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**Towards a new Approach to Regulation and  
Supervision in the EU:  
Post-FSAP and Comitology**

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## **Abstract**

The aim of this paper is to analyse the progress made in the process of European integration from two points of view: regulation and supervision.

We first briefly outline the main steps in the development of the Financial Services Action Plan - FSAP and the process of Comitology, defined by the Committee of Wise Men (Lamfalussy Committee).

We then provide an initial evaluation of the new regulatory system, with its merits and flaws: while the definition and completion of the FSAP has been an undoubted success, some aspects still have to be dealt with, several of them with problematical connotations, considered in the Financial Services Agenda 2005-2010. The transposition into national regulations of a complex body of wide-ranging standards is a difficult process in terms of both times and procedures, although the functioning of the Comitology structure has been met with general approval.

There is also the problem of a supervisory structure which retains its national basis, but onto which the output generated by the Committees envisaged by the Lamfalussy process is gradually being grafted, possibly leading towards a new framework of controls at a European level.

*Key words: Single Financial Market, FSAP, Lamfalussy Report, Committee of Wise Men, Comitology, Regulation, Supervision, Eu directives, Financial Services Agenda 2005-2010.*

# 1 Introduction

Financial integration can be defined as a situation where there are no sources of friction discriminating between economic players with regard to accessing or investing capital, particularly as a result of their geographical origin<sup>1</sup>.

The achievement of financial integration implies the removal of the obstacles preventing the use of network externalities and the economies of scale and scope available to participants in an expanded market; it also allows the development of common rules, practices and standards for all participants and service providers.

The integration of financial services and markets is considered fundamental for the success of the European Union's economy, and a number of bodies of research have assessed the effects of financial integration. According to some theories, international financial integration facilitates the sharing of risk, increases specialisation, and improves the allocation of capital and economic growth<sup>2</sup>. Moreover, neo-classical theory maintains that international financial integration facilitates the flow of capital-poor economies, with positive effects. According to Levine<sup>3</sup>, another effect is the improvement of the efficiency of the domestic financial system, through the intensification of competition and the importation of more up-to-date financial services.

However, where distortions are already present, financial integration may retard growth. Boyd and Smith<sup>4</sup> show that in states with weak institutions and an inefficient policy line, which generates an unreliable legal system, integration may trigger an outflow of capital from these economies towards economies with better developed, more efficient financial systems.

In short, many benefits are forecast from European financial integration, for both investors and companies. Investors should benefit from an improvement in risk-adjusted earnings, thanks to the expanded opportunities for portfolio diversification and more liquid, competitive capital markets. In fact, increased competition amongst financial intermediaries offers firms a wider range of financial products, on more advantageous terms. A larger economic context improves the allocation of financial resources to support investment projects, with a positive impact on the level of equilibrium of the GDP, and potentially also on GDP growth rates.

During the last few years, Europe has been the stage for an ambitious action plan on the subject of financial regulation, the Financial Services Action Plan (FSAP), launched in 1999 to facilitate the construction of the single market in financial services within the European Union. The FSAP has been accompanied by the Lamfalussy process, which modifies the entire procedure for the approval of European legislation, with the intervention of regulatory and supervisory committees in specific phases, in a mechanism known as Comitology.

The aim of this paper is to analyse the evolution of financial regulation within the European Union, as it emerges from the Financial Services Action Plan (FSAP), the working of the Committee-based approach recommended by the Lamfalussy Committee's Report, and the implications for a supervisory function at the EU level.

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<sup>1</sup> See ECB, 2003, *THE INTEGRATION OF EUROPE'S FINANCIAL MARKETS*, MONTHLY BULLETIN, OCTOBER.

<sup>2</sup> See. OBSTFELD M., 1994, *RISK-TAKING, GLOBAL DIVERSIFICATION, AND GROWTH*, AMERICAN ECONOMIC REVIEW; ACEMOGLU, D., F. ZILIBOTTI, 1997, *WAS PROMETHEUS UNBOUND BY CHANCE? RISK DIVERSIFICATION, AND GROWTH*, JOURNAL OF POLITICAL ECONOMY.

<sup>3</sup> See LEVINE R., 2001, "INTERNATIONAL FINANCIAL LIBERALIZATION AND ECONOMIC GROWTH," *REVIEW OF INTERNATIONAL ECONOMIC*, 9, 688-702.

<sup>4</sup> See BOYD J.H., SMITH B.D., 1992, *INTERMEDIATION AND THE EQUILIBRIUM ALLOCATION OF INVESTMENT CAPITAL: IMPLICATIONS FOR ECONOMIC DEVELOPMENT*, JOURNAL OF MONETARY ECONOMICS.

To achieve this, first and foremost, after briefly outlining the aims and structures of the FSAP, we assess the work done so far and provide hypothesis concerning the development of the regulatory framework during the coming years, known as the Post-FSAP period: Financial Services Agenda 2005-2010.

In the next section, after running through the characteristics of the Comitology approach, we analyse the state of the art in the application of Comitology to the regulatory system of the FSAP, concentrating on the main securities sector Directives affected by this process: at this stage, the Market Abuse Directive (2003/6/EC) and its three technical implementing Directives (2003/124/EC, 2003/125/EC and 2004/72/EC) and the Prospectus Directive (2003/71/EC). In future, it will also cover the Market in Financial Instruments Directive ("MiFID", 2004/39/EC) and the Transparency Directive (2004/109/EC) as well as their implementing measures<sup>5</sup>.

To conclude, we provide brief comments about the possible evolution of the regulatory framework and of the supervisory architectures in Europe, on the basis of an initial assessment of the work done by the Committees, and the Committee of European Securities Regulators (CESR) in particular. At one extreme there is the maximum level of uniformity, to be achieved through the creation, at the Community level, of a single authority or even a number of authorities competent for the various sectors of the financial services industry; at the other extreme, at least greater co-ordination will be necessary between the national supervisory authorities, especially with regard to intermediaries active at the cross-border level. Between the various extremes there are a number of options, envisaging a growth in the importance of the Committees.

## 2 Post-Fsap

The Financial Services Action Plan (FSAP), presented by the Commission in 1999, identifies a series of measures considered necessary to complete the European single financial market; it comprises 42 measures of different kinds (Directives, Regulations and Recommendations) which refer to the various sectors of the financial services market: securities, banking, insurance, UCITS (Undertakings for Collective Investment in Transferable Securities) and pension funds.

All the Plan's legislative measures are based on the principles of minimal harmonisation, mutual recognition and home country control, adopting the usual methods for dividing regulatory competencies between European Institutions and member States.

The FSAP is a key document in the political process for the construction of a common regulatory framework for the European Union's financial markets, as reference framework for the new policy initiatives relating to the regulation of European capital markets and firms<sup>6</sup>, to be implemented before the end of 2005. This document, launched as already stated in 1999, was also drawn up with a view to the subsequent enlargement of the European Union, which took place in 2004.

Its contents and those of its accompanying reports also embrace topics such as fiscal, monetary and competition policy, giving it the connotations of a genuine system-wide document, setting itself clear strategic objectives with regard to:

- 1) a single wholesale capital market;
- 2) open, secure retail markets;
- 3) prudential and supervisory rules;
- 4) general objectives relating to a miscellaneous set of conditions necessary for the achievement of a single financial market<sup>7</sup>.

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<sup>5</sup> <http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/857&format=HTML&aged=0&language=EN&guiLanguage=fr>

<sup>6</sup> See THE EUROPEAN COMMISSION, 2004, FINANCIAL SERVICES, *TENTH PROGRESS REPORT*, JUNE.

<sup>7</sup> See EUROPEAN COMMISSION, 1999, FINANCIAL SERVICES: *IMPLEMENTING THE FRAMEWORK FOR FINANCIAL MARKETS: ACTION PLAN*, COM(1999)232, 11<sup>TH</sup> MAY.

The FSAP's innovative scope is due to the fact that it is a plan structured in relation to objectives to be pursued through the adoption of actions featuring a scale of priorities and the compliance with a specific set of deadlines:

- 1 – actions which have received broad consent;
- 2 – actions which adapt existing legislation or structures to the evolutions that have taken place on the financial markets;
- 3 - actions on topics on which debate is in progress.

As of today, 39 of the 42 measures envisaged have been launched, with an undoubted improvement in the regulation of the financial sector. The three missing measures are two in the area of Corporate Governance (10<sup>th</sup> Corporate Directive on cross-border merger operations; 14<sup>th</sup> Directive on transfers abroad) and one more, the most significant, concerning the adoption of a proposal for new capital adequacy measures for banks and investment companies (Basel 2): Capital Adequacy Directive, CAD 3.

However, the effects of the new regulations will only become apparent with time: many measures have only recently been adopted and have not yet been implemented in the various states. Therefore, while on the one hand the FSAP's regulations have still to bed themselves into national regulatory frameworks, on the other it is useful to assess the efficacy and speed with which the European regulatory process is being completed. Obviously, these two aspects are intrinsically inter-connected.

