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The transatlantic capital market - Fulfilling its true potential

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Introduction

Ladies and Gentleman,

It is a pleasure to be here in the US. I am grateful to Tom Donohue, whom I met in September last year in Brussels, for inviting me here today to meet with US business leaders. Tom, you have an enviable reputation, in the EU at least, for straight talking – I will try and rise to the challenge…

State of health of capital markets

Ladies and Gentleman, I would like to start with some good European news. Over the last few years the foundations for an integrated financial market in Europe have been laid. We are now seeing real progress on the ground. A large, deep and well-functioning Euro bond market has been created. International issuance in Euros is increasing exponentially – almost reaching the level of the US. Merger and acquisition activity is high. IPOs and private equity are strong. We do not have policies that dissuade outside investors from investing in our capital markets. EU companies now have a much larger range of financing options. Our equity markets at the moment are solid; financial market players are realizing good profit levels. Pan-European financial business is developing. Optimism is high.

But there is still room for improvement. Financial services play a crucial role in our economies and that role is becoming even more important in the global economy. In the EU and elsewhere. Ageing populations mean growing demand for asset and pension products. An EU market of 25 Member States and 450 million consumers today (and more in the future as we enlarge further) means huge potential for cross-border consolidation, economies of scale and improved corporate structures. Opening markets worldwide means huge new opportunities for cross-border investment.

I believe in open markets, letting competitive advantage play.

Recent attempts to block foreign take-over bids and moves towards cross-border consolidation in the EU and the US have again demonstrated the need for the supporters of open markets to stand up and be counted. Some may claim that they support the idea of free flow of capital. But underneath all the fine words, there are those in both the EU and US who, when faced with the choice between a takeover bid by a well-run foreign company that would deliver increased jobs and benefits to the community as a whole and a takeover by a "turkey", will choose the latter, provided that it is a domestic "turkey".

Since 1999, almost half of all merger volume in the non-financial sectors in Europe was cross-border. In the financial sector this figure was only one fifth, suggesting sub-optimal market functioning. When you look at the structure of Europe's financial sector you see a lot of second division champions but hardly any companies that compete or lead in the world league. Not the kind of structure you would expect in a fully functional and open market of 450 million consumers with a GDP of 13 trillion $. The rules for the supervisory approval processes in the EU are too complex and costly at the moment. They must be streamlined and made more transparent.

In the US too there were hot debates on the Exon-Florio provisions in the Senate following a Chinese take-over bid. The tendency to blame each and every economic problem on globalisation and competition from abroad is a strong one.

I am not disputing that many industries go through difficult and often painful transitions. But protectionism is not the answer. Openness is often the harder option but it is the one which delivers the greatest benefits. For people first.

With Jobs. With thriving businesses. By releasing human energies – not capping or constraining them. You don't need rocket science, lawyers or economists to discover this!

The job of politicians, legislators and regulators is to ensure that business and markets can reap the opportunities of open markets. We must adapt our regulatory structures to the demands of the 21st century economy.

Let me say a few words about the reforms we are undertaking in Europe. Then I will address the transatlantic dimension of financial markets policy.

Building on solid foundations: Capital market reform in the EU

As I mentioned, the regulatory foundations for an integrated capital market in the EU have been laid. In securities, corporate governance, accounting, auditing, banking and insurance major steps forward have been taken. The prospectus and transparency Directives have considerably facilitated raising capital in the EU and we are finalising our rules on investment services. A process of convergence of corporate governance rules in the EU has been started. Since the beginning of 2005 International Accounting Standards apply to all listed companies in the EU and the rest of the world is starting to follow. Auditing provisions have been reinforced and harmonised throughout the EU. In corporate governance our emphasis lies on improving transparency, empowering shareholders, encouraging best practice across Member States, principle based approaches, "comply-or-explain" – but no one-size-fits-all solutions. The Basel II framework has now been adopted for the EU and will be fully in place in all Member States by 2008. Solvency II will do the same in insurance. The recently adopted EU Reinsurance Directive installs a state-of-the-art frame for supervision in the EU and gives additional potential to further opening reinsurance markets worldwide.

The transatlantic capital market

When working on all these issues, the external dimensions came quickly to the fore. In parallel, I think there has also been a growing realization in the US and the EU that each of our rules affects the other, often in a significant way. It does not make sense any longer to separate the internal and the external aspects of financial services policy. Just as national markets integrate in the EU so do the European, the American and other global markets. Today, therefore, the transatlantic and the international dimension must become a standard feature of our policy-making process.

There should be no more drawing up legislation in closed and smoke-filled rooms with only a window to the domestic backyard and hidden from the outside world. We talk a lot about the better regulation agenda. I think every policy measure should also be tested for its external effects. There should be transparency and consultation – informal or formal, with industry and with other rule-makers.

