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*Conditionalities for
Romania's accession into
the European Union*

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Introduction

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Romania belongs to the group of ten Central and Eastern European Countries that have signed Association Agreements with the European Union. As a result, our country will enter, at a certain moment, the process of negotiating the more than 30 files which assess the adoption in its entirety of the *acquis communautaire* and the capacity of facing competition. Already, the countries more advanced in this process, the Czech Republic, Estonia, Poland, Slovenia and Hungary, have started the respective negotiations in the last part of 1998. The majority of them have already reviewed some 8 files (it is true, the least contentious ones) and are preparing to tackle soon the more 'delicate' ones.

The countries that until recently were considered to belong to 'the second wave' of candidates (distinction which seems will be abandoned at the Helsinki summit, in December 1999) are, in their turn, caught in a screening exercise, that assesses periodically their advance concerning the transposition of Community legislation. Romania is among these countries, together with Bulgaria, Latvia, Lithuania and the Slovak Republic.

The several thousand pages of *acquis*, translating into hundreds of Directives, represent the result of a legislative process of harmonisation that took more than four decades. What was for the founding members of the European Union (initially, the European Community of Coal and Steel) a smooth and lengthy process, appears to the new candidate countries as an enormous amount of work, to be performed against the clock.

The present study attempts to describe the stage of Romania legislation's harmonisation with the Community's one in two fields of the above 30 mentioned, namely in those of financial markets and, respectively, of competition. The pairing of the two fields is not at all fortuitous, since financial markets (comprising the banking market, the capital market and the insurance market) are fundamental in assuring a competitive economic environment which, thereby, benefit the consumer. Less developed or untransparent financial markets represent an obstacle to competition stimulation and to general increase of efficiency.

In the area of financial market there have appeared, in the last twenty-six years, an impressive number of Directives, which are briefly summarised, in the following table. They belong to the so-called first, second and (in the field of insurance) third stages, according to the degree of sophistication of the markets at a given moment. Many times, Directives belonging to a further stage nullify or modify some requirements from Directives of a previous stage. This is why it is necessary, for countries like Romania, to harmonise its legislation as much as possible with the Directives of the last stages, thereby eliminating the intermediary steps (when the latter can be 'leap-frogged').

Summary of the main Directives concerning the Financial Markets

Type of Financial Market	Year/No.of Directive	Field which the Directive regulates
Banking market	77/780	Co-ordination of banking Laws and regulations (First Banking Directive)
	86/635	Annual accounts and consolidated account of financial institutions
	89/117	Foreign branches' obligation to publish annual accounts
	89/299	Own funds of credit institutions
	89/646	Co-ordination of banking laws and regulation (Second Banking Directive)
	89/647	Solvency Ratio of credit institutions
	89/308	Money laundering
	92/30	Supervision of credit institutions on a consolidated basis
	92/121	Supervision and control of the large credit risks
	93/6	Own funds' adequacy
	94/19	System of deposit's guaranteeing
	95/26	Enhancing of prudential supervision (Post-BCCI Directive)
	96/10	Recognition of compensation
	Capital market	79/279
85/611		Investment funds
88/627		Publishable information for major detaining of stock
89/298		The offer prospect
89/592		Privileged information ('insider dealing')
93/22		Investment services
Insurance market	73/239	First Directive for non-life insurance
	79/267	First Directive for life insurance
	88/357	Second Directive for non-life insurance
	90/619	Second Directive for life insurance
	91/674	Consolidated accounting in insurance
	92/49	Third Directive of non-life insurance
	92/96	Third Directive of life insurance

From the simple listing of the above-mentioned Directives it becomes obvious how huge the effort of legislative adoption is. First, there is the necessity to train civil servants acquainted well enough with the respective issues for, on one hand, promoting the necessary legislative changes and, on the other hand, applying them in practice.

Countries which are more advanced in transition are in the process of creating real 'armies' of civil servants with expertise in community laws. In Romania, unfortunately, with the exception of the persons involved in the screening process, there are very few civil servants, of higher or lower rank, acquainted with this kind of legislation and able to enforce it.

Therefore, a first category of readers which this study is aimed at is represented by employees working in the financial system, that sooner or later will have to familiarise themselves with the content of the mentioned European Directives.

Concerning the strictly quantitative aspect, we can say that Romania is not much behind countries like the Czech Republic, Hungary or Poland in what regards promoting laws harmonised with the European ones. In a way, it can be inferred that we have compensated through quantity some underachievement in terms of quality. Over-legiferation, a phenomenon often found in the last years, could not have by-passed this sensitive area, of adopting Community legislation. The problems appear mainly with regard to the quality of national legislation, which is often less than desired. A worrisome finding is that even recently (1998, 1999) adopted legislation doesn't take into account some important rules from the European Directives and, therefore, will have to be amended again, soon (it is the case, among others, of the new Banking Law). When there is a strong motivation for the non-transposing, for the time being, of the Community legislation, this phenomenon can still be explained. But when some important rulings are omitted, in the legislative process, due to incomplete knowledge, the matter is completely different. Therefore, a second category of readers to which this work is destined comprises MPs and Parliamentarian experts, who by their decisions can worsen or better crucially a project of law. A special remark is to be given to the approach followed by CNVM (the capital-market regulation body) in the process of legislative transportation, which consists of a permissive general framework, leaving the harmonisation itself to be performed by means of secondary legislation (norms and regulations).

A third category to which this study is addressed is the general public, which has to be informed about the rigors and motivations of certain laws that Romania will adopt sooner or later. Within this general public, a particular category is constituted by the students at the faculties of laws and economics, the ones who will be supposed to enter the technical details of the adoption of the *acquis communautaire*.

Another idea to be drawn from this process' study is that Romania, in its quest for modernity, is again confronted with a problem older than a century: that of the form without content. Sceptics could argue that mimicking some concepts that are irrelevant on a national plan could do more harm than good, enhancing confusion. The authors of this study maintain that, quite on the contrary, any step, even a formal one, towards harmonisation with the European Union, is a step forward that sooner or later will find a practical meaning. In fact, any important institution/rule ends by being adapted to the national environment, becoming part of it.

It must be noticed that, in the years, the European Union demanded from the candidate countries not only an approximation of legislation, but a total and complete transportation of it. This kind of approach, of the type 'take it or leave it', is grounded in the necessity of eliminating from the beginning the perspective that, at the moment of admission, candidate states be an different levels of readiness, which would impede the Union's proper functioning. Another request of the European Commission, expressed in the Annual Reports that starting 1998 are written for each accession candidate, is to take into account only the legislation effectively passed, and not the one in the process of being adopted, in order to treat all the countries with an objective benchmark. From this viewpoint also, Romania's situation is less satisfactory, since important laws, like those referring to the capital market or to the insurance, are in the Parliament for more than a year now. Certainly, it can be argued that the bi-cameral structure of the Romanian Parliament, which doubles on even triples the necessary time for a law's passing, is not the most appropriate institutional setting for a country in transition and, above that, candidate to accession, where the legislative process needs a sustained rhythm.

