Kapittel 4

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The Benefits of an Integrated European Capital Market

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Introduction

Financial markets play an important role in the efficient allocation of financial resources, thereby enabling the economy to expand and develop optimally. The financial sector has not been able to realise its full potential because of fragmentation of markets.

However, in the last seven years, financial integration has really moved forward in Europe. The challenge now is to consolidate progress and ensure that the changes to date deliver real, tangible benefits for the citizens and businesses of Europe.

Expected benefits of an integrated financial market

The overall expected benefits of an integrated financial market in Europe consist of six elements:

1. Benefits of integration for international trade and cross-border investments
Financial integration will support the development of cross-border trade, both intra-EU and international. EU markets will become more attractive for domestic capital and foreign capital inflows, attracting inward investments. Liquid financial markets may provide EU companies easier pan-European access and provide them with the home base needed to expand across the EU and overseas.

2. Benefits for competition in the internal market
Financial integration will ensure a level playing field across the different markets, as well as foster competition between services providers, to the benefits of end-users in terms of lower

prices, improved quality and increased product variety.

3. Benefits for firms in terms of investment, operating costs, products and services
Financial integration will allow financial services companies to benefit from economies of scale and scope, leading to improved and more innovative products and services at lower prices.

In addition, in the non-financial sector, small and medium sized entities can access a wider availability of more innovative and lower cost finance to aid their growth, while larger companies profit from an overall reduction in the cost of capital and a wider range of financial products.

4. Benefits for firms in terms of administrative burden
Aligning national regulatory approaches to a common EU regulatory system is challenging and may entail considerable "*ex-ante*" adjustment costs for national enforcement agencies and market participants. However, over time, successful harmonisation can considerably reduce the administrative burden for pan-EU businesses, by replacing 25 sets of diverging rules by a single set.

5. Benefits for consumers
The impact of further integration on consumers is twofold. First, there is a direct effect of increased product variety, improved quality and lower prices. There is also an indirect positive impact. Through pooling of liquidity and risks across the EU financial markets and improved efficiency of capital allocation, consumers have access to wider investment opportunities, they can benefit from improved returns over a longer period, and from reduced financing costs.

6. Overall macroeconomic impact
Given its growth potential, its share of GDP and its role in financing other sectors of the economy, the financial services sector has a direct and decisive impact on the aggregate competitiveness of modern economies.

With integration, financial stability can improve. The public sector can meet its financing needs at lower cost. Integration supports society in financing the major structural economic challenge Europe faces – namely its long run pension deficit – by introducing more efficient pan-European markets for long-term savings products.

Steps taken to improve the single market in financial services

The EU single market for financial services has been under construction since 1973. In that year, two crucial judgments were issued by the European Court of Justice opening up the financial services market in Europe. Also in that year, the first Banking Directive and first Insurance Directive were launched. Yet, even by the late 1990's, Europe's financial markets remained fragmented – 15 local markets – and segmented. With the introduction of the euro, there was a unique window of opportunity to equip the EU with a more modern financial apparatus.

In recognition of this changing financial landscape the Commission published a Communication in which five priorities for action were highlighted:

1. the EU should be equipped with a legislative apparatus capable of responding to new regulatory challenges;
2. any remaining capital market fragmentation should be eliminated, thereby reducing the cost of capital raised on EU markets;
3. users and suppliers of financial services should be able to exploit freely the commercial opportunities offered by a single financial market, while benefiting from a high level of consumer protection;
4. closer co-ordination of supervisory authorities should be encouraged; and
5. an integrated EU infrastructure should be developed to underpin retail and wholesale financial transactions.

The Financial Services Action Plan

Based on these five priorities, the Commission came forward with a programme to promote rapid progress towards a single financial market, the Financial Services Action Plan (Action Plan), in 1999. EU Heads of State and Government called for the completion of the Action Plan by 2005 and the integration of the EU securities market by the end of 2003: a demanding, but necessary, timetable.

Effective and complete delivery of all 42 original measures of the FSAP was the only way to tackle the major areas of weakness[1].

