

EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 30 September 2003

at the request of the Council of the European Union on a proposal for a directive of the European Parliament and of the Council on the harmonisation of transparency requirements with regard to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC (COM(2003) 138 final)

(CON/2003/21)

(2003/C 242/06)

Introduction

1. On 28 April 2003, the European Central Bank (ECB) received a request from the Council of the European Union for an opinion on a proposal for a directive of the European Parliament and of the Council on the harmonisation of transparency requirements with regard to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC (hereinafter the 'proposed directive').
2. The ECB's competence to deliver an opinion is based on the first indent of Article 105(4) of the Treaty establishing the European Community, since the proposed directive is essential to ensure the integrity of the Community financial markets and to enhance investor confidence and financial stability. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, this opinion has been adopted by the Governing Council of the ECB.
3. The main objective of the proposed directive is to improve investor protection and market efficiency by increasing the transparency of information provided by the issuers of shares and debt securities admitted to trading on European regulated markets. More specifically, the proposed directive improves annual financial reporting of issuers, in particular by harmonising the deadline for submitting annual reports; revises the existing rules concerning half-yearly reporting, taking into account international accounting standards (IAS), and extends half-yearly reporting to debt securities issuers; introduces a new requirement for quarterly financial reporting; improves the existing harmonised framework for disclosure of changes to major shareholdings in securities issuers and modernises the existing Community rules on information provided by issuers.

General assessment

4. The ECB generally welcomes and supports the proposed directive, as it provides an effective means of improving the efficiency of European financial markets, advancing their integration and enhancing financial stability. Moreover, the development of efficient and competitive financial markets in Europe increases the economy's growth potential. The ECB notes that the proposed directive is an essential component of a complex project to modernise securities markets legislation in Europe, as envisaged by the Financial Services Action Plan⁽¹⁾. The Regulation on the application of international accounting standards⁽²⁾, the Market Abuse Directive⁽³⁾ and the future Prospectus Directive⁽⁴⁾ constitute the basis for a fundamental improvement in the overall efficiency of the European financial markets. The proposed directive complements the said project by modernising the European regulatory framework on financial reporting and disclosure to shareholders.
5. The introduction of harmonised and enhanced disclosure standards will have beneficial effects on the European economy as it will improve market efficiency, further the integration of European financial markets and contribute to the financial stability of the euro area. Market efficiency will be improved as the disclosure of timely, complete and accurate information by issuers ensures better price

⁽¹⁾ Endorsed by the Heads of State and Government at the Lisbon European Council in March 2000.

⁽²⁾ Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards (OJ L 243, 11.9.2002, p. 1).

⁽³⁾ Directive 2003/6/EC of the European Parliament and of the Council of 28 January 2003 on insider dealing and market manipulation (market abuse) (OJ L 96, 12.4.2003, p. 16).

⁽⁴⁾ Common Position (EC) No 25/2003 of 24 March 2003 adopted by the Council, acting in accordance with the procedure referred to in Article 251 of the Treaty establishing the European Community, with a view to adopting a directive of the European Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC (OJ C 125 E, 27.5.2003, p. 21).

discovery. That in turn reduces hidden distortions by allowing markets, issuers and investors to compare similar investment opportunities in Europe, increasing competition and reducing uncertainty. A coherent European Union (EU) framework for financial reporting, properly and uniformly enforced, will also improve investors' confidence in the integrity of the European financial system and in investing in a broader range of European companies. This will yield a more efficient allocation of resources to the companies that can best utilise them.

6. Furthermore, enhanced disclosure requirements are likely to lower companies' capital costs. Very important in this regard are the proposals for stricter standards on interim financial reporting and for the provision of reliable financial information on a periodic basis. Increased disclosure reduces the amount of uncertainty associated with the present and future affairs of companies. This will increase investors' confidence in companies' announcements about their performance and will tend to lower companies' capital costs. The justification for relating availability of funds to level of disclosure has been provided by agency theory. In an environment in which there is asymmetry of information between management, shareholders and bondholders, the disclosure of additional information helps to alleviate adverse selection and moral hazard problems, which will be rewarded by a lower capital cost. In addition, disclosure requirements have a beneficial effect on issuers by acting as a disciplinary device on corporate managers.

