

NEW DEVELOPMENTS RELATING TO THE
INTERNATIONALIZATION OF THE
CAPITAL MARKETS:
A COMPARISON OF LEGISLATIVE REFORMS IN THE
UNITED STATES, THE EUROPEAN COMMUNITY,
AND GERMANY

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1. INTRODUCTION

1.1. The Internationalization Of The Securities Markets

The internationalization of the world's business activities has been reflected in the internationalization of securities markets. This globalization appears in various areas of the different national securities markets. On the one hand, the number of foreign investors trading in U.S. securities and U.S. investors trading in foreign securities has greatly increased. On the other hand, the number of U.S. corporations issuing securities abroad as well as the number of securities issued by foreign corporations and countries in the United States has grown rapidly. This remarkable expansion includes the issuance and trading of both debt and equity securities. Commentators have described the foregoing developments as "major," "dramatic," "tremendous," and even "revolutionary."¹

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¹ To analyze and describe the extent of the internationalization in the different market segments in the United States and abroad would go beyond the scope of this Article. For general statistical information of this kind, see *Globalization of Securities Markets: Hearings Before The Subcomm. on Telecommunications & Finance of the House Comm. on Energy & Commerce*, 100th Cong., 1st Sess. 4 (1987) (statement of Charles C. Cox, Chairman,

Distinct national markets have emerged into truly supra-national trading markets. The Eurobond market is just one example.²

The causes and effects of this internationalization are manifold, often overlapping, and thus cannot be clearly distinguished.³ Commentators Cox, Hillman and Langevoort provide a very short but illuminating explanation: "Fiber optics, the microwave relay, and the satellite, not to mention changes in the tax laws and the cooperative efforts of government regulators, have each contributed greatly to the internationalization of securities offerings. . . ."⁴

Internationalization of the world's securities markets also implies interdependency between markets.⁵ The interdependence of the markets was underscored on "Black Monday" in October 1987 when prices plunged in all major markets, even though some national economies did not themselves face the economic problems identified by some as causes of the U.S. market decline (i.e., declining currency values, trade deficit and budget deficit).⁶ In addition to the

SEC). For examples of the extent of internationalization, see Aulana L. Peters & Andrew E. Feldman, *The Changing Structure of the Securities Markets and the Securities Industry: Implications for International Securities Regulation*, 9 MICH. Y.B. INT'L LEGAL STUD. 19, 22-24 (1988); David E. Van Zandt, *The Regulatory and Institutional Conditions for an International Securities Market*, 32 VA. J. INT'L L. 47, 56-58 (1991). For figures showing the trade of foreign securities on different national exchanges, see Friedrich Kübler, *Regulatory Problems in Internationalizing Trading Markets*, 9 U. PA. J. INT'L BUS. L. 107, 107-08 (1987) [hereinafter *Regulatory Problems*]. For statistics showing to what extent foreign securities are traded in Germany and to what extent German securities are traded abroad, see ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992, 142-69 (1992); DEUTSCHE BÖRSE AG, FRANKFURTER BÖRSENSTATISTIK (1992).

² See *Regulatory Problems*, *supra* note 1, at 109.

³ For descriptions and analyses, see HEINZ-DIETER ASSMANN, HANDBUCH DES KAPITALANLAGERECHTS 26-27 (Assmann & Schütze eds., 1990); HAROLD BAUM & STEFAN BREIDENBACH, DIE WACHSENDE INTERNATIONALE VERFLECHTUNG DER WERTPAPIERMÄRKTE UND DIE REGELUNGSPOLITIK DER SECURITIES AND EXCHANGE COMMISSION: NEUE ENTWICKLUNGEN IN DER INTERNATIONALEN ANWENDUNG DES AMERIKANISCHEN KAPITALMARKTRECHTS, WERTPAPIER-MITTEILUNGEN/SONDERBEILAGE NR. 6 4-6 (1990); *Regulatory Problems*, *supra* note 1, at 107-11; Van Zandt, *supra* note 1, at 60-66.

⁴ JAMES D. COX ET AL., SECURITIES REGULATIONS: CASES AND MATERIALS 327 (1991).

⁵ See ASSMANN, *supra* note 3, at 24.

⁶ See DIVISION OF MARKET REGULATION OF THE U.S. SECURITIES AND

economic interdependence of the securities markets, the legal systems regulating the securities markets have also become interdependent, thereby decreasing the regulatory autonomy of national legislators.⁷

1.2. *Effects Of The Internationalization*

The growing globalization of the capital markets has enhanced competition between the different national marketplaces. To ensure supply and demand of capital, a competitive market must attract both investors and issuers. The most attractive market will be the one having the least government intervention, the highest liquidity, the lowest transaction costs, the most freedom to innovate, and the lowest tax burden.⁸ In addition, market depth and market stability are important considerations.⁹

This Article will describe how the different national legislatures have dealt with the internationalization of the capital markets (i.e., the reforms countries have adopted to keep their markets competitive). The analysis will focus on the regulation of securities issuance and trading. It is, however, beyond the scope of this Article to describe the impact of globalization on the regulation of investment services, notwithstanding their importance in securities and capital markets regulation. Section 2 will describe the legislative concerns relating to the globalization of the capital markets in general and will present an overview of national reforms and their conceptual differences. Section 3 will outline the recent reforms of U.S. securities laws adopted to increase the competitiveness of the U.S. market. Section 4 will describe recent developments in Europe. Legislative developments in the European Community and the recent reforms in the German market will be explored. Section 5 will compare the different approaches underlying the national reforms and posit reasons for existing differences. Finally,

EXCHANGE COMMISSION, THE OCTOBER 1987 MARKET BREAK REPORT (1988); Peters & Feldman, *supra* note 1, at 35-36;

⁷ See ASSMANN, *supra* note 3, at 28.

⁸ See *id.*

⁹ See *id.*; Daniel L. Goelzer et al., *Securities Regulation in the International Marketplace: Bilateral and Multilateral Agreements*, 9 MICH. Y.B. INT'L LEGAL STUD. 53, 54 (1988).

this Article provides an outlook on the future of further internationalization.

2. REGULATORY CONCERN WITH REGARD TO INTERNATIONAL DEVELOPMENTS

Two regulatory concerns are associated with internationalization. One concern, mentioned above, is the enhanced competition between the different securities markets. The other concern is the increasing possibility of fraudulent conduct by market participants as internationalization moves forward. The Securities and Exchange Commission (the "SEC") expressed these regulatory concerns in the following way: "The challenge facing regulators of these global securities markets is to ensure efficiency and honesty."¹⁰ Due to the various structures of securities markets around the world, the regulatory measures necessary to ensure both "efficiency and honesty" are very different in each market. A highly regulated securities market, like that of the United States, will have problems maintaining efficiency (i.e., preventing business from flowing offshore and attracting foreign investors) much more so than a deregulated system, like the German securities market. Such a deregulated market may, however, face other problems in attracting foreign investors, such as trying to provide the necessary framework for a modern and functioning marketplace.

Participants in cross-border securities transactions are often beyond the reach of the regulatory agencies and the courts of the state where the securities are issued or traded. This leads to an additional regulatory concern: the regulator must either apply its own legislation extraterritorially or cooperate with regulators of other securities markets to achieve harmonization or unification of the national securities laws.¹¹

¹⁰ *Policy Statement of the Securities and Exchange Commission on the Regulation of International Securities Markets*, [1988-1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,341, at 89,576 (Nov. 1988).

¹¹ For an analysis of the problems associated with reaching the participants in cross-border security transactions and the different possible legislative solutions, see BAUM & BREIDENBACH, *supra* note 3, at 7-10 (describing in detail the problems of unilateral and extraterritorial application of national legislation).

2.1. *The Responses Of U.S. Regulators*

The securities market in the United States is characterized by its enormous size and its high level of regulation. The perceived complexity of the U.S. regulatory system, the related cost of attaining and maintaining access to the U.S. market, and fears about the level of disclosure required have made the U.S. securities market unattractive to foreign issuers.¹² These problems have also induced business to move off-shore to securities markets which have lower costs and require less effort to raise capital.¹³

The above-mentioned effects were reinforced through the extraterritorial application of U.S. securities laws. The U.S. securities laws pursuant to section 5 of the Securities Act of 1933 (the "Securities Act") apply when a transaction is accomplished by use of "interstate commerce and the mails."¹⁴ Under section 2(7) of the Securities Act and section 3(a)(17) of the Securities Exchange Act of 1934 (the "Exchange Act"), "interstate commerce" also includes "trade or commerce . . . or any transportation or communication . . . between any foreign country and any State . . ."¹⁵ Thus, the U.S. securities laws apply to nearly any cross-border securities transaction, including the issuance of foreign securities in the United States, the resale of securities which were issued in third countries in the U.S. market, and the issuance of U.S. securities abroad.¹⁶

The SEC traditionally sought to enforce U.S. securities laws even in the aforementioned extraterritorial situations. This led to the proposal of the "waiver by conduct" rule, suggesting that whoever engages in trading on the U.S.

¹² See Gregory K. Palm & Donald C. Walkovik, *United States*, INT'L FIN. L. REV., July 1990 Supp., at 62.

¹³ For statistical figures on the decline of the U.S. share of the world equity market and the decline of foreign issues registered in the United States, see Roberta S. Karmel, *SEC Regulation of Multijurisdictional Offerings*, 16 BROOK. J. INT'L L. 3, 15-16 (1990); Van Zandt, *supra* note 1, at 78.

¹⁴ Securities Act of 1933 § 5, 15 U.S.C. § 77(e) (1988).

¹⁵ Securities Act of 1933 § 2(7), 15 U.S.C. § 77(b)(7) (1988); Securities Exchange Act of 1934 § 3(a)(17), 15 U.S.C. § 78(c)(17) (1988).

¹⁶ For a description of the extraterritorial application of the U.S. securities laws, see DAVID L. RATNER, *SECURITIES REGULATIONS* 295-304 (1992).

market should be "presumed to have waived the protection of domestic secrecy laws."¹⁷ The secrecy laws of foreign countries were aimed at protecting the confidentiality of the relationship between a non-U.S. financial institution and its customer.¹⁸ The expansive extraterritorial enforcement of these laws, however, led to discrimination against U.S. investors by foreign issuers (i.e., U.S. investors were excluded from international rights, tender and exchange offers).¹⁹

Over time, the SEC realized that extensive investor protection could result not only in making a market less competitive, but also in disadvantaging domestic investors. Thus, in recent years the SEC has changed its attitude and recognized the need to harmonize the requirements of the U.S. securities laws with those of other jurisdictions. Furthermore, the SEC has acknowledged the need for flexibility in applying existing U.S. requirements to non-U.S. issuers in order to provide U.S. investors with more of those increasingly significant opportunities to invest in foreign securities.²⁰ As Sara Hanks, former Chief of the Office of International Corporate Finance at the SEC, stated: "[T]he SEC wants to meet the demands of U.S. investors to invest in foreign securities [W]hile the SEC does not want to 'engage in a race to the bottom' or lowering of standards, it is willing to be more flexible to increase the attractiveness of U.S. markets."²¹ This movement has led to a series of new

¹⁷ *Regulatory Problems*, *supra* note 1, at 116.

¹⁸ For a critique of the waiver by conduct rule, see *id.* at 116-17.

¹⁹ See *infra* note 44 and accompanying text.

²⁰ SEC Order, 52 Fed. Reg. 24,230 (1987). The recent listing of Daimler-Benz AG at the New York Stock Exchange, the first German Company to list its shares in the United States, shows that the U.S. market is still very attractive to foreign issuers, and that the SEC's willingness to attract foreign investors may ultimately be successful. See Ferdinand Protzman, *Ferdinand Protzman With Grand Rollout on Wall St., Daimler Flies in Face of Bad News*, N.Y. TIMES, Oct. 6, 1993, at D8; *Germany's Daimler-Benz Finds Parking Spot on NYSE*, L.A. TIMES, Oct. 6, 1993, at D2; *Daimler-Benz Cheers Being 1st German Firm to be Listed on NYSE*, CHI. TRIB., Oct. 5, 1993, at C3; Timothy Aepfel, *Daimler-Benz Discloses Hidden Reserves Of \$2.45 Billion, Seeks Big Board Listing*, WALL ST. J., Mar. 25, 1993, at A10; Floyd Norris, *Daimler-Benz Is Ready to Sign Up With Wall St.*, N.Y. TIMES, Mar. 25, 1993, at D1; David Waller & Martin Dickson, *Daimler Discloses DM4bn of Reserves*, FIN. TIMES, Mar. 25, 1993, at 23; see also *infra* notes 217-18 and accompanying text.

²¹ Hanks cites SEC 'Practical Stance' on International Securities Issues,

legislative measures and proposals.²²

2.2. *The Responses Of European Regulators*

The European²³ securities market is characterized by different legislation in the different member states. Although the level of regulation in Europe generally is much lower than in the United States, the degree of regulation varies widely. Due to the different regulatory systems in the twelve member states and the restrictions on the transfer of capital which have existed until recently,²⁴ the term "European securities market" is misleading. One can only speak of twelve different securities markets which are harmonizing and integrating, at a growing speed, into a truly unified European securities market.

As part of the European Commission's 1992 program to create a single common market for goods, labor, capital, and services in Europe, the Commission has worked on the harmonization of the member states' laws that regulate the securities markets.²⁵ The program to harmonize the securities industry (the "1992 program") mirrors the basic principles of European Community law: mutual recognition, harmonization of minimum standards, and coordination of regulation among national authorities.²⁶ The 1992 program is aimed at achieving the internationalization of the Communities' capital markets.²⁷

22 Sec. Reg. & L. Rep. (BNA) No. 3, at 103 (Jan. 19, 1990).

²² For a detailed description of these measures and proposals, see *infra* Section 3.

²³ As used hereafter, "Europe" or "European" refers to the territory of the Member States of the European Community.

²⁴ See *infra* notes 92-93 and accompanying text.

²⁵ The creation of a single market in the Community goes far beyond the harmonization of the capital markets. Thus, the harmonization of the capital markets in the Community must be understood as being only a part of a more general movement towards harmonization within the Community. See EDDY WYMEERCH, *EEC*, in INTERNATIONAL SECURITIES REGULATION 3 (Rosen ed., 1991); see also *infra* note 85.

²⁶ For a description of the legislative measures which were taken under the 1992 program, see *infra* Section 4.

²⁷ See David Reid & Andrew Ballheimer, *The Legal Framework of the Securities Industry in the European Community under the 1992 Program*, 29 COLUM. J. TRANSNAT'L L. 103, 142 (1991).

Two motivations exist for legislative developments in the member states' securities laws: (i) there is a desire to harmonize the various systems in order to create a single market in the European Community, and (ii) there is a need to maintain a competitive marketplace. Several member states introduced reforms to ensure the above-mentioned "efficiency and honesty" of the markets.²⁸ Great Britain's "Big Bang" reform in 1986 is generally viewed as the most revolutionary.²⁹

The German securities market is an example of a highly deregulated system. Nevertheless, Professor Kübler describes this stock market as "narrow, thin and boring."³⁰ Two figures show the limited size of the German stock market: "there are no more than 2,300 German stock corporations, and fewer than 630 are listed on one of the German stock exchanges."³¹ In comparison with the U.S. industries, the German industries seem to be undercapitalized.³² Thus, the German securities market has no regulatory barriers which would make it unattractive to foreign investors and issuers. However, its limited size seems to make the German market less attractive.

Germany has traditionally had a virtually unregulated system. The reform in 1984-85 was limited to the so-called "*Restliberalisierung*," which was a further deregulation that abolished some existing limitations vis à vis foreign investors and issuers.³³ Other changes in the recent German legislation reflect the legislative harmonization efforts of the European Community and are designed to provide the necessary framework for a modern and functioning

²⁸ See *supra* note 10 and accompanying text.

