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## Recent Developments in European Union Securities Law

### Keywords

Comparative Law, European Union, Securities Law

# RECENT DEVELOPMENTS IN EUROPEAN UNION SECURITIES LAW

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## I. OVERVIEW

The European Union (EU) is engaged in a major effort to develop the single financial market. The oddly named "Committee of Wise Men" ("Committee") published an influential report in February 2000 calling for reform of the law-making procedures in the EU.<sup>1</sup> One of the Committee's main objectives is to speed up legislative action needed to bring new life to the single financial market.<sup>2</sup> Despite the considerable and impressive work that the EU has already done in the area of listings and public offerings, true integration of European capital markets is not yet achieved, particularly in the area of corporate finance and capital formation.<sup>3</sup> In May 2001, the European Commission ("Commission") submitted a proposal to the European Parliament and the Council of Ministers for a new directive that would represent a combined version of the Prospectus<sup>4</sup> and Listing Particulars Directives,<sup>5</sup> which would later be repealed.<sup>6</sup> In March 2002, the European Parlia-

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1. See Initial Report of the Committee of Wise Men on the Regulation of European Securities Markets (Nov. 7, 2000), available at [http://www.europa.eu.int/comm/internal\\_market/en/finances/banks/report.pdf](http://www.europa.eu.int/comm/internal_market/en/finances/banks/report.pdf) (last visited Nov. 19, 2002). [hereinafter Nov. 7 Committee of Wise Men].

2. See *id.* at 7.

3. See *id.* at 9-19.

4. 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. (L124) [hereinafter Council Directive 89/298/EEC].

5. Council Directive 80/390/EEC of 17 March 1980 Coordinating the Requirements for the Drawing-Up, Scrutiny and Distribution of the Listing Particulars to be Published for the Admission of Securities to the Official Stock Exchange Listing, 1980 O.J. (L100) [hereinafter Council Directive 80/390/EEC]. In May 2001, the Listing Particulars Directive was consolidated with the Listing Conditions Directive (79/279/EEC), another Directive (82/121/EEC) on periodic reporting, and a fourth Directive (88/627/EEC) on disclosure of major shareholdings. The Consolidated Directive is hereinafter referred to as Council Directive 2001/34/EC, 2001 O.J. (L184/1) [hereinafter Council Directive 2001/34/EC]. References to the "Listing Particulars Directive" or "Listing Conditions Directive" have been retained for purposes of this article, but such directives are now technically components of Council Directive 2001/34/EC; accordingly, citations are to Council Directive 2001/34/EC unless otherwise indicated.

6. See Proposal for a Directive of the European Parliament and of the Council on the Prospectus to be Published When Securities are Offered to the Public or Admitted to Trading, COM(01)280 final at 16 [hereinafter Revised Prospectus Directive or RPD].

ment approved its own version of a new Prospectus Directive<sup>7</sup> and the measure was before the Council when the Commission, "to speed up the legislative process" published an amended proposal in August 2002.<sup>8</sup> Significantly, the new system would substantially rely upon the International Disclosure Standards promulgated by the International Organization of Securities Commissions ("IOSCO") in 1998.<sup>9</sup> The Commission also proposes to enact a registration system similar to shelf registration in the United States.<sup>10</sup> In addition, under the Prospectus/Listing Particulars Directive, as proposed, the host state would have less power to interfere with a prospectus that has been approved by the home state, which should facilitate cross-border securities offerings within the EU.<sup>11</sup> No longer would the prospectus necessarily have to be translated into the language of the host country, although it would be required to be drawn up in a language accepted by the competent authority in the home Member State.<sup>12</sup> In certain cases, it may be necessary to translate the prospectus into a language "customary in the sphere of international finance."

The Commission also proposes to revise the mutual recognition provisions of the Prospectus and Listing Particulars Directives.<sup>13</sup> Although the current Prospectus and Listing Particulars Directives already contemplate the possibility of reciprocity for issuers located outside of the EU, both in the context of listings and public offerings, recognition throughout the EU on the basis of a prospectus of a non-EU issuer has failed to materialize. The proposed directive lays the foundation for an issuer from outside the EU to make an offering or effect a listing throughout the EU on the basis of a prospectus prepared in accordance with IOSCO standards and approved by one EU Member State.<sup>14</sup> Presumably, the exercise of this privilege will also depend upon the issuer's use of accounting standards acceptable to the member country supervising the offering.<sup>15</sup> In February 2001, the EU Commission presented a proposal, which will require a mandatory application of International Accounting Standards for listed companies in the EU by 2005.<sup>16</sup> Under the legislation, all companies listed on a regulated market in the EU, or offering securities publicly in tandem with a listing, must prepare their accounts in accordance with

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7. European Parliament Legislative Resolution on the Proposal for a European Parliament and Council Directive on the Prospectus to be Published When Securities are Offered to the Public or Admitted to Trading (COM) (2001) 280-C5-0263/2002-2001/0117 (COD), March 14, 2002.

8. Amended Proposal for a Directive of the European Parliament and of the Council on the Prospectus to be Published When Securities are Offered to the Public or Admitted to Trading (Aug. 9, 2002), 2002/0117 COD, COM (2002) 460 Final (hereinafter 2002 RPD).

9. See Report of the Technical Committee, International Disclosure Standards for Cross-Border Offerings and Initial Listings by Foreign Issuers (May 1998), available at [http://www.iosco.org/docs-public/1998-intnl\\_disclosure\\_standards.htm](http://www.iosco.org/docs-public/1998-intnl_disclosure_standards.htm) (last visited 12/10/02). See generally Samuel Wolff, *Implementation of International Disclosure Standards*, 22 U. PA. J. INT'L ECON. L. 91 (Spring 2001).

10. See RPD, *supra* note 6; 2002 RPD *supra* note 8, at arts. 5, 12.

11. See Council Directive 2001/34/EC, *supra* note 5, at art. 7, at 14.

12. See *id.* at ch. III, art. 103 at 59.

13. See *id.* at 3; 2002 RPD, *supra* note 8, at art. 17.

14. 2002 RPD, *supra* note 8, at art. 20.

15. See *id.*

16. See Proposal for a Regulation of the European Parliament and of the Council on the Application of International Accounting Standards, COM(01)80 final at 2.

International Accounting Standards.<sup>17</sup> The proposal for mandatory applications of International Accounting Standards for listed companies in the EU was endorsed by the European Parliament, with amendments, in March 2002, and adopted in July 2002.<sup>18</sup> Conceivably, someday, an issuer from outside the EU preparing its prospectus in accordance with IOSCO standards will be able to make an offering throughout the EU on the basis of a single prospectus.

A legislative dialogue is also being conducted in the EU with respect to amending the Investment Services Directive.<sup>19</sup> The most important area of reform in this regard is the diminution of power on the part of host member countries to impose conduct of business rules on investment firms authorized by their home states. In November 2002, as this article went to press, the Commission published a proposal for a new directive on investment services and regulated markets. In May 2000, the Commission issued a proposal for a new directive on insider dealing and market manipulation.<sup>20</sup> The main effect of this directive is to set minimum standards for market manipulation in the EU.<sup>21</sup> The EU already has a directive on insider trading, but a new one has been adopted to apply to it the same framework for allocation of responsibilities and enforcement as would apply to market manipulation and to simplify administrative matters. As this article went to press, the European Parliament approved the Commission Proposal on Insider Dealing and Market Manipulation, with substantial amendments, and the measure subsequently was adopted.<sup>22</sup> In early 2002, the EU adopted new directives on investment companies, amending prior EU legislation<sup>23</sup> on this subject.<sup>24</sup> The Undertakings for Collective Investment in Transferable Securities (UCITS) directive is beyond the scope of this article. The proposed Takeover Directive, also beyond the scope of this article, died by tie vote in the European Parliament in July 2001.<sup>25</sup>

## II. BACKGROUND

The EU is a supranational organization, its activities and relations governed

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17. See Proposal for a Regulation of the European Parliament and of the Council on the Application of International Accounting Standards, COM(01)80 final at 2.

18. European Parliament Legislative Resolution on the Proposal for a European Parliament and Council Regulation on the Application of International Accounting Standards, COM(01)80.

19. See *infra* note 50, at § V.

20. See *infra* note 284 and accompanying text.

21. See *id.*

22. See European Parliament Legislative Resolution on the Proposal for a European Parliament and Council Directive on Insider Dealing and Market Manipulation, COM(01)281.

23. Council Directive 85/611/EEC, 3, 1985, O.J. (L 375).

24. See Council Directive 2001/107/EC, 2002 O.J. (L 41/20) (amending Council Directive 85/611/EEC on the Coordination of Laws, Regulations and Administrative Provisions Relating to Undertakings for Collective Investment in Transferable Securities [UCITS] with a View to Regulating Management Companies and Simplified Prospectuses); Council Directive 2001/108/EC, 2002 O.J. (L 41) (amending Council Directive 85/611/EEC on the Coordination of Laws, Regulations and Administrative Provisions Relating to UCITS, with regard to Investments of UCITS).

25. See R. Karmel, *The Failed European Union Takeover Directive*, N.Y. L. J., Aug. 16, 2001, at 3.

by a system of European law.<sup>26</sup> The Council of Ministers, the principal decision-making body of the EU, consists of ministers from each Member State.<sup>27</sup> The Council may consider legislative proposals, which the European Commission presents, must consult with the Parliament, and is subject to review by the European Court of Justice.<sup>28</sup> The Commission is composed of members, at least one from each state, appointed by mutual agreement of Member States.<sup>29</sup> The members of the Commission may not receive instructions from any national government and are subject to the supervision of the European Parliament which is the only body that can force them collectively to resign.<sup>30</sup> The Commission proposes legislation to the Council, implements EU policies, and attempts to ensure that the rules of the EU are followed.<sup>31</sup> The EU's law making procedure is expedited through the "comitology" procedure described *infra* section IV, C.<sup>32</sup>

There has been considerable discussion regarding both the merits and difficulties of creating an EU securities regulator to oversee the entire community. In a November 1999 "action plan," the European Commission discussed several of the shortcomings of the current regulatory environment.<sup>33</sup> The Commission recognized that the creation of a formal regulatory committee could be in the best interest of the EU securities markets and indicated a desire that further study should be made in this area.<sup>34</sup> The influential "Committee of Wise Men," however, did not endorse the idea of a "European SEC."<sup>35</sup> Some commentators, however, have argued in favor of an SEC-type institution for Europe, on grounds that a European SEC is necessary to foster a true pan-European securities market.<sup>36</sup> There also is the development of the Forum of European Securities Commissions ("FESCO"), but to date, this is merely an advisory body with no actual regulatory authority over the EU as a whole.<sup>37</sup>

The major securities laws in the EU are comprised of a number of directives, which seek to harmonize the laws of the EU Member States by providing minimum standards to be followed by each Member State in the regulation of securities

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26. See generally The European Union Online, at <http://www.europa.eu.int> (last visited December 1, 2002).

27. See generally *id.*

28. See *id.* at 22.

29. See generally The European Union, *supra* note 26.

30. EC TREATY arts. 213-16, available at [http://europa.eu.int/eur-lex/en/treaties/dat/ec\\_const-treaty\\_en.pdf](http://europa.eu.int/eur-lex/en/treaties/dat/ec_const-treaty_en.pdf) (last visited Dec. 23, 2002).

