

European Financial Market Lawyers Group

EFMLG

FIRST DRAFT UPDATE REPORT

**THE MONEY MARKET:
LEGAL ASPECTS OF SHORT-TERM SECURITIES**

FIRST DRAFT 12 September 2003

EXECUTIVE SUMMARY

One year has past since the publication of the two consultative Reports of the Euribor ACI and of the EFMLG of 2 September 2002, on the short term paper market in Europe and on the legal aspects of short-term securities, respectively. The purpose of the present report is to follow up on the publication of these two Reports and to assess the extent to which the Recommendations contained in these Reports have been entirely or partially implemented or otherwise affected by developments over the last 12 months.

- The EU Financial Services Committee (FSC) was mandated in July 2003 by the ECOFIN to report on the areas where progress needs to be made as a matter of priority in order to create a truly integrated financial services market in the EU. The work undertaken in respect of the short term European paper (STEP) project is an example of a market initiative intended to promote the integration of European short-term securities markets. In this respect, it might be conveyed to the FSC that the avenues explored so far in the context of the STEP project would constitute a valuable contribution for any legislative action in the area of the short-term securities markets.
- Since last year, much additional work has been undertaken within the STEP project in order to prepare for the possible launch of STEP. The focus of this further work has been on issues related to:
 - the definition of minimum common features for the information memorandum for a short term European paper wholesale market;
 - the definition of requirements for the calculation and the release of the primary index, as well as for the publications of market statistics; and
 - the definition of user requirements with respect to settlement systems.
- As a result, a joint ACI and EFMLG working group, the ACI-EFMLG Working Group on STEP Information Memoranda, has prepared a Report on the Information Memorandum for STEP. This Report addresses not only the possibility to adopt a standardised Information Memorandum which would be submitted by issuers in order to obtain the STEP label, but also the adoption by market associations of a Market Convention which would deal with the conditions of eligibility of STEP and the procedural aspects related to the obtention of the STEP label and to which STEP issuers would adhere. The Report on the Information Memorandum for STEP is available on the EFMLG's website together with the 2002 Report on legal aspects and this Update.
- According to the EFMLG, the STEP project, including in particular the adoption of a standardised format for European Short Term Paper, will contribute to the increased harmonisation of the features of domestic papers. These short-term papers are mainly traded on OTC markets but can

be also dealt in on regulated markets within the meaning of the Investment Services Directive. It is the EFMLG's view that the still differing conditions for admission to trading and listing in the EU Member States should not give rise to regulatory arbitrage to the detriment of transparency for issuers and security for investors.

- The EU UCITS Contact Committee should ensure that Article 19 of the UCITS Directive (which concerns the possibility for UCITS to invest in money market instruments) is transposed in a consistent manner across Member States and in line with the purpose of the Directive which was initially to expand the categories of instruments in which UCITS may invest. The EFMLG is of the view that the parameters set up for the STEP label would constitute an adequate basis for a consistent implementation of Article 19 of the UCITS investments Directive.
- The "minimum common features" of STEP for the purpose of the UCITS Directive could be described as follows:
 - publication of a standard Information Memorandum comprising several mandatory elements of information, available in English, updated annually, the issuer being responsible for the accuracy of the information provided;
 - public availability of the Information Memorandum to all issuing and paying agents, market dealers, rating agencies, investors and any other market participants; this document should be made accessible in electronic form at a single entry point by an independent public authority;
 - production and publication by an independent public authority of statistics on prices and flows on the primary market and on outstanding amounts for every issuer and every category of issuer;
 - guarantees offered in terms of "domiciliation" and (same day) settlement functions¹.
- The EFLMG welcomes the clarification in the Prospectus Directive that money market instruments are excluded from its scope. The EFMLG believes that the STEP project will contribute to the harmonisation of the domestic legal requirements applicable to money market instruments -in particular in terms of information disclosure-. On the other hand, in the EFMLG's view, the exemption of the Prospectus Directive should not constitute an incentive for the adoption of diverging rules in terms of prospectus requirements from one Member State to another.
- As regards the surveillance of the markets for short-term securities in Europe, the EFMLG notes that, in order to achieve a level playing field in this respect, central banks are well placed to be the authority organising and monitoring the market for short-term paper. The EFMLG therefore