In transition countries in general and in Romania in particular, financial system are dominated by a few banks, the role of the capital and insurance markets being a secondary one. The explanation for this state of affairs can be found in the following factors:

- centralised economies have maintained remnants of banking institutions, whereas stock exchanges have been dismantled and insurance institutions played a peripheral role;
- capital markets have developed in the West only relatively recently (in the last 20-30 years), needing a range of rather sophisticated pre-conditions;
- the model most available for transition countries was that of Continental Europe, when the majority of firm's financing is done through the banking sector (as opposed to the USA and Great Britain, where the stock exchange plays an outstanding role).

Given these aspects, developing the banking system means, for a transition country, firstly focusing upon the banking Directives. In this field, Romania's performance to date is a mixed one, there existing a large number of banking Directives partially taken over, but also an important number of banking Directives that haven't even been tackled.

Some Directives (like 86/635 concerning the annual accounts and the consolidated accounts of financial institutions, or 93/6 concerning the adequacy of own funds) are conceived to address not only banks, but also a large gamut of financial institutions. This interdisciplinarity was hard to ensure, for the time being, in Romania, since some institutions (like the capital market) have only recently been created, while the accountancy framework is not adequate for a suitable treatment of the problem. Also here one can raise the issue of co-operation between the authorities of the financial market (NBR, NCVM, OSAIR), both in the legiferation and in the supervision activities. Romania, like the vast majority of Central and Eastern European Countries, opted for having three distinct supervisory authorities, with tasks being specific to the three types of activity, because historical reasons made unattractive the passage to a single supervisory authority, as in the British model.

The study is structured as follows: the first part is dedicated to the analysis of the adoption of acquis communautaire in the field of financial markets. Thus, there are three sections, dealing respectively with the banking market, the capital market, and the insurance market, where a review of the adoption of Directives is done. This adoption is compared to the one realised in three countries more advanced in the transition process (the Czech Republic, Poland and Hungary), illustrating the advancements and the lagging behind of Romania for each individual Directive. Also, each section deals with presenting the competition in the respective sector, structured around the following main ideas:

- the degree of concentration of that particular sector and its historical evolution, as an indicator of competition;
- the existence or non-existence of hindrances for foreign firms' entering of the market, with the advantages and disadvantages that would stem from here;
- freedom of entry and freedom of exist in the market, the bankruptcy being a way of protecting the sector from unwelcome practices;
- consumer's protection through various methods, like periodical and transparent information, the establishing of a deposit-guaranteeing system or the reinforcement of supervising system.

The second part of the study deals with competition policies and their current status of implementation in Romania. From the viewpoint of financial markets, competition is crucial for consumer's protection against abuses, as well as for the general enhancement of economic efficiency.

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Chapter I: The Banking Market

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1. Objectives and principles of European banking regulation

The Treaty establishing the European Economic Community, signed in Rome on March, 25th, 1957, put the foundation of the creation between member states of an economic space without frontiers, based on free circulation of persons, goods, services, and capitals and on equal conditions of competition. The realisation of this “Single market” is based on the adoption of some regulations of the Council or of the Commission, which aim at the harmonising of the member states’ legislation.

The Agreement upon the European Single Space has enlarged the single market, starting January 1st 1994, for several EFTA countries. In parallel, the member states of the European Community have strengthened the links uniting them, through the adoption of the Treaty regarding the European Union (EU).

The fulfilment of a single banking market, starting January 1st, 1993, implied a minimal harmonisation of member states’ banking regulations. To this end, a minimum basis of regulation was adopted, having as goals:

- (1) to ensure free exercising of banking activities in all member countries;
- (2) to ensure equality of competition conditions;
- (3) to avoid arbitrage in the field of banking supervision;
- (4) to ensure solid banking systems.

In order to define this minimum basis of regulation, the following principles were retained:

- a) *total freedom of capital movements within the EU*;
- b) *freedom of establishment*: any institution authorised in a member state has the right to set a branch in any other member state, without requiring the approval of the host country;
- c) *freedom to provide services*: any credit institution authorised in a member state may provide banking services for a client located in another member state without needing to detain a branch in that state;
- d) *mutual recognition of authorisations and of banking practices*: exercising the above mentioned liberties is allowed for all credit institutions which are authorised in their country of origin;

- e) *supervising by the country of origin*: the EU didn't create an European organism of banking supervision but, based on the principle of subsidiarity, left competence in this matter to the member states.

2. Directives of stage I

2.1. First Directive of banking co-ordination

The Council Directive 77/780/EEC concerning the co-ordination of laws, regulations and administrative provisions related to the starting and operating of credit institutions, was adopted on December 12, 1977 and entered into force on December 17, 1979.

The Directive has a limited area of regulation, but it represented the first step in the implementation of the present framework of Community banking regulation, establishing common rules concerning the starting and the operating of credit institutions.

This Directive introduces the principle of home country control and imposes a series of rules regarding the supervision of credit institutions. It applies to credit institutions that are defined as entities attracting reimbursable funds from the public and extending credit on their own account. The Directive doesn't however apply to Central Banks, to institutions of postal transfers' and to other categories of institution specifically named in its text.

The Directive sets the obligation for the credit institutions to be authorised before starting functioning. The functioning authorisation may be granted only if the following conditions are fulfilled: (1) the credit institutions dispose of adequate and permanent minimum funds; (2) the activity of the institutions is effectively managed by at least two persons (the "four eyes" principle) that have to have a good reputation and enough experience to fulfil their attributions.

At the same time, the Directive abolishes the criterion of "economic necessity" as a requirement upon which a functioning authorisation may be granted.

According to the Directive, member states may subject the branches of credit institutions that have their headquarters in another member state to the same authorising criteria that are applicable to the credit institutions set up on their territory. Also, according to the Directive, member states have full liberty in establishing the criteria of granting functioning authorisations to branches of extra-Community banks, but they may not offer more favourable terms than the ones offered to the Community credit institution's branches. Moreover, the Directive establishes the basic principles of co-operation between the supervisory authorities of member states, in special with regard to the exchange of information concerning the management and the structure of shareholders of credit

institutions. The Directive introduces the obligation of professional secret for the persons hired by competent authorities. The same obligation applies to confidential informations about credit institutions, that are transmitted to competent authorities from other member states.