²⁹ For a short description of the 1986 U.K. Big Bang and the reforms of other European Countries, see Peters & Feldman, *supra* note 1, at 25-26; HAROLD S. BLOOMENTHAL, *EMERGING TRENDS IN SECURITIES LAW* §§ 10.05-.08 (1989).

³⁰ Friedrich K. Kübler, *Institutional Owners and Corporate Managers: A German Dilemma*, 57 *BROOK. L. REV.* 97, 106 (1991) [hereinafter *German Dilemma*].

³¹ *Id.* at 101. The number of German stock corporations listed at the German exchanges in 1992 was 665, the respective number of foreign stock corporations listed in Germany was 594. *ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES* 1992 35, 165 (1992). For a description of the size of the German market, see also *infra* note 145 and accompanying text.

³² *German Dilemma*, *supra* note 30, at 106.

³³ *ASSMANN*, *supra* note 3, at 27.

marketplace. The recent discussion in Germany also focuses on increasing measures to protect investors and ensure the element of "honesty" in the market. Several legislative proposals³⁴ are aimed at establishing a federal securities supervisory agency and promulgating legislation on insider trading.³⁵

3. NEW LEGISLATIVE DEVELOPMENTS IN THE UNITED STATES

The foregoing difficulties in ensuring the competitiveness of the U.S. securities market have prompted the SEC to adopt a number of legislative measures to adapt its regulatory system to the globalized market.³⁶ The new legislative measures³⁷ address three main points: (i) registration and reporting requirements for foreign issuers; (ii) multinational offerings of securities; and (iii) application of section 5 of the Securities Act to offshore transactions.

3.1. *Registration And Reporting Requirements For Foreign Issuers*

Amendments to registration and reporting requirements for foreign issuers under the U.S. disclosure rules addressed foreign concerns.³⁸ For example, in adopting registration forms F-1, F-2, and F-3, and in changing Form 20-F, the SEC has lightened the disclosure burdens for foreign issuers.³⁹

³⁴ For a description of the different legislative developments in recent years, see *infra* section 4.

³⁵ See *infra* notes 185-92 and accompanying text.

³⁶ See *supra* notes 20-21 and accompanying text.

³⁷ For recent publications describing the different new developments, see EDWARD F. GREENE ET AL., U.S. REGULATION OF THE INTERNATIONAL SECURITIES MARKETS: A GUIDE FOR DOMESTIC AND FOREIGN ISSUERS AND INTERMEDIARIES (1992); HAROLD S. BLOOMENTHAL, 10A INTERNATIONAL CAPITAL MARKETS AND SECURITIES REGULATION ch. 5 (1990); HAROLD S. BLOOMENTHAL, GOING PUBLIC AND THE PUBLIC CORPORATION ch. 4A (1993); Karmel, *supra* note 13; Baum & Breidenbach, *supra* note 3; Palm & Walkovik, *supra* note 12.

³⁸ See COX ET AL., *supra* note 4, at 328; GREENE ET AL., *supra* note 37, at ch. 2; Robert P. Austin, *Regulatory Principles and the Internationalization of Securities Markets*, 50 LAW CONTEMP. PROBS. 221, 234-36 (1987); for further bibliographic references, see *supra* note 37.

³⁹ These amendment and changes lightening the disclosure burden for

Such foreign issuers have the option not to disclose certain categories of information or to have lower disclosure obligations (i.e., information regarding management compensation).⁴⁰ For example, foreign issuers which are listed on the NYSE or the AMEX are not required to report quarterly, but are allowed to report semiannually if such reporting is consistent with the regulation in their home country.⁴¹

These legislative amendments are deregulatory in nature and they only address foreign issuers who want to undergo the cumbersome process of registering their securities in the United States. Thus, only a limited number of issuers will be affected by these changes. For those foreign issuers, however, the amendments make compliance with the registration requirements a much less burdensome task.

3.2. *The United States - Canada Multijurisdictional Disclosure System*

Multijurisdictional offerings of securities demonstrate that the securities markets are becoming increasingly international. One of the main difficulties of simultaneous multijurisdictional

foreign issuers were proposed in *Integrated Disclosure System for Foreign Private Issuers*, [1981-1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,054 (Nov. 20, 1981); *Age of Financial Statements of Non-North American Foreign Private Issuers*, [1981-1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,055 (Nov. 20, 1981); *Financial Statements of Foreign Issuers*, [1981-1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,056 (Nov. 20, 1981); and adopted in 17 C.F.R. §§ 200-60 (1993).

⁴⁰ See GREENE ET AL., *supra* note 37, at 110.

⁴¹ See SEC Order, 52 Fed. Reg. 24,230 (1987); GREENE ET AL., *supra* note 37, at 50, 101; Karmel, *supra* note 13, at 8.

However, companies that publish financial statements only semiannually can find that they are unable to conduct a public offering in the U.S. during several months of the year (a "black out period"), because the requirements of having current financial statements for the offering of securities under Rule 3-19 of Regulation S-X mandates more recent financial information than the reporting requirements. The SEC has released proposed amendments to Rule 3-19 that would remove these major impediments for foreign issuers. See *Amendments to Rule and Form Requirements Which Govern Age of Financial Statements of Foreign Private Issuers*, [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,801 (June 5, 1991). See also Harold Schimkat, Note, *The SEC's Proposed Regulations of Foreign Securities Issued in the United States*, 60 FORDHAM L. REV. S203, S211-15 (1992).

offerings is the different prospectus requirements in the securities markets in which the securities will be issued.⁴² In response to this problem, the SEC issued in 1985 a concept release, *Facilitation of Multinational Securities Offerings*,⁴³ with the intent to harmonize the disclosure standards and distribution systems of the United States and other countries. In this concept release, the SEC discussed two possibilities: either a common prospectus approach, (different regulators adopt unified disclosure standards for an offering document), or a reciprocity approach, (different regulators accepting one another's home country's standards of disclosure). The SEC chose the reciprocity approach in adopting the United States-Canada multijurisdictional disclosure system (the "MJDS").⁴⁴ Under the MJDS, Canada and the United States have each agreed to recognize the disclosure documents of issuers if they are prepared and reviewed under the standards of the issuer's home country.⁴⁵ Even under the new rules, issuers are still

⁴² For a detailed description of the problems of multinational offerings see Austin, *supra* note 38, at 246-48; for a description of problems regarding the protection and representation of bondholders in multinational debt offerings, see Frederic C. Rich, *International Debt Obligations of Enterprises in Civil Law Countries: The Problem of Bondholder Representation*, 21 VA. J. INT'L L. 269 (1981).

⁴³ [1984-1985 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,743 (Feb. 28, 1985).

⁴⁴ The MJDS was initially proposed in *Multijurisdictional Disclosure*, [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,432 (July 26, 1989); repropoed in *Multijurisdictional Disclosure and Modification to the Current Registration and Reporting System for Canadian Issuers*, [1990-1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,701 (Oct. 16, 1990); and finally adopted in *Multijurisdictional Disclosure and Modification to the Current Registration and Reporting System for Canadian Issuers*, [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,812 (June 21, 1991).

⁴⁵ The MJDS states, "good faith compliance with the disclosure requirements of the home jurisdiction, as construed by Canadian regulatory authorities, will constitute compliance with the applicable U.S. federal securities disclosure requirements, even if such compliance results in the omission of information which might otherwise have been required as a line item in registration statements filed by U.S. issuers on the Commission's other registration forms." *Multijurisdictional Disclosure and Modification*, [1991 Transfer Binder], *supra* note 44, ¶ 84,812 at 81,881.

For a description of the MJDS, see HAROLD S. BLOOMENTHAL & SAMUEL WOLFF, *EMERGING TRENDS IN SECURITIES LAWS*, Ch. 8 (1991); Alan Goggins, Comment, *Taking That First Step: The Securities and Exchange Commission's Proposed Multijurisdictional Disclosure System*, 14 MD. J. INT'L L. & TRADE 43 (1990); Sarah Hanks & Elizabeth Jacobs, *United States*

subject to the anti-fraud and civil liability provisions of the offering country. Furthermore, the MJDS does not apply to every filing made in accordance with the home country's requirements, but is limited instead to certain major issuers which qualify under the MJDS's rules,⁴⁶ and to certain specific rights, tender and exchange offers.

The MJDS is a deregulatory step in U.S. legislative history. Despite the fact that the MJDS is limited to cross-border transactions between the United States and Canada, it is of considerable interest to others. The MJDS marks the first time the SEC has recognized disclosure documents established under the standards of an issuer's home country. The SEC itself described the new provisions as "a logical first step in meeting the needs of transnational securities transactions."⁴⁷ Thus, agreements with other nations, especially the United Kingdom, seem possible in the future. An agreement with the United Kingdom could have further effects on the other member states of the European Community, given the above mentioned harmonization efforts already underway in the Community.⁴⁸ One must bear in mind, though, that the SEC's acceptance of reciprocal recognition of disclosure standards was largely influenced by the similarity of the regulatory systems and the accounting and auditing standards⁴⁹ of Canada and the United States, and by the significant presence of Canadian issuers in the U.S. market.

and Canada: A New System for Multijurisdictional Disclosure, INT'L FIN. L. REV., Sept. 1989, at 19; Edward B. Claxton et al., *Multijurisdictional Disclosure: A Practitioners' View*, INT'L FIN. L. REV., Oct. 1989, at 11. The MJDS applies not only in cases of multinational offerings, but also in case of single foreign offerings.

⁴⁶ Issuers eligible to rely on the MJDS are "Canadian eligible issuers," having fulfilled certain requirements of total capitalization, public market float, reporting or listing history, or some additional criteria (in other words, they must be "substantial issuers").

⁴⁷ *Multijurisdictional Disclosure*, [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,432, at 80,282 (July 26, 1989).

⁴⁸ See Baum & Breidenbach, *supra* note 3, at 28.

⁴⁹ Financial statements are the basis of disclosure in every regulatory system. Therefore, reciprocal recognition of disclosure documents standards will depend largely on the development of international accounting and auditing standards. For a short description of the efforts towards the development of international GAAP and GAAS, see Karmel, *supra* note 13, at 11-12; ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992 110 (1992).

Therefore, it is doubtful whether this "first step" really indicates a new willingness by the SEC to adapt the U.S. regulatory system to the demands of market internationalization.⁵⁰ However, the U.S. market will attract a significant portion of foreign market participants only if the "first step" is followed by a "second step" that expands the concept of the MJDS beyond Canada.

3.3. *The SEC Proposal On The Regulation Of Cross-Border Rights, Tender And Exchange Offers*

Internationalization of securities markets has also occurred in the context of cross-border rights, tender and exchange offers. In these offers, U.S. shareholders were often excluded by foreign issuers who concluded that the burdens of complying with U.S. securities laws were more cumbersome than the benefits of including the U.S. shareholders. The result was not only that those U.S. shareholders lost the possibility of realizing a premium on their shares, but also that they often had to sell in the market below the offering price in order to avoid remaining minority shareholders subject to a possible freeze-out.⁵¹ To eliminate this disadvantage, the SEC proposed new regulations concerning foreign tender and exchange offers, foreign rights offers, and financial reporting requirements for foreign issuers.⁵² The

⁵⁰ See Karmel, *supra* note 13, at 9-11; Claxton et al., *supra* note 45, at 14 (warning not to be too optimistic).

⁵¹ For a detailed description of the various problems arising in the context of international tender and exchange offers, including the exclusion of U.S. security holders from such transactions, see John C. Maguire, *Regulatory Conflicts: International Tender and Exchange Offers in the 1990s*, 19 PEPP. L. REV. 939 (1992).

⁵² See *Concept Release On Multinational Tender and Exchange Offers*, Securities Act Release No. 6866, [1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,606 (June 6, 1990); *Cross-Border Rights Offers; Amendments to Form F-3*, Securities Act Release No. 6896, [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,802 (June 5, 1991); *International Tender and Exchange Offers*, Securities Act Release No. 6897, [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,803 (June 5, 1991); *Amendments to Rule and Form Requirements Which Governs Age of Financial Statements of Foreign Private Issuers*, Securities Act Release No. 6895, [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,801 (June 5, 1991); these proposals are not expected to be adopted before the end of 1993.

main changes would occur on two levels.⁵³ First, the proposals provide an exemption from the registration requirements of the Securities Act if the aggregate dollar amount of securities offered to U.S. holders in a tender, exchange or rights offer does not exceed \$5 million (Rules 801 and 802). Second, the proposals introduce new forms, F-11 and F-12, to facilitate the registration of securities by foreign bidders. Form F-11 could be used for rights offerings of unlimited size by qualified foreign private issuers. Form F-12 could be used for exchange offers and business combinations when only five percent or less of the class of securities subject to the offer is held by U.S. holders. Furthermore, several exemptions from the Williams Act and the Trust Indenture Act would be granted in the case of tender and exchange offers if ten percent or less of the securities are held by U.S. holders. Under the proposals, foreign issuers generally would be able to use documents prepared in accordance with the laws and accounting standards of their, or the target company's, home jurisdiction. This is the so-called "principle of full recognition."

The new proposals seem to be the "second step" following the enactment of the MJDS with Canada. In several respects, the new proposals go beyond the MJDS which is based on the fact that the framework of the securities laws, accounting systems, and auditing standards are very similar in the United States and in Canada. Therefore, whereas the MJDS is mainly based on harmonization of the various systems, the new proposals are based on the principle of mutual recognition. This is evidenced, for example, by the fact that the regulatory authorities under the MJDS retain discretion to intervene in various circumstances, while under the new proposals, registration statements on the new Forms F-11 and F-12 become effective without the SEC's review. The MJDS's reach, however, is much broader, providing special registration forms for offerings of *any* securities by Canadian issuers,

⁵³ For a description of the new proposals see Baum & Breidenbach, *supra* note 3, at 29; Daniel L. Goelzer & Anne H. Sullivan, *The Continuing Disclosure System: Problems and Participants*, in SECURITIES AND EXCHANGE COMMISSION REGULATION OF TRANSNATIONAL TENDER OFFERS, II SELECTED ARTICLES OF FEDERAL SECURITIES LAW 435 (1991); James M. Bartos, *A New Deal for U.S. Investors in Foreign Markets*, INT'L FIN. L. REV., July 1991, at 27; Bloomenthal & Wolff, *supra* note 45, § 7; Schimkat, *supra* note 41, at S215-25.

whereas the new proposals only address securities offerings of limited size in the context of mergers and acquisitions, as well as rights offerings by qualified foreign private issuers.

While this "second step" shows the continuing effort of the SEC to adapt the U.S. regulatory system to the internationalization of the markets, these new proposals are limited to a small group of securities issuers. Thus, a "third step," which would extend the scope of the MJDS to other countries, is necessary to attract a more significant group of market participants from abroad.

3.4. Limitations On The Scope Of The Application Of Section 5 Of The Securities Act

As previously mentioned, the U.S. securities market remains unattractive for many foreign issuers of securities due to the extensive reach of section 5 of the Securities Act.⁵⁴ Despite the adoption of measures to facilitate compliance, the extensive registration and disclosure requirements of the U.S. securities laws remain burdensome for foreign issuers. The SEC addressed this problem by adopting two new proposals which limit the applicability of section 5. Regulation S exempts offshore transactions, such as securities issued outside the United States, from the registration requirements of section 5. Rule 144A is designed to facilitate the resale of restricted securities, that is, securities which have not been registered with the SEC because they were issued under a private placement exemption.⁵⁵ Thus, under both Regulation S and Rule 144A, foreign issuers are exempt from the proscriptions of section 5.

⁵⁴ See *supra* note 12 and accompanying text.

⁵⁵ For a description of Regulation S and Rule 144A, see Bevis Longstreth et al., *Regulation S and Rule 144A: Has the SEC got it right?*, INT'L FIN. L. REV., Sept. 1989, at 30; HAROLD S. BLOOMENTHAL ET AL., 1992 GOING PUBLIC HANDBOOK: GOING PUBLIC, THE INTEGRATED DISCLOSURE SYSTEM AND EXEMPT FINANCING, §§ 2.07, 2.08. (1992); HAROLD S. BLOOMENTHAL ET AL., EMERGING TRENDS IN SECURITIES LAW, §§ 8, 9 (1989 ed.); for further bibliographic references, see *supra* note 37.