¹ It is noted that these parameters would need to be further refined on the basis of the outcome of the activities undertaken by the two ACI working groups which deal with statistics and settlement issues in the framework of the Euribor- ACI STEP project.

welcomes the proposal, in the context of the STEP project, to confer this role upon the ECB/ESCB. The EFMLG also welcomes the initiatives of the national authorities to clarify the allocation of responsibilities on the domestic markets for short-term securities.

- The adoption of a Market Convention for STEP, including a standardised Information Memorandum, will undoubtedly constitute an important progress in terms of harmonisation of market documentation. The market associations might consider to further study the feasibility of harmonisation and standardisation for other aspects which were not covered by the STEP project.
- There is no specific EU legislation regarding the withholding tax regimes for short-term money market paper. However, the EFMLG would recommend to examine with the relevant fiscal experts the implications of the provisions of the Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments relating to negotiable debt securities on the short-term paper market.

NOTICE

This Report is published by the European Financial Market Lawyers Group (EFMLG). The members of the EFMLG, whose names are set out in the Annex 3, are each expert in the field of financial markets law in the legal system of their Member State with a high degree of practical experience. The members of the EFMLG participate in its work on a strictly personal basis. The views expressed in this paper are those of the EFMLG members and do not necessarily reflect those of their institutions or of the European Central Bank (ECB).

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**THE MONEY MARKET:
LEGAL ASPECTS OF SHORT-TERM SECURITIES
UPDATE (SEPTEMBER 2003)**

INTRODUCTION/BACKGROUND

In its consultation report on the short term paper market in Europe of 2 September 2002, the Euribor-ACI Short Term European Paper Task Force (the ACI-STEP Task Force) has made several recommendations for the development of a pan-European market. They concern respectively:

- the establishment of a standard format for the Information Memorandum of Short Term European Paper (STEP) available in English for all domestic EU markets (recommendation 1);
- the availability of this Information Memorandum at the ECB (recommendation 2);
- the possible creation of a primary index; the collection and publication by the ECB of statistics on the STEP market (recommendation 3);
- the eligibility of STEP as Tier 1 collateral for the purpose of monetary policy operations (recommendation 4);
- the consistent implementation of the UCITS investments Directive as regards its Article 19 (recommendation 5);
- the exclusion of STEP from the scope of the new Prospectus Directive (recommendation 6),
- the same-day settlement as a medium-term objective for domestic and cross-border transactions (recommendation 7);
- a common format of domestic legislations in the Euro-zone (recommendation 8).

Since last year, much additional work has been undertaken within the STEP project in order to implement some of these recommendations and to prepare for the possible launch of STEP. The focus of this further work has been on issues related to:

- the definition of minimum common features for the information memorandum for a short term European paper wholesale market;
- the definition of requirements for the calculation and the release of the primary index, as well as for the publications of market statistics; and
- the definition of user requirements with respect to settlement systems.

As a result, a joint ACI and EFMLG working group, the ACI-EFMLG Working Group on STEP Information Memoranda, has prepared a Report on the Information Memorandum for STEP. This Report addresses not only the possibility to adopt a standardised Information Memorandum which would be submitted by issuers in order to obtain the STEP label, but also the adoption by market

associations of a Market Convention which would deal with the conditions of eligibility of STEP and the procedural aspects related to the obtention of the STEP label and to which STEP issuers would adhere².