The Directive was largely implemented in Hungary and Poland and partially in the Czech Republic. In all these countries, the provisions concerning professional secret must be amended to become fully compatible with those of the Directive under discussion. Also, in the Czech Republic, there is a need to revise the conditions established for foreign banks in order to operate on the national market. In the majority of cases, the remaining amendments will be implemented at the moment of these countries' accession.

With regard to Romania, the vast majority of the Directive's provisions were transposed into national legislation. There still remain some differences, such as those linked to the regime applied to foreign banks' branches; the exchange of information's with the supervisory authorities of the Community countries; the maintaining of a permanent minimum level of own funds. Concerning the first issue, it must be mentioned that, according to the Directive, branches established in the same member state by a credit institution having its headquarter in another member state must be treated as a single branch. On the contrary, Romanian banking legislation treats individually each branch established on the national territory by a bank with its headquarters abroad:

As a consequence, in conformity with Romanian authorities' declarations, the provisions concerning foreign bank branches (including the Banking Law) will be amended until the end of 2000. Referring to the second aspect, it is foreseen to amend the legislation and the relevant provisions concerning foreign banks branches supervision within the same time horizon. Finally, there must be brought corresponding amendments to the banking legislation in order to respect the Community principle of the permanence of minimum own funds, which applies to credit institutions.

2.2. Directive of the Council of April 17, 1989 concerning the own funds of the credit institutions (89/299/CEE)

The Directive concerning the own funds of credit institutions was adopted on April 17, 1989 and entered into force on January 1, 1991, together with the Directive of December 18, 1989 concerning the solvency ratio.

The Directive provides a common definition of credit institutions' "own funds" and the determining criteria of their structure. It represents a key element in creating a single market in the banking field, because the existence of adequate own funds ensures the stability of credit institutions and protects the public's savings. At the same time, through harmonising the standards relating to own funds, one can avoid the distortion of competition in the banking sector due to different national definitions and can create equal competitive conditions for banks at the Community level.

The Community definition of own funds follows to a great extent the regulations of the Bale Agreement of 1988 concerning capital standards. As a result, own funds are divided into core capital and supplementary capital.

Core capital (tier I) consists of elements pertaining to capital of the highest quality, as for instance: social capital, legal reserves and funds for general banking risks. The high quality of these elements consists of the fact that they have an internal nature and can absorb the losses. Supplementary capital (tier II) consist of reserves from revaluation, value corrections, latent reserves, titles with an undetermined value, commitments of the co-operative companies' members, subordinated debt and other financial instruments that fulfil certain conditions expressly specified in the Directive.ⁱ

The Directive rules that member states may foresee stricter rules for their credit institutions. To this end, member states may not include certain elements in the national definition of own funds or to foresee more severe conditions to include them, to demand more important or more numerous deductions etc. It must be specified that, in conformity with the principle of mutual recognition of supervision, the member state that has foreseen stricter rules may not apply them onto credit institutions authorised in other member states, where only the Directive's provisions are applied. In the context of competition, national credit institutions will be more penalised as their own state's legislation will be more severe in defining own funds.

The main provisions of the Directive have already been implemented in Hungary, the Czech Republic, and Poland. The definition of core capital and of supplementary capital establish by relevant Magyar provisions departs in a number of ways from the Community one. At the same time, the Hungarian Banking Law foresees more numerous deductions than those established by the Directive in the computation of core capital, which leads to stricter requirements than the EU standards. This situation, in the absence of further modifications, is bound to affect the competitiveness of Hungarian credit institutions in the post-accession period. In Poland, the differences between the Directive and relevant national provisions can be considered insignificant, being subject to complete elimination by year 2004. It is worth mentioning that, in certain respects, the solutions adopted by Polish authorities are more restrictive than the Directive's. Concerning the Czech Republic, experts consider that the provisions relating to own funds of the credit institutions correspond to the Directive's provisions.

The Directive is implemented in the Romanian legislation through Law no. 58/1998 – the Banking Law – and through NBR's Norms no. 7/1999 concerning banks' own funds. Although these regulations are relatively recent, they are not fully harmonised with the Directive's provisions.

The main differences refer to the definition and structure of own funds. In accordance to actual Romanian regulations, both own capital (which correspond to the Community's notion of basic own funds) and supplementary capital contain addition elements that are not to be found in the definition used in the Directive.ⁱⁱ *Solving these differences will require amending both accounting legislation and banking legislation.* Also, Romanian provisions regarding subordinated debt are only partially harmonised with the Community ones.ⁱⁱⁱ Another difference consists in the fact that Romanian legislation does not contain provisions concerning the recognition of co-operative companies members' commitments as an element of own capital; *this last aspect will be possible to solve in the context of adopting a new framework for the credit co-operatives.* Lastly, the problem of the absence of provisions concerning the consolidated accounts will have to be solved. *To this end, it is*

necessary for the National Bank of Romania to issue specific norms, immediately after the Ministry of Finance will establish general rules about accounts' consolidation.

2.3. Directive of the Council of December 18, 1989 concerning the solvency ratio of credit institutions (89/647/EEC)

The Directive concerning the solvency ratio of credit institutions was adopted on December 18, 1989 and entered into force on January 1, 1993.

The Directive has two objectives: 1) to harmonise prudential supervision rules necessary for the completion of internal market; 2) to strengthen the solvency standards of Community credit institutions in order to protect the deponents, the investors and to ensure the stability of the banking system within the EU.

The Directive rules that the solvency ratio is computed as a rate between own funds of credit institutions (the numerator) and assets and off-balance items weighted in accordance to credit risk (the denominator).

Starting January 1, 1993, credit institutions are obliged to permanently maintain the solvency ratio, as previously defined, at a level of 8%. The harmonisation being a minimal one, national authorities may fix a higher level of the solvency ratio; this supplementary constraint will only apply to those institutions under the supervision of the competent authority that has announced them. If the solvency ratio falls below 8% (or below the higher national standard), the competent banking supervision authorities must take measures to re-establish the situation. The solvency ratio must be computed on a consolidated basis, but additional unconsolidated ratios are asked for all credit institutions.

Computing the solvency ratio implies applying some technical rules that are not established in detail in the Directive. Thus, article 6 of the Directive indicates for each bilateral asset the category to which it belongs and the share that must be applied. Wishing to have a simpler method, only four shares were retained: 0%, 20%, 50% and 100%, which are attributed in accordance to the nature of the debtor, of his origin country or of the operation's nature.^{iv} Annexes I and II ensure a classification of the off-balance items and establish the treatment that must be applied to those items, concerning the interest rate and the exchange rate risks, while article 6(2) establish as the risk weights for off-balance assets. Annex II was replaced by Directive 96/10 of March 21, 1996, which introduced specific rules concerning contractual compensation.