7. The proposed directive will also further the integration of European financial markets, therefore allowing the exploitation of all the potential benefits of the euro. The harmonisation of transparency standards across the EU will encourage greater cross-border participation in the market, especially for corporate securities. Investors who seek reliable guidance for their decisions will be safeguarded by harmonised arrangements relating to transparency, consistency and comparability of listed companies' financial statements.

8. Finally, the ECB expects that the proposed directive will also have beneficial effects on financial stability. Firstly, with the price of securities reflecting more accurately the earning prospects of and risks faced by issuers, investors will be better equipped to monitor issuers and to take corrective action in case of financial imbalances, thus reducing risks to financial stability. Secondly, the improved timeliness, accuracy and consistency of information made available to investors will make the

belated discovery of a serious misallocation of capital less likely, thus reducing the need for sharp price corrections. It cannot be ruled out that greater frequency and detail of financial information may be associated with more short-term price fluctuations. However, in the medium-term price fluctuations associated with sharp corrections of expectations should be less pronounced. Overall, there should be a positive impact on market volatility. Thirdly, the expected improvement in market efficiency will also increase market liquidity, which will allow markets to absorb shocks more effectively. Finally, the greater degree of cross-border diversification of investors' portfolios will contribute to alleviating the home bias in investment decisions. This will in turn enhance the overall resilience of the European financial system to shocks emanating from individual financial markets.

9. However, as explained below the ECB considers that some issues require further consideration. In particular: the application of some provisions of the proposed directive to the ECB and the national central banks (NCBs), the rules concerning half-yearly financial reports, consistency with supervisory reporting requirements, the rules concerning the competent authorities and the need to refer to European statistical standards.

The application of the proposed directive to the ECB and the NCBs

10. The ECB notes that Article 8 of the proposed directive exempts the ECB and the NCBs, as sovereign debt issuers, from the rules concerning periodic information (Articles 4 to 6) but not from other disclosure provisions. This means that the proposed directive does not take into account the special tasks of the ECB and, in particular, its responsibility for the monetary policy of the euro area. The application of the proposed directive to the ECB could have a negative effect on the fulfilment of its tasks. In fact, the implementation of the single monetary policy may in certain circumstances rely on the issuance of debt certificates as an instrument of monetary control, which may take place with the aim of adjusting the structural liquidity position of the Eurosystem vis-à-vis the banking system so as to create (or enlarge) a liquidity shortage in the banking system. Indeed, the General documentation on Eurosystem monetary policy instruments and procedures⁽¹⁾ states that it is competent to issue debt certificates. The ECB considers that the

⁽¹⁾ Annex I to Guideline ECB/2000/7 of 31 August 2000 on monetary policy instruments and procedures of the Eurosystem, OJ L 310, 11.12.2000, p. 1. Guideline as amended by Guideline ECB/2002/2 (OJ L 185, 15.7.2002, p. 1).

special nature of the issuance of debt certificates as an instrument of monetary control justifies the non-application of some of the provisions of the proposed directive to itself.

11. The application of some provisions of the proposed directive to the ECB and the NCBs may also impair the fulfilment of their specific monetary policy tasks. For instance, according to Articles 9 to 12 NCBs are under the obligation to disclose information about major holdings. In this respect, the ECB notes that such rules may subject central banks to disclosure duties in respect of securities given to them as collateral when performing their monetary policy tasks, with potentially negative effects on the smoothness and efficiency of central banking operations. The application of disclosure provisions in respect of securities received as collateral may also affect the smooth functioning of the European repo market, and may be seen as contravening the goal of simplifying the use of financial collateral through the limitation of administrative burdens pursued by Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements⁽¹⁾. Therefore, the ECB considers that further reflection on this matter is necessary.