3.4.1. Regulation S

The purpose of Regulation S⁵⁶ is to clarify the extraterritorial application of section 5.⁵⁷ Section 901 contains the general statement that offers and sales of securities made outside the United States are not subject to the Securities Act registration requirement. Before the enactment of Regulation S, the scope of the extraterritorial application of section 5 was defined in Release 4708.⁵⁸ Under this release, section 5 did not apply if the offer was (i) distributed abroad; (ii) distributed only to foreign nationals; and (iii) had "come to rest abroad." The interpretation of whether an offer has "come to rest abroad" was especially unclear and resulted in frequent requests to the SEC for "no-action letters." In contrast to the approach under the old Release 4708, Regulation S takes a strict geographic approach: offers and sales occurring outside the United States, even if made to U.S. citizens, are beyond the scope of section 5.⁵⁹

⁵⁶ Regulation S was initially proposed in Securities Act Release No. 6779, [1987-1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,242 (June 10, 1988); repropoed in Securities Act Release No. 6838, [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,426 (July 11, 1989); and finally adopted in Securities Act Release No. 6863, [1989-1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,524 (Apr. 24, 1990).

⁵⁷ For a description of Regulation S, see Don Berger, *Offshore Distributions of Securities: The Impact of Regulation S*, 3 TRANSNAT'L LAW. 575 (1990); Ronald R. Adee, *Regulation S: The Safe Harbor for Offshore Securities Transactions*, 58 C.P.S. (BNA) (1991); Samuel Wolff, *Offshore Distributions Under the Securities Act of 1933: An Analysis of Regulation S*, 23 LAW & POL'Y INT'L BUS. 101 (1992); Beller & Pergam, *Regulation S: SEC seeks comment*, INT'L FIN. L. REV., Aug. 1988, at 15; for further bibliographic references, see *supra* notes 37, 53.

⁵⁸ See Securities Act Release No. 4708, Fed. Sec. L. Rep. (CCH), ¶¶ 1361-63 (July 9, 1964).

⁵⁹ See Berger, *supra* note 57, at 581; Securities Act Release No. 6863, states:

The Regulation . . . is based on a territorial approach to Section 5 of the Securities Act. The registration of securities is intended to protect the U.S. capital markets and investors purchasing in the U.S. market, whether U.S. or foreign nationals. Principles of comity and the reasonable expectations of participants in the global markets justify reliance on laws applicable in jurisdictions outside the United States to define requirements for transactions effected offshore. The territorial approach recognizes the primacy of the laws in which a market is located. As investors choose their markets, they choose the laws and regulations applicable in such

The general statement in section 901 provides several guidelines for determining whether a particular offer or sale occurs outside the United States. Following the general statement, Regulation S contains two safe harbor provisions, sections 903 and 904, which provide prospective issuers planning a foreign-targeted offering clearer guidance than the predecessor to Regulation S.⁶⁰ Both safe harbors are only available if two criteria, defined in section 902, are met: (i) the offer or sale must occur in an "offshore transaction;" and (ii) no "directed selling efforts" may be made in the United States. Section 903, the "issuer safe harbor," is designed for offers and sales by issuers and securities professionals involved in the distribution process. The "issuer safe harbor" is subdivided into three categories, taking into consideration (i) whether the issuer is a U.S. issuer, (ii) whether it is a reporting company under the 1934 Act, and (iii) the degree of interest in its securities in U.S. markets. Depending on which category applies, the offshore issue of securities is allowed either without further restrictions, or if certain restrictions designed to prevent a "flow-back" of the issued securities to the United States are met. These restrictions include selling periods, lock-up procedures, and legends on the securities. Section 904 is the "resale safe harbor," which applies to the resale of restricted securities outside the United States.

3.4.2. Rule 144A

The SEC adopted Rule 144A for two main reasons.⁶¹ The first was to provide greater liquidity in the secondary market

markets.

Securities Act Release No. 6863, *supra* note 56, at 80,665.

⁶⁰ "While certainly much more complex in its detailed definitional approach than old Release 4708, Regulation S has the potential advantage of obviating or reducing the need to seek administrative clarification from the Commission by way of no-action letters for particular transactions." Berger, *supra* note 57, at 582.

⁶¹ Rule 144A was initially proposed in Securities Act Release No. 6806, [1988-1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,335 (Oct. 25, 1988); repropoed in Securities Act Release No. 6839, [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,427 (July 11, 1989); and finally adopted in Securities Act Release No. 6862, [1989-1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,523 (April 23, 1990) (codified at 17 C.F.R. § 230.144A (1991)).

for privately placed securities. The second was to attract more foreign issuers to the U.S. market through greater liquidity of the secondary market, and to prevent domestic issuers from considering foreign securities markets as alternatives to the U.S. market. The issuance of securities in a private placement, without registering under section 5 of the Securities Act, results in a considerable cost reduction, up to two thirds less than a public distribution,⁶² and avoids the reporting requirements of a public company.⁶³

Resales are not "distributions" under Rule 144A⁶⁴ and thus qualify under the registration exemption of section 4(1) of the Securities Act. Thus, Rule 144A is another safe harbor provision designed to remove regulatory uncertainties. To qualify under Rule 144A, the restricted securities must be sold to a "qualified institutional buyer" ("QIB").⁶⁵ The rule defines

⁶² See Baum & Breidenbach, *supra* note 3, at 23; Glenn M. Reiter & Stephen B. Grant, *Resales of U.S. Privately-Placed Securities*, INT'L FIN. L. REV., Jan. 1989, at 20, 23.

⁶³ The SEC states in the initial proposal of Rule 144A:

Providing a framework in which institutional resales could be made freely may increase the efficiency of the private placement market. The potential increase in efficiency and liquidity could significantly lower the discount commonly associated with private placements Greater participation by foreign issuers in the U.S. capital markets also would have the benefit of reducing the costs borne by U.S. institutional investors that wish to invest in foreign securities and are compelled at present to go overseas to obtain such securities.

Securities Act Release No. 6806, *supra* note 61, at 89,533.

⁶⁴ For a detailed description of Rule 144A, see EDWARD F. GREENE ET AL., RULE 144A: THE EXPANDED PRIVATE PLACEMENT MARKET (1990); Sara Hanks, *Rule 144A: Another Cabbage in the Chop Suey*, 24 GEO. WASH. J. INT'L L. & ECON. 305 (1990); Vickie Kokkalenios, *Increasing United States Investment in Foreign Securities: An Evaluation of SEC Rule 144A*, 60 FORDHAM L. REV. S179 (1992); Lawrence R. Seidman, *SEC Rule 144A: The Rule Heard Round the Globe - Or the Sounds of Silence?*, 47 BUS. LAW. 333 (1991); Kellye Y. Testy, *The Capital Markets in Transition: A Response to New SEC Rule 144A*, 66 IND. L.J. 233 (1990); Reiter & Grant, *supra* note 58; for further bibliographic references see *supra* notes 37, 55.

⁶⁵ See 17 C.F.R. § 230.144A(a)(1). The SEC states in the initial proposal of Rule 144A: "The key to the analysis of proposed Rule 144A is that certain institutions can fend for themselves . . ." Securities Act Release No. 6806, *supra* note 61, at 89,539. The notion of being "able to fend for themselves" was introduced by the Supreme Court in *SEC v. Ralston Purina Co.*, 346 U.S. 119, 125 (1953). For a more detailed analysis of the theory behind Rule 144A, see Hanks, *supra* note 64, at 321-31; Seidman, *supra* note 64, at 337.

a QIB as an institution with a portfolio of securities valued at more than \$100 million owned or under its management.⁶⁶ The rule applies only to securities which are not "fungible." For example, it excludes those securities which are already traded on a national stock exchange or on the NASDAQ.⁶⁷ Furthermore, Rule 144A provides that the issuer, if it is not a reporting company under the Exchange Act or an eligible Schedule B⁶⁸ issuer, is obligated at the request of the seller or the buyer, to provide investors with certain reasonable and current business and financial information.⁶⁹ Finally, the seller is required to ensure that the purchaser is aware of the seller's reliance on Rule 144A to sell unregistered

⁶⁶ See 17 C.F.R. § 230.144A(a)(1)(i). Additional requirements exist for banks and savings and loan associations, including foreign banks and their U.S. branches. See 17 C.F.R. 230.144A(a)(1)(vi). \$10 million threshold is applied to brokers and dealers. For specific transactions no threshold applies. See 17 C.F.R. § 230.144A(a)(1)(ii). The definition of qualified institutional buyer as originally proposed by the SEC would have included institutions with assets in excess of \$5 million. Some commentators expressed fear that the rule would encourage the development of a private, unregulated securities market alongside the public market. The SEC, however, stated in its adoptive release of Rule 144A that it was open to further comment on this threshold and suggested expanding the scope of the safe harbor if experience proves the rule a success. See *supra* note 57. In October 1992, the SEC adopted Securities Act Release No. 6963, expanding the definition of qualified institutional buyer to include certain collective and master trusts and insurance company separate accounts. The amendment also permits any institution to include its holdings of U.S. government and similar securities in determining whether it is a QIB. See Securities Act Release No. 6963, [1992 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,052, 83,383 (Oct. 22, 1992)

⁶⁷ See Securities Act Release No. 6806, *supra* note 61, at 89,534. This exclusion is also designed to prevent the establishment of a private, unregulated market alongside the public regulated markets.

⁶⁸ Schedule B lists the matters which foreign governments or their subdivisions issuing debt securities must disclose.

⁶⁹ See 17 C.F.R. § 230.144A(d)(4). Many foreign issuers request an exemption from the reporting requirements of the Exchange Act under Rule 12g3-2(b). If an issuer qualifies for this exemption, it must furnish to the SEC on an ongoing basis material information which it (i) makes public in its home country; (ii) files with stock exchanges on which its securities are traded and which is made public by such exchanges; or (iii) distributes to its shareholders. This "home country information," which is on file with the SEC after obtaining the 12g3-2(b) exemption, is sufficient to comply with the aforementioned Rule 144A information requirements. For a description of Rule 12g3-2(b) see Sara Hanks & Daniel Bushner, *Rule 12g3-2(b): Backdoor or Thudoor?* INTL. FIN. L. REV. Apr. 1991, at 36.

securities.⁷⁰

3.4.3. *Combination Of Regulation S And Rule 144A*

Foreign investors that were not attracted to the U.S. securities market because of the extensive registration and reporting requirements have completely new opportunities through the combination of Regulation S and Rule 144A.⁷¹ Two ways of combining these sets of rules are particularly appealing. First, under Regulation S, non-U.S. issuers can sell securities offshore to a U.S. dealer who can buy the securities for immediate resale to a QIB under Rule 144A.⁷² Second, the acquisition of securities in a private placement is even more attractive since a resale is not only possible under Rule 144A, but also in an offshore transaction under Regulation S.

3.4.4. *An Evaluation Of The New Sets Of Rules Limiting The Scope Of Applicability Of Section 5 Of The Securities Act*

Regulation S and Rule 144A may have the most significant impact of all the recent legislative measures designed to increase the interest of foreign issuers in the U.S. market and decrease the migration of U.S. business offshore.⁷³ Under

⁷⁰ See 17 C.F.R. § 230.144A(d)(2).

⁷¹ For a description of the effects of such a combination of Regulation S and Rule 144A, see Longstreth et al., *supra* note 55, at 33; Hanks, *supra* note 64, at 333 n.149; Reiter & Grant, *supra* note 62, at 22-23; Palm & Walkovik, *supra* note 12, at 77; BAUM & BREIDENBACH, *supra* note 3, at 27.

⁷² The offer and sale of securities offshore to a U.S. dealer and the resale to a qualified institutional buyer in the United States relieves foreign issuers of the risk of being subjected to U.S. disclosure requirements under the 1934 Act. If foreign issuers would enter the U.S. market directly under Rule 144A, and their securities leak into the public markets, they could lose their Rule 12g3-2 exemption from the 1934 Act reporting requirements. See *supra* note 69. Thus, only a combination of these rules will increase the attractiveness of the U.S. securities markets. See *Proposed Rule 144A May Not Attract Foreign Issuers to U.S. Markets*, SEC Told, 21 Sec. Reg. & L. Rep. (BNA), at 413 (Mar. 17, 1989); Longstreth et al., *supra* note 55, at 32.

⁷³ The impact of Rule 144A is strengthened through the creation of PORTAL (Private Offerings, Resales and Trading through Automated Linkages). PORTAL is an SEC-approved screen-based computer and communication system which is operated by the NASD since the summer of 1990. PORTAL established an exempt marketplace for the trading of unregistered foreign securities under Rule 144A. See COX ET AL., *supra* note 4, at 485; Seidman, *supra* note 64, at 344-46.

these measures, foreign issuers can issue securities in the U.S. private placement market, and U.S. securities can be issued and traded abroad, without registration under the Securities Act. Thus, the burden of compliance with the U.S. securities laws is reduced significantly by Regulation S and Rule 144A, even more so than under the new reporting requirements for foreign issuers,⁷⁴ or under the MJDS⁷⁵ and the new proposals regarding cross-border rights, tender and exchange offers.⁷⁶ The reach of the new reporting requirements for foreign issuers and the MJDS, however, is much broader. The requirements apply to the issuance of *any* securities by foreign issuers. Regulation S and Rule 144A, on the other hand, only apply to offshore transactions or to transactions in the private placement market.

Nevertheless, several commentators have criticized Rule 144A. One commentator highlighted the inconsistency between the requirements to qualify as an "accredited investor" under Regulation D (for example, an institution with only \$5 million in assets or individuals with even fewer assets), and to qualify as a QIB under Rule 144A (for example, an institution with \$100 million in securities).⁷⁷ It does not seem just that a small institution may buy securities directly from the issuer under Regulation D, but may not buy the same securities under Rule 144A from another source.⁷⁸ Further, limiting the number of potential buyers under Rule 144A also limits the scope of this rule.

A second criticism is that under current Rule 144A, foreign issuers are encouraged to participate only in the private

The adoption of Rule 144A is a qualified success. "As of April 1993, approximately \$5.30 billion in equity and \$5.57 billion in debt securities of foreign issuers have been sold in Rule 144A placements in the United States." Securities Act Release No. 33-6999, 58 Fed. Reg. 27,686, 27,687 n.6 (1993). For more detailed information about the success of Rule 144A see SEC, STAFF REPORT ON RULE 144A (Jan. 27, 1993).

⁷⁴ See *supra* Section 3.1.

⁷⁵ See *supra* Section 3.2.

⁷⁶ See *supra* Section 3.3.

⁷⁷ See Seidman, *supra* note 64, at 349. In addition to the general exemption for private placements under § 4(2) of the Securities Act, Regulation D establishes exemptions for non-public and other limited offerings.

⁷⁸ See Hanks, *supra* note 64, at 341; Kokkalenios, *supra* note 64, at S193-94; Seidman, *supra* note 64, at 348-504.

market, and not in the public market. Several commentators suggest that the changes of the reporting and disclosure requirements do not reach far enough, and that the only way to attract foreign issuers into the U.S. capital market is to extend the harmonization previously achieved under the MJDS to other countries.⁷⁹

The effect of Regulation S was limited by the enactment of the "TEFRA D"-rules by the Internal Revenue Service (the "IRS").⁸⁰ The IRS is concerned about bearer bonds, which are very common in Europe, and which may provide ways for people to avoid U.S. taxes. The previous IRS regulations were designed to correspond with the old Release 4708. The new rules of the IRS, however, do not correspond to Regulation S. They are far more stringent for U.S. reporting issuers. Thus, these issuers have to take into consideration two different sets of rules, one from the IRS and one from the SEC. The more stringent IRS rules prevent Regulation S from achieving its goals, at least as far as bearer debt obligations are concerned. This indicates that efficient capital markets can only be achieved if tax and other laws comport with the goals of the securities laws.