To a large extent, the provisions concerning the solvency ratio have been transposed into the national legislation in Poland, Hungary, and the Czech Republic. In Romania, most of the provisions are transposed into the legislation, the main differences which will require its amendments being the following:

- the lack of provisions concerning credit institutions that themselves are affiliated to a central institution. This aspect will be solved through modifying Law 109/1996 concerning credit co-operatives;
- the lack of provisions concerning supervision on a consolidated basis;
- the lack of provisions concerning the treatment of the off-balance positions concerning and exchange rates. For these, the NBR has asked the assistance of Banque de France, within a twinning agreement.

2.4. Directive 94/19/CE of the European Parliament and of the Council, of May 30, 1994, concerning the system for deposits guaranteeing

Deposits guaranteeing is, together with prudential regulations and Central Bank's interventions as a lender of last resort, one of the instruments that can be used to reduce or eliminate the negative effects which the bankruptcy of a credit institutions can induce upon the rest of the financial system.

The Directive 94/19/CE of the European Parliament and of the Council, of May 30, 1994, concerning the systems of deposits guaranteeing, has entered into force on July 1, 1995. The adoption of this Directive is justified by the fact that deposit guaranteeing is a central element for a single banking market and an indispensable complement of the supervisory system, by virtue of solidarity which it creates among all institutions of the same financial market in the case of one's bankruptcy. The Directive has in view ensuring a minimum harmonised level of deposit guaranteeing, irrespective of deposits' localisation within the European Union.

The main features of Directive 94/19/CE are the following:

- each EU country must have one or several schemes of deposit guaranteeing;
- the Directive imposes the principle of mandatory participation in a system of deposits guaranteeing for every credit institution authorised within the EU. The Directive admits an exception from this principle only for credit institutions that belong to a system that protects both the credit institutions and its liquidity and solvency and only if this protection is equivalent to the one ensured by the relevant scheme(s) of that state. In this case, beside other conditions that must be fulfilled, it is necessary for the guaranteeing scheme not to represent a guarantee extended to the credit institutions by a member state or by any the local/regional authorities;
- credit institutions that are not member of a guaranteeing scheme may not attract deposits;
- the deposits' protection rests upon the modified principle of origin country;^v
- branches established by an extra-Communitarian credit institution must dispose of a guaranteeing ceiling equivalent to the one established in the Directive, otherwise these branches having to adhere to the host country's scheme;

- the minimum level of guarantees was established at EURO 20,000 (EURO 15,000 until December 31, 1999 for the member countries having already a limit smaller than EURO 20,000);
- the guarantee is given per deponent and not per deposit;
- interbank deposits, commitments of the nature of own funds and deposits arising from money laundering operations are not protected by guaranteeing schemes;
- certain deponents or deposits may be exempted or may be granted a lower level of guaranteeing;
- payment of verified liabilities should be done within three months since deposits' indisponibility; prolonging this period is allowed in exceptional circumstances;
- the Directive does not contain harmonisation features regarding the legal status of guaranteeing funds (of public or private nature) or financing mechanisms (capitalising or repartition schemes).

As it can be noticed, the EU Directive contains explicit harmonisation provisions concerning the minimum level of protection; the co-responsibility; the types of deposits which are guaranteed; the scope of the guarantee; the status of Community or extra-Community branches. As a consequence, candidate countries will have, sooner or later, to implement these provisions into their national legislation. Conversely, these countries are free to chose from a relatively wide set of options, concerning the financing mechanism and the administrative structures of the guaranteeing systems.

In the last years, a series of countries from Central and Eastern Europe have set up guaranteeing schemes, in the next chronological order: Hungary (March 1993), the Czech Republic (December 1994), Poland (February 1995), Slovakia (July 1996), Romania (August 1996). All these countries have adopted explicit systems of deposit guaranteeing. Their institutional scope and the types of guaranteed deposits differ from country to country, depending on the structure of the banking system and on the adopted philosophy of prudential regulation. For instance, Poland, the Czech Republic and Hungary guarantee the deposits of certain legal persons, while Romania and Slovakia cover only natural persons.

Regarding the maximum limits of deposits guaranteeing in the above mentioned countries, they are the following: Hungary – 1 million Forints, Poland – 5000 Euros, Czech Republic – 400 000 Korunas, Romania – 46,2 million lei (corresponding to the second semester of 1999, semestrially adjustable with the inflation index CPI), Slovakia – 30 monthly average wages for deposits placed with commercial banks and 60 monthly average wages for deposits placed with savings banks for construction. In all these countries, the guaranteeing ceiling is well below the one imposed by Community legislation, due to the much lower level of revenues as compared to the EU. Because the Community level of protection is too high, Hungary intends to ask for a transition period of five years, while Poland has decided to gradually increase the ceiling, so as to harmonise fully with the Community by January 1, 2003.

In view of EU accession, the Romanian legislative should introduce into national legislation the minimum requirements of the Directive. Hereafter are presented the main modifications needed to ensure compatibility with the European legal framework:

1. Mandatory participation of all credit institutions in a scheme of deposits guaranteeing. In this context, it should be analysed whether credit co-operatives should adhere to the existing scheme

or should rather create their own scheme. Also, full harmonisation will require CEC (the Savings Bank) to renounce the state guarantee and to adhere to the scheme of deposit guaranteeing.

2. Abandoning the obligation of EU banks' branches to adhere to the Romanian system of guaranteeing.
3. Extending the guarantee of the Romanian scheme upon the deposits constituted in EU countries by Romanian banks' branches.
4. Extending the guarantee upon certain legal persons. Such a decision will however lead to higher costs for the Fund, while the restructuring process of the Romanian banking system is not over yet. As a result, this extension should be done in a wider frame of time.
5. Establishing a minimum level of protection equivalent to Euro 20000. For the Fund's resource the match its liabilities, it is advisable to have the increase of the guarantee ceiling to this level after Romania's accession into the EU. *It could be necessary to negotiate a transition period of five to ten years (similar to Hungary).*
6. Excluding from guaranteeing the deposits linked to money laundering operations.
7. The guaranteeing to be done per deponent and not (as currently) per deposit. This will reduce the Fund's liabilities.

3. Directives of stage II

3.1. Second Directive of the Council (89/646/EEC) of December 15, 1989 concerning the co-ordination of laws, regulations and administrative provision linked to the starting and operating of credit institutions, amending Directive 77/780/EEC.