31. See Reynolds, *Introduction to the European Economic Community: Its History and Institutions*, 8 LEGAL REFERENCE SERVICES Q. 7, 10 (1988).

32. See Council Decision 1999/468/EC, *infra* note 165.

33. See Financial Services: Implementing the Framework for Financial Markets: Action Plan, COM (99)232 final at 14 [hereinafter referred to as Financial Services Action Plan]; see also *Action Plan*, available at <http://europa.eu.int/scadplus/leg/en/lvb/l24210.htm> (last visited Dec. 23, 2002).

34. See *id.* at 30.

35. See Bengt Ljung, *International Developments: EU "Wise Men Group" Cool to Creating SEC-Style Agency to Streamline System*, 32 SEC. REG. & L. REP., 1588 (Nov. 20, 2000).

36. See, e.g., Gilles Thieffry, *Comment: European Securities Regulation*, 20 INT'L FIN. L. REV. 5 (May 2000) (arguing that European SEC is best response to consolidation of securities markets, exchanges and clearing systems in Europe).

37. See *Securities Regulators Start Euro Forum*, INSTITUTIONAL INVESTOR, 2 (1997).

within its borders.<sup>38</sup> The principal EU securities directives are those, which govern stock exchange listing, prospectuses, reporting requirements, banking, investment services, capital adequacy, investment funds and insider trading.<sup>39</sup> The EU's two stock exchange directives are the Listing Conditions Directive<sup>40</sup> and the Listing Particulars Directive.<sup>41</sup> The Listing Conditions Directive sets forth minimum conditions for the admission of securities to listing on a stock exchange located in the EU.<sup>42</sup> The Listing Particulars Directive aims to coordinate the differences in Member State disclosure requirements applicable to stock exchange listing and to ensure that disclosure is made to the extent that it enables investors to make informed decisions regarding the financial position and prospects of the issuer.<sup>43</sup> The Prospectus Directive<sup>44</sup> provides that Member States must require that any offer of securities to the public be subject to the publication of a prospectus by the offeror,<sup>45</sup> which must be published or made available no later than the time when the offer is made to the public.<sup>46</sup>

The Second Banking Directive<sup>47</sup> establishes a single license applicable throughout the EU for the provision of banking and other financial services.<sup>48</sup> Banks operating under the Second Banking Directive may provide a wide variety of financial services, including investment services, authorized by the home Member State, without obtaining an additional license.<sup>49</sup> The Investment Services Directive<sup>50</sup> provides for a home state license that allows investment firms to provide, in any Member State, the investment services that are authorized by the home Member State.<sup>51</sup> Under this directive, an investment firm is able to provide in-

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38. The purpose of the directives is to establish "the minimum regulatory foundation necessary for the correct operation of the markets and for the protection of investors," while leaving the application of the directives and the enforcement of securities laws to the individual regulatory authorities of the Member States. *See also*, Completing the Internal Market: White Paper from the Commission of the European Council, COM (85)310 final at 8; Fabrice Demarigny, *One Year After the Euro: What Type of Regulation for the European Financial Market?*, No. 19, 10 FUTURES & DERIVATIVES L. REP. 11 (2000).

39. *See* Completing the Internal Market: White Paper from the Commission of the European Council, COM (85)310 final at 8; Demarigny, *supra* note 38.

40. Council Directive 79/279/EEC of 5 March 1979 Coordinating the Conditions for the Admission of Securities to Official Stock Exchange Listing, 21, 1979 O.J. (L 66), replaced by Council Directive 2001/34/EC, *supra* note 5.

41. Council Directive 80/390/EEC, *supra* note 5, replaced by Council Directive 2001/34/EC, *supra* note 5.

42. *See id.*

43. *See id.*

44. Council Directive 89/298/EEC, *supra* note 4.

45. *See id.* at art. 4.

46. *See id.* at arts. 9, 16.

47. Council Directive 89/646/EEC of 15 December 1989 on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Credit Institutions, 1, 1989 O.J. (L 386) (amending Council Directive 77/780).

48. *See id.*

49. *See id.*

50. Council Directive 93/22/EEC of 10 May 1993 on Investment Services in the Securities Field, 27, 1993, O.J. (L 141) [hereinafter Council Directive 93/22/EEC, Investment Services Directive or ISD].

51. *See* Council Directive 93/22/EEC, *supra* note 50 at art. 3.

vestment services directly or by establishing a branch in another Member State.<sup>52</sup> The Capital Adequacy Directive<sup>53</sup> requires both investment firms and credit institutions to maintain a specified amount of capital for risks associated with certain activities, including trading.<sup>54</sup>

The Insider Dealing Directive<sup>55</sup> prohibits specified persons who possess "inside information" from using that information "with full knowledge of the facts" by purchasing or selling transferable securities of the issuer to which the information relates.<sup>56</sup> This prohibition applies to any person who possesses inside information by virtue of his membership in the structure of the issuer, his share ownership, or his access to information through his employment, profession or duties.<sup>57</sup>

### III. THE REPORT OF THE COMMITTEE OF WISE MEN

In the Communication from the Commission-Risk Capital Action Plan,<sup>58</sup> and the Communication from the Commission, Implementing the Framework for Financial Markets Action Plan,<sup>59</sup> the European Commission published a program for completing the internal market for financial services and facilitating capital formation in the EU. The Financial Services Action Plan serves as a guide toward development of the single financial market.<sup>60</sup> In July 2000, the Council of Ministers formed the Committee of Wise Men on the Regulation of European Securities Markets ("Committee").<sup>61</sup> The Committee released its initial report in November, 2000<sup>62</sup> and its final report in February, 2001.<sup>63</sup> In its Final Report, the Committee set forth the following priority items: a single prospectus for issuers with a system of shelf registration; modernization of listing standards; mutual recognition for wholesale markets; modernization of rules for investment funds and pension plans; adoption of international accounting standards; and a single passport for recognized stock markets.<sup>64</sup>

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52. See *id.* at art. 14, § 1.

53. Council Directive 93/6/EEC of 15 March 1993 On the Capital Adequacy of Investment Firms and Credit Institutions, 1, 1993 O.J. (L 141).

54. See *id.* at art. 4.

55. Council Directive 89/592/EEC of 13 November 1989 Coordinating Regulations on Insider Dealing, 30, 1989, O.J. (L 334) [hereinafter Council Directive 89/592/EEC or Insider Dealing Directive].

56. *Id.* at art. 2.

57. See *id.*

58. SEC (1998) 552 final.

59. Financial Services Action Plan, *supra* note 33.

60. *Id.*

61. See generally Financial Services: Initial Report of the Committee of Wise Men on the Regulation of European Securities Markets, at [http://europa.eu.int/comm/internal\\_market/en/finances/banks/wisemen.htm](http://europa.eu.int/comm/internal_market/en/finances/banks/wisemen.htm) (last visited Nov. 19th, 2002).

62. See Nov. 7 Committee of Wise Men, *supra* note 1.

63. Final Report of the Committee of Wise Men on the Regulation of European Securities Markets (2001), available at [http://europa.eu.int/comm/internal\\_market/en/finances/general/lamfalussyen.pdf](http://europa.eu.int/comm/internal_market/en/finances/general/lamfalussyen.pdf) (last visited Nov. 22, 2001).

64. See *id.* at 13.



## IV. PUBLIC OFFERINGS

A. *Prospectus Directive — Current Law*

The Council adopted the Prospectus Directive on April 17, 1989 to coordinate the requirements for the "drawing-up, scrutiny and distribution" of a prospectus to be used when securities are offered to the public.<sup>65</sup> Member States must require (absent an exemption) that any offer of securities to the public "within their territories" be subject to the publication of a prospectus by the offeror.<sup>66</sup> The prospectus must be published or made available no later than the time when an offer is made to the public.<sup>67</sup>

The Prospectus Directive approaches public offerings on the basis of whether the securities in question will be listed in a Member State.<sup>68</sup> If a public offer of transferable securities is made in a Member State and at the time of the offer the securities are the subject of a listing application in the same state, prospectus requirements must be determined in accordance with the Listing Particulars Directive, as distinguished from Article 11 of the Prospectus Directive.<sup>69</sup> This rule applies to both the prospectus content requirements and the procedures for reviewing and distributing the prospectus, subject to "adaptations appropriate to the circumstances of a public offer."<sup>70</sup> Thus, in effect, the Prospectus Directive incorporates the Listing Particulars Directive to establish the content of and review procedures relating to the prospectus.<sup>71</sup> If a public offer is made in one Member State and listing is sought on a stock exchange in another Member State, the individual making the public offering must have the possibility of using, in the offering, a prospectus governed by the Listing Particulars Directive as opposed to the Prospectus Directive, both in terms of content and procedure, and subject to any changes necessary to reflect the circumstances of the public offer.<sup>72</sup>

Article 11 of the Prospectus Directive applies to public offerings of securities for which listing is not sought.<sup>73</sup> Article 11 sets forth the minimum prospectus disclosure requirements Member States must adopt with respect to prospectuses, for a public offer of securities not to be officially listed on an exchange in a Member State.<sup>74</sup> Article 11 requires a prospectus to contain information concerning, among other things:

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65. See Council Directive 89/298/EEC, *supra* note 4, at preamble.

66. *Id.* at art. 4.

67. See *id.* at arts. 9, 16.

68. See RPD, *supra* note 6.

69. See Council Directive 89/298/EEC, *supra* note 4, at art. 7.

70. *Id.*

71. See *id.* at preamble.

72. See *id.* at art. 8(1). This possibility shall exist only in Member States, which in general provide for the prior scrutiny of public offer prospectuses. *Id.* at art. 8(2).

73. See *id.* at art. 7.

74. See *id.* at § III, art. 11.

- (1) Those responsible for the prospectus;<sup>75</sup>
- (2) The offer to the public and the transferable securities being offered;<sup>76</sup>
- (3) The issuer<sup>77</sup> and its principal activities;<sup>78</sup>
- (4) The issuer's assets and liabilities, financial position and profits and losses; interim accounts if any have been published since the end of the previous financial year;<sup>79</sup>
- (5) The issuer's administration, management and supervision.<sup>80</sup>

Prospectuses for unlisted securities must be published or made publicly available pursuant to procedures established by each Member State.<sup>81</sup> The Member States may provide, however, that the person making the offering may prepare the prospectus, in terms of its content, and subject to appropriate adaptation, in accordance with the Listing Particulars Directive, even though the securities in question are not subject of a listing application.<sup>82</sup> In this event, authorities designated by the Member States must make prior scrutiny of the prospectus.<sup>83</sup> A prospectus so prepared and approved by a Member State in the three months preceding application for listing must be recognized, *subject to translation*, as listing particulars in the Member States in which application for listing is made.<sup>84</sup> A prospectus so prepared in accordance with the Listing Particulars Directive must also be deemed to satisfy the prospectus requirements of other Member States in which the same securities are, simultaneously or within a short time period, offered to the public.<sup>85</sup>

A Member State may choose to allow issuers not proposing to apply for official listing to comply with Article 11 disclosure rather than compelling them to satisfy the same disclosure standards applicable to issuers concurrently applying for

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75. See Council Directive 89/298/EEC, *supra* note 4, at art. 11(2)(a).