Adjoining regulatory reform and supervisory cooperation

As progress was made in delivering the measures in the Action Plan, it became clear that framework legislation alone would not deliver the desired benefits. The Commission was the first EU institution to endorse the so-called “Lamfalussy” recommendations[2] for regulatory reform; a judicious combination of framework legislation, adaptable implementing measures, day-to-day regulatory and supervisory co-operation and convergence, and effective implementation and enforcement. The “Lamfalussy” approach is based on intensive and

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[1] Just over half of these were legislative measures, *i.e.* directives or regulations, with the remainder being mostly communications or recommendations from the Commission, which either set out planned actions in specific areas or made non-binding recommendations to Member States.

[2] European regulatory and supervisory process via a four-level approach: (1) framework legislation adopted in co-decision (between Council and European Parliament) at “level-1”, concentrating on the core political principles; (2) “level-2” implementing measures to fill in the details of “level-1” legislation subject to precise constraints fixed in that legislation; (3) day-to-day cooperation by national supervisors and regulators to ensure consistent implementation and enforcement; and (4) more effective enforcement of Community law. The Lamfalussy report, published on 15 February 2001, can be found on the Commission’s website:
http://europa.eu.int/comm/internal_market/securities/lamfalussy/index_en.htm.

continuous consultation of all stakeholders, cooperation between regulatory and supervisory authorities, underpinned by binding obligations to ensure coherent enforcement throughout the EU. The new approach is up and running in all financial services areas.

State of play of the Action Plan

Currently, 41 out of 42 measures of the Action Plan have been adopted, including major pieces of legislation of real benefit to European businesses, markets, investors and consumers. This represents an unprecedented achievement in European terms. To give just a few examples:

- The two Undertakings for the Collective Investment of Transferable Securities (UCITS) Directives and the Pension Funds Directive, giving investment and pension fund managers much greater freedom to invest and operate on a cross-border basis;
- The Market Abuse Directive, giving investors the confidence that markets will be effectively policed against manipulation or abuse of any kind;
- The Prospectus Directive, replacing 25 sets of requirements with a single set of documents, valid across the EU;
- The Markets in Financial Instruments Directive, enabling investment firms, banks and exchanges to provide their services across borders, allowing for processing of client orders outside of regulated exchanges and governing the level of investor protection;
- The Regulation moving EU listed companies to International Accounting Standards (IAS) by 2005, cutting costs for businesses and allowing investors to compare the results of companies on a like with like basis.

Regulations were used in the areas where it was essential for the proper working of their provisions that they were applied in exactly the same way in each Member State. Directives were used in other areas so that Member States were freer to reconcile achieving a level playing field for financial services in Europe with their national conditions[3].

The Action Plan and its economic benefits in terms of EU financial integration are more and more recognised as one of the pioneer, flagship areas for strengthening the EU's future growth and jobs. This was emphasised in the report from the High Level Group chaired by Wim Kok, published in November 2004:

> Dynamic and highly competitive financial markets are not only desirable in themselves – they are an essential driver of growth in all other sectors of the economy and must be a cornerstone of efforts to boost the EU's economic performance.

[3] Of the legislative measures in the original Action Plan, actually only two are Regulations (the Regulation on the European Company Statute and the Regulation on International Accounting Standards). The Regulation on Cross-Border Payments in euro was added later.

IAS Regulation

One measure of the Action Plan which has had an effect on all companies listed in the EU is the IAS Regulation. It has received much attention from the press, the EU institutions, Member States, companies and many other stakeholders and therefore deserves a closer look.

Comparable, transparent and reliable financial information is fundamental for an efficient and integrated capital market. Lack of comparability discourages cross-border investment because of uncertainty as regards the credibility of financial statements. EU companies should be able to raise capital throughout the EU using financial statements prepared on the basis of a single set of financial reporting requirements.

At the same time, capital-raising does not stop at the EU's frontiers: our companies may also wish to raise finance on international capital markets. So a solution was sought to both enhance comparability within the EU market and mirror developments in internationally accepted best practice.

International Accounting Standards (IAS)[4] were seen as the most appropriate bench-mark for such a single set of financial reporting requirements. After widespread consultation and with considerable political backing – the Regulation was approved in a first reading in the European Parliament in 2002.

