

**International Swaps and Derivatives Association
International Securities Market Association
London Investment Banking Association
Association of Private Client Investment Managers and Stockbrokers
Bond Market Association (European Office)
Futures and Options Association,
Swedish Securities Dealers Association,
Danish Securities Dealers Association
Finnish Association of Securities Dealers
Association of Norwegian Stockbroking Companies
Bankers and Securities Dealers Association of Iceland**

C/o Mark Harding, Chairman of ISDA's European Regulatory Committee,
One New Change, London EC4M 9QQ, UK. Tel: 44 (20) 7330 3550. e-mail: isda@isda-eur.org

**Investment Services Directive ("ISD2"), now called Financial Instruments Markets Directive
Second Reading, ECON Committee vote, 24th February 2004**

A briefing paper by associations representing investment firms

The Associations listed at the end of this paper urge Members of the European Parliament to support the following amendments to the Council Common Position of the Investment Services Directive, now renamed the Financial Instruments Markets Directive, at the Committee vote on 24th February 2004.

Summary

The Parliament's Position at First Reading is widely recognised as being more in line with the objectives of the Directive than the Common Position, more practical, and more relevant to the needs of investors. The Common Position is significantly deficient in a number of important respects. We recognise that there may be limited scope for amendments to the Common Position at this stage. But unless the Directive is improved by the amendments we recommend below, the result could be:

- Only limited opening of the investment services single market, and in some respects a more restricted market than at present;
- European markets that provide investors with poorer and more costly financial services;
- European markets that are less competitive internationally;
- Lower returns for investors and higher cost of capital for issuers, harming the European economy.

Comments on specific amendments

Article 4.1.7: Definition of systematic internalisation – SUPPORT Amendment 7

Parliament's definition of "systematic internalisation" is widely considered by market participants to be much more appropriate and workable than the common position's definition of "systematic internaliser" (which would include almost every investment firm indiscriminately). The focus on internalisation carried out continuously within a system, and the restriction to standard market size, are vital to ensure that firms' complex intermediation between customers and exchanges, particularly in professional markets, is not disrupted. A more detailed explanation of the complex issues at stake is provided in our separate briefing paper on Articles 4.1.7 and 27.

Article 27: Quote obligations for systematic internalisation – SUPPORT Amendments 13, 14, 15, 16, 17

Parliament's approach to quoting obligations for systematic internalisers is widely considered by market participants to be much more appropriate and workable than the common position's approach (which risks

significant disruption to investment firms' ability to provide investors with a wide range of services not available from exchanges). The avoidance of restrictive disruption of wholesale markets, and the greater ability for quoting firms to control their risk exposure, but also to provide the best service to investors, through price improvement and protection against multiple hits, are particularly important if European markets are to continue to be able to provide investors with the range of low-cost and competitive execution services that is available today. A more detailed explanation of the complex issues at stake is provided in our separate briefing paper on Articles 4.1.7 and 27.

Recital 44: No extension of transparency obligations to bonds and derivatives – SUPPORT Amendment 3

It is not appropriate to include in the Directive a specific option for Member States to extend transparency requirements, developed for equity markets, to bonds and derivatives. Such optionality would mean continued market fragmentation. It is not appropriate to pre-judge the review of possible extension of transparency obligations in Article 65. Optional extension would significantly disrupt what are at present largely professional markets in bonds and derivatives, where price formation takes place in a very different way from equity markets.

Article 24: Definition of eligible counterparties – SUPPORT Amendments 12, 29, 52

It is vital to ensure that large, sophisticated corporates can continue to choose to participate in inter-professional markets without inappropriate and costly restrictions.

Articles 2.1(i), 2.1(k), Recitals 16, 24: Exemptions from definition of investment firm – SUPPORT Amendments 26, 27, 33, 34

These technical amendments are necessary to ensure that the same activity is regulated in the same way, regardless of group structure, and that financial groups are not at a competitive disadvantage when they conduct non-financial activities.

Annex I: B6a(new), C(5), C(6), C(6a)(new), C(8a)(new), C(8b)(new), Recital 4: Commodity derivatives – SUPPORT Amendments 24, 80, 82, 84, 85, 87, 88

These technical amendments are necessary:

- (1) to ensure that firms are able to perform services and activities related to commodities as an ancillary service without encountering national barriers in the single market;
- (2) to include in the Directive cash-settled derivatives relating to weather, freight, emissions allowances, and economic statistics, and to allow extensions to cover other classes of derivatives that have the characteristics of financial instruments. This is vital if Europe is to participate fully in these new and growing global markets.

Article 2.1(d), Article 4.1.8, Recital 8: Own-account dealing – SUPPORT Amendments 25, 32, 39

These technical amendments are necessary to ensure that licensing requirements do not inadvertently apply to professional investors.

Article 32.7, Recital 31: Regulation of branches – SUPPORT Amendments 28, 71

The amendment to Article 32.7 would reinstate the Parliament's first reading support for the country of origin regulation of cross-border services provided by branches. The amendment to Recital 31, following the Electronic Commerce Directive 2000, would nevertheless ensure that the home State continued to have control where the centre of activities for services provided through a branch remained in the head office.

Article 19: Conduct of business rules – SUPPORT Amendments 11, 41, and 42 or 43 or 10

The amendment to Article 19.6 is necessary to ensure that customers can continue to choose to obtain low-cost execution services when making their own investment decisions and not receiving advice.

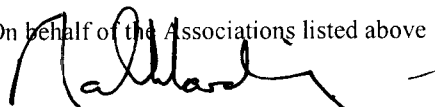
The amendment to Article 19.10(c) would enable implementing measures to make clear where appropriate that conduct of business rules should not apply to professional customers, and to enable firms to continue existing client relationships without costly recategorisation.

Article 21: Best execution – SUPPORT Amendments 45, 46, 47, 49

Focusing the obligation on the ‘best reasonably achievable’, and on retail investors, will enable firms better to meet investors’ need for high quality execution.

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On behalf of the Associations listed above



Mark Harding
Chairman of ISDA’s European Regulatory Committee

International Swaps and Derivatives Association (Mark Harding, +44 207 699 5000; Daniela Marilungo, +32 2 401 8760/+44 20 7330 3550)

International Securities Market Association (Richard Britton, +44 20 7431 1661)

London Investment Banking Association (Sir Adam Ridley, Timothy Baker, +44 20 7367 5513)

Association of Private Client Investment Managers and Stockbrokers (Angela Knight, +44 20 7247 7080)

Bond Market Association (European Office) (Scott Rankin, +44 20 7743 9300)

Futures and Options Association (Anthony Belchambers, +44 20 7426 7252)

Swedish Securities Dealers Association (Per-Ola Jansson, Lars Nordström, +46 8 679 7280)

Danish Securities Dealers Association (Søren Gade, +45 33 70 10 90)

Finnish Association of Securities Dealers (Hannu Hulkkonen, +358 9 6689 1715)

Association of Norwegian Stockbroking Companies (Frede Rognlien, + 47 22 00 74 12)

Bankers and Securities Dealers Association of Iceland (Guðjon Runarsson, +354 591 0000)