In this context, it should be noted that some of the ACI Recommendations, and in particular the recommendations 1, 2, 3 and 7 are currently being considered in the context of the activities of the ACI-EFMLG working group on the Information Memorandum (see the ACI- EFMLG Report on the Information Memorandum for Short-Term Paper) and of the two ACI working groups on statistics and settlement. Some other ACI Recommendations have a different time horizon and would imply some different developments, for instance of a legislative nature (as an example, recommendation 8). Recommendations 5 and 6 mirror two corresponding EFMLG recommendations. As regards the ACI recommendation 4, the ACI-EFMLG Report on the Information Memorandum suggests that paper which meets the STEP criteria and obtains the STEP label should meet with favourable consideration by the European Central Bank in determining whether it is an eligible asset for Eurosystem credit operations, provided that the established eligibility criteria are met.

In its Report of September 2002 on the legal aspects of short-term securities, the EFMLG has also made several recommendations for an increased integration of the short-term securities markets in Europe. In view of the quick legislative developments during the last months, the purpose of the present exercise is to examine to what extent the recommendations of the EFMLG Report have already given rise to a partial or complete implementation since the time they have been made, i.e. in September 2002.

² The Report on the Information Memorandum for STEP is available on the EFMLG's website together with the 2002 Report on legal aspects and this Update.

IMPLEMENTATION OF THE EFMLG RECOMMENDATIONS: STATE OF PLAY

EFMLG Recommendation No. 1:

The EFMLG recommends that EU Member States adapt their legislation to the extent relevant in view of the common standards recommended by the Euribor ACI in its Preliminary Report. In addition, the EU Financial Services Policy Group [now entitled the Financial Services Committee] may consider the common regime suggested by the Euribor ACI Preliminary Report as a basis for a Community legal act in the context of [the possible new initiatives following the] Action Plan for Financial Services.

In its Report on Information Memoranda, the ACI-EFMLG Working Group made a distinction between different time horizons, considering that legislative reform would require a fair amount of time to be prepared, adopted and implemented. The ACI-EFMLG Working Group has focused on what the market can achieve in the short term without such legislative change, which means that the proposals made by the Working Group take account of the existing national legislation. On the other hand, the recommendation of the EFMLG to adapt national legislation and to consider a Community legal act as well as the last ACI Recommendation on a common format for Eurozone domestic legislations are still valid. The findings of the different Working Groups involved in the STEP project can hopefully promote a better understanding of the kind of legislation which may in the end be appropriate.

The original EU Financial Services Action Plan of 1999 did not contain any specific initiative in the field of the money market and of short-term securities in particular. On 15 July 2003, the ECOFIN Council has invited the Financial Services Committee (which is the successor of the Financial Services Policy Group) to examine overall progress on financial integration and its economic benefits, notably in the context of the FSAP and its follow up; to examine those key areas where further financial integration could deliver significant increased economic benefits to the EU, and to advise on those areas where progress needs to be made as a matter of priority in order to create a truly integrated financial services market in the EU.

The FSC will report back on its work in order to prepare a political debate in the Council during the spring of 2004 on priority areas for further action. The EFMLG considers that the work undertaken in respect of the STEP project promotes the integration of European short-term securities markets. It might be conveyed to the FSC that the avenues explored so far in the context of the STEP project would constitute a valuable contribution for any legislative action in the area of the short-term securities markets.

EFMLG Recommendation No. 2:

The EFMLG recommends that the legal qualification of the CP market(s) as either “regulated” or “non-regulated” markets should be clarified in legislation and be uniform across EU Member States.

The on-going discussion on the review of the ISD highlight the fact that a clear distinction should be made between the respective features of the assets and of the markets where these assets are traded (regulated markets; Multilateral Trading Facilities; OTC markets). It is of interest in this respect to note the suggestion currently discussed by the Council to convert the title of the revised ISD into Directive on financial instruments markets instead of "investment services and regulated markets".

