

Must we wait for crises to enact regulatory change?

These last few years, it seems to have become a tradition to which we have become accustomed!

After Enron came *late trading* in the funds industry, the stock option *pricing* and usage, and today, the *sub prime*-prompted severe liquidity crisis.

It is time to place regulation in perspective with the very real economic, and therefore political, challenges that the finishing of the European construction and the development of the global financial markets represent.

Over and above the crises that underline the growing complexity of financial instruments regulation is seen more and more from a competitive angle.

More than ever before regulation is at the heart of national and regional “base camp” strategies to conquer “users” who are ready to go wherever service is best.

Globalization clearly pushes towards the reorganization of services offered. In finance, the situation used to be simple.

The U.S. dominated, and still dominates, international finance with its world liquidity pool. But London dominates Europe and starts to rival New York’s world standing after the successful change in the 1980s of the City’s Big Bang.

Globalization and the accelerated European integration have changed the deck of cards.

“Mechanically the roles should balance out and market shares reallocated in a more homogenous way. A recent analysis in *The Economist (1)* observes a proliferation of market places around the world indicative of local domestic markets reaching maturity and requiring domestic financing.

As far as Europe is concerned, it has a double challenge: to use regulation as best possible in order to accelerate the constitution of a financial market place, the world’s first if measured by GNP and by population; and to assure that this regulation is compatible with the rest of the world’s in order to accompany world financial innovations and needs.

These two challenges must be met in concertation and without confusion. Although the objective is clearly to serve European “domestic” users, Europe as a region must also attract more capital, talent and services than other competing regions of the world. How to advance regulatory change to meet these objectives? Two ways: accelerate the process of European integration on the basis of the principle of *better regulation*; and pilot the collective interest in global regulation.

### **The EU / US convergence Project**

On 1<sup>st</sup> June 2007, the European Parliament adopted two reports recommending the signature of a privileged partnership agreement between the EU and the USA as well as the creation of a “transatlantic market free of constraints” by 2015.

Is this a win/win negotiation for players on both sides of the Atlantic?

MiFID has only just become effective and we can already see emerging a still more ambitious initiative than those of MiFID and FSAP put together as it concerns nothing less than the creation of a huge European-American financial market.

In other words, the project involves creating completely new conditions for wholesale banking activities between Europe and the USA by relaxing strongly access to these markets.

### **Let's come back on origin of the project.**

In the very early days of this project, an initiative of the financial markets regulators who, faced with the technical difficulties linked to the different regulations applicable to the same actors, wished as early as 2002 to set up within the Informal Financial Markets Regulatory Dialogue a forum between the US and European regulators.

The ambition was then modest commensurate with the few resources: to facilitate a better mutual understanding of the regulations specific to each of these two economic areas and to identify possible conflicts stemming from regulations to try and devise practical solutions.

In no way a revolution, but rather the recognition of the need to work together to tackle common issues.

The participants to this workforce, on the American side, include the Treasury Department, the Federal Reserve, the SEC and CFT and, on the European side, the EC and the CESR which very quickly felt that they had to go beyond the simple European aspects and broaden the scope.<sup>1</sup>

These completely informal and non binding discussions already yielded concrete results such as a revision of the US rules permitting European companies to delist from US stock markets or progress in the areas of accounting standards and cooperation in the supervision of audits.

However such a technical exchange, however useful it can be, suffers from the lack of political impulse to move on to a much more radical phase, *i.e.* the creation of a large transatlantic financial market.

This ambition was rekindled a few months ago during the April 2007 EU-US Summit.

While indeed, for many years the dialogue between the EU and the US on economic issues has been increasing, it took a dramatic turn with the creation on 30<sup>th</sup> April 2007 of the Transatlantic Economic Council (TEC) which held its first meeting on 1<sup>st</sup> November 2007 in Washington which wishes to be a place of discussion and exchange so as to reduce obstacles and regulatory barriers in areas such as international trade, intellectual property, the security of exchange and the integration of financial markets.

It is in the perspective of these economies moving closer that the European Parliament after long and sometimes tumultuous discussions in the name of Europe's economic independence passed two reports on 1<sup>st</sup> June 2007 recommending the signature of a privileged partnership agreement between the European Union and the USA as well as the creation of a "transatlantic market free of constraints" by 2015.

The initiative of the politicians – supported by some central administrations such as the British Treasury Department<sup>2</sup> met with the enthusiasm of leading edge and high performance companies in the area of financial markets.

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<sup>1</sup> EUROPEAN COMMISSION « A STRONGER EU-US PARTNERSHIP AND A MORE OPEN MARKET FOR THE 21<sup>ST</sup> CENTURY » COM (2005) 196 P.9.

<sup>2</sup> HM TREASURY, FINANCIAL SERVICES AUTHORITY AND BANK OF ENGLAND. AFTER THE EU FINANCIAL SERVICES ACTION PLAN: A NEW STRATEGIC APPROACH" (2004) P.3.

Among the 17 priorities for convergence established by EU / US coalition on Financial Regulation, I propose to select 4 items to be the basis of the discussion for the next Quadrilateral Meeting in N.Y :

The rationale of my selection is based on 4 considerations:

- (i) the practicality to find in a short term basis common definitions,
  - (ii) the absence of change laws or directives or at least possibility to adapt this laws or directives quickly, without waiting years;
  - (iii) the absence of conflicts of views or interests between twos sides of Atlantics,
  - (iv) last but not least, the absence of politician obstacles (reason why I don't put on this list the recommendation n° 1 concerning the exemptive relief principle).
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- N° 2 : Standardisation in the classification of counterparties : this is in practice one of the more complex issue to manage for all participant of the industry and I don't see any major obstacles to harmonize such definitions
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- N° 6 : Formulation and agreement on a common set of registration and examination requirements for those countries that operate licensing regimes or other forms of competence standards for individuals active in financial services : the flexibility of employment work and the possibility to work with the same licence in two side on Atlantic is one of the easiest and shortest goal;
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- N° 8 : Common understanding of stabilization practices : the new definition of stabilization in Europe from the Market Abuse directive is derived from the US approach. It should be not difficult to adapt the differences between the regulations.
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- N° 12 : Convergence towards global standards on conflicts of interest : I don't see any reason why the concept of conflict of interest and the implementation of such definition should be different from UE to US .

This selection doesn't mean that the rest of the list is not relevant but the role of the quadrilateral should be to propose practical proposals for a number of limited items which can be implemented quickly.

Of course, my suggestion reflects only my view and the purpose of the discussion is to add or cancel items. But I strongly recommend to keep a few number of items, no more than 4 and to keep in mind the criterion proposed of the selection.