76. See *id.* at art. 11(2)(b).

77. See *id.* at art. 11(2)(c). In the case of shares, in so far as they are known, indication of the shareholders who directly or indirectly exercise or could exercise a determining role in the management of the issuer. See *id.*

78. See *id.* at art. 11(2)(d).

79. See *id.* at art. 11(2)(e). In addition, the name of the person responsible for auditing the accounts should be included. See *id.*

80. See *id.* at art. 11(2)(f) (including names, addresses, functions; in the case of an offer to the public of shares in a limited-liability company, remuneration of the members of the issuer's administrative, management and supervisory bodies).

81. See *id.* at art. 15.

82. See *id.* at art. 12(1).

83. See *id.* at art. 12(2).

84. See Council Directive 90/211/EEC of 23 April 1990 in Respect of the Mutual Recognition of Public Offer Prospectuses as Stock Exchange Listing Particulars, art. 2, 1990 O.J. (L 112) (amending the Listing Particulars Directive, *supra*, note 5, at art. 24(b)(1)) [hereinafter Council Directive 90/211/EEC].

85. See Council Directive 89/298/EEC, *supra* note 4, at art. 21(1).

admission to official listing on an exchange in a Member State.<sup>86</sup> Further, a Member State is not compelled to give such issuers the alternative of complying with the more stringent disclosure standards of the Listing Particulars Directive.<sup>87</sup> Under the Prospectus Directive, a Member State has no obligation to recognize a prospectus meeting the requirements of another Member State that satisfies only the Article 11 requirements.<sup>88</sup>

Where public offers are made within short intervals of one another in two or more Member States, a public offer prospectus prepared and approved in accordance with the Prospectus Directive (other than an Article 11 prospectus) must be recognized as a public offer prospectus in such Member States.<sup>89</sup> The Member States may not impose any approval requirement or require additional information to be included in such prospectus, other than certain country-specific information.<sup>90</sup> Specifically, Member States may require that the prospectus include "information specific to the market of the country in which the public offer is made concerning in particular the income tax system, the financial organizations retained to act as paying agents for the issuer in that country, and the way in which notices to investors are published."<sup>91</sup> The directive permits Member States to limit the reciprocity requirement to issuers having their registered offices in a Member State.<sup>92</sup> The EU may negotiate agreements with non-EU countries pursuant to which it would recognize, for purposes of the Prospectus Directive, prospectuses prepared and reviewed in accordance with the foreign law of non-member countries, provided such foreign law gives equivalent protection, even if it differs from the directive.<sup>93</sup> This possibility, however, is subject to "reciprocity,"<sup>94</sup> meaning subject to acceptance by the foreign country involved of prospectuses prepared in accordance with EU law.<sup>95</sup>

The Prospectus Directive is expressly inapplicable to certain types of offers, including offers of securities to a "restricted circle of persons," or to "persons in the context of their trades, professions or occupations," offers where the selling price of all the securities offered does not exceed ECU 40,000, or finally, where the securities offered can only be "acquired for a consideration of at least 40,000 euros per investor."<sup>96</sup> Various types of securities also are excluded from the directive's provisions including, among others:

- (1) Transferable securities offered in individual denominations of at least ECU

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86. See Council Directive 89/298/EEC, *supra* note 4, at III, art. 11.

87. See *id.* at art. 12(1).

88. See *id.* at art. 21(1).

89. See *id.* at art. 21.

90. See *id.* at art. 21(1).

91. *Id.*

92. See *id.* at art. 21(4).

93. See *id.* at art. 24.

94. *Id.*

95. See *id.* at arts. 12(1), 13.

96. *Id.* at art. 2(1).

40,000;<sup>97</sup>

(2) Transferable securities issued by a state or by one of a state's regional or local authorities or by public international bodies of which one or more Member States are members;<sup>98</sup>

(3) Transferable securities offered in connection with a take-over bid;<sup>99</sup>

(4) Transferable securities offered in connection with a merger;<sup>100</sup>

(5) Shares allotted free of charge to the holders of shares;<sup>101</sup>

(6) Shares or transferable securities equivalent to shares offered in exchange for shares in the same company if the offer of such new securities does not involve any overall increase in the company's issued shares capital;<sup>102</sup>

(7) Transferable securities offered by their employer or by an affiliated undertaking for the benefit of current or former employees;<sup>103</sup>

(8) Transferable securities resulting from the conversion of convertible debt securities or from the exercise of the rights conferred by warrants or to shares offered in exchange for exchangeable debt securities, provided that a public offer prospectus or listing particulars relating to those convertible or exchangeable debt securities or warrants was published in the same Member State;<sup>104</sup>

(9) Transferable securities issued, with a view to their obtaining the means necessary to achieve their disinterested objectives, by associations with legal status of non-profit bodies recognized by the Member State;<sup>105</sup> and

(10) Euro-securities, which are not the subject of a generalized campaign of advertising or canvassing.<sup>106</sup>

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97. See Council Directive 89/298/EEC, *supra* note 4 at art. 2(2)(a).

98. See *id.* at art. 2(2)(c).

99. See *id.* at art. 2(2)(d).

100. See *id.* at art. 2(2)(e).

101. See *id.* at art. 2(2)(f).

102. See Council Directive 89/298/EEC, *supra* note 4 at art. 2(2)(g).

103. See *id.* at art. 2(2)(h).

104. See *id.* at art. 2(2)(i).

105. See *id.* at art. 2(2)(j).

106. See *id.* at art. 2(2)(l). "Eurosecurities" are transferable securities which are to be underwritten and distributed by a syndicate, at least two of the members of which have their registered offices in different states; are offered on a significant scale in one or more states other than that of the issuer's registered office; and may be subscribed for or initially acquired only through a bank or other financial institution. *Id.* at art. 3(f).

*B. Listing Directives — Current Law*

The Listing Conditions Directive sets forth minimum conditions for the admission of securities to listing on a stock exchange located in the EU.<sup>107</sup> These listing conditions involve matters such as the size of the issuer, its period of existence, and the distribution of its shares in the market.<sup>108</sup> With regard to specific quantitative thresholds, the directive requires that: (1) the company's market capitalization, or capital and reserves from the financial year preceding the year in which listing is sought, be at least equivalent to one million euro; (2) its annual financial accounts must have been published for the three financial years preceding the application for official listing; and (3) a sufficient number of shares must have been issued to the public no later than the time of admission to official listing.<sup>109</sup> Additionally, the directive imposes numerous responsibilities on issuers of listed securities, including reporting obligations.<sup>110</sup> The directive does not prohibit the listing of shares from non-EU countries, but provides that if shares of such a company are not listed in the issuer's home country or principal market, they may not be listed in an EU country unless the authorities are satisfied that the absence of the home country/principal market listing "is not due to the need to protect investors."<sup>111</sup> Non-EU issuers listing in an EU country are required to meet the minimum conditions and obligations of the directive as enacted into national law in the particular country involved.<sup>112</sup>

The purpose of the Listing Particulars Directive is to coordinate the differences in Member State disclosure requirements applicable to stock exchange listing.<sup>113</sup> The directive requires Member States to ensure that the listing of securities upon a stock exchange in their territory is contingent upon the publication of a disclosure document referred to as "listing particulars."<sup>114</sup> The disclosure document must contain the information necessary to enable investors to make an "informed assessment" of the financial position and prospects of the issuer, as well as the rights attaching to the securities at issue.<sup>115</sup> In addition to basic information regarding the person responsible for the listing particulars, the directive requires certain information concerning the characteristics of the shares sought to be listed.<sup>116</sup> The admission to official listing must contain information concerning the number, price or nominal value and rights or restrictions attaching to all shares, as well as the information detailing the methods and time of delivery of the shares and the intended application of the proceeds accruing to the issuer as a result of the is-

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107. See generally, Council Directive 89/298/EEC, *supra* note 4.

108. See Council Directive 2001/34/EC, *supra* note 5, at tit. III.

109. See *id.* at arts. 43, 44, 49.

110. See *id.* at tit. IV.

111. *Id.* at art. 51.

112. See *id.* at art. 50.

113. See *id.* at preamble.

114. *Id.* at art 20.

115. *Id.* at art 21.

116. *Id.*

sue.<sup>117</sup> The issuer must also identify any persons who “directly or indirectly, severally or jointly, exercises or could exercise control over the issuer, and particulars of the proportion of the capital held giving a right to vote.”<sup>118</sup> Additionally, the issuer is required to identify any shareholders who hold a portion of the issuer’s capital, the precise amount being determined by the Member States, but in no event to exceed twenty percent.<sup>119</sup> Under the terms of the Listing Particulars Directive, the issuer must also provide the last three balance sheets and profit and loss accounts, as well as notes on the annual accounts for the most recent financial year.<sup>120</sup> The issuer must provide the name, address and function of all members of the company’s administrative, management or supervisory bodies.<sup>121</sup> The information provided by the issuer must include the total remuneration paid to members of the administrative, management or supervisory bodies.<sup>122</sup> The issuer need disclose only total amounts for each category of body, not amounts paid on an individual basis.<sup>123</sup> Disclosure must also be made of the “total number of shares in the issuing company held by the members of its administrative, management and supervisory bodies and options granted to them on the company’s shares.”<sup>124</sup> In addition, information must be given about the nature and extent of the interests of members of the administrative, management and supervisory bodies in transactions affected by the issuer, which are unusual in their nature or conditions during the preceding and current financial years.<sup>125</sup>

Listing particulars may not be published until they have been approved by the appropriate authorities,<sup>126</sup> at which time they must be published for use by the investing public.<sup>127</sup> Listing particulars may be published either by insertion in one or more newspapers circulated throughout the Member State or as a brochure made available to the public.<sup>128</sup>

The Listing Particulars Directive provides that when applications for listing the same securities on stock exchanges in several Member States are made within short intervals of each other, the authorities in each state should cooperate with each other and make arrangements to expedite and simplify the listing proce-

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117. See Council Directive 2001/34/EC, *supra* note 5, at sched. A, ch.2. The disclosure schedules in Council Directive 2001/34/EC appear to restate the disclosure schedules from the 1980 Listing Particulars Directive, and have not been revised to reflect the International Disclosure Standards (IDS) of the International Organization of Securities Commissions (IOSCO). See International Disclosure Standards, *infra* note 143.

118. See *id.* at sched. A, § 3.2.6.

119. See *id.* at sched. A, § 3.2.7.

120. See *id.* at sched. A, § 5.1. This report must include a detailed breakdown of the profit or loss per share, the amount of dividend per share, and a table showing the sources and application of funds for the last three financial years. See *id.* §§ 5.1.2, 5.1.3, 5.1.4.

121. See *id.* at sched. A, § 6.1.

122. See *id.*

123. See *id.* at sched. A, § 6.2.

124. *Id.* at sched. A, § 6.2.1.