We have now entered the period known as Post-FSAP, covered by the regulatory agenda for 2005-2010<sup>8</sup>. The FSAP process was concluded at the start of the new European legislature. There is unanimous agreement on the decisive importance of the FSAP's contribution to the emergence of an all-inclusive legislative plan, aimed at the completion of the single market in financial services.

Most people accept that further legislation is not feasible, except maybe in a few areas, until the FSAP itself has first been "digested", i.e. until the regulations have been implemented in the various national contexts, with a clearer, more efficient division of labour between the various levels of the Lamfalussy process, giving market forces the opportunity to work with the new rules, put them to the test and develop responses to the obstacles to integration<sup>9</sup>. There is, in fact, a general awareness that, in the words of the Commissioner for the Internal Market Charlie McCreevy : "*Sequels to even the best originals tend to exhaust people's enthusiasm, so there will be no FSAP 2*"<sup>10</sup>.

In this area, in May 2005, the European Commission produced a "*Green Paper on Financial Services Policy (2005-2010)*" setting out the policy objectives in the field of financial services for the next five years. After consultation with market participants, which revealed broad support for these political priorities, a "*White Paper on Financial Services Policy (2005-2010)*" was issued in December 2005<sup>11</sup>. These documents recall the progress made towards an integrated financial market in Europe during 1999-2005, with the drafting of the FSAP, with regard to the legislative framework, and with the introduction of the Lamfalussy process with reference to the rationalisation of the decision-making process and regulatory structure.

For the future, the *leitmotif* of the Commission's approach is defined as "dynamic consolidation" and the focus of financial services policy priorities is placed on four main objectives: consolidating progress, completing unfinished business, enhancing supervisory cooperation and convergence

<sup>8</sup> See THE HIGH LEVEL GROUP – KOK GROUP, 2004, *FACING THE CHALLENGE, THE LISBON STRATEGY FOR GROWTH AND EMPLOYMENT*.

<sup>9</sup> AMONGST OTHERS, SEE: SPAVENTA L., BREUER ROLF-E., GREEN PAPER, FREIAAS ET AL..

<sup>10</sup> See: <http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/527&format=HTML&aged=0&language=EN&guiLanguage=en...>

<sup>11</sup> See EUROPEAN COMMISSION, 2005 GREEN PAPER ON FINANCIAL SERVICES POLICY (2005-2010), BRUSSELS, JUNE.; WHITE PAPER ON FINANCIAL SERVICES POLICY (2005-2010), BRUSSELS, DECEMBER;

and removing the remaining economically significant barriers<sup>12</sup>: The Commission will work with Member States to monitor progress, ensure accurate implementation and avoid regulatory addition, so-called “goldplating”.

Many of the key elements of the White Paper are of a practical nature and the Commission commits itself to a “Better Regulation” approach, by deploying the most open, transparent, evidence-based method of policy making, based on:

1- open consultation, including stakeholder groups, on any legislative proposal

2- impact assessments, in order to determine the most appropriate option, focusing on a costs and benefits analysis of any new Commission proposal

The various players in the process (European Commission, Member States, regulatory bodies and market participants) are required to contribute to the objectives set by the White Paper: Annex 1 presents an overview of the concrete tasks assigned.

The priorities identified within the 2005-2010 agenda pick up on some of the aspects found to be critical in the recent past: the use of consultation mechanisms at all levels with the aim of achieving a transparent decision-making process; simplification of financial regulations at both the European and national level; convergence of supervisory standards and practices (to be discussed in greater detail below) in compliance with the current institutional structure and political areas of jurisdiction; activities in cooperation with the Member States to improve the transposition of regulations, with coherent implementation; evaluation of the ability of the existing regulations to deliver the expected economic benefits, so called “impact assessment”, with the possibility of reviewing the ones which do not pass the test; and reinforcement of measures in case of violation proceedings. For an immediate overview of the Directives’ transposition status, see table 1.

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<sup>12</sup>See EUROPEAN COMMISSION, 2005, WHITE PAPER ON FINANCIAL SERVICES POLICY (2005-2010). SEE ALSO ANNEX I, ANNEX II AND ANNEX III TO THE WHITE PAPER, BRUSSELS, DECEMBER;

<b>TABLE 1: Transposition of FSAP Directives (State of Play 15/03/2006).</b>				
	<b>Transposition deadline</b>	<b>Done</b>	<b>On going</b>	<b>Partially notified/ no notification received</b>
Directive on E-Money Institutions	27 April 2002	25		
Directive amending the Insurance Directives and the ISD to permit information exchange with third countries	17 November 2002	25		
Directive on the reorganisation and winding-up of banks	05 May 2004	21	1	3
Directive on the reorganisation and winding-up insurance undertakings	20 April 2003	25		
Directive amending the 4th and 7th Company Law Directives to allow fair value accounting	01 January 2004	17	6	2
Directive supplementing the Statute for a European Company with regard to the involvement of employees	10 October 2004	12	8	5
Directive amending the Money Laundering Directive	15 June 2003	23	1	1
Directive on Insurance Mediation	15 January 2005	18	1	6
Directive on Conglomerate	11 August 2004	19	1	5
Directive on Market Abuse	12 October 2004	12	9	4
Directive on the taxation of savings income in the form of interest payments	01 January 2004	25		0
Modernisation of the accounting provisions of the 4th and 7th Company Law Directives	01 January 2005	16	5	4
Prospectus Directive	01 July 2005	0	21	4
Two directives on UCITS (D 2001/107/EC - D 2001/108/EC)	13 August 2003	25		
Directive on the prudential supervision of pension funds	23 September 2005	12		13
Two directives amending the solvency requirements in the Insurance Directives (D 2002/83/EC - D 2002/13/EC)	20 September 2003	25		
Directive on financial collateral arrangements	17 December 2003	24	1	
Directive on the distance marketing of Financial Services	09 October 2004	20	0	5
Directive on Markets in Financial Instruments (update of ISD)	30 April 2006	0	0	25
Directive on Take-Over Bids	20 May 2006	0	0	25
Transparency Directive	20 January 2007	0	0	25
Legend: in yellow the Directives for which the transposition deadline already passed				
Source: our elaboration on European Commission, Internal Market, Financial Services, Action Plan				

The agenda also identifies specific areas on which the Commission is to concentrate its attention. First and foremost, the process of consolidation of cross-border financial operators, the level of which, as revealed by assessments of the integration process's progress, is disappointingly low.



Secondly, special attention will be focused on the level of application of European regulations by the new Member States.

Finally, with regard to forthcoming measures in the financial services area, a Green Paper on Asset Management was published in July 2005 on the existing legislation governing UCITS, currently managing over 5 trillion euro of assets, and the problem of transposing it correctly, with an evaluation of the existing system's adequacy for the protection of retail investors, also considering the profound structural changes in the asset management industry<sup>13</sup>. A White Paper is due by the second half of 2006, aiming at improving the single market framework and eliminating hitches in the functioning of the UCITS passport.<sup>14</sup>

Another topic on the 2005-2010 agenda to receive top priority concerns the sector assessed as least integrated: retail financial services<sup>15</sup>. While the FSAP focused mainly on the wholesale market, retail integration is to be fostered from now on. In this area, the Commission intends to draw up a limited number of actions aimed at eliminating the most significant cross-border barriers and risks for consumers:

Payments area: the proposal for a Payments Services Directive was adopted by the Commission on the 1<sup>st</sup> December 2005, aiming at the creation, by 2010, of a Single European Payment Area (SEPA) with payments as easy and convenient throughout the Eurozone as they are domestically today;

Consumer credit: with the aim of creating a true internal market for consumer credit and improving consumer protection, a modified proposal for a Directive was published on 10<sup>th</sup> October 2005;

Mortgage credit: necessary, economically justified measures for the integration of the EU market will be announced by a White Paper in 2006.

### 3 The Comitology Process

While on the one hand the FSAP has the undoubted merit of having completed the preparation of the regulatory framework necessary for the effective exercise of freedom of establishment and to provide services within the European Union<sup>16</sup>, on the other, although it was produced with a clearly defined set of aims and priorities, by its very nature it could not and cannot bring about the financial single market in itself. In order to achieve this aim, attention was simultaneously focused on the decision-making and procedural process for European regulations.

With this in mind, and with specific reference to the securities sector, on 17 July 2000 the EU Economic and Finance Ministers created a Committee of independent experts, known as the Wise Men Committee, chaired by Baron Alexander Lamfalussy, with the task of assisting the European Commission, with three main objectives<sup>17</sup>:

- ? to assess the conditions for implementation of the regulation of the securities markets in the European Union;

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<sup>13</sup> FOR A CRITICAL ANALYSIS OF THIS TOPIC SEE V. VENTURELLI, 2005, , *Profili Regolamentari del Comparto dell'Asset Management*, in G. N. Mazzocco (Editor) *Asset management: prospettive di convergenza tra banche e assicurazioni. Profili regolamentari e gestionali*, Giappichelli, Torino

<sup>14</sup> See McCreevy 2005, *Recent Developments in The Internal Market for Financial Services and Financial Reporting; 2006, The next steps to financial Europe*

<sup>15</sup> See: EUROPEAN COMMISSION, 2005, WHITE PAPER ON FINANCIAL SERVICES POLICY (2005-2010). SEE ALSO McCreevy 2005, *Recent Developments in The Internal Market for Financial Services and Financial Reporting; 2006, The next steps to financial Europe; 2006 Financial Market Integration*

<sup>16</sup> SEE ECB, 2004, MONTHLY BULLETIN, NOVEMBER.