12. More generally, the ECB notes that both itself and the NCBs, have been assigned, either by the Treaty and the Statute of the European System of Central Banks and of the European Central Bank, or by their statutes in the case of non-participating NCBs, specific monetary policy tasks, which may be difficult to reconcile with the application of the proposed directive to central banking activities which are related to the implementation of monetary policy. The ECB notes that the special characteristics of the central banks have already been acknowledged in the directives concerning securities regulation. More particularly, securities issued by the ECB and by NCBs are to be exempt from the abovementioned future Prospectus Directive⁽²⁾. If the application of harmonised rules on disclosure to securities issued by the ECB and the NCBs is not requested when they are offered to the public, for the sake of consistency the rules on ongoing disclosure envisaged by the proposed directive should also not apply to them. This is not to deny that in specific cases NCBs may have to disclose information to investors, as their shares are in some cases admitted to trading on regulated markets. In those cases, appropriate national laws should provide for such disclosure by NCBs, taking into account their specific situation. In accordance with the Treaty, the ECB would have to be consulted on these laws, to allow it to assess their compatibility with the

Treaty and Statute. In the light of the above, the ECB believes that the proposed directive should not apply to any of the members of the ESCB.

Half-yearly financial reports (Article 5)

13. The ECB notes that according to Article 5 of the proposed directive issuers will have to disclose half-yearly financial reports, which will include a condensed set of financial statements and an update of the last management report. The ECB welcomes in principle this Article, which will improve and harmonise price discovery across the EU and takes into account IAS. The reference to IAS is welcomed as it supports the ECB's statistical tasks. IAS are broadly consistent with European and international statistical standards. In this context, the ECB underlines the advantages of ensuring that European and international statistical and accounting standards are as consistent as possible. Such harmonisation will enable the same data source to be used for several purposes. In turn, the reliability of statistics will be increased and the reporting burden on issuers reduced. However, the ECB notes that the proposed directive does not make half-yearly financial reports subject to a mandatory auditors' review. Article 5(5)(c) provides that the Commission shall adopt implementing measures, under the comitology procedure, to make such auditing mandatory 'if there is evidence of an urgent need to enhance investor protection throughout the Community'. As half-yearly financial reports are already subject to a mandatory auditors' review in some Member States, the ECB is in favour of making auditing mandatory EU-wide in order to avoid differences at national level that could lead to an uneven level of quality of financial and statistical data, and their reporting.

Quarterly financial information (Article 6)

14. The ECB notes that Article 6 imposes an obligation to disclose quarterly financial information on issuers whose shares are admitted to trading on regulated markets. As noted above the ECB generally welcomes moves towards higher levels of disclosure, in terms of both frequency and quality, for issuers of financial assets. As highlighted by the Commission⁽³⁾, many publicly-traded European companies already disclose quarterly information. The ECB welcomes the proposed rule, which will harmonise standards for such reporting. In practice, this has already become an important reference for investors in their monitoring of companies. Timely disclosure of periodic information ensures that all financial market participants have access to relevant financial information, thus helping the efficient price discovery of financial assets. However, the quarterly reporting should only include information deemed most important for investors and thereby reduce to a minimum the burden imposed on issuers.

⁽¹⁾ OJ L 168, 27.6.2002, p. 43. See recital 9.

⁽²⁾ Article 1(2)(a) and (b) of Common Position (EC) No 25/2003.

⁽³⁾ Explanatory memorandum, page 14.

Consistency with supervisory reporting requirements

15. The ECB notes that issuers of securities, in particular regulated entities, will not only be subject to the rules on disclosure contained in the proposed directive, but will also have to comply with the reporting requirements set out in other EU directives. For instance, publicly-traded credit institutions have to observe the disclosure requirements set out in Directive 2000/12/EC of the European Parliament and of the Council of 20 March 2000 relating to the taking up and pursuit of the business of credit institutions⁽¹⁾ and both credit institutions and investment firms will be subject to the rules on disclosure that will be included in Pillar III of the Capital Adequacy Directive⁽²⁾ following its revision. In order to ensure that the overall reporting burden on listed financial institutions is not excessive, the Commission might wish to check whether improved consistency could be achieved between EU reporting requirements with different purposes. For instance, according to Article 9(1) of the proposed directive, an issuer must be notified where a security holder holds, as the result of an acquisition or disposal, a minimum of 5 % of voting rights or capital. According to Articles 1(10) and 16(1) of Directive 2000/12/EC, the supervisory authority must be notified of an intention to hold major holdings so that the proportion of voting rights or capital held would reach 10 % or more. In the same vein, the Commission might also consider whether further uniformity should be sought between the disclosure requirements for listed companies set out in the proposed directive and those for financial institutions which are currently being developed in the context of the revision of the Capital Adequacy Directive.