However, it can be concluded that despite the SEC's rather cautious retreat from their traditional approach vis à vis international securities transactions, Regulation S and Rule 144A have already had a significant impact in attracting foreign issuers into the U.S. securities markets.⁸¹

4. NEW LEGISLATIVE DEVELOPMENTS IN EUROPE

Legislative developments relating to the internationalization of the European capital markets are two-fold. On one hand, within its general efforts to create a single common market for goods, labor, capital, and services, there is a movement toward harmonization of securities laws within the European Community. On the other hand, individual

⁷⁹ See Hanks, *supra* note 64, at 350-51; Karmel, *supra* note 13, at 15-16; see *infra* text accompanying note 204.

⁸⁰ See Treas. Reg. § 1.163-5(c)(2)(i)(D) (as amended in 1990). For a short description of the "TEFRA D"-rules and their effect on Regulation S, see Robert Clow, *All Quiet on the Euromarket Front*, INT'L FIN. L. REV., Feb. 1991, at 13.

⁸¹ See *supra* note 73 and accompanying text.

member states are instituting legislative changes to adapt their respective national regulatory system to the European Community in order to attain a competitive securities market.⁸² In the following description, Germany, having one of the least regulated systems in the European Community, is used as a representative model of the different national reforms taking place. All of these legislative changes can be characterized as both deregulatory and re-regulatory in nature.⁸³

4.1. *Legislative Developments Within The European Community*

The legislative harmonization within the Community regarding the different national regulations of the securities markets is only a part of the more general efforts of the Community to create a single market.⁸⁴ A description of the history and the institutions, as well as the legislation with respect to the Community's creation of a single market, is beyond the scope of this Article.⁸⁵ Nevertheless, a short explanation of the legislative mechanism through which harmonization will be achieved is useful.

The principle instruments of Community action under the EC Treaty are the "Regulation," the "Directive" and the "Recommendation."⁸⁶ The harmonization measures of the

⁸² See *supra* text accompanying notes 27, 29.

⁸³ For an explanation of the interference of deregulation and regulation, see NORMAN S. POSER, *INTERNATIONAL SECURITIES REGULATION: LONDON'S "BIG BANG" AND THE EUROPEAN SECURITIES MARKETS* 1-5 (1991), who entitles this section "The Paradox of Simultaneous Deregulation and Regulation"; Manning G. Warren III, *Global Harmonization of Securities Laws: The Achievements of the European Communities*, 31 HARV. INT'L L.J., 185, 187-89 (1990) [hereinafter *Harmonization*].

⁸⁴ See *supra* text accompanying notes 25-26.

⁸⁵ For a short description of the background of the Community and the different measures to create a single market, see BLOOMENTHAL & WOLFF, *supra* note 45, at § 10-5-10 with further bibliographical references; WYMEERCH, *supra* note 25, at 1-3; *Harmonization*, *supra* note 83, at 195-97; Manning G. Warren III, *Regulatory Harmony in the European Communities: The Common Market Prospectus*, 16 BROOK. J. INT'L L. 19, 22-25 (1990) [hereinafter *Prospectus*]; DIETHER HOFFMANN, *BANKEN- UND BÖRSENRECHT DER EWG* ch. 1-3 (1990); *Common Market in Profile*, 1 Common Mkt. Rep. (CCH) ¶ 100 (1988); *id.* at ¶ 101 (1987).

⁸⁶ For a short explanation of these different legislative instruments see

Community have been carried out mostly through the adoption of Council "directives" which must be implemented by legislation in each member state. These directives are binding on each member state to which they are addressed, but leave to the member states the choice of form and the method of implementation into national law.⁸⁷

The legislative efforts of the Community to harmonize the national regulations of the securities markets are manifold. Directives which are directly related to the area of securities regulation will be discussed in the following sections of this Article. The company law directives are also related to the Community's efforts to harmonize the securities markets. Although these company law directives are not the focus of this Article,⁸⁸ they must be mentioned to understand the scope and the magnitude of the Community's initiatives in the financial services area. Furthermore, it is also outside the scope of this Article to describe the existing and proposed directives relating to investment services, notwithstanding their importance to the internationalization of the securities markets.⁸⁹ Thus, the following description will be limited to the existing and proposed directives concerning the issuance, and trade of, securities. The underlying purpose of most of these directives is the removal of barriers resulting from the conflicting regulatory requirements of the individual member states. The enacted and proposed directives aim to provide greater flexibility in, and greater access to, the capital markets of the Community, and an equivalent standard of protection

WYMEERCH, *supra* note 25, at 2-3; *Law Making Powers of the Institutes*, 3 Common Mkt. Rep. (CCH) ¶ 4902 (1976).

⁸⁷ For a short description of the legal status of directives and their implementation into national law, see WYMEERCH, *supra* note 25, at 10-11; *Law Making Powers of the Institutes*, *supra* note 86, at 4116-17.

⁸⁸ For a short description of the Company law directives, see *Harmonization*, *supra* note 83, at 197-209.

⁸⁹ For a description of the two Banking Directives, the Own Funds Directive, the Solvency Ratio Directive, a draft of Investment Services Directive (which is not expected to be adopted until the end of 1993), and the Capital Adequacy Directive, see Reid & Ballheimer, *supra* note 27, at 103-20 (outlining all six directives); HOFFMANN, *supra* note 85; WYMEERCH, *supra* note 25, at 29-32; BLOOMENTHAL & WOLFF, *supra* note 45, § 10.03 (examining all six directives); POSER, *supra* note 83, at 347-53; *Harmonization*, *supra* note 83, at 221-24 (outlining the Investment Services Directive).

for investors.⁹⁰

4.1.1. *The Council Directive Implementing Article 67 Of The EC Treaty*

One of the four “founding freedoms” upon which the Community is based is the free movement of capital.⁹¹ The free movement of capital is especially important for the creation of a truly integrated single securities market. After a series of directives, the Council finally passed a directive implementing Article 67 of the EC Treaty, which required the abolition of all restrictions on the movement of capital between residents of the Community.⁹² Under this directive, the member states were required to eliminate these restrictions by July 1, 1990, with transitory provisions for some member states lasting until December 31, 1992. Until the passage of the directive, the major restrictions on the free movement of capital had been exchange controls. The goal of free movement of capital encompasses, among many other monetary transactions, all transactions in listed and unlisted securities.⁹³

4.1.2. *The Admissions Directive*

The Admissions Directive,⁹⁴ which was adopted in 1979, defines the minimum requirements⁹⁵ for the listing of equity and debt securities on stock exchanges in the Community. These minimum requirements are defined in schedules A and B for equity and debt securities, respectively. Moreover, the Admissions Directive imposes continuing obligations, such as, reporting requirements, under schedules C and D for issuers

⁹⁰ See Reid & Ballheimer, *supra* note 27, at 123.

⁹¹ See EEC Treaty, pt. 2, tit. III.

⁹² See Council Directive 88/361, 1988 O.J. (L 178) 5, 7.

⁹³ For a short description of the directive implementing Article 67 of the EEC Treaty see Reid & Ballheimer, *supra* note 27, at 123; WYMERCH, *supra* note 25, at 7.

⁹⁴ See Council Directive 79/279, 1979 O.J. (L 66) 21, *as amended by*, Council Directive 82/148, 1982 O.J. (L 62) 22.

⁹⁵ Generally, the directives define minimum standards giving the member states the discretion to impose more stringent requirements than set forth in the directives, as long as these requirements are applied on a non-discriminatory basis.

of equity and debt securities, respectively.⁹⁶

4.1.3. *The Listing Particulars Directive*

The Listing Particulars Directive,⁹⁷ which was adopted in 1980, defines minimum requirements⁹⁸ for drafting, scrutinizing, and distributing an information statement (the "listing particular"), which must be filed in connection with the listing of securities on a stock exchange. The listing particular also aims to facilitate the simultaneous and consecutive listing of a security in a number of different member states.⁹⁹ Layout and detailed disclosure requirements are defined in schedules A and B for equity and debt securities, respectively.¹⁰⁰

4.1.4. *The Interim Reports Directive*

The Interim Reports Directive,¹⁰¹ which was adopted in 1982, sets forth certain requirements for semiannual reporting, complementing the annual and current reporting requirements of the Admission Directive. It defines certain minimum financial information¹⁰² which must be disclosed and requires the publication of an explanatory statement which must refer to the company's financial prospects for the remainder of the fiscal year.¹⁰³

⁹⁶ For a further description of the Admissions Directive, see Reid & Ballheimer, *supra* note 27, at 124-25; *Harmonization*, *supra* note 83, at 209-11; WYMEERCH, *supra* note 25, at 14, 16-17; HOFFMANN, *supra* note 85, at 107-08; Admission of Securities to Official Listing, 1 Common Mkt. Rep. (CCH) ¶ 1725 (Aug. 30, 1983).

⁹⁷ See Council Directive 80/390, 1980 O.J. (L 100) 1, as amended by, Council Directive 82/148, 1982 O.J. (L 62) 22.

⁹⁸ See *supra* note 95.

⁹⁹ See *infra* notes 108-14 and accompanying text.

¹⁰⁰ For a more detailed description of the Listing Particulars Directive, see Reid & Ballheimer, *supra* note 27, at 125-26; *Harmonization*, *supra* note 83, at 211-13; WYMEERCH, *supra* note 25, at 14, 16-17; HOFFMANN, *supra* note 85, at 107-08; Publication of Listing Particulars, Commentary, 1 Common Mkt. Rep. (CCH) ¶ 1735 (June 1990).

¹⁰¹ See Council Directive 82/121, 1982 O.J. (L 48) 26, 27-28.

¹⁰² See *supra* note 95.

¹⁰³ For a more detailed description of the Interim Reports Directive, see Reid & Ballheimer, *supra* note 27, at 126-27; *Harmonization*, *supra* note 83, at 214-15; WYMEERCH, *supra* note 25, at 14, 20; HOFFMANN, *supra* note 85,

4.1.5. *The Public Offer Prospectus Directive*

The Public Offer Prospectus Directive, which was adopted in 1989, requires the publication of a prospectus in connection with the public offering of securities, regardless of whether or not these securities are listed on a stock exchange.¹⁰⁴ Thus, before a public offering is effective, any issue of securities in the Community now requires the publication of a prospectus, either through the listing particular or under the Public Offer Prospectus Directive.¹⁰⁵ The prospectus' minimum requirements¹⁰⁶ are similar to those of the listing particulars, and, thus, eliminate disclosure disparities that may discourage listing on a stock exchange. If the security is to be listed on an exchange, the prospectus requirements are fulfilled by the requirements of the Listing Particulars Directive. If no such listing is required, the prospectus must comply with the requirements of the Public Offer Prospectus Directive. The directive, therefore, harmonizes the disclosure standards for the offering of securities and marks the first step toward a Community prospectus which could be used interchangeably in all member states.¹⁰⁷

at 107-08; Interim Reports by Listed Companies, Explanation, 1 Common Mkt. Rep. (CCH) ¶ 1745 (Aug. 30, 1983).

¹⁰⁴ See Council Directive 89/298, 1989 O.J. (L 124) 8.

¹⁰⁵ Notwithstanding the general requirement to publish a prospectus before any public offering of securities, certain classes of securities or types of offers are excluded. Furthermore, member states have the option to exempt certain classes of securities from the prospectus requirement if equivalent information is available to investors as a result of the stock exchange disclosure requirements. For more details about these exemptions, see POSER, *supra* note 83, at 363-64; Reid & Ballheimer, *supra* note 27, at 130; Commentary: Investor protection in public offer of shares (Directive 89/298), 1 Common Mkt. Rep. (CCH) ¶ 1753, at 1393-16 (June 1990) [hereinafter Investor Protection].

¹⁰⁶ See *supra* note 95.

¹⁰⁷ For a more detailed description of the Public Offer Prospectus Directive see Reid & Ballheimer, *supra* note 27, at 129-32; *Prospectus*, *supra* note 85, at 31-48; *Harmonization*, *supra* note 83, at 215-18; WYMERCH, *supra* note 25, at 14-16; HOFFMANN, *supra* note 85, at 108; POSER, *supra* note 83, at 359-64; *Investor Protection*, *supra* note 105, ¶ 1753.

4.1.6. *Directives Conferring Mutual Recognition For Listing Purposes And Prospectus Requirements*

Originally, these stock exchange directives (the Admissions Directive, the Listing Particulars Directive, and the Interim Reports Directive) attempted to harmonize the listing requirements throughout the Community so that a single listing document would be recognized by all stock exchanges within the Community. However, soon after their passage, it became apparent that the harmonization effort would not be successful. Accordingly, the Council limited the harmonization attempt to two goals: mutual recognition of (i) listing documents and (ii) offer prospectuses.¹⁰⁸

The Mutual Recognition Directive,¹⁰⁹ adopted in 1987, provides that listing particulars which are approved by a competent authority in one member state must be recognized in all other member states without further action or information requirements.¹¹⁰ The Second Mutual Recognition Directive,¹¹¹ adopted in 1990, extends the principle of mutual recognition to public offer prospectuses which are used in the sale of listed securities in another member state. If a public offer prospectus meets the standards of the listing particulars and is approved in one member state within the three preceding months, then other member states are required to recognize the prospectus as a valid listing particular.¹¹² A proposed amendment to the Mutual Recognition Directive¹¹³ extends mutual recognition to all public offer prospectuses. Thus, mutual recognition would also apply if the securities have not been previously listed on a

¹⁰⁸ See Reid & Ballheimer, *supra* note 27, at 127.

¹⁰⁹ See Council Directive 87/345, 1987 O.J. (L 185) 81 (amending the Listing Particulars Directive).

¹¹⁰ The listing particular, however, must be translated and additional information specific to the markets of the member state which recognizes the document must be included.

¹¹¹ Council Directive 90/211, 1990 O.J. (L 112) 24 (amending the Listing Particulars Directive).

¹¹² Again, the translation requirement and the requirement of incorporation of specific information relating to the markets of those other member states must also be met in this case.

¹¹³ Eur. Parl. Doc. (COM 133) art. 24(b)(1) (1989).

member state's exchange.¹¹⁴

Mutual recognition, however, is not always required. If an exemption or partial release from the requirements of the listing particular or public offer prospectus has been granted in one member state, mutual recognition is not required, if such an exemption is not allowed in the member state in which recognition is sought. Additionally, recognition is not required if the conditions under which such an exemption has been granted in one member state are not met in the other member state. Therefore, issuers that seek listing on stock exchanges in several member states should consider carefully whether they want to qualify under an exemption or waiver.

If an issuer is from outside the Community, mutual recognition may be granted on an optional basis. The Community may agree with outside countries that listing particulars drawn up and approved in accordance with the rules of such outside countries may be recognized if two conditions are met: (i) there must be reciprocity, and (ii) the rules of the outside country must guarantee equivalent investor protection.¹¹⁵

4.1.7. *The Insider Trading Directive*

The Insider Trading Directive, which was adopted in 1989, establishes the prohibition against insider trading throughout the Community.¹¹⁶ Until the Directive's adoption, national laws on insider trading within the individual member states was considerably disparate. Some member states had legislation against insider trading, other member states had no prohibition against insider trading at all, and Germany had only self-regulatory rules under which market operators agreed not to engage in insider trading.¹¹⁷ Thus, in

¹¹⁴ See *Harmonization*, *supra* note 83, at 214.

¹¹⁵ For a more detailed description of the Mutual Recognition Directives, see HOFFMANN, *supra* note 85, at 108; POSER, *supra* note 83, at 362-63; WYMERCH, *supra* note 25, at 15; Reid & Ballheimer, *supra* note 27, at 127-29; *Harmonization*, *supra* note 83, at 213-14, 217-18; *Prospectus*, *supra* note 85, at 29-31, 46-49.

¹¹⁶ Council Directive 89/592, 1989 O.J. (L 334) 30.