<sup>17</sup> See COMMITTEE OF WISE MEN, 2000, *THE INITIAL REPORT ON THE REGULATION OF EUROPEAN SECURITIES MARKETS*, BRUSSELS, NOVEMBER.

- ? to assess how the mechanism for regulating the securities markets in the EU can best respond to the changes underway on these markets, while still guaranteeing their effective and dynamic operation, to achieve a regulatory level playing field;
- ? to eliminate barriers and obstacles by proposing scenarios for the adaptation of current practices in order to ensure greater convergence and cooperation in day-to-day implementation, taking new developments in the market into account.

The report<sup>18</sup> of the Wise Men Committee, or Lamfalussy Committee, approved the FSAP approach, but nevertheless highlighted the risk that the measures it contained might not be implemented with the necessary speed and to the necessary standards. In order to benefit from an integrated capital market, it is essential to have a regulatory system with clear, well-defined objectives, which operates more efficiently and is flexible enough to adapt to the continuous, rapid, deep-seated changes involving the operators, products and financial markets.

The analysis conducted by the Wise Men Committee revealed that the regulatory system failed to meet these requirements. Level by level, it found that:

- ? at the level of primary regulations, the process for the adoption of Directives was often too slow. Even when political problems did not arise, it took three years on average to agree a Directive or a Regulation. Such a time-scale was unacceptable when legislation was meant to bring an appropriate response to a fast-changing world;
- ? the search for a political consensus sometimes led to the adoption of ambiguous texts or texts with levels of harmonisation so low that no real integration was achieved;
- ? too many delays were occurring in the implementation of legislation by individual Member States.<sup>19</sup>

The solution proposed by the Wise Men Committee to solve these problems was the adoption of a different approach to regulatory and supervisory procedures, on four levels, all involving the European Commission, but backed up by different bodies in each context (figure 1). The Comitology structure, initially proposed for the securities industry and subsequently extended to the other financial sectors, is based on different types of Committee: Regulatory and Supervisory, with different tasks in the various levels. The Regulatory Committees assist the Commission in its regulatory function, with the aim of streamlining legislative procedures and making them more efficient. The Supervisory Committees provide the Commission with technical advice with regard to second level legislation, with reference to the contents of implementation measures.

In the first place, the structure proposed recognises two levels in the legislation for the regulation of financial markets, with legislative powers balanced and attributed to different bodies:

- ? Level 1: basic political choices relating to principles that can be translated into broad but sufficiently precise framework norms; within a politically negotiated joint decision-making process, these choices are made by the European Council and Parliament, acting on the recommendations of the Commission<sup>20</sup>.

<sup>18</sup> See COMMITTEE OF WISE MEN, 2001, *THE FINAL REPORT ON THE REGULATION OF EUROPEAN SECURITIES MARKETS*, BRUSSELS, FEBRUARY.

<sup>19</sup> THE PROBLEM OF THE TRANSPOSITION SPEED OF DIRECTIVES IS CONSTANTLY MONITORED. THE TRANSPOSITION DEFICIT SHOWS THE PERCENTAGE OF DIRECTIVES FOR WHICH NOTIFICATION OF TRANSPOSITION HAS NOT BEEN RECEIVED, COMPARED TO THE TOTAL DIRECTIVES ISSUED FOR WHICH THE DEADLINES HAVE PASSED. ACCORDING TO THE LATEST STATISTICS AVAILABLE, THE TRANSPOSITION DEFICIT CONCERNING ALL DIRECTIVES ON THE INTERNAL MARKET HAS WORSENED SIGNIFICANTLY AND AVERAGES 3.6%. THIS FIGURE IS WELL AWAY FROM THE INTERMEDIATE TARGET OF 1.5% AND THE REAL TARGET OF 0%. FOR FURTHER DETAILS SEE *COMMUNICATION FROM THE COMMISSION TO THE COUNCIL, THE EUROPEAN PARLIAMENT, THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE AND THE COMMITTEE OF THE REGIONS – SECOND IMPLEMENTATION REPORT OF THE INTERNAL MARKET STRATEGY 2003-2006*. BRUSSELS, 27.01.2005.

<sup>20</sup> IN ACCORDANCE WITH THE TREATY OF AMSTERDAM, THE SIMPLIFIED JOINT DECISION-MAKING PROCEDURE SHARES DECISION-MAKING POWERS EVENLY BETWEEN THE EUROPEAN PARLIAMENT AND THE COUNCIL. AN ACT OF LAW IS APPROVED IF IT RECEIVES THE CONSENT OF THE COUNCIL AND THE PARLIAMENT AT ITS FIRST READING. IF THESE TWO INSTITUTIONS ARE IN DISAGREEMENT, A "CONCILIATION COMMITTEE" CONSISTING OF AN EQUAL NUMBER OF MEMBERS OF THE PARLIAMENT AND THE COUNCIL MEETS, WITH THE COMMISSION PRESENT, TO AGREE A COMPROMISE TEXT WHICH THE COUNCIL AND THE PARLIAMENT CAN SUBSEQUENTLY APPROVE. IF THIS MECHANISM FAILS TO GENERATE AN AGREEMENT, THE PARLIAMENT CAN REJECT THE PROPOSAL COMPLETELY WITH

? Level 2: more detailed technical measures (second level legislation), which make the achievement of the objectives pursued by the legislation possible, in full conformity with the framework principles defined in level 2. The Commission is required to use the technical advice of the competent Supervisory Committee, working on the mandate of the Commission itself, which also consults market participants. This is followed by the qualified majority vote of the Member States represented on the competent Regulatory Committee. The European Parliament must be kept constantly informed and may issue a resolution if the intended measures are in excess of the powers delegated to the Committee; once the final text has been drafted, the Parliament has one month to check that the powers defined in level 1 have not been exceeded<sup>21</sup>.

Subsequently, the Lamfalussy Committee proposes two additional levels:

- ? Level 3: based on the input of the competent Supervisory Committees, it has the task of ensuring the uniform, coherent transposition of first and second level legislation into national law. These Committees, consisting of representatives of the national supervisory bodies, draw up guidelines and best practices for the administrative regulations to be adopted at the national level, as well as issuing joint interpretative recommendations, even on matters not covered by specific EU legislation. This modus operandi aims to assure a very high degree of supervisory and regulatory convergence among Member States.
- ? Level 4: aims at strengthening the Commission's control over the application of EU legislation. If necessary, the Commission brings legal proceedings against defaulting Member States before the Court of Justice.

The Committees' current structure (Figure 1) is the outcome of a number of measures. Initially, in fulfilment of its mandate, which focused on the securities industry, the Wise Men Committee planned to introduce two Committees, one Regulatory, the European Securities Committee (ESC) and the other Supervisory, the Committee of European Securities Regulators (CESR).

In view of the success of the *ESC* and the *CESR*, in November 2003 the Commission decided to extend the Comitology approach to the other sectors of the financial services industry. In fact, the foundations for this extension had already been laid by the Report of the Wise Men Committee, which had the undoubted merit of reaching beyond its mandate, covering the securities markets, and making a general analysis of factors hindering the achievement of the single market, which affected the various sectors of the financial services industry in different ways and to different extents. These aspects included fragmentation, high transaction costs, regulatory differences and consumer safeguards, as well as problems relating to regulation and supervision.

Reinforcing this approach, in 2000 the Brouwer I Report<sup>22</sup> had highlighted the need to act to improve supervision at the European level, in particular by reinforcing cooperation with regard to large financial groups, improving the exchange of information between the various supervisory authorities and with central banks, and working on the convergence of supervisory practices. In 2001, the Brouwer II Report<sup>23</sup>, on crisis management, confirmed the need for closer cooperation between national supervisory authorities in order to prevent and properly manage systemic crises.

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AN ABSOLUTE MAJORITY. THE JOINT DECISION-MAKING PROCESS STRENGTHENS THE ROLE OF THE PARLIAMENT SINCE IT BECOMES A JOINT LEGISLATOR, AND IS APPLIED TO A WIDE RANGE OF TOPICS.

<sup>21</sup> See COMMITTEE OF WISE MEN, 2001, *FINAL REPORT ON THE REGULATION OF EUROPEAN SECURITIES MARKETS*. BRUSSELS, FEBRUARY, PAGE 36.

<sup>22</sup> See ECONOMIC AND FINANCIAL COMMITTEE, 2000, *SOUND EU SUPERVISORY STRUCTURES AND PRACTICES ("BROUWER I REPORT")*, JANUARY.

<sup>23</sup> See ECONOMIC AND FINANCIAL COMMITTEE, 2001, *REPORT ON FINANCIAL CRISIS MANAGEMENT ("BROUWER II REPORT")*, APRIL.