The second Directive on banking co-ordination was adopted on December 15, 1989 and entered into force on January 1, 1993.

The Directive represents the main instrument for the creation of a single banking market. It founded the freedom of establishment and providing service by a credit institution within the EU, on the basis of mutual recognition of the authorisation received in another Member State where it has its headquarters. Once a credit institution has been authorised in a member state, it can establish branches or provide services in other member countries, on a transboundary basis, without the need to be authorised by the competent authority of the host country. This freedom, labelled "single European passport", applies both to the Community banks and to the subsidiaries set in EU countries by extra-Community credit institutions. It does not apply to branches of extra-Community banks, which must obtain a functioning authorisation within each EU country of operation.

The single authorisation allows a credit institutions to perform throughout all of the EU not only “classical” banking activities, but also other financial services presented in the Annex^{vi} to the Directive, on the condition that the concerned institution has been authorised to perform those activities in its home country. Thus, if a credit institutions provides “universal bank” services within its home country, then it can offer them in any other EU country, even if domestic credit institution are not allowed to provide such services.

From the principle of mutual recognition of authorisations follows logically the principle of prudential supervision of credit institutions by the authority of the member state that gave the authorisation (“authority of origin country”). However, the Directive stipulates that, until further co-ordination, the competent authority of the host country remains responsible for the supervision of a bank branch’s liquidity, in collaboration with the authority of the home country. Moreover, while the home country authority must take the necessary measures to stop the wrongdoings of a credit institution on the territory of another member state, the competent authority of the host country may take, in emergency cases, steps indispensable for protecting clients’ interests or adequate measures to prevent or repress on its territory acts which go against the legal dispositions it has issued for general interest purposes.

The Directive harmonises also the authorising and supervising conditions of the credit institutions’ shareholders, the minimum level of own capital and limits the non-financial participations.

A first authorisation requirement imposed by the Directive is that credit institutions dispose of an initial capital of at least ECU 5 million. Member states are free to apply higher levels of initial capital for their credit institutions. Under certain conditions and for a limited number of credit institutions (e.g., for banking co-operations), the initial minimum capital requirement may be reduced to the amount of ECU 1 million. Before the authorisation’s granting, the credit institution must inform the competent authority about the identity of its shareholders/associates. The respective authority may refuse granting the authorisation if it is not satisfied with the quality of shareholders/associates that detain a qualified participation.^{vii} As to the permanence of own capital of a credit institution, the Directive foresees that this may not fall below the initial minimum capital amount from the moment of authorisation.

The Directive introduces strict requirements as to the control of capital participation in credit institutions. Beside the mandatory condition that competent authorities verify carefully the quality of shareholders which detain a qualified participation before granting an authorisation of functioning, the Directive rules that if a legal or natural person intend to acquire a qualified participation in a credit institution or intend to increase such a participation, they must first notify the competent authority which may raise objections within three months.

If the influence of shareholders/associates that detain qualified participation is detrimental to a strong and healthy management of credit institutions, the Directive establishes adequate measures for remedying this situation, such as suspending the voting rights attached to the shares detained by the said shareholders. Also, when a capital participation is obtained despite the banking supervision

authorities' refusal, the Directive foresees the following sanctions: suspending of the corresponding voting rights, nullity of the given votes or the possibility to nullify them.

According to the Directive, a credit institution may not detain qualified participations that exceed 15% of its own capital in another entity, with the exception of participations in other financial institutions or in insurance companies. At the same time, the total sum of these participations may not exceed 60% of a credit institution's own capital.

The Directive's provisions have been partially implemented in Poland, Hungary and the Czech Republic. In general, banking prudential regulations in these countries impose restrictions on foreign credit institutions' free access onto the national market and do not take into account the principle of supervision's mutual recognition.

All these countries, with the exception of the Czech Republic, consider that the Community regulations concerning the single market (the principle of a single license, the principle of origin country control) can only be adopted at the moment of accession. The Czech Republic intends to transpose entirely the regulations into the national legislation before becoming an EU member.

In its turn, Romania has implemented partially the Directive's regulations. The main differences still existing are presented below:

- in order to open a branch in Romania, a foreign bank must obtain a functioning authorisation from the NBR and must have a starting capital. These requirements are not compatible with the relevant Community legislation which stipulates the freedom of establishment and does not require starting capital for branches. *These aspects may be solved through amending the banking legislation at the moment of accession;*
- Romanian regulations do not foresee the principle of permanent maintaining of minimum own capital for credit institutions;
- Romanian regulations concerning the control of capital participation for credit institutions do not establish a deadline within which competent authorities can oppose the intention of a significant acquisition, nor a maximum period for enforcing this in the case of the reduction of a significant participation;
- in the banking legislation there are missing specific regulations concerning banking mergers;
- also, there is a lack of regulations concerning the relations with the Stock Exchange, and those concerning the information exchange between the competent authorities of the state;
- as mentioned for other Directives, there is a lack of regulations concerning credit institutions affiliated to a central body (these will be corrected through the amendment of the Credit Co-operatives Law), as well as of those concerning supervision on a consolidated basis.

Solving these differences will require the amendment of the Banking Law.

3.2. *The Directive concerning the supervision and the control of large credit risk (92/121/EEC)*

The Council Directive concerning the supervising and the control of large exposures was adopted on December 21, 1992 and entered into force on January 31, 1994.

Monitoring and controlling large exposures represents an intrinsic part of banking supervision, because excessive concentration of credit risks vis-à-vis a client or a group of clients connected between them^{viii} may lead to important losses able to affect the solvency of banking institutions.

The Directive establishes the criteria for determining large exposures and fixes limits for them in relation to credit institutions' own capital, which are mandatory at the EU level.

Exposures are defined as credit risks established by the Directive concerning the solvency ratio.^{ix} With regard to the definition of a large exposure, according to Directive 92/121/EEC, it represents a risk incurred by a credit institution vis-à-vis a client or a group of clients connected between them, whose value amounts to or exceeds 10 percent of its own capital. Large exposures have to be reported to supervision authorities and may not exceed 25% of own capital of the credit institution. In the case when credits are extended to persons which are linked to the credit institutions (mother-institution, own subsidiary or subsidiary of the mother-institution), the Directive establishes a stricter limit, of 20%.^x Beside these individual limits, the Directive introduces a ceiling to be applied to the sum of large exposures. To this end, in order to prevent the accumulation of a clustering of big exposures, the Directive forbids a credit institution to incur a total amount of large risks in excess of 800 percent of its own capital. In expressly specified cases, the Directive authorises member states to except from the limits it sets (20%, 25% or 800%) certain risks.^{xi} Also, the Directive asks the credit institutions to implement adequate internal procedures for identifying and accounting large exposures and sets transitory periods in order to allow the credit institutions to adapt themselves to the new limits.^{xii}

The Directive's requirements have largely been transposed into national legislation in Hungary and Poland and partially in the Czech Republic. In Hungary, the requirements concerning subsidiaries and mother-companies are more restrictive than the Communitarian ones, in order to compensate for the lack of an efficient framework of consolidated supervision. In Poland, the Communitarian rules concerning large exposures of consolidated groups have not been applied yet.