¹¹⁷ For a comprehensive description of the various national regulations on insider trading, see Christine A. McGuinness, Note, *Toward the Unification of European Capital Markets: The EEC's proposed Directive on Insider Trading*, 11 FORDHAM INT'L L.J. 432, 438-47 (1988); see also KLAUS

prohibiting insider trading through certain minimum requirements,¹¹⁸ the Insider Trading Directive aims to harmonize the various existing laws of the member states.¹¹⁹

The Insider Trading Directive defines "inside information"¹²⁰ and prohibits insider trading for primary and secondary insiders¹²¹ in "transferable securities."¹²² The directive does not specify sanctions for violations of its prohibitions. Instead, it provides that sanctions must be determined by the individual member states that enact the directive into national law.¹²³ Furthermore, the directive

J. HOPT, EUROPÄISCHES UND DEUTSCHES INSIDERRECHT, ZEITSCHRIFT FÜR UNTERNEHMENS-UND GESELLSCHAFTSRECHT 17, 51-65 (1991) [hereinafter INSIDERRECHT]; for an extensive collection of studies about insider trading in Europe, see generally EUROPEAN INSIDER DEALING (Klaus J. Hopt & Eddy Wymeersch eds., 1991). For a discussion of the variety of European insider trading law and the developments which led to the adoption of the insider trading directive, see THOMAS C. PAEFGEN, INSIDERHANDEL ZWISCHEN GEMEINSCHAFTSRECHTLICHER INTEGRATION UND NATIONALSTAATLICHER REGELUNG -E PLURIBUS UNUM, DIE AKTIENGESELLSCHAFT 380 (1991).

¹¹⁸ See *supra* note 95.

¹¹⁹ For a more detailed description of the Insider Trading Directive see Reid & Ballheimer, *supra* note 27, at 137-40 (describing both the insider dealing directive and the sanctions for violation); *Harmonization*, *supra* note 83, at 219-21; WYMEERCH, *supra* note 25, at 23-24; HOFFMANN, *supra* note 85, at 109-10; Commentary: Control of Insider Dealing (Directive 89/592), 1 Common Mkt. Rep. (CCH) ¶ 1763 (June 1990); POSER, *supra* note 83, at 353-57; BLOOMENTHAL & WOLFF, *supra* note 45, § 10.05[1]; Klaus J. Hopt, *The European Insider Dealing Directive*, 27 COMMON MKT. L. REV. 51, 57-72 (1990); *Insiderrecht*, *supra* note 117, at 28-51. See generally Raffaello Fornasier, *The Directive on Insider Dealing*, 13 FORDHAM INT'L L. J. 149, 149-77 (1990) (examining the provisions of the insider dealing directive from conception, to passage, to planned implementation); McGuinness, *supra* note 117, at 432 (examining the individual nations' laws on insider trading and analyzing the Community's directive).

¹²⁰ Inside information is defined in art. 1(1) as: "[i]nformation which has not been made public of a precise nature relating to one or several issuers of transferable securities, . . . which, if it were made public, would be likely to have a significant effect on the price of the transferable security or securities in question." See Council Directive 89/592, *supra* note 116, at 31.

¹²¹ A secondary insider is defined in art. 4 being one who knowingly possesses inside information, the origin of which could only be a primary insider. Thus, the Insider Trading Directive applies also to "tippees." *Id.* at 31.

¹²² Under art. 1(2) such transferable securities include shares, debt securities, futures, options and index contracts that are traded on an organized market which is accessible to the public and regulated by authorities. See *id.* at 31.

¹²³ Article 13 only requires penalties that are "sufficient to promote
<https://scholarship.law.upenn.edu/jil/vol14/iss4/2>

supplements the current reporting requirements set forth in the Admissions Directive by requiring all companies whose securities are traded on recognized markets to disclose promptly any major developments which would likely have a material effect on the price of securities.¹²⁴

4.1.8. Other Legislative Developments

Besides the above-mentioned legislative developments, several other directives concerning the issuing and trading of securities were adopted or proposed in recent years. Since neither the Listing Particulars Directive, nor the Public Offer

compliance." *See id.* at 31. It remains unclear whether such penalties have to be criminal or civil. Therefore, the member states may adopt different penalties, thereby contributing to the lack of harmonization of insider trading laws.

¹²⁴ *See id.* at 36. This disclosure requirement seems to be stronger than comparable requirements in the United States, where companies are permitted in certain cases to remain silent or take a "no comment" position in case of merger negotiations and other early stages of transactions, see, e.g., *Basic, Inc. v. Levinson*, 485 U.S. 224, 239 n.17 (1988) (silence is equivalent to no comment position and both are acceptable in defending against a misleading statement). The directive provides however, that the competent authority may relieve the issuer of this disclosure obligation if the disclosure would prejudice the companies legitimate interests. For a description of the extent of these disclosure requirements and the interpretative questions which may arise, see POSER, *supra* note 83, at 356-57.

The Insider Trading Directive differs in various other respects from the regulation of insider trading in the United States. *See McGuinness, supra* note 117, at 449-51. One of the most significant differences lies in the fact that liability for insider trading in the United States traditionally required a fiduciary relationship. *See Chiarella v. United States*, 445 U.S. 222, 227-28, 232 (1980) (duty to disclose arises when one has fiduciary duty to another) and *Dirks v. SEC*, 463 U.S. 646, 653 (1983) (citing *Chiarella* and noting the necessity of a fiduciary relationship for liability). The Community directive however, does not require a fiduciary relationship and instead adopts the "misappropriation theory." *Compare Carpenter v. United States*, 484 U.S. 19, 27 (1987) (concept of fraud in an insider information scheme includes "fraudulent appropriation of information") and *United States v. Chestman*, 947 F.2d 551, 564 (2d Cir. 1991), *cert. denied*, 112 S. Ct. 1759 (1992) (distinguishing the application of the misappropriation theory in *Dirks* and *Chiarella* and denying its application in case at bar which involved familial relationships).

The second major difference lies in the fact that under the directive insiders cannot be sued for damages by other holders of securities as permitted under Rule 10b-5. The third major difference is that the United States seems to have a great advantage over the Community in the area of enforcement.

Prospectus Directive apply to mutual funds, a Mutual Funds directive¹²⁵ was adopted in 1985. It defines a separate system for the recognition and marketing of mutual funds throughout the Community. The Major Shareholder Directive, which was adopted in 1988, requires the disclosure of transactions involving significant holdings in listed companies.¹²⁶ Furthermore, an amended proposal for a Takeover Directive¹²⁷ was published in 1990. This directive is designed principally to protect the shareholders of target companies when faced with a takeover bid.

4.2. An Evaluation Of The Legislative Developments Of The European Community

The many directives which have been adopted in recent years have greatly harmonized the securities law throughout the Community. Traditionally, securities regulation in Europe has been described as "virtually nonexistent outside the United Kingdom."¹²⁸ The European stock exchanges are organized under self-regulatory systems, and exist practically without supervision by national governments. Most member states did not have a system of full disclosure for the issuance and trading of securities, and insider trading was not prohibited in many member states. Once the member states have fully implemented the directives into their respective national bodies of law, a harmonized system of securities regulations will exist throughout the Community. Based on a mandatory disclosure philosophy, this regulatory system will generally mandate higher disclosure standards than those which have previously existed in the member states with the goal of giving to the public fair, accurate, clear, adequate and timely information. The directives achieve harmonization by establishing both minimum standards for issuance of securities and mutual recognition.

¹²⁵ Council Directive 85/611, 1985 O.J. (L 375) 3, *as amended by*, Council Directive 88/220, 1988 O.J. (L 100) 31.

¹²⁶ Council Directive 88/627, 1988 O.J. (L 348) 62.

¹²⁷ Commission Proposal 90C 240/09, 1990 O.J. (C 240) 7.

¹²⁸ See *Harmonization*, *supra* 83, at 194-95 (citing an interview with Professor L.C.B. Gower discussing the lack of regulation of securities transactions outside the United Kingdom and the self-regulatory characteristics of the other European stock exchanges).

The overall goal of the harmonization efforts is to establish an integrated securities market throughout the Community. Both listing particulars and public offer prospectuses, which are mutually recognized, facilitate the listing and public offering of securities throughout the Community and lower the related costs significantly. This, as well as raising public confidence and heightening the analysis of corporate disclosure, increases the attractiveness of the European securities market. Therefore, this market may become more competitive vis à vis other major capital markets, namely, the U.S. market. Another goal of the harmonization efforts is the promotion of greater competition in the financial services sector, which would again reduce the costs of raising capital.¹²⁹

Despite these goals, the harmonization efforts within the Community have not been entirely successful. Under the 1992 harmonization deadline only minimum standards, accompanied by mutual recognition, were established. Thus, many regulations have the character of a compromise. Commentators have stated that the Community chose "harmony now" at the price of "discord later."¹³⁰

Several factors contribute to the limitations of the harmonization efforts. The minimum standard approach, for instance, does not preclude certain member states from imposing more stringent requirements when enacting the directives in their national laws.¹³¹ Furthermore, many directives provide several exceptions and exclusions¹³² which reduce both their scope and effectiveness. Moreover, although directives themselves are binding on each member state, member states can choose the form and method of

¹²⁹ For a description of the benefits of the harmonization of the security laws in the Community see Reid & Ballheimer, *supra* note 27, at 142-44 (noting that harmonization efforts may increase attractiveness to investors, attract companies from the U.S. market, and promote cooperation among the nations' financial sectors); *Harmonization*, *supra* note 83, at 224-29 (noting the benefits resulting from increased regulation and harmonization to include investor protection and better access to non-EC companies).

¹³⁰ See *Harmonization*, *supra* note 83, at 231 (quoting THE ECONOMIST, 1992 Survey).

¹³¹ See *supra* note 95.

¹³² See *supra* note 105.

implementation into national law,¹³³ which creates another limitation on harmonization goals. The sanctions for violations of the insider trading prohibition, for example, are determined by each member state according to the Insider Trading Directive.¹³⁴ Further limitations on the harmonization efforts result from some areas of the securities market which still lack any regulation. Finally, the absence of an institutional mechanism for the coordination and enforcement of the new regulatory system reduces the chance of efficient and effective harmonization.¹³⁵ The enforcement efforts of the national government authorities, therefore, will vary greatly among the member states.¹³⁶

On the other hand, several existing factors will strengthen harmonization. Commentators suggest that once the directives are implemented in the national legislation of the member states, a larger class of "European corporations" which engage in a multijurisdictional common securities market may develop. These "European corporations" may develop a new corporate psychology which would produce higher disclosure levels.¹³⁷ This may result from managements' desire to develop a "world class image" or through the influence of third party professionals whose services will be needed for operation on an European level.¹³⁸ Commentators further suggest that mutual recognition provided by the directives mandates regulatory cooperation among the respective national authorities. This cooperation, which will increase contact and cooperation between those authorities, will likely lead to a consensus among them about optimal disclosure levels.¹³⁹ Furthermore, competition among member states may lead to a "regulatory meltdown," that is, a deregulation down to the minimum standards provided by the directives.¹⁴⁰

¹³³ See *supra* note 87 and accompanying text.

¹³⁴ See *supra* note 123 and accompanying text.

¹³⁵ See *Harmonization*, *supra* note 83, at 231 (suggesting the establishment of an international securities commission).

¹³⁶ For a description of the shortcomings of the Community's security laws see *Harmonization*, *supra* note 83, at 229-32.

¹³⁷ See *Prospectus*, *supra* note 85, at 49-50.

¹³⁸ *Id.*

¹³⁹ *Id.*

¹⁴⁰ *Id.*

It can be concluded that despite the differences between the national regulations in the member states which will still exist in the future, the Community's "will to harmonize has produced an unprecedented convergence of disparate regulatory standards."¹⁴¹ Indeed, "[n]o other bilateral or multilateral international accords have approached this degree of success."¹⁴² The Community has "established the world's only multinational disclosure system . . . and the first multi-state prohibition of insider trading."¹⁴³ Indeed, the Community is "the world's only multinational securities regime"¹⁴⁴ Accordingly, even if the degree of harmonization achieved is incomplete, the achieved system will be a significant step toward a single European securities market that is capable of attracting more investors and issuers than ever before.

4.3. Legislative Developments In Germany

4.3.1. The Present Regulation Of The Securities Markets In Germany

As indicated above, the German securities market is limited in size, but highly deregulated.¹⁴⁵ The regulation of the securities market in Germany gives a "diffuse and confusing impression."¹⁴⁶ The German securities market is

¹⁴¹ *Id.* at 52.

¹⁴² *Id.* at 52-53.

¹⁴³ See *Harmonization*, *supra* note 83, at 232.

¹⁴⁴ *Id.* at 193.

¹⁴⁵ See *supra* notes 31-32 and accompanying text. For further figures on the size of the German securities market, see Feddersen & Skala-Kuhmann, *Germany*, in *INTERNATIONAL SECURITIES REGULATION* 12-14 (Rosen ed., 1991); Röhm, *Germany*, in *INTERNATIONAL CAPITAL MARKETS AND SECURITIES REGULATION* 8C:19-22 (Bloomenthal ed., 1990); Gerhard Wegen, *Germany*, in *INTERNATIONAL SECURITIES LAW* 127-28 (Euromoney ed. 1992) [hereinafter *Germany*]; Claudius Dechamps, *West Germany*, *INT'L FIN. L. REV.*, July 1990 Supp., at 85 (Euromoney ed.); POSER, *supra* note 83, at 392-93; for the newest available figures, see *ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES* 1992 (1992); for figures about the influence of institutional investors in Germany see Thomas C. Paefgen, *Institutional Investors Ante Portas: A Comparative Analysis of an Emergent Force in Corporate America and Germany*, 26 *INT'L LAW.* 327, 328-31 (1992).

¹⁴⁶ Eberhard Schwark, *Regulation of the German Capital Markets - Present Situation, Problems and Outlook*, 1 *J. COMP. CORP. L. & SEC. REG.*

regulated by a variety of statutes. No general statute regulating issuance and trading of securities exists which would be analogous to the U.S. Securities Act or the U.S. Exchange Act. The legislation of the securities markets in Germany is contained in the corporation law, in market-related statutory rules, and in several self-regulatory rules promulgated by the industry.¹⁴⁷ Furthermore, although a federal securities supervisory agency will be established in the upcoming legislative reform,¹⁴⁸ no such agency exists today. Therefore, there is still a fragmentation of the organs of control, which leads to certain loopholes in the supervision of the market.¹⁴⁹

The German securities market consists of different market segments. One principal distinction must be drawn between the traditional stock exchange market and "off exchange trading."

The trading on the three different segments of the stock exchanges occurs under the regulation of the Stock Exchange Act (the "*Börsengesetz*").¹⁵⁰ The three segments are the official trading (the "*Amtlicher Handel*"), the regulated market (the "*Geregelter Markt*") and the free market (the "*Freiverkehr*").¹⁵¹ Germany has eight regional stock exchanges, located in Berlin, Bremen, Düsseldorf, Frankfurt,

299, 299 (1978) [hereinafter *German Capital Markets*]. Although this article is partly outdated, it still gives a thorough and accurate description of the structure of the German securities market.

¹⁴⁷ For a description of the German legal system in general see Feddersen & Skala-Kuhmann, *supra* note 145, at 1-2. For a description of the legal rules with respect to the German securities market, see *German Capital Markets*, *supra* note 146, at 301-10; Röhm, *supra* note 145, at 8C:19-22, 8C:49-56; ASSMANN, *supra* note 3, at 11-12; Robert J. Dilworth, Germany, *Exemptions for Institutional Investors or Concepts on Non-Public Offerings: A Comparative Study*, 13 U. PA. J. INT'L BUS. L. 529, 530-31 (1993); for references on the regulation of legal entities versus the regulation of the market see *infra* note 197.

¹⁴⁸ See *infra* notes 191-93 and accompanying text.

¹⁴⁹ For a description of the existing organs of control, see Feddersen & Skala-Kuhmann, *supra* note 145, at 8; Röhm, *supra* note 145, at 8C:6-8; ASSMANN, *supra* note 3, at 12-14; *Germany*, *supra* note 145, at 128.