None of the domestic CP markets in EU Member States, nor the ECP market, is today formally qualified as a “regulated market” within the meaning of the Investment Services Directive. This is mainly due to the OTC nature of these markets, in a context where a "regulated market" is currently defined as "*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 non-discretionary rules - in a way that results in a contract, in respect of the financial instruments³ admitted to trading under its rules and/or systems, and which is authorised and functions regularly and in accordance with the provisions of Title III ("regulated markets")*"⁴.

The legal regimes applicable to the domestic CP markets vary considerably from one country to another, and although they are all characterised by a certain degree of regulation, a case-by-case assessment of these markets is warranted in order to determine their respective features⁵.

Under EU law, in addition to the other features of money market instruments (liquidity, value which can be accurately determined at any time; low interest risk and low credit risk), one of the main characteristics of their instruments is that they are normally dealt in on the money market are normally not traded on regulated markets.

The expression "*normally not traded on regulated markets*" reflects also some different definitions in the domestic context. For instance, under French law, the TCN (French short-term instruments including French CP and CD) are defined as "*negotiable debt securities issued at the issuer's initiative*

³ The notion of financial instruments includes money market instruments.

⁴ See the Proposal for a Directive of the European Parliament and of the Council on financial instruments markets, Council working document, 28 August 2003

⁵ In the context of the Eurosystem's General Documentation on monetary policy instruments and procedures and of eligibility criteria for collateral purposes, some of these markets belong to the category of "non-regulated markets" within the meaning of the General Documentation, although the assets themselves might be traded on a regulated market.

and traded on a regulated market or over the counter". It should be noted however that one market development consists of the more frequent practice for credit institutions in particular to have their programmes listed on stock exchanges (for instance Euro-CP programmes listed at the Irish Stock Exchange). Money market instruments such as Euro-CP can be also traded on platforms like TradeWeb.⁶

According to the EFMLG, the STEP initiative will contribute, in particular with the adoption of a Market Convention and a standardised format for European Short Term Paper Information Memoranda, to an increased harmonisation of the features of domestic papers in Europe. As regards the markets where these short-term papers are traded, it is the EFMLG's view that the different conditions for admission to trading and listing and regulatory arbitrage should not be favoured to the detriment of transparency for issuers and security for investors.

EFMLG Recommendation No. 3:

The EFMLG recommends that the amended UCITS Directive is implemented by Member States in a uniform manner regarding money market instruments, with the aim of exempting such instruments from the 10 % ceiling established in Article 19(2)(a) of the UCITS Directive.

According to Directive 2001/108/EC of the European Parliament and of the Council of 21 January 2002 amending Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to UCITS, with regard to investments of UCITS (the UCITS Directive), Member States had to adopt the measures to comply with the Directive no later than 13 August 2003 for an application of these measures no later than 13 February 2004.

In its consultative Report of September 2002, the EFMLG reminded the importance to avoid any inconsistencies, in the context of the implementation of Article 19 of the amended UCITS Directive in Member States, in respect of the treatment among EU Member States of CP, ECP and other money market instruments, to the extent they are equivalent. Similarly, Recommendation 6 of the STEP Task Force calls for the implementation of the UCITS Directive in a harmonised manner so that "short term papers" can be purchased without restriction by UCITS in every Member State.

The Annex 1 contains a summary report of the current status of the transposition of the UCITS Directive, 2001/108/EC, into the national law of EU Member States on this specific topic

[To be completed by the EFMLG].

⁶ Other projects of platforms seem to be envisaged, for instance for the French negotiable debt securities: see Agefi, 28 August 2003

*The 10% rule and UCITS investments in money market instruments*⁷

The conditions under which UCITS may invest in money market instruments, including CP, are set out in Article 19 of the amended UCITS Directive. In particular, Article 19 (2) (a) contains the so-called 10% rule which limits the possibility for UCITS to invest in certain categories of money market instruments, including the criteria that need to be fulfilled for the 10% limitation not to apply.⁸

Article 1(5) amends Article 19(1) inter alia to add “*money market instruments other than those dealt in on a regulated market*” to the eligible investments. This means in practice that the 10% limitation does not apply to money market instruments admitted to or dealt in on a regulated market within the meaning of the ISD. Therefore and for instance, a French UCITS can invest 100% of its assets in Euro-CP listed on a regulated market within the meaning of the ISD (for instance, the Irish or Luxembourg Stock Exchanges).