125. See *id.* at sched. A, § 6.2.2.

126. See *id.* at art. 35.

127. See *id.* at art. 20.

128. See *id.* at art. 98.

ture.<sup>129</sup> In 1987, the Council adopted a directive requiring significantly more reciprocity in the listing process.<sup>130</sup> This directive applies when applications are made to list securities on two or more exchanges located in the EU, in which event listing particulars are to be prepared in accordance with home state rules and approved by home state authorities.<sup>131</sup> These provisions are now codified in Articles 38 through 41 of Directive 2000/34/EC.<sup>132</sup> Once so approved, "listing particulars must, subject to any translation, be recognized by the other Member States in which admission to official listing has been applied for, without it being necessary to obtain the approval of the competent authorities of those States and without their being able to require that additional information be included in the listing particulars."<sup>133</sup> The authorities of any EU country may, however, compel the inclusion of certain limited information specific to the country in which listing is sought.<sup>134</sup> The host state may require that the listing particulars include information specific to the market of the host country concerning in particular the income tax system, the financial organizations retained to act as paying agents for the issuer in that country, and the way in which notices to investors are published.<sup>135</sup> If the issuer's registered office is not located in a Member State, it must choose an EU country to supervise its listing.<sup>136</sup> The directive allows EU countries to restrict application of the foregoing mutual recognition rules to listing particulars of issuers having their registered office in a Member State.<sup>137</sup> Member States may allow the competent authorities to exempt from the requirement to publish full listing particulars where: (1) the securities or the shares of the issuer have been officially listed in another Member State for not less than three years before the application for listing; (2) during such period (or such shorter period that the issuer's securities have been listed), "the issuer has complied with all the requirements concerning information and admission to listing imposed by Community Directives on companies the securities of which are officially listed;" and (3) a simplified disclosure document is published.<sup>138</sup>

### C. 2001 Proposal for New Prospectus/Listing Directive

On May 30, 2001, the Commission, following up on the Committee's Report, submitted a proposal for a new, combined Prospectus and Listing Particulars Directive that would replace and repeal the existing Prospectus Directive and Listing

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129. See Council Directive 2001/34/EC, *supra* note 5, at art. 13.

130. See generally Council Directive 87/345/EEC of 22 June 1987 Coordinating the Requirements for the Drawing Up, Scrutiny and Distribution of the Listing Particulars to be Published for the Admission of Securities to Official Stock Exchange Listing, 81, 1987 O.J. (L 185) (amending Council Directive 80/390/EEC).

131. See *id.*

132. See Council Directive 2001/34/EC, *supra* note 5, at arts. 38-41.

133. *Id.* at art. 38.

134. See *id.*

135. See *id.* art. 37.

136. See *id.*

137. See *id.* at art. 38, no. 5.

138. *Id.* at art. 23(4).

Particulars Directives.<sup>139</sup> The Commission issued an amended proposal on August 9, 2002.<sup>140</sup> In November 2002, as this article went to press, the Council of Ministers reached political agreement on the prospectus proposal. Because the proposed directive was and is highly controversial, and has been under consideration by both the Parliament and a Council Working Party, it is unclear whether the final legislation, if adopted, will more closely resemble the first Commission proposal (the 2001 proposal), with Parliament's amendments, or the second Commission proposal.<sup>141</sup> Therefore in many instances both the 2001 and 2002 Commission proposals, as well as Parliament's amendments, are set forth below. The principal purpose of the proposed amendment is to introduce a "single passport" for issuers offering securities in the EU.<sup>142</sup> Among the features of the new system are the following: (1) the prospectus would be based to a large degree upon the International Organization of Securities Commissions' (IOSCO) International Disclosure Standards;<sup>143</sup> (2) issuers would be entitled to use a registration system similar to U.S. shelf registration, by virtue of this system, issuers would have the possibility of effecting an offering or a listing "on the basis of a simple notification of the prospectus approved by the home competent authority;"<sup>144</sup> (3) the host state would have diminished power to influence the disclosure document; (4) the disclosure document (except a summary) would not necessarily have to be translated into the language of the host country; (5) the provisions governing recognition of prospectuses from issuers outside the EU would be changed, potentially increasing the possibility for recognition of prospectuses from outside the EU, provided they are prepared in accordance with IOSCO standards; (6) issuers will be entitled to use incorporation by reference; (7) the prospectus must be made publicly available in electronic form; and (8) the existing Prospectus Directive and Listing Particulars Directive would

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139. See RPD, *supra* note 6.

140. See 2002 RPD, *supra* note 8.

141. The Commission stated in its second proposal that, "[t]o speed up the legislative process and meet the expectations expressed at the Barcelona Council on the early adoption of a directive on prospectuses, the Commission wishes to put forward an amended proposal for a Directive that takes account of many of Parliament's and the Council's wishes and concerns. The presentation of the proposal has been changed as regards form to make the text more understandable and readable." 2002 RPD, at Explanatory Memorandum, General Comments.

142. See Opinion of the European Central Bank, 2001 O.J. (C344/5). [hereinafter European Central Bank Opinion]. "The main goal of the proposal adopted by the Commission on 30 May 2001 is to create a true European passport for issuers by giving community-wide validity to the prospectus approved by the issuer's home supervisor." Council of the European Union Progress Report on the RPD (Nov. 30, 2001), 2001/0117 (COD) [hereinafter Progress Report].

143. See International Organization of Securities Commissions, International Disclosure Standards for Cross-Border Offerings and Initial Listings by Foreign Issuers, Final Communique of the 23rd Annual Conference of the International Organization of Securities Commissions, available at [www.iosco.org/iosco.html](http://www.iosco.org/iosco.html) (Sept. 18, 1998) [hereinafter International Disclosure Standards] (for purposes of the Revised Prospectus Directive [RPD], a "prospectus" serves as both a prospectus for a public offering and listing particulars for a listing; these are essentially one and the same document, though the disclosure may vary somewhat based upon whether a public offering, listing, or both are contemplated).

144. "[N]o role is assigned to the host supervisors any longer (except in certain exceptional emergency situations)." Progress Report, *supra* note 142, at 14275/1/01, rev. 1.



be repealed.<sup>145</sup>

The European Central Bank fully endorsed the concept behind the RPD, even though it had specific comments on certain issues.<sup>146</sup>

On account of the new language regime for multinational offerings and admissions to trading, costly translation will be significantly reduced. Regulatory compliance will be simplified, since host Member States will be deprived of the possibility of requiring adherence to additional national rules. As a consequence, raising capital should become easier and cheaper for companies of all sizes. The introduction of harmonized and enhanced disclosure standards in line with international standards for public offer of securities and admission to trading is likely to increase investor confidence, in particular as regards investing on an EU-wide basis.<sup>147</sup>

Nonetheless, the publication of the proposed RPD led to a torrent of criticism throughout Europe.<sup>148</sup> As initially proposed, the RPD applies equally to all public offers of securities and listings, irrespective of the size of the offering, the nature of the issuer or whether the securities are to be admitted to the official list or a second- or third-tier market.<sup>149</sup> Numerous market participants, including the London Stock Exchange, objected strenuously to this approach. The London Stock Exchange argued, for example, that the RPD would destroy "Europe's second markets, including AIM in the United Kingdom."<sup>150</sup> "European second markets, such as AIM, would be virtually impossible to sustain in the framework set out in the Directive."<sup>151</sup> The controversy generated by the RPD was taken up by the European Parliament, in particular, the European Parliament's Committee on Economic and Monetary Affairs (EMCA).<sup>152</sup> The EMCA's proposals, spearheaded by Rapporteur Christopher Huhne, surfaced in a Draft Report in late November 2001.<sup>153</sup> The Committee voted in a number of amendments designed generally to ease regulation on small businesses and Euromarket transactions.<sup>154</sup> Subsequently, the

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145. See Progress Report, *supra* note 142, at 14275/1/01, rev. 1.

146. See European Central Bank Opinion, *supra* note 142.

147. See *id.*

148. See e.g., Dickson, et al., *Passport to Discord*, FIN. TIMES, Nov. 22, 2001; FSA's Howard Criticizes EU Prospectus Rules, DOW JONES INT'L NEWS, Sept. 13, 2001; W. Wright, *Bankers Warn EU Could Cripple Eurobond Market*, FIN. NEWS, June 25, 2001.

149. See RPD, *supra* note 6.

150. Comments from the London Stock Exchange on the Proposed Prospectus Directive, available at [www.londonstockexchange.com/newsroom/pdfs/pdwebstory.pdf](http://www.londonstockexchange.com/newsroom/pdfs/pdwebstory.pdf) [hereinafter London Stock Exchange Comments].

151. *Id.* at para. 2.7.

152. See generally [www.europarl.eu.int/committees/econ\\_home.htm](http://www.europarl.eu.int/committees/econ_home.htm) (last visited Nov. 21, 2002).

153. See European Parliament, Committee on Economic and Monetary Affairs, Draft Report on the Proposal for a European Parliament Directive on the Prospectus to be Published When Securities Are Offered to the Public or Admitted to Trading, Provisional 2001/0117(COD).

154. See Chris Huhne, *Key Parliamentary Amendments Remove Threats to Small Companies*, available at [www.chrishuhnemep.org](http://www.chrishuhnemep.org). See also Kit Dawnay, *MEP Huhne Praised for Role in EU Prospectus Directive Amendments*, THE FIN. NEWS (Mar. 4, 2002); Committee on Economic and Monetary Affairs, Draft Report on the Proposal for a European Parliament and Council Directive on the Prospectus to be Published When Securities Are Offered to the Public or Admitted to Trading (2001),

European Parliament approved the Commission proposal on the basis of dozens of substantive amendments.<sup>155</sup> Although it is too early to predict with certainty, it is likely that the institutions of the EU will be responsive enough to the concerns of market participants that the RPD will eventually become law in the EU.

The RPD would apply to securities offered to the public in one or more Member States, or admitted to trading (or subject to a procedure for admission to trading) on a regulated market in a Member State.<sup>156</sup> As with the current Prospectus Directive, under the RPD, Member States must ensure that "any offer of securities to the public within their territories is subject to the publication of a prospectus by the person making the offer."<sup>157</sup> The obligation to publish a prospectus would not apply to certain offers, "excluding any subsequent resale to the public,"<sup>158</sup> namely:

where securities are offered to qualified investors for their own account;<sup>159</sup>

where the offer is addressed to fewer than 100 persons per Member State, other than qualified investors;

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2001/0117(COD); Committee on Economic and Monetary Affairs, Amendments 60-138, *Draft Report*, P.E. 307.441/60-138 (2002).

155. See European Parliament Legislative Resolution on the Proposal for the Public or Admitted to Trading, COM(01)280, available at <http://www.europarl.eu.int/meetdocs/committees/juri/20011121/449285en.pdf> (last visited August 30, 2002).

156. See RPD, *supra* note 6, at art. 1(2). The RPD does not apply to offerings by open-end investment companies; securities issued by a Member State or subdivision thereof; securities issued by public international bodies of which a Member State is a member; or by the European Central Bank. *Id.* at art. 1(3). A "regulated market," in general, means a market for securities, money market instruments, financial futures, interest rate forwards, swaps, and options that functions regularly, is characterized by the fact that regulations issued by the competent authorities define conditions for the operation of the market, for access to the market and, where applicable, conditions governing admission to listing, and requires compliance with certain reporting and transparency rules. See *id.*, at art. 2(1)(f); Council Directive 93/22/EEC, *supra* note 50, at art. 1(13).

157. RPD, *supra* note 6, at art. 3(1). An "offer of securities to the public" means any communication "presenting sufficient information on the terms of the offer and the securities to be offered, that might enable an investor to decide to purchase or subscribe to these securities. This definition shall also be applicable to the placing of securities through financial intermediaries." *Id.*, art. 2(1)(b). The 1989 Prospectus Directive did not contain a definition of "public offer," but, instead, left this matter to the Member States.

158. As this article went to press, the exclusions set forth below from the obligation to publish a prospectus were substantially amended by the European Parliament on March 14, 2002. See European Parliament Legislative Resolution, *supra* note 155, at amend. 20.