¹⁵⁰ For a description of the regulations contained in the Stock Exchange Act, see Röhm, *supra* note 145, at 8C:49-53; Feddersen & Skala-Kuhmann, *supra* note 145, at 3-4 (description does not contain the reform of 1986).

¹⁵¹ For a description of the three stock exchange segments, see Röhm, *supra* note 145, at 8C:22-28; Dilworth, *supra* note 147, at 530-31.

Hamburg, Hannover, München, and Stuttgart. After the German reunification, plans were created to re-establish the former stock exchange in Leipzig.¹⁵² Of all the regional exchanges, Frankfurt is by far the most important.

Trading in securities outside the stock exchanges¹⁵³ is not specifically regulated, even though several statutes, such as, the Stock Corporation Act (the "*Aktiengesetz*") or the new Offering Prospectus Law (the "*Verkaufsprospektgesetz*") may apply to transactions occurring on this market. Trading on this "off exchange market" primarily takes place among institutional investors, such as banks, insurance companies, and mutual funds. This trading includes the securities of listed and unlisted corporations (including Eurobonds) and Public limited partnerships (the "*Publikumskommanditgesellschaften*"). Other investment vehicles are also offered to private investors (trading in securities and other investment vehicles which are not admitted to a stock exchange market is also called the "gray market"). Traditionally, there was no real marketplace for the "off exchange market"; instead, special "door-to-door" sales forces marketed the securities.¹⁵⁴ The recent development of electronic information and trading systems, however, has created a market place for the securities included in such systems.¹⁵⁵

The distribution of securities in Germany is subject to different legislative regulations corresponding to the respective markets on which a security is to be offered and traded. A general duty to register securities similar to section 5 of the U.S. Securities Act¹⁵⁶ does not exist in Germany. Traditionally, Germany did not even mandate a general duty to publish and distribute a prospectus with the offering of a security.¹⁵⁷

¹⁵² *Frankfurt - Former East German State Looks at Opening Exchange*, 5 Int'l Sec. Reg. Rep. (BNA) No. 10, at 8 (Apr. 21, 1992). However, it is doubtful that these plans will be carried out in the foreseeable future.

¹⁵³ For a description of the different forms of "off exchange trading," see VON RÜDIGER ROSEN, *HANDBUCH DES KAPITALANLAGERECHTS* 65-68 (Assmann & Schütze eds., 1990).

¹⁵⁴ Feddersen & Skala-Kuhmann, *supra* note 145, at 9.

¹⁵⁵ See *infra* notes 173-77 and accompanying text.

¹⁵⁶ Securities Act of 1933, § 5, 15 U.S.C. § 77(f) (1988).

¹⁵⁷ ASSMANN, *supra* note 3, at 192; Dilworth, *supra* note 147, at 531-32.

Stocks or bonds issued by the more important corporations are traded on one of the three segments of the stock exchange. In order to be admitted to such an exchange, the issuer must file an application with the intended stock exchange.

If the securities are to be listed on the *Amtlicher Handel*, the first segment, the application must be filed with the admissions board for the exchange and accompanied by both a draft of the prospectus and supporting documents.¹⁵⁸ The listing requirements and the requirements for the prospectus are set forth in the *Börsengesetz*, the Stock Exchange Admission Regulation (the "*Börsenzulassungs-Verordnung*") and in the rules and regulations of the particular stock exchange where the listing is sought (the "*Börsenordnung*"). These requirements are primarily intended to protect the investing public and ensure sufficient market liquidity.

If the securities are to be traded on the *Geregelter Markt*, the second segment, the admissions requirements are less restrictive in order to encourage smaller issuers to go public and to facilitate the introduction of securities having a limited turnover to stock exchange trading. An application for trading on the regulated market must be filed with the admissions committee. Instead of a prospectus, a business report, which has significantly fewer requirements than the prospectus, must accompany the application.

Trading on the *Freiverkehr*, the third official market segment, is not governed by the *Börsengesetz*, but only by the *Börsenordnung* of the respective stock exchange. In the Frankfurt exchange, for instance, the decision to include a security in the free market trading is made by the editorial committee of the Association of Frankfurt Securities Dealers.

(*Verkaufsprospektgesetz*) such a duty was created for most of the publicly traded securities (on or off exchange). However, many investment vehicles of the "gray capital market" are not subject to the Act. On the other hand, it should be noted that the courts in Germany created a civil liability for misrepresentation in offering materials (*Prospekthaftung*) used in connection with interests in Public Limited Partnerships (*Publikumskommanditgesellschaften*). For a description of this liability, see ASSMANN, *supra* note 3, at 195-214.

¹⁵⁸ Generally, foreign issuers can file these documents according to their home countries' GAAP. Thus, documents which are established under the U.S. GAAP are recognized under the *Börsengesetz*. This also applies for all other filings which have to be made under the Stock Exchange Act (*Börsengesetz*) or the Stock Corporation Act (*Aktiengesetz*).

Here, the application does not require an accompanying prospectus or business report. If a security is being offered for the first time to the public, however, the *Verkaufsprospektgesetz* requires the publication of a prospectus when the security shall be traded on the *Geregelter Markt* or the *Freiverkehr*.¹⁵⁹

If shares of a stock corporation (a "*Aktiengesellschaft*") or bonds are not to be traded on an exchange, the sale of such securities may nevertheless be subject to certain regulations. Under the *Aktiengesetz*, certain procedures are required to be followed upon initiating the formation of a *Aktiengesellschaft*, including the disclosure of specific information in order to protect contributing shareholders. This information must be filed in certain documents, such as the articles of incorporation and financial statements, with the commercial register administered by the local court.¹⁶⁰ This court reviews only if the filed documents are complete, and it does not express an opinion as to the inherent risks of the corporation. After the formation of such *Aktiengesellschaft*, its shares are freely negotiable without further disclosure requirements. Since the adoption of the *Verkaufsprospektgesetz*, on January 1, 1991, however, a public offering of shares of a *Aktiengesellschaft* which does not occur within the official trading of a stock exchange must also comply with the prospectus requirements.

The issuance of bonds traditionally required the prior approval of the Federal Minister of Finance. This requirement was abolished with the adoption of the *Verkaufsprospektgesetz*. Thus, today the issuance of bonds requires only the publication of a prospectus that fulfills its prospectus requirements.¹⁶¹

¹⁵⁹ For a more detailed description of the admission of securities to one of the three segments of exchange trading, see Röhms, *supra* note 145, at 8C:67-75; Dechamps, *supra* note 145, at 86-88; Thomas Buhl & Wolfram Fischer, *Changes to Germany's Stock Exchange Act*, INT'L FIN. L. REV., Mar. 1988, at 34; Freys & Zeller, *Germany's New Capital Market Law*, INT'L FIN. L. REV., Oct. 1988, at 32; EBERHARD SCHWARK, DAS NEUE KAPITALMARKTRECHT, NEUE JURISTISCHE WOCHENSCHRIFT 2041 (1987) [hereinafter *Kapitalmarktrecht*]; FRANKFURT STOCK EXCHANGE, BASIC PRINCIPLES OF ADMISSION OF SECURITIES TO STOCK EXCHANGE TRADING (1991); VON ROSEN, *supra* note 153, at 53-62; Dilworth, *supra* note 147, at 533-35; *Germany*, *supra* note 145, at 135-44.

¹⁶⁰ For a description of the necessary filings upon formation of a stock corporation, see Röhms, *supra* 145, at 8C:66-67.

¹⁶¹ For a description of public offerings of unlisted securities, see

The *Aktiengesetz*, the Limited Liability Company Act (the "*Gesetz über Gesellschaften mit beschränkter Haftung*"), the Commercial Code (the "*Handelsgesetzbuch*"), and the *Börsengesetz* require continuous disclosure by companies issuing stocks or bonds. Thus, these companies must publish either annual or semiannual reports.¹⁶²

The regulation of the securities markets in Germany still does not contain a statutory prohibition on insider trading, although such prohibition will be introduced in the upcoming legislative reform.¹⁶³ Today, insider trading is only restricted by the Insider Trading Rules (the "*Insiderhandels Richtlinien, Händler- und Beraterregeln*" and the "*Insiderverfahrens-ordnung*") which were adopted by the stock exchange expert commission. These rules are a voluntary set of guidelines which German banks and most public companies have agreed to observe. Violations of such guidelines are investigated by a commission established at the exchange where the purported violation has taken place.¹⁶⁴

4.3.2. *Recent Reforms Which Led To The Present Regulation In Germany*

The capitalization of German corporations has been a continuing concern.¹⁶⁵ One part of this problem was attributable to the relatively unfavorable conditions of the

Dilworth, *supra* note 147, at 535-37.

¹⁶² For a description of the disclosure requirements under the different statutes, see Röhm, *supra* note 145, at 8C:80-90; Germany, *supra* note 145, at 134.

¹⁶³ See *infra* notes 185-90 and accompanying text.

¹⁶⁴ For a description of the voluntary Insider Trading Rules see Christof V. Dryander, Germany, INT'L FIN. L. REV., Dec. 1991 Supp., at 9, 11; Röhm, *supra* note 145, at 8C 111-17; Siegfried H. Elsing & Donna Shook-Wiercimok, *New German insider trading regulations*, INT'L FIN. L. REV., Oct. 1988, at 30; Feddersen & Skala-Kuhmann, *supra* note 145, at 23-24; McGuinness, *supra* note 117, at 442-44; Hans-Bernd Schäfer & Claus Ott, *Economic Effects of EEC Insider Trading Regulation Applied to Germany*, 12 INT'L REV. L. ECON. 357, 358-60 (1992); Carsten P. Claussen, *Neues zur kommenden Insidergesetzgebung (I)*, 4 ZEITSCHRIFT FÜR BANKRECHT UND BANKWIRTSCHAFT 73, 75-76 (1992) [hereinafter *Insidergesetzgebung I*]; Klaus J. Hopt, *The German Insider Trading Guidelines - Spring-Gun or Scarecrow?*, 8 J. COMP. BUS. & CAP. MARK. L. 381 (1986) [hereinafter *Insider Guidelines*].

¹⁶⁵ See *supra* notes 30-32 and accompanying text.

German capital market. Among these unfavorable conditions were the relatively high barriers to entry into the official capital market and the high transaction costs on the German stock exchanges. Moreover, the transaction costs were accompanied by unfavorable tax conditions which provided for preferential tax treatment of debt over equity financing and imposed a stock transfer tax. Another concern was the hostility of the German market regulation vis à vis new financial instruments and new forms of trading, such as electronic trading systems. A further disadvantage to international competition was the regional structure of the German stock exchanges which led to a lack of one central market place.¹⁶⁶

The 1986 Amendment to the *Börsengesetz* was the first step in a series of reforms to keep Germany as a financial center competitive among other financial markets. The 1986 reform implemented several Community Directives¹⁶⁷ and created a new market segment, the *Geregelter Markt*, which is today's second segment of stock exchange trading. The introduction of the *Geregelter Markt* was intended to facilitate equity capital financing for small and medium-sized enterprises, for which the new listing requirements seemed to be unduly cumbersome.¹⁶⁸

Another important reform was the establishment of the German financial futures exchange (the "*Deutsche Terminbörse*" or the "*DTB*") which opened in January 1990. Before the creation of the *DTB*, financial futures were traded only to a very limited extent in Germany. This lack of trading was due to restrictive laws and a strict interpretation of such laws by the courts, under which futures contracts were not enforceable.¹⁶⁹ At the *DTB*, the trading includes options on

¹⁶⁶ See Buhl & Fischer, *supra* note 159; *Kapitalmarktrecht*, *supra* note 159; POSER, *supra* note 83, at 394-97.

¹⁶⁷ These directives were the Admissions Directive (*supra* note 94), the Listing Particulars Directive (*supra* note 97), and the Interim Reports Directive (*supra* note 101).

¹⁶⁸ For a description of the 1987 reform see *Kapitalmarktrecht*, *supra* note 159; Buhl & Fischer, *supra* note 159; Freys & Zeller, *supra* note 159.

¹⁶⁹ For details about the former legal situation concerning futures, see EBERHARD SCHWARK, NEUES RECHT FÜR BÖRSETERMIN-GESCHÄFTE - DAS GESETZ ZUR ÄNDERUNG DES BÖRSENGESETZES 1989, NEUE JURISTISCHE WOCHENSCHRIFT 2675 (1989) [hereinafter *Börsentermingeschäfte*].

stocks, bonds, indexes, and financial futures based on bond and share indices. In contrast to the previous trading system at the exchanges, which occurred entirely on the exchange floors, trading on the *DTB* is fully computerized.¹⁷⁰ Therefore, access to the *DTB* is independent of the user's location.¹⁷¹ In the first two years of its operation the trading on the *DTB* has reached a considerable volume.¹⁷²

Another main area of reform of the German securities markets was the introduction of new technology. Since 1987, the Frankfurt Stock Exchange has operated a new price quoting system (the "*Kurs-Informationen-Service-System*" or the "*KISS*") which quotes prices for stock, bonds, convertible debentures, options, and warrants on a real time basis during the trading time of the exchange. The *KISS* is only an information system, not an electronic trading system. Since January 1992, the Frankfurt Stock Exchange, in addition to the *KISS*, has operated a new system called the *Ticker Plant Frankfurt* (the "*TPF*"). This system is also a real time price quotation system which includes the prices on the trading floors of the Frankfurt Stock Exchange, the *DTB* and the *Inter-Bank-Information-System* (the "*IBIS*"). Through introduction of *pcKISS* software, which can also be used in connection with the *IBIS*, the *TPF* became available on-line for market participants.¹⁷³

The *IBIS* was launched in December 1989. Originally, the *IBIS* was only an information system, not a trading system. After its successful operation, however, the *IBIS* was

¹⁷⁰ Schwark has characterized the authorization of computerized trading as opposed to traditional floor trading, as "revolutionary." *Id.* at 2676.

¹⁷¹ For a more detailed description of the *DTB*, see *Börsentermingeschäfte*, *supra* note 169; Friedrich Hey, *Establishing the German Financial Futures Exchange*, INT'L FIN. L. REV., Aug. 1989, at 22; Röhm, *supra* note 145, at 8C: 34-41; ANNUAL REPORT OF THE FEDERATION OF GERMAN STOCK EXCHANGES 1990, 34-35, 92-93 (1990).

¹⁷² The volume of futures traded on the *DTB* made it the leading futures exchange in Europe, see ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992, 38, 54 (1992). However, a great part of the trading volume is due to market making activities; therefore, the success of the *DTB* is actually lower than initially expected.

¹⁷³ For a description of *KISS* and *TPF*, see ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992, *supra* note 172, at 90-94; ANNUAL REPORT OF THE FEDERATION OF THE GERMAN STOCK EXCHANGES 1991, 37 (1991); Röhm, *supra* note 145, at 8C:61.

transformed in April 1991 into a trading system. The *IBIS* is integrated in the Frankfurt Stock Exchange and includes the 30 stocks listed on the *Deutscher Aktienindex* (the "*DAX*"),¹⁷⁴ as well as a number of widely traded bonds issued by public authorities. The *IBIS* is designed primarily for use by institutional investors, such as banks, insurance companies, and investment funds. Although the *IBIS* is linked to the Frankfurt Stock Exchange,¹⁷⁵ members of the *IBIS* can also be members of other stock exchanges. It is also possible to be a member only of the *IBIS* trading system without being a member of one of the German stock exchanges. Thus, the *IBIS* is a separate trading system (operating as a market-maker system), which currently operates in competition with the traditional floor trading (operating as an auction system). Some market participants, therefore, fear that computerized exchanges like the *IBIS* may lead to the closing of the exchanges' trading floors.¹⁷⁶ This occurred at the International Stock Exchange in London. For this reason the official brokers (the "*Kursmakler*") of the stock exchange promoted a more limited information system: the *Makler-Tele-Informationssystem* (the "*MATIS*"). However, the *MATIS* was discontinued in 1992 because it could not successfully compete with the *IBIS*.¹⁷⁷ The upcoming reform¹⁷⁸ of the

¹⁷⁴ The *DAX* is a market performance indicator comparable to the Dow Jones Industrial Average.