The Comitology structure was expanded in 2003 with the issue of a draft Directive<sup>24</sup> proposing the creation, at levels 2 and 3, of sectorial committees competent for the various sectors of financial intermediation. The new regulatory Committees are: the *European Banking Committee (EBC)* for the banking sector, the *European Insurance and Occupational Pensions Committee (EIOPC)* for the insurance industry and pension funds and the *European Financial Conglomerates Committee (EFCC)* for financial conglomerates<sup>25</sup>. Like the *European Securities Committee* for the securities sector before them, their task is to assist the Commission in adopting the implementing measures for their respective sectors: banking, insurance and pension funds, and financial conglomerates.

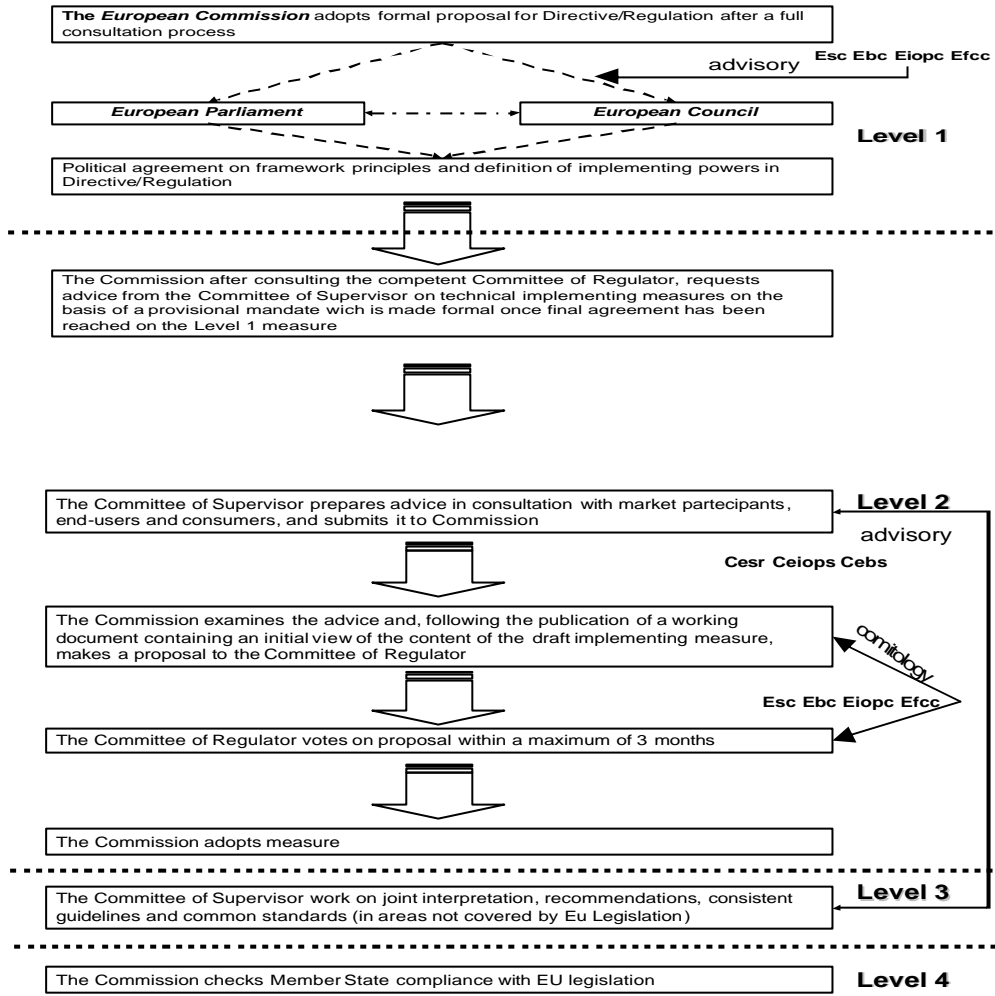
In the area of Supervisory Committees, the *Committee of European Banking Supervisors (CEBS)* and the *Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS)* have been established alongside the *CESR*.

**Figure 1: The Lamfalussy process: the four -level regulatory structure**

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<sup>24</sup> See COM(2003) 659 DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL AMENDING COUNCIL DIRECTIVES 73/239/EEC, 85/611/EEC, 91/675/EEC, 93/6/EEC AND 94/19/EC AND DIRECTIVES 2000/12/EC, 2002/83/EC AND 2002/87/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL, IN ORDER TO ESTABLISH A NEW FINANCIAL SERVICES COMMITTEE ORGANISATIONAL STRUCTURE, 5 NOVEMBER 2003.

<sup>25</sup> See COMMISSION DECISION 2004/5/EC of 5.11.2003 ESTABLISHING THE COMMITTEE OF EUROPEAN BANKING SUPERVISORS, COMMISSION DECISION 2004/6/EC of 5.11.2003 ESTABLISHING THE COMMITTEE OF EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS SUPERVISORS, COMMISSION DECISION 2004/7/EC of 5.11.2003 ESTABLISHING THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS, COMMISSION DECISION 2004/8/EC of 5.11.2003 ESTABLISHING THE EUROPEAN SECURITIES COMMITTEE, COMMISSION DECISION 2004/9/EC of 5.11.2003 ESTABLISHING THE EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS COMMITTEE, COMMISSION DECISION 2004/10/EC of 5.11.2003 ESTABLISHING THE EUROPEAN BANKING COMMITTEE.



Legend

	Securities	Banks	Insurance Companies	Financial Conglomerates
<b>Regulatory Committees Level 2</b>	European Securities Committee	European Banking Committee	European Insurance and Occupational Pensions Committee	European Financial Conglomerates Committee
<b>Supervisory Committees Levels 2 &amp; 3</b>	Committee of European Securities Regulators	Committee of European Banking Supervisors	Committee of European Insurance and Occupational Pensions Supervisors	

Competence in relation to UCITS has been assigned to the ESC and the CESR<sup>26</sup>.

In practice, the new procedural structure is grafted onto an existing process, known as *Comitology*, already in use at the EU level, which is thus reinforced at the institutional level, giving it greater visibility

## 4 The State of the Art in Comitology

An initial evaluation of the new regulatory structure can be derived from the analysis of the procedure followed for four new Directives relating to the securities sector, the first sector to be subjected to the effects of Comitology, as we have seen, on the recommendations of the *Lamfalussy* group. These cover Market Abuse, Prospectuses, the Market in Financial Instruments and Transparency.

The work done is clearly set out in the Third Report of the Inter-Institutional Monitoring Group (established in 2003 and consisting of a group of independent experts, with the task of assessing the progress made in application of the Lamfalussy method) and the CESR reports.<sup>27</sup> Market participants have used these documents as the basis for their comments and criticisms<sup>28</sup>. As things now stand, an effective analysis can be performed on the first two levels and some comments can be provided on the third level, but for the fourth level no useful evaluation can be made until the relative regulations have been incorporated into national legislation and start to have their first effects.

### 4.1 Levels 1 and 2

The results of the analysis, which are however only partial, are contrasting and reveal that the approach adopted has brought both benefits and drawbacks.

The most interesting aspects concern an examination of the speeding-up of the legislative process, the efficacy of the work done and the precision with which tasks were split between the first two levels.

With regard to the first aspects, the time which passed between the presentation of the drafts of the first three Directives and their approval (policy agreement for the fourth), i.e. level 1, averaged 16.5 months (Table 2)<sup>29</sup>. Level 2 has only been completed for the Market Abuse and Prospectus Directives, for which the time granted for technical and detailed aspects was 18 months. The legislative procedure for these two Directives (from presentation of the draft proposal to the date set for implementation in national legislation) was 41 and 35 months respectively. A comparison with the times taken in the past between presentation of the draft and publication in the EU Official Gazette points to a substantial improvement: 4.5 years for the Investment Services Directive in 1993, and 9 years for a previous Prospectus Directive in 1989, while other Directives did manage to pass all the hurdles more quickly: 2.5 years for the Insider Dealing Directive in 1989, 3 years for the Interim Reports Directive which opened the way to the Transparency directive, and finally 3.5 years for the UCITS Directive in 2002. The signs of an acceleration in the legislative procedures, which are still not completely satisfactory, can be attributed to a number of factors: the deadlines

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<sup>26</sup> Venturelli V., 2005, *Profili Regolamentari del Comparto dell'Asset Management*, in G. N. Mazzocco (Editor) *Asset management: prospettive di convergenza tra banche e assicurazioni. Profili regolamentari e gestionali*, Giappichelli, Torino

<sup>27</sup> See INTER-INSTITUTIONAL MONITORING GROUP, 2004, *THIRD REPORT MONITORING THE LAMFALUSSY PROCESS*, BRUSSELS, 17 NOVEMBER; THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS, 2004, *THE ROLE OF CESR AT "LEVEL 3" UNDER THE LAMFALUSSY PROCESS*, ACTION PLAN FOR 2005, PARIS, OCTOBER.

<sup>28</sup> See: <http://www.cesr-eu.org/>

<sup>29</sup> See. INTER-INSTITUTIONAL MONITORING GROUP, 2004, *THIRD REPORT MONITORING THE LAMFALUSSY PROCESS*, BRUSSELS, NOVEMBER.

set by the FSAP, the use of systematic consultation mechanisms, and the application of the approach by levels which concentrates the key principles in level 1.