The new Article 19 of the Directive goes on to provide that: “*if the issue or issuer of such instruments is itself regulated for the purpose of protecting investors and savings, and provided that they are:.....[one of four kinds of issuers]*”.

These requirements raise two problems of interpretation. First, the requirement for an **issue or an issuer** to be “*regulated for the purpose of protecting investors and savings*” is relatively obscure. Presumably an issuer is regulated for the purpose of protecting investors and savings if it is a credit institution or an insurance company, which are subject to prudential supervision and for which there are deposit guarantee/investor protection schemes.

This provision might be interpreted as referring to the conditions applicable to the issuance of money market instruments which ensure protection of investors and savings, and in particular the conditions of issuance and the obligations incumbent upon issuers. It must be therefore be examined whether these conditions sufficiently protect investors and savings.

Second, in addition to having to meet the foregoing requirement, the instruments must also be issued by one of four types of issuers. The issuers must therefore be either:

- credit institutions, insurance companies (i.e subject to prudential supervision);
- national or international public entities;
- corporates having securities dealt in on a regulated market; or

⁷ For more details, see the EFMLG Report of September 2002 on the legal aspects of short-term securities

- some specific entities belonging to categories approved by competent authorities in the field of UCITS.

In second reading, the European Parliament's Rapporteur addressed the problem of the interpretation of this first requirement (in connection with the application of second requirement). In particular, the Rapporteur was of the view that:

“(…) There is some uncertainty relating to the interpretation of certain provisions and it is to be hoped that these can be ironed out by the Contact Committee, if not before. An example of this unclear language is Article 19.1.h which contains the undefined concept “regulated for the purpose of protecting investors and savings”. Although some market actors tend to interpret this as meaning credit or deposit guarantees in the strictest sense (i.e. banks only), it is clear from the context and from the discussions in the other institutions that this is meant to have a wider meaning, that is that a given MMI [money market instrument] to the issuer thereof must be subject to either initial or ongoing supervision, e.g. by a stock market regulator. Additional, any other interpretation would render the following four indents completely superfluous.”

The STEP eligibility criteria as a standard for European money market instruments

In the above context, there is a debate on whether all types of money market instruments, especially those which benefit from a lesser degree of organisation would meet the requirements of Article 19 of the UCITS Directive, and in particular that *"the issue or issuer of such instruments is itself regulated for the purpose of protecting investors and savings"*.

The UCITS Contact Committee⁹ should ensure that this provision is transposed in a consistent manner across Member States and in line with the purpose of the UCITS Directive (which was initially to expand the categories of instruments in which UCITS may invest to include -inter alia- money market instruments).

The EFMLG is of the view that the parameters set up for the STEP label would constitute an adequate basis for a consistent implementation of Article 19 of the UCITS Directive. These "minimum common features" could be described as follows:

⁸ See Chapter 3.3.2.

⁹ The functions of the Contact Committee, as set up by the UCITS Directive alongside the Commission and composed of representatives of Member States and of the Commission are in particular to facilitate the harmonised implementation of the Directive through regular consultations on any practical problems arising from its application and to advise the Commission on additions or amendments to be made to the Directive

- publication of a standard Information Memorandum comprising several mandatory elements of information, available in English, updated annually, the issuer being responsible for the accuracy of the information provided;
- public availability of the Information Memorandum to all issuing and paying agents, market dealers, rating agencies, investors and any other market participants; this document should be made accessible in electronic form at a single entry point by an independent public authority;
- production and publication by an independent public authority of statistics on prices and flows on the primary market and on outstanding amounts for every issuer and every category of issuer
- guarantees offered in terms of "domiciliation" and (same day) settlement functions¹⁰.