In Romania, the requirements of the Directive are only partially transposed. If for some minor aspects it is enough to have secondary legislation approved by NBR's board, for other aspects it is necessary to amend the existing legislation. Such problems concern mainly the definition of such terms as "financial holding company", "financial institution", or "activity of mother-company", which may be solved only in the context of defining the supervision on a consolidated basis. At the same time, it is necessary to improve the regime of the consolidated accounts.

3.3. Council Directive (92/30/EEC) concerning the supervision of credit institutions on a consolidated basis

The Directive concerning the supervision of credit institutions on a consolidated basis was adopted on April 6, 1992, and entered into force on January 1, 1993.

Prudential supervision only makes sense when it allows the assessment of the totality of risks assumed, directly or indirectly, by a credit institution. Credit institutions are often part of a larger framework of legal persons, which form a group (at a national or supra-national level): mother-company, subsidiaries, under-subsidiaries. In this case, a credit institution must be subjected to supervision on the basis of consolidated financial statements, in other words by taking into account all risks assumed by the group.

The legal framework for introducing supervision on a consolidated basis at the Community level was created by adopting Directive 83/350/EEC on June 13, 1983. This Directive had, however, a series of deficiencies, the most important being that it foresaw consolidation only 'in downstream' and only if the mother-company was a credit institution. As a result, it was enough to place all the credit institutions of the group under the control of a holding company, to get them out of the supervision on a consolidated basis.

The new Directive (92/30/EEC) extends the obligation of supervising the banking activity on a consolidated basis to the cases when the mother-company of a group is a financial holding company, i.e. a financial institution which has at least one credit institution as a subsidiary. In the case when the mother-company of a group is a mixed activity holding company,^{xiii} the Directive imposes to all its subsidiaries the obligation to transmit informations to the prudential supervision authority.

Also, the Directive contains rules concerning the competent authority or authorities who will perform the supervision on a consolidated basis and establishes the consolidated methods that can be applied. An important feature of the Directive is that it allows, based on mutual agreements, to transfer the primary supervision responsibility towards the member state in which the largest part of activity is being performed. This way, banking supervision will substantially improve.

Consolidated supervision is efficient only if it can be performed at the level of the whole group. To this end, the Directive grants the European Commission the power to negotiate agreements with extra-Community countries in order to extend consolidated supervision and exchange of confidential informations with the countries having branches on EU territory or having themselves branches of a Communitarian mother-company.

The rules of the Directive were not or were only partially implemented in countries belonging to the first wave of accession negotiations with the EU. In Poland, the banking supervision authority is entitled to exchange informations with other internal or external prudential control organisations. Also, the Banking Law requires completing the financial statements on a consolidated basis. Nevertheless, there remain numerous important differences which are planned to be solved before the moment of accession, through issuance of detailed requirements in the field of consolidated

supervision. Also, in Hungary, the implementation of a consolidated supervision system for credit institutions is planned before its EU accession.

Currently, the Directive's requirements are not transposed into Romanian legislation. This situation will be solved through NBR's issuing of specific norms concerning supervision on a consolidated basis. Using this technique is, however, conditional upon the Ministry of Finance's issuing of general accounting standards concerning the consolidation of accounts.

3.4. Directive of the Council 86/635/EEC of October 8, 1986 concerning the annual accounts and the consolidated accounts of banks and other financial institutions

Accounting rules play an important role in evaluating the financial health of a credit institution. Also, the nature and the scope of informations that have been published represent a competition element. For these reasons, the Community authorities have decided to harmonise the accounting rules applicable to credit institutions even before the creation of a single banking market. The Directive of December 8, 1986 harmonises the way of balance presenting by the credit institutions through establishing a standard format, where assets and liabilities are registered in descending order of liquidity and through imposing specific requirements for some positions in the balance. Also, the Directive sets two versions for the profit and losses account (one horizontal and one vertical), together with the specific rules for certain of its elements. The harmonisation had in view by the Directive includes methods of evaluating different categories of balance and off-balance items, and also informations that must accompany the annual accounts and the conditions under which they may be published. At the same time, the Directive obliges the credit institutions to use and to publish consolidated accounts when they detain subsidiaries performing banking activities, and it establishes the way of presenting them.

The requirements of the Directive have been partially implemented in Hungary and in the Czech Republic, while Poland reported that they have been fully transposed into national legislation. In the case of Romania, differences persist concerning the structure of the balance, the structure of off-balance accounts, of the profit and losses account and the methods of evaluation.

In order to harmonise the legislation with the European one, the Ministry of Finance has to issue new accounting norms.

3.5. The Directive of the European Parliament and of the Council 95/26/EC of June 29, 1995, amending Directives 77/780/EEC and 89/646/EEC concerning credit institutions, Directives 73/239/EEC and 89/646/EEC concerning non-life insurance, Directives 79/267/EEC and 92/96/EEC concerning life insurance, Directive 93/22/EEC concerning investment firms and Directive 85/611/EEC concerning entities for collective investment in stock, related to strengthening prudential supervision

The Directive 95/26/EEC was adopted on June 29, 1995 and entered into force on July 18, 1996.

The Directive, also called the post-BCCI Directive, sets measures to strengthen the prudential supervision of financial institutions. Its goal is to offer extra powers to the authorities in order to allow them to prevent the appearance of frauds and irregularities similar to those that led to the fall of Bank for Credit and Commerce International (BCCI). The Directive recognises that the problems experienced in the BCCI case are not only related to the banking sector and that they may appear also in the process of supervising financial groups. Thus, the Directive amends a series of Directives concerning credit institutions, insurance firms and investment companies.

The amendments introduced by the Directive refer to:

1. introducing measures to ensure the transparency of the financial group and to allow supervision authorities to efficiently supervise each financial institution member of the group;
2. introducing the requirement that the headquarters of the financial institution be located in the member state where the authorisation was issued;
3. extending the list of the organisations to which supervision authorities may communicate confidential informations; within these organisation are, *inter alia*, the authorities that supervise the liquidations or the auditors of the respective financial institutions;
4. introducing the requirement that statutory auditors immediately report to the competent authorities the irregularities they have discovered.