Even if the results for the first two levels can be considered partially satisfactory, extremely discouraging signs are emerging from the only case in which level 3 should have been concluded: there has been a complete failure to meet the schedule for implementation of the Market Abuse Directive (Directive on insider dealing and market manipulation - 2003/03/EC), which none of the 25 states had adopted by the date of 12 October 2004<sup>30</sup>. As of July 2005 sixteen countries had given notification of its implementation (seven already checked by the Commission), two had given partial notification, while seven had given no notification at all. As of March 2006, twenty-one countries had given notification of its implementation (twelve already checked by the Commission), two had given partial notification, while two had given no notification at all (see Annex 2).

There is therefore an obvious problem in timing, and alongside this there are also fears concerning Member States' ability to transpose EU law into national legislation correctly and accurately; verification of this point must focus on the work done in level 3.

Directive	Date of presentation	Agreement	Time	Time for level 2	Dead line for implementation	Total time
Market Abuse	30 May 2001	28 January 2003	20 months	18 months	12 October 2004	41 months
Prospectus	30 May 2001, amended on 9 August 2002	4 November 2003	15 months	18 months	1 July 2005	35 months
Market in Financial Instruments (MiFID)	19 November 2002	21 April 2004	18 months	24 months	30 April 2006	--
Transparency	26 March 2003	12 May 2004 political agreement	14 months	--	--	--

SOURCE: our elaboration on Inter-Institutional Monitoring Group, 2004, Third Report Monitoring the Lamfalussy Process, Brussels, November.

The second point of interest regards the effectiveness of the work done in the first two levels. The main critical factor appears to be the division of labour between the first level, responsible for defining the basic principles, and the second level, where the technical details of norms are thrashed out. It is not always easy to distinguish between these two areas, and thus there is a risk that technical factors will be discussed at level 1: from the first years of application of the process it emerges that the opinions of the various members of the European Parliament, and the market participants, may vary considerably with regard to what is a principle and what is a technical aspect.

Experience has shown that the degree of detail introduced in level 1 of a Directive, and thus the borderline between basic principles and technical rules, is determined by the political joint decision-making process. It is therefore more a political than a legal matter, settled by negotiations between the Commission, the Council of Ministers and the European Parliament<sup>31</sup>. The level of detail included in level 1 increases for very controversial topics, on which there has been constant pressure from various national interest groups, with the result that the primary legislation has contained technical aspects which should have been left to level 2.

There are two possible consequences: firstly, the entire structure of the Lamfalussy process may be put in jeopardy, while secondly, excessive detail at level 1 conflicts with the aim of achieving speed and flexibility in the legislative process, because any subsequent amendments become lengthy, problematical affairs, depending on the time-consuming political joint decision-making process, rather than the work of the Committees.

<sup>30</sup> See Inter-Institutional Monitoring Group, 2004, *Third Report Monitoring the Lamfalussy Process*, Brussels, November.

<sup>31</sup> See FERRARINI G., 2005, *CONTRACT STANDARDS AND THE MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE MiFID. AN ASSESSMENT OF THE LAMFALUSSY REGULATORY ARCHITECTURE*, ERCL 1.

The debate has involved both academics and market participants. According to some<sup>32</sup>, the fact that it has not proved possible to prevent the discussion of technical aspects in level 1 is simply a political fact of life, and although it contradicts the basic approach of the entire process, it should decrease with time; in any case, the system is considered sufficiently robust to withstand a certain amount of rule-breaking in the allocation of legislative questions. Others<sup>33</sup> affirm that the system has gone too far in inserting excessive details in level 1, because as a consequence the first two levels end up regulating factors which should be assigned to the third. Those in this camp cite the case of the *MIFID*, in which they claim there was a substantial re-regulation of the rules of conduct for securities firms, with negative effects on private autonomy, giving the system forms of rigidity in obvious conflict with the original spirit of the Lamfalussy process. The problem, they state, derives not so much from the new regulatory framework, as from the European institutions' unwillingness to delegate powers to the levels downstream of level 1.

Market participants express a fear of over-regulation in general, especially at level 1, which they state should be avoided in favour of flexibility, trusting in the market's capability for self-regulation. They therefore generally point to the need to strike a careful balance when selecting the aspects to be assigned to the first three levels, giving due consideration to the different status and authority of the players involved.

In the final analysis, on the basis of events so far, an improvement in the distinction between the different roles and tasks of levels 1 and 2 is one of the most urgent problems if the aim is to achieve a flexible, coherent set of regulations for the securities sector also capable of facilitating cross-border transactions. It is therefore necessary for level 1 to deal strictly with guiding principles only, leaving greater scope for the subjects discussed at level 2<sup>34</sup>.

Another problematical aspect of the work done so far is that, with the aim of speeding up the CESR's proceedings in level 2, in some cases proceedings have been conducted simultaneously, with the mandate conferred on the CESR before the completion of level 1. Conducting the first two levels simultaneously rather than consecutively has allowed the CESR's consultations with market participants to take place more quickly, while also making more time available for this operation. However, this methodology may mean that the approaches adopted at level 2 influence the decisions to be taken at the first level. Basically, there is a risk of blurring the distinction between the policy and technical levels, giving the latter inappropriate influence over the former.

One suggestion to emerge from consultations with market participants is that work should only be conducted simultaneously on those points of principle for which the level 1 policy decision has already been taken.

The market participants' comments on their direct involvement in this initial period of operation of the Lamfalussy process are also worthy of further consideration. While in general the participants are in favour of the Comitology approach, there is no lack of criticism of various aspects of the work done so far, especially the fact that Directives are still too complex. It also emerges that in general the role played by market forces is seen as insufficient and ineffective.

Firstly, the market participants' own direct involvement in the level 2 consultations is often judged to be insufficient, as is their contribution to the drafting of the rules. One commentator even claimed that market participants should be assigned the task of judging the regulation's impact and deciding the speed with which changes should be introduced.

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<sup>32</sup> See FERRAN E., 2004, *BUILDING AN EU SECURITIES MARKET*, CAMBRIDGE UNIVERSITY PRESS (CIT. IN FERRARINI).

<sup>33</sup> See FERRARINI G., 2005, *CONTRACT STANDARDS AND THE MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE MIFID. AN ASSESSMENT OF THE LAMFALUSSY REGULATORY ARCHITECTURE*, European Review of Contract Law, 1/2005

<sup>34</sup> See ECB, 2004, *THE INTEGRATION OF THE SINGLE MARKET FOR FINANCIAL SERVICES: THE EUROSISTEM PERSPECTIVE*, KEYNOTE SPEECH BY JEAN-CLAUDE TRICHET, PARIS, 6 DECEMBER; *REVIEW OF THE APPLICATION OF THE LAMFALUSSY FRAMEWORK TO EU SECURITIES MARKET LEGISLATION*, 17 FEBRUARY 2005.



Participants also highlight a lack of attention to the new rules' impact on them, especially in terms of the costs of compliance. Moreover, consultation times are often considered to be too short, with a failure to agree them with participants. One common comment was that too much emphasis has often been placed on the speed of the legislative process, at the expense of the quality of the regulations produced. Therefore for the future, in the "post-FSAP" period we will be discussing in greater detail in our conclusions, there is a demand for more attention to quality, especially since the planned regulatory system is now virtually complete and the focus will shift to its implementation.

#### 4.2 Levels 3 and 4

Level 3 concerns Member States' implementation of the legislation produced in the first two levels. Its importance is clear, since the success of the Lamfalussy process is strongly dependent on the rapid, accurate, coherent transposition of EU legislation into national law. Otherwise, there may be a failure to create a level playing field, with obvious negative knock-on effects for the construction of the single market<sup>35</sup>.

The Committee most active at level 3 is currently the CESR<sup>36</sup>, engaged on the Market Abuse Directive and the Prospectus Directive. And it is from the CESR's documents themselves that we can trace the lines along which this Committee is working to ensure uniform implementation of securities sector regulations and the critical points encountered<sup>37</sup>:

1. the coordinated implementation of EU legislation in the Member States, with regard to both the incorporation of Directives into national law and rules for their application on a day to day basis. The main problem here appears to be that the various national bodies do not have the same powers. All modifications in this area have to be made by national governments;
2. regulatory convergence, with the production of shared approaches and standards to facilitate harmonised implementation, through the issue of guidelines, recommendations and standards, which however do not have the status of EU law. They are only adopted by the supervisory authorities on a voluntary basis;
3. convergence in the performance of supervisory activities and the fulfilment of the tasks assigned by European regulations. Above all, this objective requires cooperation and the efficient exchange of information between the various national authorities. The Monitoring Group goes further, encouraging the CESR to act as mediator in case of disagreement between the authorities of different states. There is the possibility of failure to reach an agreement, on specific topics linked to the principle of mutual recognition, between the authorities of the country of origin and the host country; such cases might be resolved by mediation between equals, i.e. the CESR members. In addition, it may suggest an expansion of the context of joint interventions, such as inspections and investigations for market participants working cross-border, training activities, and the establishment of databases, enabling the national supervisory authorities to make joint interpretations and decisions and perhaps generating a body of EU jurisprudence in the future.