EFMLG Recommendation No. 4:

The EFMLG recommends that the still draft Prospectus Directive and national legislation exempt the issuers of money market paper of less than one year maturity from the obligation to adopt, register and update a prospectus.

This EFLMG recommendation was taken on board in the context of the discussion on the new Prospectus Directive.

The purpose of the Prospectus Directive, as finally adopted on 15 July 2003 by the ECOFIN¹¹ is to harmonise requirements for the drawing up, approval and distribution of the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market situated or operating within a Member State¹². For the purposes of this Directive, ‘securities’ means transferable securities as defined by Article 1(4) of Directive 93/22/EEC (ISD) **with the exception of money market instruments as defined by Article 1(5) of Directive 93/22/EEC having a maturity of less than 12 months**. The Directive also provides that, for these instruments, national legislation may be applicable.

¹⁰ It is noted that these parameters would need to be further refined on the basis of the outcome of the activities undertaken by the two ACI working groups which deal with statistics and settlement issues in the framework of the Euribor- ACI STEP project.

¹¹ Directive 2003/ /EC of the Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC. Not yet published in the EC Official Journal

¹² The current "listing particulars" Directive (80/390/EC) and the current "prospectus" Directive (89/298/EC) are to be merged into a single text, i.e. the new Prospectus Directive (2003/.../EC). One of the main purposes of the new Prospectus Directive is to ensure full coverage of equity and non-equity securities offered to the public or admitted to trading on regulated markets as defined by the ISD and not only on securities which have been admitted to the official lists of stock exchanges.

The EFMLG welcomes this exemption of money market instruments from the scope of the Prospectus Directive and believes that the STEP project, and in particular the adoption of a Market Convention including a Standardised Information Memorandum, will contribute to the harmonisation of the domestic legal frameworks applicable to money market instruments in terms of disclosure requirements (see in this respect the Report on the ACI/EFMLG Working Group on the STEP Information Memorandum). The EFMLG also welcomes the efforts of the national authorities to clarify these requirements (for instance in France with the law on financial security or in the UK with the dematerialisation process of money market instruments). In the EFMLG's view, the exemption of the Prospectus Directive should not constitute an incentive for the adoption of diverging rules in terms of prospectus requirements from one Member State to another.

EFMLG Recommendation No. 5:

The EFMLG recommends national and Community authorities, and the ECB, to consider the establishment of a common overseer, or at least a similar kind of overseer, across EU Member States, taking account of the above considerations.

The EFMLG notes that some Member States assimilate short-term money market instruments with securities, and subject such paper to the supervision of the securities market supervisor and regulator. However, the EFMLG also notes that in some other countries such supervision or regulation, or other kind of monitoring, is entrusted to the central bank.¹³ In some other Member States, there is no such specific regulation and the market is instead monitored by authorities entrusted with general financial markets supervision or regulation.¹⁴ To achieve a level playing field in this respect, the EFMLG considers that central banks are well placed to be the authority organising and monitoring the market for short-term money market paper for a number of reasons detailed in the consultative Report of September 2002.

The EFMLG welcomes therefore the proposal, in the context of the STEP project, to confer a specific role upon the ECB/ESCB in terms of collection, processing and publication of statistics and of market surveillance (e.g. monitoring of market developments and assessment of the smooth functioning of market infrastructures). In the same vein, the EFMLG also welcomes the initiatives of the national authorities to clarify the allocation of responsibilities on the domestic markets for short-term securities.

In France, the law on financial security as published on 1st August 2003 clarifies, within the French Financial and Monetary Code, the respective roles and functions of the new market authority, i.e. the

¹³ The most important such CP market is located in France, regulated and supervised by the Banque de France; other cases are Italy, Portugal, Ireland. In Finland the central bank is closely associated to the supervisory authority in this particular market.