159. See RPD, *supra* note 6, at art. 3(2)(a). A "qualified investor" is a bank, investment firm, other authorized or regulated financial institution, insurance company, investment company, pension fund, commodity dealer, supranational institution, or government or central administrative authority. See *id.* at art. 2(1)(c). The definition of "qualified investor" was substantially revised in amendments passed by the European Parliament on March 14, 2002. See European Parliament Legislative Resolution, *supra* note 155, at amend. 15. The definition in the 2002 RPD extends to other legal entities authorized or regulated to operate in financial markets, as well as entities not authorized or regulated whose corporate purpose is solely to invest in securities. 2002 RPD at art. 2(1)(e). In addition, "qualified investors" includes other legal entities which are not small and medium-sized enterprises (as defined) and natural persons meeting specified standards.

where the securities can only be acquired for at least 50,000 Euro per investor per discrete offer.<sup>160</sup>

securities offered in the Euromarket or otherwise would be exempted if offered in individual denominations of at least EUR 50,000.<sup>161</sup>

an offer of securities with total consideration of less than Euro 2.5 million calculated over a twelve-month period

Exemptions are also provided in the RPD for certain types of securities, *to-wit*:

securities offered in connection with a merger or takeover bid, provided a disclosure document containing information regarded by the competent authority as equivalent to that of a prospectus is available;

securities offered to existing or former directors or employees provided a disclosure document meeting certain specification is published;"

shares issued in substitution for shares already traded on the same regulated market, if the issuance does not involve any increase in capital;

shares offered to existing shareholders or allotted free of charge, provided a disclosure document meeting specified conditions is published.

shares offered in exchange with no overall increase of capital to existing shareholders or allotted free of charge.<sup>162</sup>

The EMAC voted to give the Member States authority to exempt companies with a market capitalization below 350 million euros from the requirement to publish a full prospectus.<sup>163</sup> The revision was adopted in substance by the European Parliament.<sup>164</sup> The Commission may clarify the foregoing exemptions in accordance with Article 22(2) of the RPD, which reflects the so-called "comitology" procedure set forth in a 1999 Council Decision.<sup>165</sup> In its August 2002 re-proposal,

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160. See RPD, *supra* note 6 at art. 3(2)(c).

161. See European Parliament Legislative Resolution, *supra* note 155. It appears that the RPD, as initially published, would regulate Eurobond transactions only to the extent that they involve an "offer to the public or an admission to trading." Progress Report, *supra* note 142, at 14275/1/01, rev. 1.

162. See RPD, *supra* note 6 at arts. 3(2) & (3).

163. See Huhne, *supra* note 154.

164. See European Parliament Legislative Resolution on the Proposal for a European Parliament and Council Directive on the Prospectus to be Published When Securities are Offered to the Public or Admitted to Trading (COM) (2001) 280-C5-0263/2002-2001/0117 (COD), Mar. 14, 2002, Amendment No. 35.

165. See 1999/468/EC, Council Decision of 28 June 1999 Laying Down the Procedures for the Exercise of Implementing Powers Conferred on the Commission, O.J. L 184 (July 17, 1999) [hereinafter Council Decision 1999/468/EC].

the Commission did not include this provision although it would exempt small offerings (under Euro 2.5 million) and contemplates a more abbreviated prospectus for small and medium sized enterprises.

The Commission may clarify the foregoing exemptions in accordance with Article 22(2) of the RPD, which reflects the so-called "comitology" procedure set forth in a 1999 Council Decision.<sup>166</sup> This procedure essentially allows the Council to delegate implementing powers to the Commission.<sup>167</sup> The Commission is advised by a comitology committee consisting of representatives of the Member States.<sup>168</sup> Pursuant to the 1999 comitology decision of the Council, the comitology committee responds to a proposal of the Commission, by delivering its opinion on the measure within a specified time frame.<sup>169</sup> The Commission then adopts the measures "if they are in accordance with the opinion of the committee."<sup>170</sup> During the comitology process the European Parliament performs a supervisory role.<sup>171</sup> If the measure is not in accord with the opinion of the comitology committee, the Commission submits the measure to the Council as a Commission proposal and informs Parliament.<sup>172</sup>

Under the RPD, Member States must ensure that any admission of securities to trading on a regulated market in their territory is subject to the availability of a prospectus.<sup>173</sup> The RPD thus extends the Listing Particulars Directive to lower-tier markets, as the Listing Particulars Directive only applies where securities were subject to admission to the official list of the stock exchange.<sup>174</sup> The prospectus is essentially the same document as the public offering prospectus although the disclosure may vary somewhat depending upon which action the issuer is taking. The version adopted by the European Parliament would provide an exception for an issuer with a market capitalization of less than EUR 350 million, where an offering or listing is to be restricted to the home Member State, and where the home Member State provides for an exception from the prospectus requirements. The provision is not in the Commission's second proposal. Under the 2001 RPD, an issuer is considered to have fulfilled its obligation to publish a prospectus if it files a "registration document" with its home country's competent authority, has filed "where necessary, the securities note," and updates the registration document in accordance with Article 9 of the RPD.<sup>175</sup> Under the 2002 RPD, the issuer may

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166. See Council Decision 1999/468/EC, *supra* note 165.

167. See Nov. 7 Committee of Wise Men, *supra* note 1.

168. See *id.*

169. See RPD, *supra* note 6, at art. 3(2).

170. Council Decision 1999/468/EC, *supra* note 165, at art. 5.

171. See *id.* at art. 7(3)

172. See *id.* at art. 5(1).

173. See RPD, *supra* note 6, at art. 4. A "regulated market," in general, means a market for securities, money market instruments, financial futures, interest rate forwards, swaps and options that functions regularly, is characterized by the fact that regulations issued by the competent authorities define conditions for the operation of the market, for access to the market and, where applicable, conditions governing admission to listing, and requires compliance with certain reporting and transparency rules. RPD, art. 2(1)(f) and Investment Services Directive 93/22/EEC (May 10, 1993), at art. 1(13).

174. See Council Directive 80/390/EEC, *supra* note 5, at art.1(1).

175. See RPD, *supra* note 6, at art. 4.

choose whether the prospectus will consist of such documents or simply will be composed of a single document. The disclosure requirements will be amplified by detailed rules to be adopted by the Commission, but these rules must be consistent with IOSCO standards.<sup>176</sup> The registration document is filed with and reviewed by the competent authority of the home Member State.<sup>177</sup> Note that under the current prospectus and listing directives, the issuer need not choose the home country authority for scrutiny of the document.<sup>178</sup> The issuer may apply for approval of the prospectus by a competent authority in another member state under specified circumstances.

Significantly, the European Commission proposes to rely upon the IDS promulgated by the IOSCO to satisfy the disclosure requirement of prospectuses for both public offerings and listings.<sup>179</sup> In this regard, the Commission explained as follows:

Disclosure requirements provided for by Directive 80/390/EC are no longer sufficient to meet the needs of investors in modern global financial markets. Increasingly, investors want to make decisions on the basis of a continuum of standardized company financial and non-financial information. The current requirements need to be replaced by new European disclosure standards. Fostering best practices will enhance market confidence and attract capital. The upgrade of EU disclosure standards shall be in accordance with the International Disclosure Standards approved in 1998 by the IOSCO (International Organization of Securities Commissions). This new approach is designed to provide key information on certain topics such as risk factors, related party transactions, corporate governance or management's discussion and analysis, which are not currently dealt with at EU level.<sup>180</sup>

March 2002 revisions passed by the European Parliament would give the European Commission authority to implement disclosure requirements with reference to the IOSCO Standards.<sup>181</sup> Further, under the revisions, the competent authority of the home Member State could authorize the omission from the prospectus of information required by the RPD under certain circumstances.<sup>182</sup> This latter provision was carried over in the 2002 Commission proposal. Under Article 7 of the 2002 proposal, specific disclosure standards are to be developed pursuant to the comitology procedure but shall be based on IOSCO standards (and on the ANNEXES to the RPD).

Under the 2001 RPD, a prospectus may be published as a single document or

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176. Since IOSCO International Disclosure Standards only relate to equity securities, it will be necessary for the Commission to promulgate further disclosure standards for debt and other securities.

177. *See id.* at art. 4.

178. *See* Giovanni Nardulli & Antonio Segni, *EU Cross-Border Securities Offerings: An Overview*, 19 FORDHAM INT'L L. J. 887, 896 (1996).

179. *See* RPD, *supra* note 6, at explanatory memorandum (1), general comments.

180. *Id.*

181. *See* European Parliament Legislative Resolution, *supra* note 155, at amend. 23.

182. *Id.* at amend. 25.

may be composed of separate documents.<sup>183</sup> Companies trading on a regulated market in the EU (or which are applying for a listing) would have been required to publish a prospectus composed of separate documents.<sup>184</sup> A prospectus composed of separate documents includes a "registration document," a "securities note" and a "summary note," and the disclosure requirements applicable to each of the segments are included in Annex II, Annex III and Annex IV to the RPD, respectively.<sup>185</sup> The registration document is intended to contain information about the issuer, whereas the securities note is intended to provide information about the offering, the plan of distribution, and the market (as well as certain information about the issuer that is duplicative with the registration document), all on the basis of the IOSCO standards.<sup>186</sup> The summary note must give "in a few pages" the most important information included in the prospectus concerning the various disclosure items otherwise covered in the registration document and securities note.<sup>187</sup> The Commission must adopt detailed rules regarding specific information, which must be included in the prospectus, in the form of models for different types of securities and issuers.<sup>188</sup> Such rules must be in accordance with IOSCO's International Disclosure Standards.<sup>189</sup> Since IOSCO International Disclosure Standards only relate to equity securities, it will be necessary for the Commission to promulgate further disclosure standards for debt and other securities.<sup>190</sup> As indicated, under the 2002 RPD, the issuer can choose whether to prepare the prospectus as a single or separate document.

Under current law, in keeping with the mutual recognition provisions of the Directives, an issuer from one Member State seeking to use in another Member State listing particulars or a prospectus approved in one Member State would be required to translate the disclosure document into the language of the host country.<sup>191</sup> Under the 2001 RPD, the prospectus "shall be drawn up in a language accepted by the competent authority in the home Member State."<sup>192</sup> This provision should reduce translation costs in multinational offerings and admissions to listing.<sup>193</sup> Host authorities can, however, require the translation of the summary note into their local language.<sup>194</sup> The 2002 RPD has a more complex scheme, in terms

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183. See RPD, *supra* note 6, at explanatory memorandum I(15).

184. See *id.*

185. *Id.* at art. 5(4).

186. See *id.*

187. See *id.* at annex IV.

188. See *id.* at art. 6(1).

189. See *id.*

190. See London Stock Exchange Comments, *supra* note 150 at §1.3.

191. See Council Directive 87/345/EEC 1987 O.J. (L 185) 81, art. 24(a) (amending Directive 80/390/EEC) [hereinafter Council Directive 87/345/EEC]; Council Directive 90/211/EEC, *supra* note 82 (prepared in accordance with Listing Particular Directive must be recognized, subject to translation, as listing particulars in other Member States); Council Directive 89/298/EEC *supra* note 4, at art. 21 (prepared in accordance with Listing Particulars Directive is deemed to satisfy prospectus requirements of other Member States subject to translation, if required by host Member State).