Whilst the IAS Regulation has been effective since 1 January 2005 for all approximately 8,000 publicly traded EU companies when preparing their consolidated financial statements, effort is still required to ensure that the benefits of having a single set of standards across the EU are obtained. To this end it is important that issues regarding consistent application, interpretation and enforcement are addressed as they come to light.

The Committee of European Securities Regulators (CESR) plays the key primary role in relation to the coordination of enforcement decisions in different jurisdictions. Some broader arrangements were also needed to complement the work by CESR. That is why the Commission has set up a temporary, informal Roundtable which will discuss issues which give cause for common concern and can recommend which issues should be referred to the International Financial Reporting Interpretations Committee (IFRIC) of the International Accounting Standards Board.

The IAS Regulation envisaged the idea of globally accepted standards and since its adoption, this idea has developed. The US supervisor on financial markets, the Securities and Exchange Commission (SEC), issued, in April 2005, a "Roadmap" which describes the conditions which must be achieved if the reconciliation requirement to US GAAP for foreign issuers is to be dropped (*i.e.* mutual recognition of IAS/IFRS) at the earliest in 2007 and the latest 2009. The Roadmap contains two major conditions: (i) progress towards convergence of accounting standards; and (ii) consistent application and enforcement of IAS/IFRS. A decision will be made at the latest by 2009. The international and US standard setters

[4] They are also known as "International Financial Reporting Standards" (IFRS). These standards are elaborated by the International Accounting Standards Board (IASB), an independent organisation, which is based in London.

published a Memorandum of Understanding in February 2006, detailing their joint work programme. In parallel, the EU must make a determination of the possible equivalence of US GAAP to IFRS. Discussions are currently ongoing on whether this will be postponed until 2009 to align the timetables on both sides of the Atlantic.

White Paper on Financial Services Policy 2005–2010

The foundations for an integrated financial market in the EU were laid with the Action Plan. However, further pan-European financial integration needs to be achieved if the EU is to receive substantial benefits.

The new strategy for the next few years, contained in the December 2005 "White Paper on Financial Services Policy 2005–2010", has a strong focus on "delivering" the benefits of EU integration and on getting things done right; the focus is *not* on proposing new legislative measures.

The White Paper has four objectives:

- To consolidate an integrated, open, inclusive, competitive, and economically efficient EU financial market;
- To remove the remaining economically significant barriers so financial services can be provided and capital can circulate freely throughout the EU at the lowest possible cost – with effective levels of prudential and conduct of business regulation, resulting in high levels of financial stability, consumer benefits and consumer protection;
- To implement, enforce and evaluate continuously the existing legislation and to apply rigorously the better regulation agenda to future initiatives;
- To enhance supervisory cooperation and convergence, deepen relations with other global financial marketplaces and strengthen European influence globally.

Whilst with the Action Plan significant progress has been achieved to integrate the business-to-business or wholesale markets, financial services offered to consumers remain deeply fragmented. Here, a limited number of well-targeted new initiatives have been identified that could bring clear economic benefits to consumers, but also to the industry and markets at large.

Furthermore, considerable effort is being made on working with Member States on the timely and coherent implementation of the measures that have already been passed. This is crucial as a re-fragmentation of the European financial market or a dilution of what has already been achieved must be avoided.

To allow the financial market to function effectively, regulatory and supervisory mechanisms need to be strengthened and joined-up across Member States and the conditions to facilitate cross-border consolidation in the EU need to improve. This also implies further enhancing global cooperation in the financial field – across the Atlantic as well as the Pacific Ocean.

Conclusion

Integration of EU financial markets is the best way to stimulate competition within the European financial services industry and thereby the competitiveness of our industry in a global setting.

EU financial markets have come a long way over the last seven years in terms of integration, thanks to the measures contained in the Action Plan, the introduction of the euro and technological developments. Today, the EU is close to establishing a comprehensive framework which enshrines effective single market freedoms and common regulatory objectives in principles-based rules. The EU financial markets are open and reliable and the balance between economic freedom and investor protection is right.

However, the EU is still at a relatively early stage in unlocking the benefits of this framework. The focus of the Commission's strategy over the next few years is to concentrate on the implementation and enforcement of existing legislation; the consolidation of EU financial markets; and enhanced global cooperation. Only then we will be able to create the best financial framework in the world.