¹⁴ Germany, United Kingdom and Belgium.

AMF and of the Banque de France as regards the rules on the organisation and supervision of the negotiable debt securities (TCN) market. For instance, Article L.213-4 of the Code, as amended, provides that the financial documentation is to be submitted prior to the first issuance of negotiable debt securities to the Banque de France which is in charge of ensuring that issuers comply with the conditions of issuance provided for in Article L.213-3 of the Code.

Under the new provisions on negotiable debt securities, the AMF will only grant a visa for prospectus in the (limited) cases of "appel public à l'épargne" (public offerings) since the TCN market is essentially between professionals. Moreover, a protocol will be concluded between the AMF and the Banque de France regarding the respective powers of the two authorities in respect of the surveillance of the TCN market.

In the United Kingdom¹⁵, the Bank of England plays a decisive role in the formulation and implementation of the dematerialisation process of money market instruments and for the future organisation of the market (see for instance the pro forma deed published by the Bank of England, terms for EDSs corresponding to CD/CP and in the involvement of the Bank in the review of the BBA Guidelines on CP and CD).

EFMLG Recommendation No. 6:

The EFMLG considers appropriate that the possibility to standardise market documentation is pursued and that market associations may entrust a law firm covering the relevant financial markets with the task of further analysing market documentation and proposing such uniform market standards.

In its consultative Report of September 2002, the EFMLG considered, despite the different national legal regimes, the possibility to standardise the market documentation used for commercial paper. The ACI-EFMLG Working Group also discussed the possibility of achieving a harmonised form for the notes used under various STEP programmes, as proposed in the EFMLG Report. It was considered that such an exercise would, however, be time-consuming and should not be considered to be priority at this point in time. It was also suggested that a common standardised approach to the issue of selling restrictions for products, such as CP, could be pursued. The Working Group finds that, although not a necessary condition for the introduction of the STEP regime, such harmonisation and standardisation of market documentation could be beneficial and, therefore, the market associations should consider to further study the feasibility of such harmonisation and standardisation.

¹⁵ See the interim guide and compendium of documents prepared by the BBA, "*Preparing for the dematerialisation of money market instruments*", August 2003

EFMLG Recommendation No. 7:

The EFMLG recommends to the Ministers of Finance of the EU that they agree to a common withholding tax regime for short-term money market paper in order to contribute to the integration of the money markets following monetary unification.

The EFMLG notes that national legislation imposes different regimes of withholding tax for interest payment on short-term money market paper, in some cases exempting payments from such withholdings and that there is no common EU regime in this respect.

However, it should be noted that the Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments (the Savings Income Directive) (EC OJ L157/38 of 26 June 2003) might be of relevance in relation to negotiable debt securities. The purpose of this Directive is to enable savings income in the form of interest payments made in one Member State to beneficial owners who are individuals resident for tax purposes in another Member State to be made subject to effective taxation in accordance with the laws of the latter Member State. For the purpose of this Directive, "interest payment" means in particular *"interest paid or credited to an account, relating to debt claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and, in particular, income from Government securities and income from bonds or debentures, including premiums and prizes attached to such securities, bonds or debentures; penalty charges for late payments shall not be regarded as interest payments"*. This includes also negotiable debt securities which benefit from some transitional measures according to Article 15 of the Savings Income Directive (see the text of Article 15 in the box below).

Article 15 (Negotiable debt securities) of the taxation of savings income Directive

1. During the transitional period referred to in Article 10, but until 31 December 2010 at the latest, domestic and international bonds and other negotiable debt securities which have been first issued before 1 March 2001 or for which the original issuing prospectuses have been approved before that date by the competent authorities within the meaning of Council Directive 80/390/EEC or by the responsible authorities in third countries shall not be considered as debt claims within the meaning of Article 6(1)(a), provided that no further issues of such negotiable debt securities are made on or after 1 March 2002. However, should the transitional period referred to in Article 10 continue beyond 31 December 2010, the provisions of this Article shall only continue to apply in respect of such negotiable debt securities:
 - which contain gross-up and early redemption clauses and;
 - where the paying agent as defined in Article 4 is established in a Member State applying the withholding tax referred to in Article 11 and that paying agent pays interest to, or secures the payment of interest for the immediate benefit of, a beneficial owner resident in another Member State.