192. RPD, *supra* note 6, at art. 7(1).

193. See European Central Bank Opinion, *supra* note 142, at §§ 4-5.

194. See RPD, *supra* note 6, at art. 7(1).

of language requirements, but reduces the instances of translation compared to current law. Where an offering is made in the home state and other member states, the prospectus must be published in a language accepted by the home state and also in the language accepted in the host states or a language customary in the sphere of international finance.

As indicated above, issuers may publish a prospectus composed of separate documents, or may prepare a prospectus as a single document if they choose. If an issuer has already filed a registration document, when preparing a securities offering it only has to file the securities note and the summary note. The securities note must provide information that would typically be included in a registration document if there were a material change or recent developments since publication of the registration document.<sup>195</sup> Under the 2001 RPD, the registration document must be updated annually.<sup>196</sup> Under the 2002 RPD (art. 10), issuers admitted to trading on a regulated market must update issuer information annually. Under the 2001 RPD, the registration document is filed with and reviewed by the competent authority of the home member state.<sup>197</sup> Under the 2002 RPD, the competent authority of the home member state has primary jurisdiction, but approval authority may be assumed by other member states under certain circumstances.<sup>198</sup> The 2001 RPD provides that EU countries may allow the issuer to use the registration document to satisfy the annual report requirements of the Fourth Directive on Accounting (Directive 78/660/EEC, Art. 46) and the Seventh Council Directive (Directive 83/349/EEC, Art. 36).<sup>199</sup> The 2002 RPD contains a similar provision.<sup>200</sup>

The RPD will allow incorporation by reference to documents that have been

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195. See 2002 RPD, *supra* note 8, at art. 12.

196. RPD, *supra* note 6, at art. 9(1). Under a proposed amendment adopted by the Economic and Monetary Affairs Committee of the European Parliament, this provision would be made optional, rather than mandatory. The Council also discussed concerns about annual updating of the registration document, and is considering a proposal to limit the mandatory nature of the registration document to issuers whose shares are admitted to trading. Under revisions passed in March 2002 by the European Parliament, annual updating is required only in order to use the document in the future for a public offer. "Accordingly, an issuer wishing to be able to offer its securities at any time shall update its registration document and obtain its approval by the competent authority of its home Member State at intervals of not more than twelve months." See *European Parliament Legislative Resolution on the Proposal for a European Parliament and Council Directive on the Prospectus to be Published When Securities are Offered to the Public or Admitted to Trading* (COM) (2001) 280-C5-0263/2002-2001/0117 (COD), Mar. 14, 2002, Amendment No. 32.

197. *Id.* Under amendments passed by the Economic and Monetary Affairs Committee of the European Parliament, the issuer would have its choice as to which competent authority would receive and review the document. See *Key Parliamentary Amendments Remove Threats to Small Companies* (Feb. 26, 2002), [www.chrishuhnemep.org](http://www.chrishuhnemep.org). In March 2002, the European Parliament passed amendments designed to allow registration documents to be filed with the Member State where the issuer has its registered office, where it was admitted to trading for the first time, or where it intends to offer the subject securities, at the choice of the issuer. See *European Parliament Legislative Resolution on the Proposal for a European Parliament and Council Directive on the Prospectus to be Published When Securities are Offered to the Public or Admitted to Trading* (COM) (2001) 280-C5-0263/2002-2001/0117 (COD), Mar. 14, 2002, Amendment No. 16.

198. 2002 RPD, *supra* note 8, at art. 13.

199. RPD, *supra* note 6, at art. 9(2).

200. 2002 RPD, *supra* note 8, at art 10(4).

filed and published in accordance with the RPD.<sup>201</sup> The Commission is instructed to adopt detailed rules concerning the privilege of incorporating by reference.

A prospectus may not be published until it has been approved by the competent authority of the home Member State.<sup>202</sup> The proposed Directive contains deadlines for approval of the prospectus by the competent authority. The home state authority must act within fifteen days of the submission of a draft prospectus, unless the submission is incomplete or the competent authority requires further information, in which case it must respond within fifteen days of the issuer's supplying the required information.<sup>203</sup> Under the 2001 RPD, if the regulator does not act within the specified time periods, the company's application shall be deemed to have been rejected and "such rejection shall give right to apply to the courts."<sup>204</sup> Under the 2002 RPD, if the competent authority fails to comment on the prospectus within the prescribed time, it shall be deemed approval of the application.

After receiving approval from the competent authority, the issuer must make the prospectus available to the public immediately, by publication in a newspaper of general circulation in the states in which the offer is made or admission to listing is sought, in the form of brochures to be made available to the public, or in electronic form on the websites of the company and the underwriters or placement agents. The competent authority of the home state must also make the prospectus available on its website, or provide a list of approved prospectuses. The Commission must adopt detailed technical rules on publication and availability of the prospectus in accordance with Article 22(2) comitology procedures.<sup>205</sup>

Orally conveyed information concerning the offer or admission to trading must be consistent with that in the prospectus. Further, information delivered to qualified investors or special categories of investors, including information disclosed in the context of meetings, must also be disclosed to the public.<sup>206</sup>

The issuer must file a prospectus supplement to disclose every significant new factor capable of affecting assessment of the securities which arises in the interval following approval of the prospectus and preceding the closing of the offering or the time when trading begins. The prospectus supplement must be filed with and reviewed by the home state and subsequently published in accordance with the rules that apply to the original prospectus.<sup>207</sup>

The revised prospectus directive contains mutual recognition provisions establishing the right to make offers or listings on a Community-wide basis under specified circumstances. Where an application has been made for a public offering

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201. 2002 RPD, *supra* note 8, at art. 11(1); RPD, *supra* note 6 at art. 10(1).

202. 2002 RPD, *supra* note 8, at art. 13(1); RPD, *supra* note 6, at art. 11(1). As indicated above, a key committee of the European Parliament recommends that the issuer be allowed to choose which competent authority would approve the prospectus.

203. 2002 RPD, *supra* note 8, at art. 13; RPD, *supra* note 6, at art. 11(2).

204. RPD, *supra* note 6, at art. 11(4).

205. 2002 RPD, *supra* note 8, at art. 12(7). Concerning Article 22(3) procedures, *see* RPD, *supra* note 6, at art. 12(7).

206. 2002 RPD, *supra* note 8, at art. 15(5); *see* RPD, *supra* note 6, at art. 13(4).

207. 2002 RPD, *supra* note 8, at art. 16; RPD, *supra* note 6, at art. 14.



or listing on a regulated market in one or more Member States, and a prospectus for the security has been approved by the home-Member State in the three months preceding the application, the competent authority of the host-Member State shall accept the prospectus for public offer or admission to trading.<sup>208</sup> This may generate some after-the-fact, inter-agency squabbling as to the adequacy of the prospectus, but if the RPD is enacted as proposed, EU law will require that the host country accept the prospectus as approved by the home state, provided the host state competent authority is properly notified.

A key purpose of the RPD is to reduce instances where the host state may object to use of a prospectus within its territory or require further information or a translation. Under the 2001 RPD, where an offer is made or admission to trading on a regulated market is sought in more than one Member State, the prospectus (or the registration document and securities note) "shall also be made available in a language customary in the sphere of finance which is generally accepted by the competent authority of the host Member State."<sup>209</sup> The host Member State may, however, require that the *summary note* be translated into the language used in the host state. The 2002 RPD has a more complex scheme, in terms of language requirements, but reduce the instances of translation compared to current law. Where an offering is made in the home state and other member states, the prospectus must be published in a language accepted by the home state and also in the language accepted in the host states or a language customary in the sphere of international finance.

The RPD contains provisions for the recognition of prospectuses of companies from outside the EU. Under current law, if the issuer's registered office is not located in a Member State, it may ask an EU country to supervise its listing.<sup>210</sup> However, EU countries may restrict application of the mutual recognition provisions to listing particulars of issuers having their registered office within a Member State.<sup>211</sup> Similarly, under current law, the Prospectus Directive permits Member States to limit reciprocity to issuers having their registered offices in a Member State.<sup>212</sup> Under the current regime, the EU is authorized to negotiate agreements with non-EU countries pursuant to which it would recognize, for purposes of the Prospectus Directive, prospectuses prepared and reviewed in accordance with the foreign law of non-member countries, provided such foreign law gives equivalent protection if it differs from the Directive<sup>213</sup>

Under both the 2001 and 2002 RPD, the competent authority of the home state responsible for approving prospectuses of issuers from third countries may allow such an issuer to use a prospectus prepared under non-EU law provided that the prospectus has been prepared according to IOSCO's International Disclosure Standards (or, under the 2002 RPD, standards set out by other "international secu-

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208. 2002 RPD, *supra* note 8, at art. 17; RPD, *supra* note 6, at art. 15(1).

209. RPD, *supra* Note 6, at art. 16.

210. See Council Directive 87/345/EEC, *supra* note 187, at arts. 24-24a.

211. See *id.* at art. 24a(5).

212. See Council Directive 89/298/EEC, *supra* note 4, at art. 21.

213. See *id.* at art. 24.

rities commission organizations") and the information requirements are equivalent as decided by the Commission to the requirements of the RPD.<sup>214</sup>

In general, the RPD places authority to supervise irregularities in the offering process on the home Member State. If a host country discovers irregularities or breaches of company obligations resulting from public trading, it must refer the matters to the home state. If the issuer persists in violating "the relevant legal or regulatory provisions," the host state may take enforcement action.<sup>215</sup>

## V. INVESTMENT SERVICES

### A. *Investment Services Directive — Current Law*

In 1993, the Council adopted the controversial directive on investment services.<sup>216</sup> The Investment Services Directive (ISD) provides for a home state license that will allow investment firms to provide in any Member State the investment services that are authorized by the home Member State.<sup>217</sup> An investment firm will be able to provide investment services directly or by establishing a branch in another Member State.<sup>218</sup> The following are "services" encompassed within the directive: receiving and transmitting, on behalf of investors, orders for securities (and other specified instruments); dealing in such securities or instruments for the firm's own account; portfolio management; and underwriting or placements.<sup>219</sup> The investment firm may render only those services specified in its

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214. See RPD, *supra* note 6, at art. 18(1). Under amendments passed by the European Parliament in March 2002, an issuer from outside the EU could file with the Member State where it intends to offer the securities or apply for a listing. See European Parliament Legislative, *supra* note 155, at amend. 16. The 2001 RPD establishes a procedure, ultimately involving the Article 22(2) comitology procedure, to resolve disputes concerning the equivalence of foreign disclosure requirements. 2001 RPD, art. 18. Under Article 18 of the RPD, member states must notify the Commission and other member states of rules adopted applicable to issuers from third countries. The Commission or other member states may raise an objection to the equivalence of the rules of third country. In this event, the Commission must subject the matter to the comitology procedure specified in Article 22(2), described above. Depending upon the outcome of this procedure, the RPD would extend the mutual reciprocity provisions of the RPD to issuers having their registered office in a third country who follow IOSCO standards. "In the case of offer or admission to trading of securities issued by an issuer incorporated in a third country in another member state the requirements set out under articles 15 [mutual recognition], 16 [language regime] and 17 [notification] shall apply." 2001 RPD, art. 18.

215. See RPD, art. 21(2), *supra* note 6; 2002 RPD, art. 23, *supra* note 8.

216. See Council Directive 93/22/EEC, *supra* note 50.

217. See *id.* at arts. 3, 12. An "investment firm" is any legal (as opposed to natural) person whose regular occupation or business is to provide any "investment service." *Id.* at art. 1, no. 2. Member states may consider natural persons to be "investment firms" under certain circumstances. See *id.*

"Investment service" is defined below. The "home Member State" is the Member State where the investment firm has its registered office, or its head office if it does not have a registered office. See *id.* at no. 6. If the investment firm is a natural person, the home Member State is the Member State where that person's head office is situated.

