minimum, a general exclusion for the negligence, errors and shortcomings of the third party supplier should be added to paragraph 1. In any event, at a minimum, if a third party provider has been approved by a competent authority, an issuer should be entitled to rely on that approval without further liability or due diligence requirements under this Article.

Article 13(2) requires that the regulated information be communicated to "an appropriate number of media." We suggest that this sentence is not necessary in view of the requirements of the first sentence to disclose 'without delay….. to the general public' and suggest that it should be deleted. If retained, it should be made clear that this does not mean communication has to be made to a number of different kinds of media (e.g. electronically and in newspapers), and a number of individual media of the same kind could also meet the requirements.

Article 13 (5) does not sit well with the idea of third party appointment. For example, the issuer will not know the time/date on which the information was communicated to the media, or the name of the person who did it. We also suggest that any reporting requirements of the issuer should be to its home competent authority, and that this should be clarified.

We do not recognise the reference to 'security validation details' in Article 13(5) as a standard term, and suggest that the information required should be explained, or the reference deleted.

Article 21 of the Directive transfers the dissemination obligations from the issuer to someone who has applied for admission to trading without the issuer's consent. This transfer of responsibility is not reflected in Article 13.

Article 14: (Equivalence of Third Country issuers)

We note that the paragraphs of Article 14 state that a third country may be deemed to be meeting equivalent requirements provided that it satisfies the criteria set out in the relevant paragraph. Article 14 is very detailed and we suggest that the Commission should encourage greater flexibility in approach than Article 14 currently suggests. As the Directive is not maximum harmonisation, competent authorities should also be able to recognise other standards if they demonstrate equivalency in another manner. Equally, however, removing uncertainty of implementation when choosing their home Member State for those issuers that do meet these criteria is important. We therefore suggest the following drafting changes (in italics):

"*Without prejudice to the powers of the competent authority of the Member State pursuant to Article 23 of the Transparency Directive*…an issuer whose registered office is in a third country *shall* be deemed to be meeting equivalent requirements to those set out in Article [ ] of the Transparency Directive *in particular if*…"

Article 14(2): a 'review of period covered' is not required by Art. 5(4) of the Directive and we suggest this should be deleted.

Article 14(3): We suggest that at least this should refer to 'persons', rather than 'person', but more generally we note that in some jurisdictions it is likely to be the issuer that is responsible for accounts, rather than an individual.

Article 14(5)(b): The phrase "minimum capital and equity requirements and liquidity issues" is unclear and should either be clarified or deleted.

Article 15 (Equivalence in relation to the test of independence for parent undertakings of management companies and investment firms)

We share the concerns of the Investment Management Association and agree with their response to the consultation.

Article 16

Implementation of this Directive should not pre-date implementation of the Transparency Directive. For the sake of clarity, we suggest adding 'not before 20th January 2007' to this Article.

Draft Recommendation

Standard forms for notification: As noted above, we strongly support the use of standard forms for notification across the Community that relate to EEA issuers. Without maximum harmonisation, there will be multiple different forms in use, which will be a significant cost and administrative issue for all market participants for no benefit, and may also lead to unintended delays or mistakes in notifying. For non-EEA issuers, there should be an equivalence provision.

We support the comments of the Investment Management Association, on the standard forms, including the following:

Discretionary fund managers should not be required to identify the custodian. As they may hold notifiable interests in the same issuer through a number of custodians, to require them to identify the custodian would be complex and potentially require costly changes to their systems, and the benefit of such disclosure is not clear. We note also that custodians are exempted from the notification requirements of Article 9 of the Directive.

Notification requirements should not include details of the triggering transaction. Global firms that offer multiple services execute many transactions daily across many time zones. It would be administratively burdensome to identify one transaction. Level 1 requires only the date on which the threshold was crossed, and the outcome in terms of voting rights.

We also suggest that for the purposes of the form, clarification is required as to which holdings should be aggregated.