The rules concerning the competent authorities (Articles 20 and 21)

16. As regards the provisions concerning the competent authorities, the ECB has two comments. Firstly, Article 20(1) requires Member States to designate a single competent administrative authority. According to Article 20(2) Member States may allow this competent authority to delegate tasks to other entities, such as to operators of regulated markets. Any delegation of tasks is subject to certain conditions. In particular, the entities in question are required to be organised in a manner such that possible conflicts of interest are avoided. As expressed in the ECB's opinion on the proposal for the Prospectus Directive⁽³⁾, the ECB considers that effective measures

⁽¹⁾ OJ L 126, 26.5.2000, p. 1. Directive as last amended by Directive 2002/87/EC (OJ L 35, 11.2.2003, p. 1).

⁽²⁾ Council Directive 93/6/EEC of 15 March 1993 on the capital adequacy of investment firms and credit institutions, OJ L 141, 11.6.1993, p. 1. Directive as last amended by Directive 2002/87/EC of the European Parliament and of the Council (OJ L 35, 11.2.2003, p. 1).

⁽³⁾ CON/2001/36.

against possible conflicts of interest will gain importance as more and more exchanges are transformed into 'for-profit' entities while they remain entrusted with listing and other 'public functions'. Consequently, there is a need to find appropriate regulatory means to address and solve potential conflicts of interest resulting from the changing nature of exchanges. The ECB would therefore welcome it if the Commission clarified better the measures that could mitigate the risks of such conflicts. In addition, further precautions against conflicts of interest could be taken by requiring entities not only to be organised in such a way as to avoid possible conflicts of interests, but also to establish mechanisms that would allow for the management of such conflicts if they did arise.

17. Furthermore, the ECB holds the view that the proposed directive might envisage a broader scope for cooperation between relevant authorities. It refers solely to cooperation between the 'competent authorities' of the home and host Member States responsible for checking compliance with its requirements. However, cooperation with national authorities responsible for enforcing the prudential and conduct of business supervision of regulated entities may also be warranted, such as credit institutions and investment firms whose securities are admitted to trading on regulated markets. This would be particularly appropriate given that some information concerning listed financial institutions will have to be disclosed both to the public and to the relevant supervisory authorities. Therefore, the Commission could consider including a provision foreseeing the possibility of close cooperation between supervisory authorities within the meaning of the proposed directive and prudential and conduct of business supervisors, as long as this is compatible with the obligation of professional secrecy.

The need to refer to European statistical standards

18. As regards Article 9 concerning the notification of the acquisition or disposal of major holdings, the ECB would welcome it if the proposed directive stipulated that information on the acquisition or disposal of major holdings had to be provided in accordance with the European statistical standards as laid down in the ESA 95⁽⁴⁾. This would increase the transparency and quality of the information, as it would be based on harmonised definitions and concepts. In addition, the separate

⁽⁴⁾ Contained in Annex A to Council Regulation (EC) No 2223/96 of 25 June 1996 on the European system of national and regional accounts in the Community (OJ L 310, 30.11.1996, p. 1). Regulation as last amended by Regulation (EC) No 1267/2003 (OJ L 180, 18.7.2003, p. 1).

collection of these data by the ECB and the participating NCBs within the framework of the ECB's statistical reporting requirements would be made redundant.

19. Similarly, the ECB would welcome the setting-up of a single electronic network, or platform of electronic networks, across Member States to facilitate public access of information to be disclosed under the future Prospectus Directive and the proposed directive, as suggested in Article 18. The ECB would however encourage the inclusion of information on the sectoral classification of the issuer and the instrument classification of the securities issued that would otherwise have to be additionally

collected by the ECB and the NCBs of the participating Member States within the framework of the ECB's statistical reporting requirements.

20. This opinion will be published in the *Official Journal of the European Union*.

Done at Frankfurt am Main on 30 September 2003.

The President of the ECB

Willem F. DUISENBERG