¹⁷⁵ Floor trading of the Frankfurt stock exchange and *IBIS* are both subject to the same regulatory regime. The official brokers (*Kursmakler*) are required to take the market developments in *IBIS* into consideration when determining prices of securities. Prices of transactions effected through *IBIS* which are affected by *Kursmakler* are also official prices, i.e., prices determined according to the rules of the *Amtlicher Handel*. See ANNUAL REPORT OF THE FEDERATION OF THE GERMAN STOCK EXCHANGES 1991, *supra* note 173, at 74.

¹⁷⁶ For a description of *IBIS*, see ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992, *supra* note 172, at 86-89; ANNUAL REPORT OF THE FEDERATION OF THE GERMAN STOCK EXCHANGES 1991, *supra* note 173, at 35-36, 74-76; ANNUAL REPORT OF THE FEDERATION OF GERMAN STOCK EXCHANGES 1990, *supra* note 171, at 78-79; Röhm, *supra* note 145, at 8C:23-25; POSER, *supra* note 83, at 399-400; *IBIS Trading System Launched, Securities Market Faces Change*, 4 INT'L SEC. REG. REP. (BNA) No. 10, 4 (Apr. 22, 1991); In the last quarter of 1992, 27.4% of the *DAX* listed stocks were traded through *IBIS* and in December 1992, 11.6% of the public sector bonds were traded through *IBIS*—see ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992, *supra* note 172, at 34, 86, 88.

¹⁷⁷ See FINANCIAL MARKETS - BEGGAR THY COLLEAGUE, GERMAN BRIEF

Börsengesetz will provide the legal framework under which computerized stock exchange trading and face-to-face floor trading can compete under equal conditions.

Traditionally, the German system of regional stock exchanges was designed to develop the surrounding geographical regions and to permit the introduction of small and medium-sized enterprises to the organized capital market. Although these goals are still valid, the internationalization of the German capital market created the need for a strong centralized major stock exchange.¹⁷⁹ Therefore, the Frankfurt Stock Exchange had already changed its legal status in preparation for its expanding role at the end of 1990. Its organization was transformed from a statutory body under the responsibility of the chamber of industry and commerce into an *Aktiengesellschaft* which is held by banks and brokers.¹⁸⁰ In December 1992, the Frankfurt Stock Exchange Corporation was transformed into a new holding company, the *Deutsche Börse AG*, which operates the Frankfurt Stock Exchange, the *DTB*, the clearing and settlement agency for German securities (the "*Deutscher Kassenverein*"), and the exchange data processing center (the "*Deutsche Wertpapierdatenzentrale*"). The new holding company is held by the regional stock exchanges (ten percent), the official brokers (ten percent), and by German and foreign banks (eighty percent).¹⁸¹ This creation of a main marketplace, which has the necessary size and which is able to perform the necessary services to attract large foreign and domestic investors, is a major step forward in the development of Germany as a financial center. The

21 (1992); *Frankfurt - MATIS Electronic System Terminated*, 5 INT'L SEC. REG. REP. (BNA) No. 21, 7 (Oct. 6, 1992).

¹⁷⁸ See *infra* note 184 and accompanying text.

¹⁷⁹ Gerhard Wegen, *Towards a German Financial Center*, INT'L FIN. L. REV., Mar. 1992, at 10 [hereinafter *Financial Center*].

¹⁸⁰ See ANNUAL REPORT OF THE FEDERATION OF THE GERMAN STOCK EXCHANGES 1990, *supra* note 171, at 40.

¹⁸¹ See ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992, *supra* note 172, at 40-42; Klaus Westrick, *Finanzplatz Deutschland Slowly Takes Shape*, INT'L FIN. L. REV., Nov. 1992, at 30, 31-32; *Proposal to Integrate Exchanges Approved - Frankfurt Takes Lead as Financial Center*, 5 Int'l Sec. Reg. Rep. (BNA) No. 22, at 1 (Oct. 20, 1992); *Exchange Merger Marks 'Milestone' In Frankfurt's Financial Evolution*, 6 Int'l Sec. Reg. Rep. (BNA) No. 3, at 1 (Jan. 12, 1993); Gerhard Wegen, *Frankfurt Exchange to be Holding Company*, INT'L FIN. L. REV., Oct. 1992, at 43, 44.

creation of the *Deutsche Börse AG*, however, is not unanimously perceived as a positive development. Recently, other market participants have criticized the strong influence of the major German banks in the new holding company.

Another change in the German Securities Laws which is designed to enhance competition in order to strengthen the German financial market occurred on August 1, 1992. On that date, the *Bundesbank* abandoned its requirement that Eurobonds and Euronotes denominated in DM be listed on a German Exchange and be subject to German law and domestic settlement procedures. Furthermore, foreign institutions not registered as banks can now issue DM debentures of less than two years directly into the commercial paper market. As a result, one can expect that in the future DM bonds will be listed increasingly in London or Luxembourg.

The *Bundesbank* still requires that DM securities be issued through a financial institution based in Germany. Under the new regime, however, it is no longer necessary to use a German bank or the German subsidiary of a foreign bank. German branches of foreign institutions may also be lead managers for DM bonds, provided that they have a listing department which is able to perform the role of such lead manager. The *Bundesbank* also still requires that: (i) it be notified of DM-denominated foreign issues on the day of their issue, and (ii) new instruments, including DM-denominated components, be submitted in sufficient time so that it may express its opinion thereof prior to the issue.¹⁸²

Until recently, two different taxes disadvantaged the issuance and the trading of securities in Germany. The corporation tax (the "*Gesellschaftssteuer*") had to be paid on the purchase price of equity securities by the first buyer. The stock exchange turnover tax (the "*Börsenumsatzsteuer*") was a transfer tax which had to be paid on the subsequent trading of equity securities and bonds. Both of these taxes were recently abolished.¹⁸³ The *Börsenumsatzsteuer* in January 1991 and

¹⁸² For a description of the new Bundesbank Guidelines see Ulrich Koch, *New Guidelines for DM-Denominated Bonds*, INT'L FIN. L. REV., Aug. 1992, at 45; *Euro-DM Wins Credibility*, EUROMONEY, Dec. 1992, at 80; ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992, *supra* note 172, at 37.

¹⁸³ See Röhm, *supra* note 145, at 8C:62; Dechamps, *supra* note 145, at 88; *Germany*, *supra* note 145, at 146-47. One tax provision which is still in

the *Gesellschaftsteuer* in January 1992.

4.3.3. *Upcoming Reforms Of The German Securities Legislation*

The upcoming reforms of the German Securities Legislation will again be inspired on one hand by the Communities' harmonization efforts (i.e., the transformation of Communities' directives into the German law) and, on the other hand, by further movements to make the German capital market more competitive in the international arena. To achieve these goals a so-called "German Financial Center Act" (the "*Finanzplatz Deutschland Gesetz*") is currently being drafted by the Federal Ministry of Finance and will be voted on by the German Parliament, the *Bundestag*, by the end of 1993.¹⁸⁴ The new legislative draft will principally address the development of sufficient market supervision to ensure the element of "honesty" in the market. The legislative reform will consist of a new Securities Trading Act (*Wertpapierhandelsgesetz*), and a law amending the *Börsengesetz*.

Traditionally, the German securities markets have operated under a system of essentially unsupervised self-regulation.¹⁸⁵ This voluntary regulatory system was strongly favored over statutory regulation of insider trading and the establishment of a central supervisory agency.¹⁸⁶

force and disadvantages foreign investors concerns the taxation of distributed profits of stock corporations. Because German stock corporations are subject to a corporate income tax and a capital yield tax, shareholders retain only 48% of their dividends in cash. Domestic shareholders, however, are allowed tax credits imputable towards their other income tax liability. See Dechamps, *supra* note 145, at 8C:62; *Germany*, *supra* note 145, 146-47.

¹⁸⁴ For a description see *Germany*, *supra* note 145, at 129-32; *Financial Center*, *supra* note 179; Westrick, *supra* note 181; *Finance Ministry Releases Plans to Revamp Securities Laws, Exchanges Reach Agreement*, 5 Int'l Sec. Reg. Rep. (BNA) No. 4, at 1 (Jan. 28, 1992); *Financial Powerhouse Starts to Take Shape*, EUROMONEY, Dec. 1992, at 74; ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992, *supra* note 172, at 94-99. The first draft was published for comments on July 12, 1993. A revised draft will be discussed in the German parliament in the upcoming months. The new law will be voted on by the end of 1993 or the beginning of 1994. It will become effective July 1, 1994.

¹⁸⁵ See notes 163-64 and accompanying text.

¹⁸⁶ *Insidergesetzgebung I*, *supra* note 164, at 76-78 (summarizing arguments pro and con concerning the self-regulatory system).

Nevertheless, international competition, a series of recent scandals,¹⁸⁷ and the necessary adoption of the Community's Insider Trading Directive¹⁸⁸ have led to a new approach in Germany.¹⁸⁹ The new legislative draft will include a prohibition against insider trading and will create a supervisory authority.¹⁹⁰

In a working paper dated January 25, 1993, a committee of representatives of the German states and the Federal Ministry of Finance presented, on agreement, the establishment of a federal supervisory authority for Germany's securities market. This supervisory authority will be comparable to the SEC.¹⁹¹ Such agreement was necessary in order to adopt the proposed legislation reforming the German securities market.

The agreement provides for the creation of a federal supervisory authority, *Bundesamt für das Wertpapierwesen*, which will administer: (i) the insider-dealing provisions to be introduced by the new *Wertpapierhandelsgesetz* adopting the EC Insider Dealing Directive into national law; (ii) the new rules designed to encourage disclosure and transparency on the German equity markets (companies will have to disclose

¹⁸⁷ See ANNUAL REPORT OF THE FEDERATION OF THE GERMAN STOCK EXCHANGES 1991, *supra* note 173, at 13, 42-44; Röhm, *supra* note 145, at 8C:116; Schäfer & Ott, *supra* note 164, at 360-62; Richard C. Morais, *Insider Auf Deutsch*, FORBES, Nov. 9, 1992, at 88; see also *Insider Guidelines*, *supra* note 164, at 391-92 (describing less current insider trading scandals).

¹⁸⁸ For a discussion of the upcoming questions with respect to the transformation of the EC-Insider Directive into German legislation, see Carsten P. Claussen, *Neues zur kommenden Insidergesetzgebung (II)*, 4 ZEITSCHRIFT FÜR BANKRECHT UND BANKWIRTSCHAFT 267, 282-83 (1992) [hereinafter *Insidergesetzgebung II*]; WOLFGANG GRUNDMANN, NEUREGELUNG DES INSIDERHANDELS-VERBOTS IN DEUTSCHLAND, ZEITSCHRIFT FÜR DAS GESAMTE KREDITWESEN 12 (1992); MARTIN SCHÖDERMEIER & EDGAR WALLACH, DIE INSIDER-RICHTLINIE DER EUROPÄISCHEN GEMEINSCHAFT, EUROPÄISCHE ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT 122 (1990).

¹⁸⁹ See ANNUAL REPORT OF THE FEDERATION OF THE GERMAN STOCK EXCHANGES 1991, *supra* note 173, at 101; *Financial Center*, *supra* note 179; *Finance Ministry Releases Plans to Revamp Securities Laws, Exchanges Reach Agreement*, *supra* note 184, at 8.

¹⁹⁰ For a description of the first proposal outlining the framework which was translated into the first draft of the legislative proposal see *Penalties and Definitions Framework Clears Path for Insider Trading Bill*, 6 Int'l Sec. Reg. Rep. (BNA) No. 6, at 1 (Feb. 23, 1993).

¹⁹¹ See *Progress Made on "Insider" Law - Central Watchdog Created*, 6 Int'l Sec. Reg. Rep. (BNA) No. 4, 1 (Jan. 26, 1993); ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992, *supra* note 168, at 96-98.

stakes in other companies if they reach a certain threshold the present threshold of twenty-five percent will be reduced to a threshold between five percent and ten percent); and (iii) a set of "rules of conduct" for market participants which will be introduced in anticipation of the EC Investment Services Directive. The new *Bundesamt für das Wertpapierwesen* will also represent the Federal Republic to foreign supervisory authorities, such as, the SEC.¹⁹²

The jurisdiction of the new *Bundesamt* will be coordinated with the several existing organs of control. The German states will remain responsible for supervision of the stock exchanges, the official brokers, and, to the extent it is not already covered by the supervisory authority's surveillance, the trading on the exchanges. The new law will provide for a close cooperation between the federal supervisory authority and the states. In order to facilitate such cooperation, the *Börsengesetz* will create a securities council (the "*Wertpapierrat*"), which will consist of representatives from all states. The *Wertpapierrat* will represent the interests of the states to the supervisory authority. Although the *Wertpapierrat* may advise, it will lack the authority to implement policies.

The legislative reform will also change the organization of the stock exchanges. The stock exchanges will retain jurisdiction over the adoption of rules and regulations governing their activities. In addition, they will retain competence over the admission of market participants and over the admission of securities for trading on the exchange. The stock exchanges, however, will be required to establish a supervisory department in order to monitor trading activities and determine any irregularities. If irregularities are discovered by the supervisory department, any investigation will be carried out by the federal supervisory authority.

The new *Börsengesetz* will also change the management structure of the stock exchanges. The exchange's current board of governors (the "*Börsenvorstand*") will be replaced by

¹⁹² For a discussion of the structure, the objective, and the jurisdiction a future supervisory authority should have, see *Insidergesetzgebung I*, supra note 164; Siegfried Kümpel, *Zur Neugestaltung der staatlichen Börsenaufsicht - von der Rechtsaufsicht zur Marktaufsicht*, 46 WERTPAPIERMITTEILUNGEN 381 (1992); RÜDIGER VON ROSEN, INTERNATIONALE ANFORDERUNGEN AN EIN DEUTSCHES WERTPAPIERAUFSICHTSAMT, ZEITSCHRIFT FÜR DAS GESAMTE KREDITWESEN 276 (1992).

an exchange council (the "Börsenrat") designed to represent all market participants. A board of management will exercise the managerial functions of the current board of governors and the exchange council will exercise supervisory functions. Only half of the seats on the exchange council will be held by representatives of the banks and only four of the nine banking representatives will be appointed by major banks. The other banking representatives will be appointed by local banks, private banks, and thrifts.

4.3.4. *Evaluation Of The Legislative Developments In Germany*

Traditionally, different national securities markets in Europe, which were organized under various regulatory systems, faced only limited competition from one another. Through the opening of national markets in accordance with the Community's efforts to create a common securities market, the competition in Europe has increased. This development was fostered by the worldwide internationalization of the capital markets. Germany, with one of the least regulated systems in Europe, initially did not feel a need to reform its legislation on capital markets.¹⁹³ However, other member states' willingness to reform pressured Germany into considering reforms to increase the competitiveness of its securities market. Thus, the reform in Germany, which had been slow at the outset, has progressed remarkably in recent years. In fact, the reform process in Germany is advancing on a continuous basis. In the last years, the *Börsengesetz* and other statutes were amended several times to transform European directives into national law as well as to introduce changes on a national level.

¹⁹³ Poser argues:

The extent to which a particular country has decided to reform its securities market has depended on several factors, including its legal system and traditions, the structure of its market, and the degree of the competitive pressures felt. For example, the willingness shown in France to move . . . 'from being one of the most highly regulated markets in Europe to one of the most deregulated' contrasts sharply with the resistance to change manifested . . . in Germany.

POSER, *supra* note 83, at 378.