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<sup>35</sup> See INTER-INSTITUTIONAL MONITORING GROUP, THIRD REPORT MONITORING THE LAMFALUSSY PROCESS, BRUSSELS, 17 NOVEMBER 2004.

<sup>36</sup> THE CEBS AND CEIOPS HAVE ALSO STARTED TO FUNCTION, BUT STILL IN A VERY LIMITED WAY. THE CEBS IS WORKING TO ACHIEVE THE COHERENT IMPLEMENTATION OF BASEL 2; SEE ECB, 2004, DEVELOPMENTS IN THE EU FRAMEWORK FOR FINANCIAL REGULATION, SUPERVISION AND STABILITY, MONTHLY BULLETIN, NOVEMBER.

<sup>37</sup> SEE THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS, 2004, THE ROLE OF CESR AT "LEVEL 3" UNDER THE LAMFALUSSY PROCESS, ACTION PLAN FOR 2005, PARIS, OCTOBER, ALSO SEE INTER-INSTITUTIONAL MONITORING GROUP, 2004, THIRD REPORT MONITORING THE LAMFALUSSY PROCESS, BRUSSELS, 17 NOVEMBER.

The CESR has also made considerable efforts during this initial period to achieve a better definition of its context of operation. These lines of discussion have generated a fertile debate on the possible development of the role of the CESR as European supervisory authority, a point to be covered in our concluding section.

As already stated, it will not be possible to make an assessment of the flexibility and coherence of level 4 until most of the FSAP measures have been implemented in the individual states and it is possible to test their coherence. However, it is clear that the development of level 4 depends to a large extent on the evolution which takes place in level 3.

## 5 The Supervisory Structure in Europe

The approach to financial supervision in Europe is another major factor in the construction of the single market. Financial integration is facilitated by the regulatory framework defined by the FSAP, and by the single currency for 12 states, but another essential precondition is a high degree of convergence, if not actual standardisation, of the supervisory function, still in the hands of national governments.

The definition of the FSAP, a body of regulations with extremely broad scope, was one necessary step towards integration: the legislative stage alone took five years to complete, and will probably require further measures, as already mentioned, but this in itself is not enough.

The problem which now arises is that of the implementation of the European legislation in the Member States, and we have already seen the failure of the time-scale to come up to expectations in the first "test" case, that of the Market Abuse Directive. Another problem concerns the procedures by which European regulations are transposed into national legislation and the quality of the implementation process. The fear is that differences may emerge between the way in which market participants are treated by the supervisory bodies in the various states, with obvious negative repercussions in terms of fair competition and effective financial integration, if operators should be impeded from obtaining uniform access to markets, or in case of discrimination on the basis of country of origin.

This fear derives from the fact that within the Union of 25, while cross-border business is growing and the compartmentalisation of the financial services industry is being reduced, there are a range of profoundly different regulatory and supervisory models. The European Union is home to no less than 60 bodies responsible for supervising markets and intermediaries, with widely varying institutional nature, powers and areas of jurisdiction, while some states have a single authority and others several operating simultaneously<sup>38</sup>.

This may hinder the completion of the single market, because the fragmentation of the supervisory bodies and areas of jurisdiction increases the cost of regulation and may generate uncertainty amongst market participants, discouraging the development of cross-border operations. Secondly, it may prove ineffective in preventing systemic risk, as the ever-increasing interconnections at the cross-border level may tend to amplify crises occurring on specific markets, with obvious repercussions on investor safeguards<sup>39</sup>.

The Lamfalussy process has begun to change the structure of supervision in Europe from the status quo of the late Nineties by introducing the Supervisory Committees which operate, at level

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<sup>38</sup> See CENTRE FOR EUROPEAN REFORM, 2004, *OVER BUT FAR FROM FINISHED, THE EU'S FSAP*, SEPTEMBER; VARIOUS AUTHORS, 2004, *REGULATION AND SUPERVISION OF FINANCIAL INSTITUTIONS AND MARKETS. A EUROPEAN PERSPECTIVE*, PAPER PRESENTED AT EFMA ANNUAL MEETING, BASEL, MIMÉQ, JUNE, PAGE 7. THE SURVEY COVERS EU 25.

<sup>39</sup> See ECB, 2004, *DEVELOPMENTS IN THE EU FRAMEWORK FOR FINANCIAL REGULATION, SUPERVISION AND STABILITY*, MONTHLY BULLETIN, NOVEMBER

three, with the aim of achieving regulatory and supervisory convergence. However, it must be remembered that this is a minimal objective, in a situation still based on supervision at the national level. And it is from this state of affairs, and an initial assessment of the first Supervisory Committee to become operational, the CESR, that we can begin to sound out the feasibility of further steps forward, analysing the options for the securities sector emerging from the ongoing debate involving the European Commission, academics, the CESR itself, the ECB and market participants.

At one extreme of the range of hypotheses put forward lies the maximum degree of uniformity, to be achieved through the creation, at the EU level, of a single authority or even a number of authorities with jurisdiction over the various sectors of the financial services industry. The other extreme envisages better coordination between the national supervisory authorities, above all for intermediaries engaging in cross-border operations. Between these two extremes there are a range of alternative options, assigning a growing level of importance to the Committees themselves<sup>40</sup>.

When assessing the various proposals, it must be remembered that the problem of the regulatory approach appears to be political rather than theoretical and is by no means easy to solve. Events have shown that European financial integration is not always the top priority of national governments, as in spite of public statements and affirmations of principle, they often opt for the defence of national interests, meaning those of their own intermediaries and markets<sup>41</sup>. We need only consider the well-known contrast between the British and continental regulatory models. British financial market participants claim that they would be placed at a competitive disadvantage by the creation of a regulatory authority based on the continental approach, while the continental states tend to fear that a body operating on the British principles would work to the advantage of London as a financial centre.

Since, as things now stand, the debate on the structure of controls in Europe is mainly inspired by the activities undertaken for the regulation of the securities industry, it is useful to base these brief comments on contributions made by the CESR itself, especially the so-called *Himalaya Report*<sup>42</sup>. According to the CESR, the Committee's current structure might evolve by adapting the supervisory instruments already envisaged to provide an appropriate response to changes in the markets, i.e. without the creation of new bodies. The conditions required for this to come about depend basically on two factors: the status and powers both of the national authorities which make up the CESR and of the CESR itself.

With regard to the first aspect, it should be remembered that the Directives introduced as part of the FSAP place heavy additional obligations on the national authorities with regard to cooperation. They therefore have to be provided with equivalent powers and resources to enable them to operate uniformly and rule out the risk of regulatory arbitrage. Reference is made to the power to supervise, investigate and impose penalties, and to exchange information, all in relation to the subject which is the target of supervision. These aspects are fundamental for the functioning of the relations between the authorities in the financial intermediary's country of origin and those of the host country, since the principle of mutual recognition might become ineffective as cross-border activities expand. National authorities might therefore receive additional legal powers to allow them to work together, overcoming a problem of *accountability* which arises in level 3. The responsibility for making the necessary changes in this area lies with the individual Member States.

With regard to the second aspect, the legal bases for the functioning of the CESR, and the other supervisory committees, are weak: they set rules, but without any legal and institutional mandate to

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<sup>40</sup> ON THIS DEBATE, SEE IN PARTICULAR: BREUER R-E., FERRARINI G., CALZOLARI M., FREIAX X., HARTMAN P., MAYER C., TRICHET J.C..

<sup>41</sup> See. BREUER ROLF-E, 2004, *THE FUTURE OF EU FINANCIAL MARKET INTEGRATION: A POST-FSAP AGENDA*, SUERF 11<sup>o</sup> ANNUAL LECTURE 25 NOVEMBER, AMSTERDAM

<sup>42</sup> See THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS, 2004, *PRELIMINARY PROGRESS REPORT. WHICH SUPERVISORY TOOLS FOR THE EU SECURITIES MARKET? AN ANALYTICAL PAPER BY CESR*, PARIS, OCTOBER.

do so, meaning that they function as a network on a mainly voluntary basis. This generates a further problem of accountability. The priority proposed is to expand the cooperation agreements within the regulatory framework established by the FSAP, in order to reinforce the relationships between the various states' authorities and improve the convergence of supervisory and decision-making approaches.

Finally, the CESR foresees a development of its role, still within regulatory restrictions, as "supervisor of national supervisors", meaning that it would formally be assigned additional supervisory powers. This option points to a role for the CESR very different from that envisaged by the Lamfalussy Committee, and has received a very mixed response, especially from market participants. On the one hand, they agree on the need for a stronger role, but only for the CESR as advisor to the national authorities and a centre for the exchange of information, envisaging a system of mediation between national authorities, as also suggested by the Inter Institutional Monitoring Group<sup>43</sup> On the other hand, as things now stand there is no consensus on the suggestion that the CESR should be awarded powers which allow it to exercise functions of governance over the individual national supervisory authorities, for which there is however no formal mandate. The role of the CESR is therefore seen as that of a network of evolving supervisory authorities: on this head the Fédération Bancaire Européenne (FBE) refers to a role as "coordinator of supervisors", rather than as "supervisor of supervisors"<sup>44</sup>.