218. See *id.* at art. 14, no. 1. The procedures for establishing a branch and for providing services are set forth in Article 17 and 18, respectively.

219. Concerning services, which may be rendered, the exact language of the directive should be con-

authorization. If an investment firm is licensed to render any of the services indicated above (i.e., those referenced in Annex A to the ISD), the home state may also authorize the firm to provide certain "non-core services" (i.e., those specified in Annex C to the ISD).<sup>220</sup> The investment firm may provide the foregoing services with respect to transferable securities; units in undertakings for collective investment in transferable securities; money market instruments; financial futures contracts (including cash-settled instruments); forward interest-rate agreements; interest rate, currency and equity swaps; options on any of the foregoing, including options on currency and interest rates.<sup>221</sup> A controversial provision requires host Member States to grant access by investment firms from other Member States to membership of stock exchanges and "regulated markets" in their country.<sup>222</sup> This provision applies to banks as well as non-bank investment firms.<sup>223</sup> This provision also applies to regulated markets that operate without a physical presence.<sup>224</sup> As section one stipulates, "Member States shall abolish any national rules or laws or rules of regulated markets which limit the number of persons allowed access thereto."<sup>225</sup> Investment firms must have the choice of becoming members of regulated markets or having access thereto either directly, by setting up branches in the host state, or indirectly, through subsidiaries or acquisitions.<sup>226</sup>

Investment firms are required to be authorized by their home state but not the

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sulted. *See id.* at A.

220. *See* RPD, *supra* note 6, at art. 3(1). The non-core services include custodial, safekeeping and administrative services with respect to securities and other specified financial instruments; extending margin under certain circumstances; financial, investment and M&A advice; services related to underwriting; foreign exchange services related to investment services. For the precise non-core services, *see* Section C to the ISD Annex. "Authorization within the meaning of this Directive may in no case be granted for services covered only by Section C of the Annex." *Id.* at art. 3(1).

221. *See id.* at Section B. As stated above, pursuant to the Second Banking Directive, credit institutions will be able, among other things, to trade securities and participate in stock issues on the basis of their banking license, if authorized by the home state. A bank may provide these services on the basis of its banking license (if covered in its authorization) without obtaining additional authorization under the Investment Services Directive. Certain provisions of the Investment Services Directive would apply to such activities, however, *see id.* at art. 2, no. 1. For example, the "prudential" rules of the Investment Services Directive would apply to all institutions doing securities business, whether banks or non-banks. *See id.* at arts. 10, 11 (conduct of business), 2, no. 1.

222. *See id.* at art. 15. The right of access applies when investment firms are authorized for brokerage (execution of orders other than for own account) and dealing (dealing for own account). *See id.* The host state must also ensure that such investment firms have access to membership of clearing and settlement systems of the host state exchanges or markets which are available to members of such exchanges and markets. *See id.* A "regulated market" is a market for securities or certain other financial instruments that is so designated by the home state, functions regularly, and is regulated as described in Article 1, no. 13. *See id.* at art. 1, no. 13.

223. *See id.* at art. 2. Article 15 (among others) applies to credit institutions the authorization of which covers one or more of the investment services listed in Section A of the Annex. *See id.* at art. 2, no. 1.

224. *See id.* at art. 15, no. 4.

225. *Id.* at art. 15, no. 1. "If, by virtue of its legal structure or its technical capacity, access to a regulated market is limited, the Member State concerned shall ensure that its structure and capacity are regularly adjusted." *Id.*

226. *See id.* at art. 15, no. 2.

host state prior to providing investment services.<sup>227</sup> To obtain home state authorization, a person must apply to the home state, furnish a plan of operations, satisfy capital requirements,<sup>228</sup> and disclose the names of principal owners who must satisfy home state suitability requirements.<sup>229</sup> While the directive allows Member States to license subsidiaries of companies governed by the law of non-EU countries, it establishes a procedure similar to that of the Second Banking Directive for monitoring the treatment of EU investment firms in third countries.<sup>230</sup> Member States, subject to review by the Council, may limit or suspend the licensing of firms from third countries, except for the establishment of subsidiaries by investment firms already authorized in the EU or the acquisition of shares of EU firms by such previously authorized firms.<sup>231</sup> The ISD expressly allows Member States to license subsidiaries of companies governed by the law of non-EU countries.<sup>232</sup> Member states may not apply to branches of non-EU investment firms provisions that result in more favorable treatment than that accorded to branches of Member State investment firms.<sup>233</sup>

One of the purposes of the ISD was to ensure that non-banks not covered by the Second Banking Directive were not put at an unfair competitive disadvantage in relation to banks, which had the benefit of the European passport.<sup>234</sup> Indeed, many of the provisions of the ISD reflect the provisions of the Second Banking Directive.<sup>235</sup>

The ISD as adopted allows Member States to require transactions to be carried out in a "regulated market."<sup>236</sup> However, in this event, Member States must give residents the right not to comply with the requirement (subject to certain conditions), "and have the transactions carried out away from a regulated market."<sup>237</sup>

#### B. Possible Amendments to ISD

In November 2000, the Commission issued a Communication to the European Parliament and the Council regarding upgrading the ISD.<sup>238</sup> In the Communication, the ISD received a mixed report card. On one hand, the ISD has "eroded

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227. See RPD, *supra* note 6, at art. 3.

228. Capital requirements that will be applicable to investment firms are treated in the Capital Adequacy Directive.

229. See RPD, *supra* note 6, at arts. 3, 4.

230. See *id.* at art. 7.

231. See *id.* at art. 7, no. 5.

232. See *id.* at art. 7.

233. See Council Directive 93/22/EEC, *supra* note 50, at art. 5.

234. See The Securities Association, *Investment Services Directive: A Commentary and Analysis*, 16 (1989) [hereinafter Securities Association].

235. See Proposal for a Directive on Investment Services in the Securities Field, COM (88)778, at explanatory memorandum I.

236. See Council Directive 93/22/EEC, *supra* note 50, at art. 14, no. 3.

237. *Id.* at art. 14, no. 4.

238. See Communication from the Commission to the European Parliament and the Council, Upgrading the Investment Services Directive (93/22/EC), COM (00)729 final [hereinafter ISD Communication or Communication].

market segmentation at the level of investment firms and access to 'regulated markets.' Large numbers of firms have made use of the single passport."<sup>239</sup> According to the Communication,<sup>240</sup> there have been over 5,885 "notifications" under Article 18 of the ISD, which requires investment firms desiring to provide investment services in another Member State to notify its home Member State; the home state forwards the notification to the host Member State.<sup>241</sup> The ISD has also "dismantled official restrictions to membership of or access to regulated markets. . ."<sup>242</sup>

On the other hand, the Commission believes there are structural limitations at work which undermine the effectiveness of the ISD.<sup>243</sup> For example, it believes that the ability of the host country to intervene and regulate investment services should be much more circumscribed than it presently is.<sup>244</sup> In addition, the Commission observes numerous discrepancies in interpretation among the Member States, with respect to matters such as core service definitions, conduct of business principles, and designation of "regulated markets."<sup>245</sup> Accordingly, a "wide-ranging overhaul of the ISD is required to overcome these difficulties so as to seize unprecedented opportunities and rise to the challenges of the new securities trading environment."<sup>246</sup>

The Commission recommends a number of amendments to the ISD. First, it believes that the exemptions from the ISD set forth in Articles 2(2)<sup>247</sup> and 2(4)<sup>248</sup> should be reconsidered. Article 2(2) currently lists multiple exemptions from the ISD,<sup>249</sup> meaning that Member States are not required to recognize the passport for firms providing such services. In addition, the Commission calls for a re-assessment of whether any of the non-core services set forth in the ISD (i.e., Annex C to the ISD) should be upgraded to core services (i.e., those referenced in Annex A to the ISD).<sup>250</sup> Investment firms authorized by their home state to provide core services may provide such services directly or by establishing a branch

239. See ISD Communication or Communication, *supra* note 238, at art. 2.1.1.

240. See *id.* at annex, fig. 1a.

241. Under Article 18, the investment firm may then start to provide investment services in the host Member State, subject to conditions, including rules of conduct, established by the host Member State. See *id.* at art. 18.

242. *Id.* at art. 2.1.2.

243. See *id.* at art. 2.1.

244. See ISD Communication, *supra* note 238, at art. 2.2.

245. See *id.*

246. *Id.*

247. Council Directive 93/22/EEC, *supra* note 50, at art. 2(2).

248. *Id.* at art. 2(4). Article 2(4) exempts their central banks or other governmental bodies performing similar functions from the passport services provided to other Member States.

249. The Investment Services Directive does not extend to, among others, insurance companies, investment services rendered in an incidental manner in the course of other regulated professional activities, investment services rendered in the administration of employee participation schemes, central banks and other governmental bodies, investment companies, commodities traders who provide investment services ancillary to their main business, and brokerage firms which function as order-takers, do not hold client funds or securities, and provide brokerage services only to certain institutional customers. *Id.*

250. See *id.*

throughout the EU.<sup>251</sup> If an investment firm is licensed to render core services, the home state may also authorize the firm to provide certain non-core services.<sup>252</sup> However, a home state may not purport to authorize solely non-core services for purposes of the single passport for financial services.<sup>253</sup> Accordingly, upgrading activities which currently constitute non-core services to core services would allow sole authorization for such services.<sup>254</sup>

Another key area of Commission concern, as expressed in the Communication from the Commission, has to do with the application of conduct of business rules by the host country.<sup>255</sup> The Commission believes that host country authority must be more strictly confined, especially with respect to investment services provided to professional investors.<sup>256</sup> "Henceforth," the Commission stated "residual host country responsibilities must be strictly demarcated and should be confined essentially to conduct of business rules for fair dealing with retail clients."<sup>257</sup> The Commission also believes that it is time to reconsider the regulation of alternative trading systems in the EU.<sup>258</sup> Currently within the EU, alternative trading systems are authorized and regulated as investment firms.<sup>259</sup> It may be necessary to revise the ISD to supplement regulation of alternative trading systems with principles applicable to regulated markets (e.g., reporting, transparency and disclosure).<sup>260</sup> The ISD, in its current form, allows Member States to require transactions to be carried out on a "regulated market."<sup>261</sup> This provision is known as the "concentration rule."<sup>262</sup> The Commission believes it may be an appropriate time to review the continued rationale for this controversial rule.<sup>263</sup> The Commission also sought comments in several other areas relating to market regulation, such as whether ISD provisions on transparency can be upgraded.<sup>264</sup>

The European Parliament responded to the Commission Communication on

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251. See Council Directive 93/22/EEC, *supra* note 50, at annex A & C.

252. See *id.*

253. "Authorization within the meaning of this Directive may, in no case, be granted for services covered only Section C of the Annex." *Id.* at art. 3, no. 1.

254. See *id.* at art. 3.

255. See *id.*

256. See ISD Communication, *supra* note 238, at art. 3.2.

257. *Id.* at art. 3.2.

258. See Forum of European Securities Commissions (FESCO), Consultative Paper on Proposed Standards for Alternative Trading Systems, (2001).