If a further issue is made on or after 1 March 2002 of an aforementioned negotiable debt security issued by a Government or a related entity acting as a public authority or whose role is recognised by an international treaty, as defined in the Annex, the entire issue of such security, consisting of the original issue and any further issue, shall be considered a debt claim within the meaning of Article 6(1)(a).

If a further issue is made on or after 1 March 2002 of an aforementioned negotiable debt security issued by any other issuer not covered by the second subparagraph, such further issue shall be considered a debt claim within the meaning of Article 6(1)(a).

2. Nothing in this Article shall prevent Member States from taxing the income from the negotiable debt securities referred to in paragraph 1 in accordance with their national laws.

The EFMLG is of the view that the potential implications of this Savings Income Directive on the short-term paper market should be further examined together with the relevant fiscal experts.

Annexes:

- Implementation of Article 19(2) of the UCITS Directive: State of play in the Member States
- Composition of the EFMLG Sub-Group on short term securities
- Composition of the EFMLG

Implementation of the UCITS Directive: Article 19¹⁶

[TO BE COMPLETED BY THE EFMLG¹⁷]

Austria

Belgium

Finland

France

The Law on Financial Security was adopted in July 2003. It provides for partial transposition of the UCITS Directives. A specific Decree should specify the conditions under which Article 19 of the UCITS (investments) Directive will be implemented.

Germany

The UCITS Directive will be transposed into German law by the Investment Act 2003 (Investmentgesetz 2003). No draft has been published or is available (as of June 2003).

The current Investment Companies Act (Kapitalanlagegesellschaftengesetz—KAGG) permits German based UCITS to invest in money market instruments even if they are not traded on a regulated market. Issuers must comply with certain criteria such as being a credit institution or an undertaking with equity capital of at least Euro 5 million.

Greece

Ireland

¹⁶ The information provided below does not prejudice the more detailed assessment which will be undertaken by the European Commission in its Report on the implementation of the UCITS Directive.

¹⁷ Accession countries might be considered at a later stage.

Ireland is adopting the approach of transposing the Directive by repeating the language of the Directive verbatim. Under the 1985 UCITS Directive, Ireland allowed Irish based UCITS to invest in ECP.

Italy

The Banca d'Italia and the Ministry of Finance are preparing draft transposition legislation. It will not be enacted by 17 August and no decision has been taken on the interpretation of Article 19(1)(h).

Luxembourg

Luxembourg adopted transposition legislation in December 2002 (Law of 20 December 2002; entry into force: 1st January 2003). It repeats verbatim the language of the Directive. However, under the 1985 UCITS Directive Luxembourg permitted Luxembourg based UCITS to invest in ECP.

The Netherlands

Portugal

Spain

Spain is in the process of adopting transposition legislation which omits the Directive's references to regulation of the issuer and the issue. The Government sent a draft Collective Investment Scheme Act (Proyecto de Ley de Instituciones de Inversion Colectiva) to the Cortes on 28 March 2003. In current Spanish law, "admitted to or dealt in on a regulated market or organized negotiation system as defined in art 17 RD 1393/1990" is not defined and in practice only listed commercial paper is eligible. Domestic pagarés de empresas are all listed and what little ECP is sold to Spanish money market funds is drawn down off of MTN programmes, which are set up to accommodate listing.

Sweden

United Kingdom

The Financial Services Authority has adopted a regulation, after consultation, which omits the requirement that the "issue is itself regulated for the purpose of protecting investors and savings" but also omitted the fourth indent, which covers asset backed issues.

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