A gradual but sweeping proposal for an effective, efficient supervisory function at the European level is put forward in the May 2005 European Commission Green Paper, which outlines an approach structured in three stages for the period 2005-2010<sup>45</sup>. The aim is that of effective regulation and supervision, which guarantees financial stability while minimising the costs of regulation for systems, intermediaries and markets. The "three-step evolutionary approach" has been largely supported by market participants in the consultation phase; the subsequent White Paper does not really add to the analysis in the Green Paper and its Annex 1, while reaffirming that convergence of supervisory practices is seen by the Commission as a key task in the next 5 years.<sup>46</sup>

1. The first stage concerns agreement on policy objectives overall: the further development of competition, in order to continue along the path marked out by the Lisbon Agenda and in the maintenance of financial stability.
2. The second stage requires the continuation and improvement of the Lamfalussy process, identifying the weak or missing points and developing the existing instruments. Special attention is paid to the avoidance of overlaps or conflicts in case of cross-border operations. Since the principle of home country control is to be retained, it becomes necessary to clarify and strengthen the roles and responsibilities of the national supervisory bodies by working on the convergence of supervisory practices, in compliance with the existing European legislation.
3. The last phase, or we might say the last solution, envisages that, if the existing system clearly proves incapable of moving towards supervisory convergence, there will be a shift to the creation of new supervisory structures.

Various commentators identify supervision for cross-border activities as a critical factor, since it is here that the principle of home country control may prove ineffective. In this area, the creation of a lead supervisor may overcome the problems of duplication of controls, but it is definitely no solution to the problem of nationally based supervision in relation to the attempt to establish a truly integrated, stable financial market. One suggestion is for two supervisory levels, with only small

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<sup>43</sup> See INTER-INSTITUTIONAL MONITORING GROUP, 2004, *THIRD REPORT MONITORING THE LAMFALUSSY PROCESS*, BRUSSELS, 17 NOVEMBER.

<sup>44</sup> See FEDERATION BANCAIRE EUROPEENNE (FBE), 2005, *RESPONSE TO CESR'S PRELIMINARY PROGRESS REPORT: "WHICH SUPERVISORY TOOLS FOR THE EU SECURITIES MARKETS? AN ANALYTICAL PAPER BY CESR"*, OCTOBER 2004.

<sup>45</sup> See EUROPEAN COMMISSION, 2005, *GREEN PAPER ON FINANCIAL SERVICES POLICY (2005-2010)*, BRUSSELS, JUNE. SEE IN PARTICULAR: ANNEX 1, SECTION 3.

<sup>46</sup> See EUROPEAN COMMISSION, 2005, *ANNEX III TO THE WHITE PAPER*, BRUSSELS, DECEMBER;

intermediaries working at the domestic level still subject to the supervision of the national authorities. For intermediaries working at the pan-European level, this proposal envisages the creation of a European System of Financial Supervision, similar to the ESCB for monetary policy, which would act as supreme authority for the interpretation and implementation of regulations in case of conflicts between national authorities<sup>47</sup>.

In the final analysis, it is obvious that the single market requires not only a single regulatory framework, but also a single supervisory system. How to achieve this, and what structure to give it, are problems it is not easy to solve, involving the various stakeholders, all called upon to play an interactive role.

First and foremost, the policy makers: on the one hand national governments, reluctant to surrender their sovereignty and subject to pressure from the market participants, and on the other hand the framers of European policy, who end up negotiating compromises between the various national demands.

Secondly, the CESR, and in the future the other Committees, which seems to have difficulty in functioning due to the influence and pressure brought to bear by the other players in the integration process. The Committee process underway is by no means perfect, but the time does not appear ripe for a leap forward to a more independent, authoritative role. If the Committees' work were to prove successful, this would leave room for market forces to determine the supervisory and regulatory approach. Otherwise, at an unspecified time in the future, we might be faced with a centralised solution, with a single regulatory and supervisory authority at the European level<sup>48</sup>.

The market participants represent another interest group. Its proposals are sometimes incoherent, because they reflect national models which differ in terms of operating practices and supervisory models, with a varying degree of willingness to proceed rapidly along the path towards integration.

Last but not least, it is important not to overlook the ECB's interest in the evolution of a supervisory function at a European level, to safeguard financial stability and the proper operation of the mechanisms for the transmission of monetary policy.

In our view, the time is not yet ripe for a pan European solution, which might be the most effective in operational terms from the theoretical point of view, but for which there is no legal basis. We are faced with a political and cultural problem, which might be solved most easily by a step-by-step approach founded on a broad consensus, concentrating on the evolution of the role of the Committees, fully exploiting the potential of the Lamfalussy process and allowing market forces to make their contribution to the emergence of a European supervisory model. The limitations of this solution are however clear: first and foremost, the times needed to complete a step-by-step approach and the difficulty in achieving progress by this method.

It must be remembered that the fast-evolving financial markets often place a premium on quick, flexible responses. While on the one hand the European supervisory structure should evolve along the lines outlined to assist in the completion of the single market, on the other hand the very process of integration itself may generate the most pressing, convincing arguments for supervision in line with its evolution.

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<sup>47</sup> See BREUER ROLF-E, 2004, *THE FUTURE OF EU FINANCIAL MARKET INTEGRATION: A POST-FSAP AGENDA*, SUERF 11<sup>o</sup> ANNUAL LECTURE 25 NOVEMBER, AMSTERDAM

<sup>48</sup> See FREIXA X., HARTMAN P., MAYER C., 2004, *THE ASSESSMENT: EUROPEAN FINANCIAL INTEGRATION*, IN OXFORD REVIEW OF ECONOMIC POLICY, VOL. 20. NO. 4

## Annex 1: Concrete tasks or activities contained in White Paper Financial Services

	What	Who	When
<b>BETTER REGULATION – CONSULTATION AND IMPACT ASSESSMENTS (2.1 / 2.2)</b>			
1)	Transparent consultation procedures	European Commission	ongoing
2)	Ex ante evaluations (impact assessments) in preparation of all new proposals	European Commission	ongoing
3)	Ex ante evaluations (impact assessments) in preparation of significant level-2 measures	European Commission	ongoing
4)	Ex ante evaluations (impact assessments) in preparation of substantive amendments to European Commission proposals	European Parliament and Council	ongoing
<b>IMPLEMENTATION AND ENFORCEMENT (2.3)</b>			
5)	Improve timely and accurate transposition and enforcement of EC Directives	Member States	ongoing
6)	Update transposition matrix of FSAP measures (web-site)	European Commission	ongoing
7)	Complete transposition matrix with hyper-links to national transposing legislation	European Commission	10/2005 until 02/2006
8)	Convene and run transposition workshops	European Commission	ongoing
9)	Publication summary notes of transposition workshops and interpretative guidance for transposition	European Commission	ongoing
10)	Launch infringement procedures in case of faulty transposition and incorrect enforcement	European Commission	ongoing
11)	Set adequate (aligned) transposition time for level-1 and level-2 measures	European Commission, European Parliament and Council	ongoing
<b>EX-POST EVALUATION (2.4)</b>			
12)	Publication of Financial Integration Monitor Report	European Commission	annually
13)	Assistance to the Inter-Institutional Monitoring Group	European Commission	2005-2007
14)	External study on impact of FSAP (measuring empirical and economic effects)	European Commission	2007-2008
15)	Workshop with economic experts (as input for full evaluation of FSAP measures)	European Commission	autumn 2006
16)	Ex-post evaluations of all new legislative measures	European Commission	4 years after transposition
<b>SIMPLIFICATION, CODIFICATION AND CLARIFICATION (2.5)</b>			
17)	Setting up and running an Advisory Committee to assist the European Commission in the Economic and legal evaluation of securities legislation	European Commission	2005 and beyond
18)	Running of Legal Certainty Group in the area of Clearing and Settlement, consisting of practitioners and market experts: support work of the network and ensure secretariat	European Commission	2005 and beyond
19)	Consistency check on information requirements and marketing and distribution requirements in financial services legislation: launch of external study	European Commission	2008
20)	Communication/Recommendation on marketing of investment funds	European Commission	2006
21)	Solvency II – codification of Insurance Directives + technical work on modernising solvency requirements	European Commission	ongoing; proposal 2007