Take auditing for example. The EU has just put the finishing touches to its new directive on Statutory Audit (the 8th Directive). During its implementation one of the key challenges will be the question of registration of third country audit firms in the EU by 2008. All third country audit firms, including US ones, auditing foreign companies listed in the EU will have to be registered with EU oversight bodies - unless their home country oversight bodies can be considered as equivalent.

Similarly, EU firms auditing SEC registrants will face inspections from the PCAOB in 2006 and 2007. The new EU directive provides for cooperation with the PCAOB on access to audit working papers. These are tricky issues where the EU and the US must have close and pragmatic cooperation or willingness to "agree to agree" as Bill McDonough, former chairman of the PCAOB, put it. Both sides have to deliver. And both sides must be willing to respect each other's rules and limitations. Deepening cooperation is the name of the game.

I have read with interest the study carried out by the US Chamber of Commerce and its action plan on auditor liability. This is a subject in which I have always taken an interest. In the EU, some Member States already have limitations or are moving in that direction. I think there are good arguments in favour of EU action. As a first step, we have launched a study on the economic impact of the alternative liability regimes, the competition in the market and the availability of insurance. We also set up a group of market experts. By the end of the year, I will be in position to assess the options and decide how to take this forward, in particular whether the Commission should make recommendations on the subject. The audit market is global in nature and there is an obvious need for further EU-US cooperation and discussion on this topic.

That is what the transatlantic agenda is all about. A transatlantic market, with fewer and fewer barriers. Free flow of capital. Not trade wars, or petty reciprocity and retribution. An agenda that focuses on practical improvements for business not grand gestures and political prestige. In my talks this week with Secretary Snow, Chairmen Shelby and Oxley, PCAOB Chairman Gradison and SEC Commissioners, I have been exploring how we can make tangible progress.

The issues we have discussed cover the nuts and bolts of a transatlantic capital market. The 4 main issues are as follows:

1. In my talks with the SEC we have fleshed out *how to achieve our goal of eliminating reconciliation requirements between IFRS and US GAAP*. Chairman Cox has confirmed his commitment to the roadmap. He also made it clear that a specific level of convergence between IFRS and US GAAP is not a precondition for dropping the reconciliation requirement. It is also of crucial importance that the SEC gives full consideration to positions of its EU counterparts regarding the application and enforcement of IFRS. We must avoid any conflicting interpretations. So, there is still work to be done but the goal is very clearly in sight.

2. We also discussed *deregistration*. I am grateful to the SEC for delivering on its promise to come forward with a proposal for reform. Both the US capital market and European issuers will gain from deregistration rules that work. The SEC proposal is a step in the right direction. It addressed the need to have a lasting deregistration solution that is easy to apply. But we are hearing that, even with the new proposal, it is likely that only a very small number of European firms will actually be eligible for deregistration. We are checking the numbers and facts. We will make a number of suggestions on how to deal with this in order to find a workable solution.

3. The EU has already adopted the *Capital Requirements Directive to fully implement the Basel accord by 2008*. In the US the implementation is progressing but will take one year longer, until 2009. Implementation is of course a domestic issue – but again, differences in timing and rules have repercussions for both domestic and foreign industry. This is why we are working closely with the US authorities to make sure practical issues arising from the timing difference are resolved in a sensible and pragmatic way, which will not lead to additional burdens for industry.

4. In *insurance*, the EU has just adopted its new Reinsurance directive and good progress continues to be made on the Solvency II project. That means new, state-of-the-art prudential and supervisory rules. It also means the need to cooperate across the Atlantic and the chance to do away with yesterday's outdated regulation. Reinsurance collateral is a case in point. The reinsurance business is global. A large share of coverage in the US is provided by EU reinsurers – which are subject to first-class supervision in their home-countries. The EU will get rid of the small number of collateral requirements it still has by 2009. The US should do the same. I am encouraged by the White Paper the National Association of Insurance Commissioners has put forward on this issue. We should be able to agree on concrete timing and deliverables soon.

Conclusion

Ladies and Gentleman. Look at the European financial sector and you can see integration at work and progress being made. A booming sector. A new, huge market with lots of potential. Hungry and eager new Member States that bring in fresh ideas. A regulatory framework that is state-of-the-art and further initiatives that will open markets and give opportunities to business. Regulation and corporate governance that does not strangle or overload companies.

But it does not stop there. I also want to see more two-way opportunities for business across the Atlantic. The way to get there is to continue and widen our close and productive cooperation. Informal but involving all the stakeholders. Input from industry. Upstream identification of problems. Anticipation instead of painful ex-post regulatory repair jobs. Practical issues, practical solutions to give the transatlantic market the chance to fulfill its true potential.

I hope you agree that the potential is huge and the cause is worth fighting for.

Thank you for your attention.