The limited size of the German capital market required the development of a new legal framework which would meet international standards and attract investors. This new framework has evolved with subsequent changes occurring on several levels. The first is the harmonization of the German system with the systems of other member states. The second is the recent replacement of the traditionally regional organization of the stock exchanges with one centralized stock exchange which will be competitive on an international level. The third is the creation of sufficient protection for investing market participants against manipulation and fraud in the market place. The fourth is the adaptation of the market place to new technologies and their integration into the existing regulatory system.

In addition to the creation of a framework for a modern and international market place, existing impediments to an efficient securities market had to be abolished. Although some deregulatory measures have already been adopted, additional measures are needed. One example of such deregulation is the abolishment of the transfer tax on the trading of securities. Deregulation is also appropriate in the area of the admission of new financial instruments by the legislator.

The reform process, despite its relatively late beginning, has already had a positive impact on the market. One observer stated: "Slowly and painfully, West Germany's stock market is being hauled into the 20th century."¹⁹⁴ The creation of the above-mentioned framework, as well as some further deregulation, is forthcoming. The market participants and the legislators in Germany are aware of the necessity for further reforms. The adoption of the new "German Financial Center Act"¹⁹⁵ will be a major step forward. Recent German legislation tends to integrate the regulation of legal entities and the regulation of the market.¹⁹⁶ Even though it seems

¹⁹⁴ *Id.* at 394.

¹⁹⁵ See *supra* note 184 and accompanying text.

¹⁹⁶ See *German Capital Markets*, *supra* note 146, at 310-11 (discussing different approaches of regulation and their relation); see also Stefan Grundmann, *Deutsches Anlegerschutzrecht in internationalen Sachverhalten*, 54 RABELSZ 283, 285-87, 321 (1990); Kumpel, *supra* note 192, at 384. For a detailed discussion of the two different approaches and the need for their integration, see Klaus J. Hopt, *Vom Aktien- und Börsenrecht zum Kapitalmarktrecht?*, 140 ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRE-

that the reaction of market participants and the legislators is leading toward a successful reform of the German market, many issues must still be resolved. Major elements of the reform will be adopted through the proposed "German Financial Center Act." The successful creation of this proposed law will determine whether German legislation can catch up with the developments that have taken place in the last few years. The success of reform will further depend on the proposed establishment of the *Bundesamt für das Wertpapierwesen*, and on the seriousness with which it will exercise its regulatory authority.

5. CONCLUSION AND OUTLOOK

5.1. *The Different Approaches To Reform, Reasons And Evaluation*

The reforms adopted in the United States in response to the internationalization of the capital markets were entirely deregulatory in nature. Comparable reforms in Europe, however, were both deregulatory and regulatory in nature.

The terms "deregulation" and "regulation" cover multiple concepts, and the use of these terms is not uniform. Deregulation often refers to the removal of restraints on competition. These restraints, also known as "access regulations," usually consist of economic regulations which restrict either access to markets or activities performed by market participants.¹⁹⁷ This type of deregulation must be distinguished from "prudential deregulation" which is the removal of rules serving the goal of investor protection.¹⁹⁸ In this Article, "deregulation" refers to both types of deregulation.

In recent years, deregulation of the capital markets in the United States was mainly prudential deregulation. The description in Section 3 pointed out that the regulation of the U.S. securities market, which was intended to ensure the

CHT 201 (1976), 141 ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTS-RECHT, 389 (1977).

¹⁹⁷ See *Harmonization*, *supra* note 83, at 187; POSER, *supra* note 83, at 1-2.

highest level of protection, brought about the opposite effect in certain cases. U.S. securities laws imposed such a significant burden upon foreign investors that the U.S. market became highly unattractive. In other cases the strong investor protection resulted even in disadvantaging U.S. investors in relation to foreign investors.¹⁹⁹ Thus, the United States had to lower investor protection standards with respect to foreign issuers in order to reduce transaction costs to the levels in foreign countries.

U.S. reforms addressed these difficulties in three different ways.²⁰⁰ First, the reforms modified foreign issuers' disclosure obligations for registration and reporting in order to ease compliance with U.S. securities laws.²⁰¹ Second, the U.S. reforms created rules (the MJDS, the proposed regulation of cross-border rights, tender, and exchange offers) to recognize disclosure documents drafted under foreign laws.²⁰² Third, the reforms placed limits on the application of section 5 of the Securities Act (Regulation S and Rule 144A).²⁰³

It is true that the third type of reform, while favoring off-shore distributions by U.S. issuers and attracting foreign investors to the private placement market, does not encourage participation in the public market.²⁰⁴ Nonetheless, the mere limitation on the application of section 5 of the Securities Act lowers investor protection standards much less than an extension of reciprocal recognition; thereby the SEC is, in fact, adapting the U.S. system to the needs of globalized markets one step at a time. Thus, an increased recognition of foreign documents, i.e., an extension of the MJDS, which would further transform the U.S. system, seems unlikely in the near future. After all, a system of full recognition of foreign disclosure documents may eventually lead to the unequal treatment of U.S. and foreign issuers.²⁰⁵ The enactment of

¹⁹⁹ See *supra* note 51 and accompanying text.

²⁰⁰ See *supra* note 40 and accompanying text.

²⁰¹ See *supra* notes 38-41 and accompanying text.

²⁰² See *supra* notes 42-53 and accompanying text.

²⁰³ See *supra* notes 54-72 and accompanying text.

²⁰⁴ See *supra* note 81 and accompanying text.

²⁰⁵ See COX ET AL., *supra* note 4, at 328 (calling this threat of unequal treatment a "regulatory dilemma" for the SEC).

Regulation S and Rule 144A have already been very effective in achieving their specific objectives without leading to unequal treatment of U.S. and foreign issuers.²⁰⁶

The deregulation in Europe consisted mainly of access deregulation, followed by a series of subsequent regulations to address the perceived shortcomings of regulatory systems after such deregulation. Simultaneous regulation and deregulation of a market is not inconsistent. In fact, deregulation often leads to further regulation.²⁰⁷ The Community's member states, to achieve access deregulation, had to abolish all restrictions on the movement of capital between residents of the Community.²⁰⁸ However, as the member states of the Community lacked securities laws comparable to those of the United States,²⁰⁹ the opening of the market necessitated the introduction of new regulatory measures.

The attempted harmonization in the Community has led only to a moderately harmonized system of securities regulation.²¹⁰ Its shortcomings were caused by the approach taken--attempting harmonization through the establishment of minimum standards as opposed to through the unification of legislative standards. One has to bear in mind, however, that even the limited harmonization attained within the Community is unique to the world.²¹¹ Besides, future reforms will reduce existing disparities over time. For example, the establishment of a European Securities Commission, recommended by certain commentators,²¹² although unlikely

domestic issuers are burdensome and many of these requirements are not imposed on foreign issuers. Furthermore, a fundamental objective of the Commission's basic information package is comparability among issuers; this objective is seriously compromised when an important segment of issuers, i.e., foreign issuers, are not subject to the same disclosure standards as apply to domestic issuers.

Id.

²⁰⁶ See *supra* note 73.

²⁰⁷ See *Harmonization, supra* note 83, at 188-89; POSER, *supra* note 83, at 1.

²⁰⁸ See *supra* notes 92-93 and accompanying text.

²⁰⁹ See *supra* note 128 and accompanying text.

²¹⁰ See *supra* notes 130-36 and accompanying text.

²¹¹ See *supra* notes 141-44 and accompanying text.

²¹² See *Harmonization, supra* note 83, at 231.

to occur in the near future, would be a major breakthrough in the unification of the European system.

5.2. *Future Developments - Outlook*

The reforms in the United States and in the member states of the Community have narrowed the gap among the different systems. Thus, a mutual recognition of foreign disclosure standards seems to be more likely now than it was a decade ago. The increased levels of disclosure generally required in the member states of the Community already make it easier for European issuers to satisfy the regulatory requirements of the U.S. system.²¹³ Furthermore, disclosure documents of U.S. issuers will almost always be recognized in the Community.²¹⁴

In fact, negotiations about a possible mutual recognition of disclosure standards between the Community and the United States are forthcoming. The Commission of the European Community and the SEC signed a cooperation agreement during the assembly of the International Organization of Securities Commissions in September 1991.²¹⁵ The Federation of the German Stock Exchanges created a committee which works in close contact with the New York Stock Exchange.²¹⁶ Even if these negotiations do not lead to an agreement in the near future, they indicate a change in attitudes among the respective national securities agencies.

In addition, the increased level of disclosure requirements in Europe may also lead to a change in attitudes among a number of market participants. The recent example of the Daimler Benz AG illustrates this point. Daimler is the first German company which has obtained a listing of its shares on the New York Stock Exchange,²¹⁷ demonstrating that the U.S. marketplace seems to be attractive enough to induce certain foreign companies to undergo the burdensome task of

²¹³ See *id.* at 225.

²¹⁴ See *id.* at 218 n.216; see also *supra* note 158.

²¹⁵ See ANNUAL REPORT OF THE FEDERATION OF THE GERMAN STOCK EXCHANGES 1991, *supra* note 173, at 91.

²¹⁶ See *id.* at 92; *Frankfurt - NYSE, German Officials Discuss Listings*, 5 Int'l Sec. Reg. Rep. (BNA) No 7, at 7 (Mar. 10, 1992).

²¹⁷ See *supra* note 20.

reconciling their financials in accordance with U.S. accounting standards.²¹⁸ The lower the differences among the disclosure levels in different countries, the less burdensome it is for a company to fulfill the higher disclosure standards of a foreign country.

The member states of the Community have also discussed additional projects with respect to the globalization of the markets. The Federation of Stock Exchanges in the EC has worked to create *Eurolist*, a special market segment which is to be created on all member stock exchanges and which shall contain European "blue chips." *Eurolist* will eliminate some procedural requirements for issuers in order to achieve multiple admission to Europe's various stock exchanges, all of which have their differing conditions and administrative demands. Admission to *Eurolist* shall entail a simultaneous admission on the *Eurolist* segments of all member stock exchanges, provided the corporation is admitted to the official market of its own national stock exchange.²¹⁹ A related project deals with the establishment of a European stock index.²²⁰

From a summary of the legislative developments which have taken place in the different markets, one can observe: (i) a deregulation of the securities regulation in the United States which is based on harmonization as well as on recognition of foreign systems, and (ii) a harmonization of the legal systems in the European Community, which is based on

²¹⁸ For a discussion of the reconciliation requirements necessary to adapt financials of foreign companies to U.S. GAAP, see James R. Doty, *The Role of the Securities and Exchange Commission in an Internationalized Marketplace*, 60 *FORDHAM L. REV.*, May 1992, at S77, S88-89.

For a description of the reconciliation of financial statements required of foreign issuers entering the U.S. securities markets, see SEC DIVISION OF CORPORATE FINANCE, *SURVEY OF FINANCIAL STATEMENT RECONCILIATIONS BY FOREIGN REGISTRANTS* (May 1, 1993) (copies may be obtained from the corporation's public reference room).

²¹⁹ *Eurolist* will be restricted to European "blue chips" with a market capitalization of at least ECU 1 billion and an annual turnover of at least ECU 250 million. The issuer must seek at least admission at four European stock exchanges in addition to its national stock exchange. For a description of *Eurolist*, see *ANNUAL REPORT OF THE FEDERATION OF THE GERMAN STOCK EXCHANGES 1991*, *supra* note 173, at 85; *ANNUAL REPORT OF THE GERMAN STOCK EXCHANGES 1992*, *supra* note 1, at 102.

²²⁰ See *ANNUAL REPORT OF THE FEDERATION OF THE GERMAN STOCK EXCHANGES 1990*, *supra* note 171, at 97.

the establishment of minimum standards and the recognition of other member states' systems.²²¹

However, further global harmonization of the securities laws beyond the scope of current undertakings within the EC seems unlikely in the foreseeable future. Even though some improvement in the assimilation of the different systems may occur in specific areas, the differences of the national systems, based on different historical experiences which have produced different "cultures of regulation," (i.e., different goals of the national regulators, severely limit further harmonization on a larger scale). Other impediments to such legislative harmonization include: (i) a variety of regulators with often overlapping authorities in some jurisdictions, or the complete lack of a central regulator in other jurisdictions; (ii) the speed with which financial innovations are created;²²² and (iii) the different character of market participants across the various jurisdictions.²²³

A higher level of harmonization seems possible only through further deregulation.²²⁴ The developments towards a single European securities market will enhance competition

²²¹ For a discussion of the conflicting principals in the harmonization efforts of the European Community, see Klaus J. Hopt, *Legal Harmonization on the Way to Europe 1992: Banking and Capital Markets*, 4 BANKING & FIN. L. REV. 309, 310-15 (1990).

²²² Many of the new financial innovations are created in reaction to regulations within a specific system. Therefore, financial innovations may be very successful in one regulatory system, but may not have the same success in other systems. The former chairman of the SEC, Richard C. Breeden summarized the problem, stating: "The market is well ahead of the regulators." See KLAUS BÖHLHOFF, KRITERIEN UND METHODEN EINER REGULIERUNG DER INTERNATIONALEN KAPITAL- UND WERTPAPIERMÄRKTE, FESTSCHRIFT FÜR HEINSIUS 49, 50 (1991).

²²³ Examples of different characters are the separation of investment and commercial banking in the United States and the concept of universal banking in other countries, and the different objectives and authorities of the national banks in various countries.

For a description of the different impediments of a further harmonization of securities laws, see BÖHLHOFF, *supra* note 222, at 49, 54; Van Zandt, *supra* note 1, at 72-74.

²²⁴ For a discussion of deregulation in order to achieve a further harmonization of the regulatory systems, see BÖHLHOFF, *supra* note 222; Markus Lusser, *Internationale Harmonisierung von Bankrecht und Finanzmarktaufsicht: Ziele und Probleme*, 1 ZEITSCHRIFT FÜR BANKRECHT UND BANKWIRTSCHAFT 101, 106-07 (1989) (discussing the harmonization of banking laws).

with other major markets like the United States, which in turn will compel further liberalization of regulations.²²⁵ Although some commentators have expressed the fear of a "race to the bottom,"²²⁶ further deregulation seems to be the only efficient way to achieve a higher degree of uniformity among different legislative systems. Commentators do agree, however, that some minimum standards of regulation are necessary to ensure "honesty" in the market, although they may not agree on a general definition of such minimum standards.²²⁷ With respect to achieving some agreement about minimum standards and about the extent to which deregulation and liberalization should take place, Böhlhoff points in the right direction - it is not methods of regulation or questions of competence which should be discussed in the first place, but rather the extent to which regulation is necessary at all.²²⁸

Therefore, one can conclude that the competition among various marketplaces should lead to further deregulation. If regulators increase the level of cooperation, establishing harmonized minimum standards of regulation of the securities markets may be easier. The result of such developments may be a further integration of regulatory systems, even though

²²⁵ See Van Zandt, *supra* note 1, at 78.

²²⁶ See Lusser, *supra* note 224, at 103.

²²⁷ The sophistication of investors is an important criterium to consider when attempting to define those minimum standards. For example, Van Zandt theorizes about the possible development of a "two-tiered structure" of securities markets:

The first tier will be an off-shore international market with fewer regulations that will approximate but be much larger than the existing Eurosecurities market. The predominant participants will be large, creditworthy, multinational borrowers from all countries and sophisticated institutional investors. The second tier will be a composite of highly regulated local or national markets in countries with significant pools of capital . . . in which start-up enterprises and lower-rated borrowers raise capital and into which smaller investors can put their discretionary investment capital at risk.

Van Zandt, *supra* note 1, at 79-80. Böhlhoff also seems to favor the two-tier approach and states that Rule 144A is a step in the right direction. See BÖHLHOFF, *supra* note 222, at 57; see also *supra* note 63.

For a selection of articles about private placements in different countries, see Albert S. Pergam, *Exemptions for Institutional Investors or Concepts of Non-Public Offerings: A Comparative Study*, 13 U. PA. J. INT'L BUS. L. 473 (1993).

²²⁸ See BÖHLHOFF, *supra* note 222, at 49.

complete harmonization seems to be very unlikely in the foreseeable future.