The post-BCCI Directive was fully implemented into the relevant Polish legislation. In the Czech Republic, the Directive was transposed to a large extent into national law, remaining to be solved aspects concerning the exchange of informations between supervision authorities and external auditors. In Hungary, only a few harmonised requirements have been so far included into the national legislation.

The Community requests concerning the strengthening of prudential supervision of financial institutions have not yet been implemented in Romania. NBR has to issue specific rules in this field.

3.6. Directive 96/10/EC of the European Parliament and of the Council, of March 21, 1996, amending the Directive 89/647/EEC concerning the recognition, by the competent authorities, of bilateral netting.

In the last years, the international fora of banking supervisors have proposed rules concerning recognition of bilateral netting. Using this technique, two credit institutions, that detain positions in opposite sense, may agree, under very strict conditions, to compensate their reciprocal debts, which will allow them to weight the risks on a net basis a not on a gross basis, when computing the solvency ratio. This situation leads to lower requirements of own capital, with corresponding impact on banking competition.

The Directive, which is in accordance with the works of banking supervision international bodies, modifies Annex II of the Directive concerning the solvency ratio. Its purpose is to allow a larger recognition of bilateral netting, at the Community's level, in order to create equal competitive conditions for both EU credit institutions, and between them and other states'. According to the

Directive, national authorities are allowed to recognise not only netting through innovation, but also other types of bilateral netting, on the condition to prove the juridical validity of bilateral netting.

Due to the problems of juridical nature concerning the validity of bilateral netting contracts, none of the countries currently negotiating their accession to the EU has implemented in its national legislation the requirements of the Directive. This situation is valid also for Romania.

3.7. Directive of the Council 93/6/EEC of March 15, 1993 concerning the adequacy of own capital of investment firms and credit institutions

Directive 96/6/EEC was adopted on March 15, 1993 and entered into force on January 1, 1996.

The Directive concerning the adequacy of own capital of investment firms and credit institutions, whose enforcement is connected to Directive 93/22/EEC concerning investment services, has in view that free provision of financial services throughout the Community should be done in safety. It identifies the risk, others than the credit ones, to which are exposed banks and investment firms when performing operations on the capital market^{xiv} and allows applying a single rate of own capital to ensure equal competitive conditions between banks and non-bank entities that perform the same type of activity.

According to the Directive, investment firms and banks that operate on the stock exchange must divide their assets into two parts: the trading book^{xv} and the non-trading book.^{xvi} The capital requirements for the non-trading book are computed in accordance to the Directive 89/647/EEC concerning the solvency ratio. The capital requirement for the trading book are set by the Directive 93/6/EEC based on the building block approach.^{xvii} Also, the Directive includes detailed rules concerning the computation of own capital requirements both for the settlement risk, for the counterparty risk, and for the exchange risk. The Directive includes also special rules referring to the treatment of large exposures.

According to the Directive, a credit institution must permanently maintain own capital equal at least to the sum between the capital requirements for the trading book and the capital requirements for its other operations. This own capital must be defined in accordance with the Directive concerning own capital of credit institutions. However, for covering the risk existing in the trading book, the Directive allows an alternative definition which includes a third category of capital (“tier 3”), more elastic and more adapted to the market’s fluctuations, constituted from short-term subordinated debt. The alternative definition allows for a substitution of the second capital category with the third one within a ceiling of 250 percent of the first level (“tier 1”) of capital. Also, the profits of the current year may be considered as an element of own capital, provided these were not taken into account when computing the first two capital categories.

The Directive extends upon non-banking investment firms the dispositions of the Directive concerning the consolidated supervision of credit institutions. However, for groups that do not include a banking institution, the capital requirements may be computed on an individual basis.

Until now, Directive 93/6/CEE was partially implemented in Poland and Hungary. In the first country, a series of requirements regarding risk measurement are to be found also in the prudential requirements issued by the Central Bank. It is, however, estimated that complete transposition in the national law of this Directive will not take place before end-2000. In the second country there exist relatively recent amendments of the legislation regarding stock, as for instance defining the financial instruments included in the trading book and the requirement to daily value them at a market price. According to disposable information, regulations concerning capital requirements for the trading book have not yet been adopted. In what concerns the Czech Republic, this country has expressed its willingness to implement the Directive's rules during 1999.

The Directive 93/6/EEC was not yet implemented into Romanian legislation. Its main requirements are, however, included in the draft law concerning the stock and the regulated markets which were submitted to the Romanian Parliament.

3.8. The Directive of the Council 89/117/EEC of February 13, 1989 concerning the obligation of credit institutions' and financial institutions' branches which are located in a member-state but have the headquarter in another state, to publish annual accounts

The Directive 89/117/EEC was adopted on February 13, 1989 and entered into force on January 1, 1991.

The Directive 89/117/EEC stipulates that member-states must require the publishing of documents referring to the annual accounts^{xvii} and to the consolidated accounts, from the credit institutions' and financial institutions' branches established on their territory.

These documents must be drafted and audited in the way required by the law of the member-state where the credit institution or financial institution has its headquarters. Branches belonging to the previously mentioned institutions may not be obliged to publish annual accounts referring to their own activity. This last feature is justified by the fact that, once the Directive 86/635/EEC, concerning the consolidated accounts, was adopted, publishing of branches' annual accounts cannot offer to the public, and especially to its creditors, a clear perspective about its financial situation, because a part cannot be judged in isolation from the whole. However, taking into account the actual stage of integration, the Directive allows member states to ask, until further co-ordination, some informations regarding the branch's activity, specified in art. 2(4) of the Directive.

Regarding the branches of credit institutions and of financial institutions, having their headquarters in extra-Community countries, member-states must ask them the same informations, drafted and

audited in accordance to the law of that country. Provided these documents are equivalent with those drafted in accordance to Directive 86/635/EEC and provided the condition of reciprocity for similar institutions is fulfilled in that country, the respective branches must not publish annual accounts regarding their own activities.

The requirements of this Directive are not yet transposed into Romanian banking legislation. According to art. 60 of the Banking Law 58/1998, branches of foreign banks must publish an accounting balance, stating both their own activity and that of their subordinated institutions.

3.9. The Directive of the Council 91/308/EEC concerning the prevention of utilising the financial system for money laundering

The Directive 91/308/EEC was adopted on June 10, 1991 and entered into force on January 1, 1993.