<b>USERS OF FINANCIAL SERVICES: INPUT, EDUCATIONS AND REDRESS (2.6)</b>			
22)	FIN-USE: support work of the group and ensure secretariat	European Commission	Ongoing 6/7 meetings per year
23)	Conference to discuss financial education and consumer literacy	European Commission	Early 2007
24)	Periodic newsletter pointing to ongoing work/initiatives of relevance for consumers/users/SME's	European Commission	2006 and beyond; twice a year
25)	Establishment and running of Financial Services Consumer Group (representatives from all MS)	European Commission	2006; 2/3 meetings per year
26)	Continuation of regular contacts with UNI-EUROPA (Trade Unions – financial services employees)	European Commission	Ongoing; twice a year
27)	FIN-NET: support work of the network and ensure secretariat	European Commission	Ongoing; 2 meetings per year
28)	FIN-NET: Task Force with a view to maximise FIN-NET's efficiency	European Commission	Ongoing; 2-3 meetings
29)	Dolceta project: web-based tool for educational institutions, governments to use for financial training	European Commission	Ongoing
30)	Investigation of redress systems in the area of financial service in place in Member States	European Commission	2006
<b>FURTHER REINFORCING THE INTERACTION WITH OTHER POLICY AREAS (2.7)</b>			
31)	Reinforcing interaction with other policy areas, e.g. competition, consumer policy and taxation.	European Commission	ongoing
32)	Fiscal Compliance Experts' group in area of Clearing and Settlement: support work of the group and ensure secretariat	European Commission	ongoing
<b>ENSURING THE RIGHT EC REGULATORY AND SUPERVISORY STRUCTURES – MAKING THE LAMFALUSSY PROCESS WORK (3.1)</b>			
33)	Aim at permanent inter-institutional stability to maintain the Lamfalussy arrangements	Council, European Parliament and European Commission	Ongoing
34)	Improve the accountability and transparency applied in the Lamfalussy process	Supervisory Committees: CEBS, CEIOPS, CESR, while informing the European Commission	Ongoing
35)	Develop cross-sectoral regulatory cooperation	Regulatory Committees: EBC, EIOPS, ESC	Ongoing
36)	Consultation + ex ante evaluations (impact assessments) in preparation of draft advice to the European Commission	Supervisory Committees: CEBS, CEIOPS, CESR	2006 and beyond
<b>SUPERVISORY CHALLENGES (3.2)</b>			
37)	Assessment of roles and responsibilities of home/host supervisors	European Commission in co-op with	Ongoing

		respective Supervisory Committees: CEBS, CEIOPS, CESR	
38)	Study on liquidity management in banks and Member States' prudential requirements	European Commission	2006
39)	Communication on Deposit Guarantee Schemes (including impact assessment)	European Commission	mid-2006
40)	Explore delegation of tasks and responsibilities between supervisors	Supervisory Committees: CEBS, CEIOPS, CESR	Ongoing
41)	Conference on Supervisory Convergence in the banking sector	European Commission in co-op with CEBS and banking industry	2007
42)	Mediation mechanisms at supervisory level	Supervisory Committees: CEBS, CEIOPS, CESR; in co-op with the European Commission	Ongoing
43)	Improving efficiency of supervision by common data and reporting templates	Supervisory Committees: CEBS, CEIOPS, CESR	By 2008
44)	Deliver common decision-making and enforcement practices (joint inspections, peer reviews, staff exchanges, joint training, exchange of information/expertise)	Supervisory Committees: CEBS, CEIOPS, CESR	By 2010
<b>FUTURE INITIATIVES – ONGOING PROJECTS (4.1)</b>			
45)	White Paper on mortgage credit	European Commission	End 2006
46)	Concrete actions in mortgage credit (follow-up White Paper)	European Commission	2007 and beyond
47)	Modified proposal for a Consumer Credit Directive	European Commission	2005
48)	Proposal for a Payments Directive	European Commission	End 2005
49)	Examination if further measures are necessary to ensure a Single European Payments Area	European Commission	By 2007
50)	Proposal for a Solvency II Directive	European Commission	Mid-2007
51)	Revision of Art. 16 Banking Directive	European Commission	proposal by mid-2006
52)	Revision of Art. 15 Insurance Directive	European Commission	In parallel to revision Art. 16 BD; in context of Solvency II work
53)	(possible) initiatives on Clearing and Settlement	European Commission	2006
<b>REFLECTIONS UNDERWAY (4.2)</b>			
54)	(possible) follow up actions after ECOFIN discussions on x-border consolidation	European Commission	2006 and beyond
55)	Report on the functioning of the E-money Directive	European Commission	spring 2006
56)	(possibly) Insurance Guarantee schemes	European Commission	A decision will be taken 1 <sup>st</sup> half 2006



57)	Legal assessment on the Hague Securities Convention	European Commission	Ongoing
58)	Optional instruments ("26 <sup>th</sup> regime"): ongoing work on CFR and impact assessment on optional instruments	European Commission	2005 and beyond
59)	Optional instruments ("26 <sup>th</sup> regime"): possible forum group, once more groundwork has been done, based on a specific product	European Commission	Possibly in 2006
<b>FUTURE INITIATIVES (4.4)</b>			
60)	White Paper on investment funds	European Commission	autumn 2006
61)	Regulation to clarify the definitions of eligible assets for UCITS	European Commission	2006 and beyond
62)	Communication on marketing of UCITS	European Commission	2006 and beyond
63)	Other concrete actions in investment funds (follow-up White Paper)	European Commission	2007 and beyond
64)	Expert group on Bank Accounts	European Commission	early 2007
65)	External study, assessing whether EU-level action on bank accounts is advisable	European Commission	end 2007
66)	Studying access to banking services throughout the EU	European Commission	2006 and beyond
67)	Work on Credit Intermediaries, building on evaluations of insurance and securities intermediation: study	European Commission	2008
<b>THE EXTERNAL DIMENSION (V)</b>			
68)	Strive for an ambitious opening of global financial services markets in the WTO	European Commission	ongoing
69)	Further deepening the Financial Markets Regulatory Dialogue with the US	European Commission	ongoing
70)	Widen dialogues and cooperation with other countries, including Japan, China, Russia and India	European Commission	ongoing
71)	Improve representation and manage co-ordination of EU-positions in international bodies	European Commission	ongoing
<b>MONITORING PROGRESS (VI)</b>			
72)	Publication of annual Progress Report to monitor progress and main developments in financial services	European Commission	December 2005 + every year

Source: European Commission, White Paper on Financial Policy 2005-2010, Bruxelles, 5 December, 2005

## Annex 2. Lamfalussy League Table – Transposition of Lamfalussy Directives – State of play 15/03/2006.

Lamfalussy League Table		Transposition of Lamfalussy Directives - State of play as at 2/03/2006																										
CP: partially notified to the Commission		NC: no notification received by the Commission										EX: notification received and under examination by the Commission										OK: notification received and checked by the Commission*						
Directive	Number	Transposition deadline	AT	BE	CY	CZ	DE	DK	EE	EL	ES	FI	FR	HU	IE	IT	LT	LU	LV	MT	NL	PL	PT	SE	SI	SK	UK	
Directive on insider dealing and market manipulation	Directive 2003/6/EC	12/10/04	OK	CP	EX	CP	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX
Commission Directive implementing Directive 2003/6 as regards the definition and public disclosure of inside information and the definition of market manipulation	Directive 2003/124/EC	12/10/04	OK	CP	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK
Commission Directive implementing Directive 2003/6 as regards the fair presentation of investment recommendations and the disclosure of conflicts of interest	Directive 2003/125/EC	12/10/04	OK	CP	EX	NC	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX
Commission Directive implementing Directive 2003/6 as regards accepted market practices, the definition of inside information in relation to derivatives on commodities, the drawing up of list of insiders, the notification managers' transactions and the notification of suspicious transactions	Directive 2004/72/EC	12/10/04	OK	CP	EX	CP	OK	EX	OK	EX	CP	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	OK	EX	CP	OK	EX	OK
Directive on prospectuses	Directive 2003/71/EC	1/07/05	EX	CP	EX	NC	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX	EX
Directive on Markets in Financial Instruments (update of ISD)	Directive 2004/39/EC	30/04/06	NC	NC	CP	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC
Transparency directive	Directive 2004/109/EC	20/01/07	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC	NC

\*1 The Commission can always initiate infringement proceedings under Article 226 of the Treaty on the basis of non-compliance of national implementing measures or incorrect application of Directives

The European Commission has published a "Lamfalussy league table" on Member States' success in meeting deadlines for writing into national law a series of securities Directives that were adopted as part of the Financial Services Action Plan (FSAP) launched in 1999

Internal Market and Services Commissioner Charlie McCreevy said: "Over the last six years we have made great strides towards a more open, integrated and competitive European financial market. However, some Member States are still lagging behind on the securities Directives. This is frankly very disappointing, bordering on the lamentable. This is going to hamper the efficiency of Europe's capital markets and the vital 'single passport for issuers'. I hope this league table will encourage these Member States to act quickly and I strongly urge them to do so. We will continue to monitor the situation like hawks."

At this stage, March 2006, the league table covers the Market Abuse Directive (2003/6/EC) and its three technical implementing Directives (2003/124/EC, 2003/125/EC and 2004/72/EC), the Prospectus Directive (2003/71/EC), the Market in Financial Instruments Directive ("MiFID", 2004/39/EC) and the Transparency Directive (2004/109/EC) as well as their implementing measures.

SOURCE: [http://europa.eu.int/comm/internal\\_market/securities/docs/transposition/table\\_en.pdf](http://europa.eu.int/comm/internal_market/securities/docs/transposition/table_en.pdf)

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