259. See ISD Communication, *supra* note 238, at art. 3.3. This generally parallels historical treatment in the United States. Although historically, determinations were made on a case-by-case basis, the Commission tended to regulate alternative trading systems as broker-dealers. Ultimately, the Commission adopted new rules designed to regulate alternative trading systems. Exch. Act Release No. 40,760 (Dec. 8, 1998), 1998 WL 849548.

260. See ISD Communication, *supra* note 238, at art. 3.3.

261. See Council Directive 93/22/EEC, *supra* note 50, at art. 14, no. 3. However, in this event, Member States must give residents the right (subject to certain conditions) not to comply with the requirement "and have the transactions carried out away from a regulated market." *Id.* at art. 14, no. 4.

262. *Id.*

263. See ISD Communication, *supra* note 238, at art. 4.1.

264. See *id.* at list of issues for comment.

the ISD with a ringing endorsement.<sup>265</sup> The Parliament made the following points, among others, in its resolution endorsing revisions to the ISD.<sup>266</sup> In many respects, the Parliament's recommendations go significantly beyond those of the Commission in its Communication. In the resolution, among other things, the Parliament:

strongly supports the Commission's intention to upgrade the ISD, although it opposes "any attempt at wholesale redrafting of the original text". . .

suggests that the European passport system be extended to the "non-core services" set forth in Annex C to the ISD;

proposes that credit derivatives be added to the list of instruments as to which investment firms may provide services;

recommends in general home country regulation for both wholesale and retail investors, including in the case of conduct of business rules; host country restrictions should be introduced "parsimoniously";

suggests that with respect to wholesale investors, a "light regulatory system, applied exclusively by the country-of-origin, should be introduced immediately";

suggests that the EU agree upon a set of core standards applicable to retail investors;

recommends that a home country system for regulating conduct of business for retail customers be in place by January 1, 2002;

suggests the development of high level rules for the integrity of securities markets which would apply to institutions "whose character involved responsibility for the integrity of a trading system" (e.g., ATSS);<sup>267</sup>

recommends that the revised directive authorize regulatory authorities to apply portions of regulations for investment services firms or regulated markets to "institutions of mixed character, or to novel situations";

"demands that Article 14(3) of the Investment Service Directive be deleted." (i.e., the concentration rule).<sup>268</sup>

Given the positions of the European Commission and the Parliament, it is

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265. See European Parliament Resolution on the Commission Communication to the European Parliament and the Council on Upgrading the Investment Services Directive (93/22/EEC) COM (00)729.

266. See *id.*

267. See European Parliament Legislative Resolution, *supra* note 155.

268. See *id.*

highly likely that the ISD will be revised.<sup>269</sup> It is likely that the EU will move further toward home state regulation of investment services firms and away from host state regulation, particularly in the case of wholesale investors.<sup>270</sup> It is also likely that the EU will seek to change the “concentration rule,” although this will probably remain controversial. In November 2002, as this article went to press, the Commission published a proposal for a new directive on investment services and regulated markets.

## VI. INSIDER TRADING

### A. *Insider Dealing Directive — Current Law*

In November 1989, a directive on insider trading was adopted<sup>271</sup> which required Member States to prohibit specified persons who possess “inside information” from using that information “with full knowledge of the facts” by purchasing or selling transferable securities of the issuer to which the information relates.<sup>272</sup> This prohibition applies to any person who possesses inside information by virtue of his membership in the structure of the issuer, his share ownership, or his access to information through his employment, profession, or duties.<sup>273</sup> The directive also applies the prohibition to other persons who possess inside information the source of which “could not be other than” one of the previously enumerated persons.<sup>274</sup> The Member States must prohibit any such person from disclosing inside information to third parties outside the normal course of his employment or professional duties, or procuring another person on the basis of such information to purchase or sell securities admitted to trading on a securities market as specified in the directive.<sup>275</sup>

“Inside information” is defined in the directive as non-public information “of a precise nature” relating to an issuer or to securities, which, if public, “would be likely to have a significant effect on the price” of the securities in question.<sup>276</sup> The directive is applicable only to securities admitted to trading on a market which is regulated by “public bodies,” that “operates regularly,” and “is accessible directly or indirectly to the public.”<sup>277</sup> The Member States must apply the prohibitions of the directive, at a minimum, to actions undertaken “within its territory” if the securities in question are admitted to trading on a market in a Member State.<sup>278</sup> The

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269. See European Parliament Legislative Resolution, *supra* note 155.

270. See *id.*

271. Council Directive 89/592/EEC, *supra* note 55.

272. See *id.* at art. 2.

273. See *id.*

274. *Id.* at art. 4.

275. See *id.* at art. 3.

276. *Id.* at art. 1.

277. *Id.* art. 1.

278. See Council Directive 89/592/EEC, *supra* note 55, at art. 5. A transaction will be deemed to be within the territory of a Member State if carried out on a regulated market (operated regularly and accessible to the public) situated or operating within such territory. See *id.*



directive only applies to purchases or sales affected through a professional intermediary,<sup>279</sup> and it specifically permits Member States to exclude transactions effected without a professional intermediary outside a regulated market.<sup>280</sup>

The Insider Dealing Directive (IDD) also adopts a disclosure provision applicable to issuers of transferable securities. Article 7 applies one of the disclosure requirements of the Listing Conditions Directive<sup>281</sup> to all companies and undertakings, the transferable securities of which are admitted to trading on one of the markets covered by the IDD.<sup>282</sup> This provision specifies that the issuer must inform the public of any major new developments in its activities that are not public knowledge and which may lead to substantial movements in the prices of its shares.<sup>283</sup>

#### *B. 2001 Proposal for New IDD/Manipulation Directive*

On May 30, 2001, the Commission issued a proposal for a directive on insider dealing and market manipulation (market abuse).<sup>284</sup> The principal purpose of the new Directive is to establish common standards throughout the EU for market abuse, which includes market manipulation and insider trading.<sup>285</sup> Currently, there is no EU Directive concerning market manipulation, although there is a Directive concerning insider trading.<sup>286</sup> Although many European countries regulate market manipulation at the national level, national rules are inconsistent.<sup>287</sup> The purpose of proposing a new insider-trading directive is to apply to insider trading the same framework for allocation of responsibilities and enforcement applicable to manipulation.<sup>288</sup> In addition, it would be "administratively simpler and reduce the number of different rules and standards across the EU" to treat both topics under the same directive.<sup>289</sup> The newly proposed insider-trading directive is similar in substance to the current directive, although several provisions have been changed.<sup>290</sup>

The proposed IDD requires Member States to prohibit any person who possesses insider information from taking advantage of that information by acquiring

279. See Council Directive 89/592/EEC, *supra* note 55, at art. 2(3).

280. See *id.*

281. Council Directive 2001/34/EC, *supra* note 5, at annex, sched. C.5(a).

282. See Council Directive 89/592/EEC, *supra* note 51, at art. 7.

283. See Council Directive 2001/34/EC, *supra* note 5, at sched. C.5(a).

284. See Proposal for a Directive of the European Parliament and of the Council on Insider Dealing and Market Manipulation (Market Abuse), COM(01)281 final [hereinafter Proposed Insider Dealing Directive" or IDD]. See also Opinion of the European Central Bank, 2002 O.J. (C24/8). As this article went to press, the European Parliament approved the Commission's *Proposal on the Insider Dealing and Market Abuse Directive*, subject to substantial amendments, see *New Curbs on Insider Trading, Market Abuse Agreed to EU Parliament*, 34 SEC. REG. AND LAW REP., 32 (2002), and the measure subsequently was adopted.

285. See IDD, *supra* note 284 at General Comments.

286. See Council Directive 89/592/EEC, *supra* note 55.

287. See IDD, *supra* note 284, at Explanatory Memorandum, § 1(b).

288. See *id.* at Explanatory Memorandum, § 1(c).

289. *Id.*

290. See IDD, *supra* note 284, at Description of Arts., arts. 2-4.

or disposing for his own account or that of a third party financial instruments to which such information relates.<sup>291</sup> This prohibition applies irrespective of whether the person has obtained the information by being an officer, director, or shareholder of the company,<sup>292</sup> or by having access to the information through the exercise of his employment, profession, or duties.<sup>293</sup> The prohibition also applies to any other person "who with full knowledge of the facts possesses inside information."<sup>294</sup> Article 1 of the IDD sets forth the following definition of inside information:

"Inside information" shall mean information which has not been made public of a precise nature relating to one or more issuers of financial instruments or two one or more financial instruments, which, if it were made public, would be likely to have a significant effect on the price of the financial instruments or on the price of related derivative financial instruments.<sup>295</sup>

Member States must prohibit a person in any of the categories set forth above (officer, director, shareholder, or other person "with full knowledge of the facts") from disclosing inside information to a third party unless made in the normal course of his employment, profession or duties, or from procuring the third party to trade in financial instruments to which that information relates.<sup>296</sup>

If an issuer or its agent discloses inside information to another party in the ordinary course of his employment, profession or duties, the issuer must disclose such information, simultaneously in the case of an intentional disclosure, or promptly in the case of a non-intentional disclosure.<sup>297</sup> This provision, which might be called "European FD," does not apply where the recipient of the information owes a duty of trust to the issuer or expressly agrees to maintain such information in confidence, or if the recipient of the information is a rating agency.<sup>298</sup> An issuer may delay disclosure of such information provided it is not misleading to do so and the issuer is able to maintain confidentiality of the information.<sup>299</sup> Member States must require persons responsible for research to "take reasonable care to ensure that information is fairly presented and disclose their interests or indicate conflicts of interest in the financial instruments to which that information relates."<sup>300</sup>

The proposed IDD would regulate market manipulation in addition to insider trading. Specifically, Member States must prohibit any person from engaging in "market manipulation,"<sup>301</sup> which is defined as follows:

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291. See IDD, *supra* note 284, at art. 2(1).

292. Actually, the IDD uses the terminology of the IOSCO International Disclosure Standards, referring membership in the "administrative, management or supervisory of the issuer." *Id.*

293. See *id.*

294. See IDD, *supra* note 284, at art. 4.

295. *Id.* at art. 1(1).

296. See *id.* at art. 3.

297. See *id.* at art. 6(2).

298. See *id.*

299. See *id.* at art. 6(3).

300. *Id.* at art. 6(4).

301. *Id.* at art. 5.

Transactions or orders to trade, which give, or are likely to give, false or misleading signals as to the supply, demand, or price of financial instruments, or which secure by one or more persons acting in collaboration, the price of one or several financial instruments at an abnormal or artificial level, or which employ fictitious devices or any other form of deception or contrivance.

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 the supply, demand, or price of financial instruments, including the dissemination of rumors and false or misleading news.<sup>302</sup>

Annex B to the Directive provides a non-exclusive list of methods used for market manipulation.<sup>303</sup>

The IDD would require a Member State to apply the provisions specified therein "at least to actions undertaken within its territory whenever the financial instruments concerned are admitted, or going to be admitted, to trade in a Member State."<sup>304</sup> The IDD would repeal the Insider Trading Directive,<sup>305</sup> which the Council had adopted in 1989.<sup>306</sup>

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302. See IDD, *supra* note 284, at art. 1(2).

303. See *id.* at annex B.

304. *Id.* at art. 10.

305. Council Directive 89/592/EEC, *supra* note 53.

306. See IDD, *supra* note 284, at art. 19.