In contrast with other international Conventions that limited themselves to define in juridical terms the concept of money laundering and had a recommendation character, the Directive 91/308/EEC introduces the obligation for EU member countries to forbid and to penally incriminate the activity of money laundering. Its scope is not limited to the capital obtained from drug trafficking but extends also upon funds derived from other criminal activities. The Directive applies to credit institutions and to financial institutions. Because money laundering activities can be performed also by entities from outside the financial system (casino, wholesale retails, lawyers, notariuses), the Directive establishes that its rules may be extended by member states to other professional activities or to enterprises that perform activities liable to be used for money laundering.

The definition given by the Directive to money laundering is similar to the one that is found in the preceding Conventions, of Vienna and Strasbourg. Broadly, money laundering activity represents an intentional act of conversion or transfer of the property obtained from a criminal activity, with the aim to hide its origin, or the assistance provided to any person in order to do this.

According to the Directive's stipulations, the financial institutions have the following duties: to identity their clients; to keep the track record of the clients and of their transactions; to pay a larger attention to transactions that might be related to money laundering; to report suspect transactions; to establish internal control procedures and personnel training programs to prevent money laundering activities.

The Directive concerning money laundering was fully implemented in Slovenia and partially in Hungary, Poland and the Czech Republic. In these last three countries, according to a relatively recent study of the Commission's Banking Consultative Committee, there still exist anonymous accounts. The Hungarian authorities have recently taken measures to abolish this type of accounts.

In Romania, the main provisions of the Directive were transposed into national legislation through Law 21/1999 concerning the prevention and the sanctioning of money laundering. *There remain still*

a number of differences between the Community and the Romanian laws, which will have to be eliminated in the next period. A first difference concerns the clients' identification requirements. According to the Directive, clients have to be identified in one of the next situations: (1) when they establish a business relation with the financial institutions; (2) when the transaction exceeds EURO 15,000; and (3) when the sum of the transaction is smaller than the previously mentioned amount, but there exists a suspicion of money laundering. The Romanian Law does not, however, require identification of permanent clients for transactions below the minimum sum. By neglecting a fundamental principle of financial activity: "know your customer", financial institutions may incur direct losses because they have accepted undesirable clients or because their employee's collusion with criminals. Moreover, as a consequence of non-observance of this principle, it will be much harder for the credit institutions to identify suspect transactions. *A second difference refers to the obligation of confidentiality from the part of credit and financial institutions* which, according to the Directive, may not inform their clients that informations have been given to competent authorities concerning them and that an investigation is under way. The Romanian Law doesn't contain any article with a similar content, which will permit criminals to be always one step ahead of authorities, making the files or the money to disappear. *As a result, in order to obtain a full harmonisation with the European requirements concerning money laundering, it is necessary to have a revisal, as soon as possible, of Law 21/1999.*

4. Competition in the banking sector

The way it was set up after the 1989 revolution, the Romanian banking system consists of universal banks offering their clients, in principle, the whole gamut of banking services. Ten years after the start of transition, this feature was preserved in that there don't exist, practically, any specialised banks. For instance, the Investment Bank's successor, the Romanian Bank for Development, deals also in commercial credit extending. Also, a credit institution very narrowly specialised, the Savings Bank (CEC) has, as a result of Law 66/1996, some involvement in the crediting of economy's real sector. In principle, the similar features of the services provided by Romanian commercial banks should have stimulated competition (as they did, to a certain extent).

4.1. Historical evolution of the banking system

At the beginning of the century and between the two world wars, the Romanian banking system developed very much, at least in numerical terms. During that period, Romania could have been considered the financial centre of the Balkans, a position that offered this country a certain rent.

After the Second World War, following the Soviet model, in Romania there functioned four banks with clearly defined attributions (the National Bank of Romania, the Romanian Bank for Foreign Trade, the Bank for Agriculture and Food Industry, the Investment Bank), as well as a credit institution for the population (the Saving Bank). During this period there couldn't have been any competition within the banking system, even more so since the foreign banks' presence was a purely symbolic one, leading to the worsening of professionalism and of the banking services' quality.

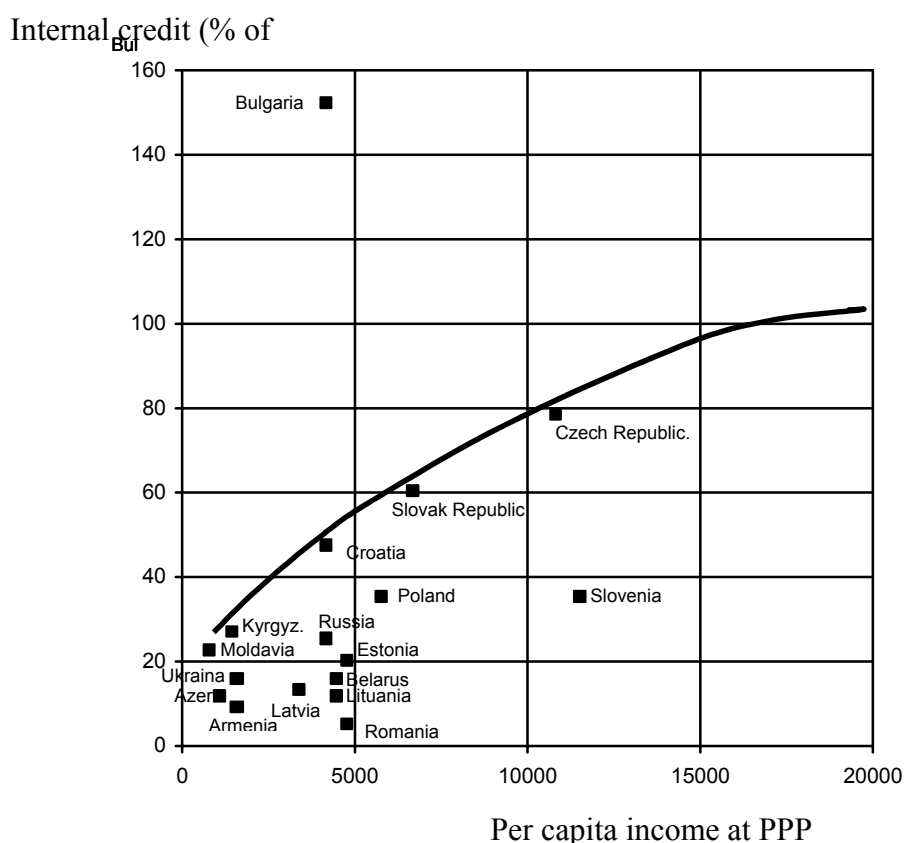
In the last decade, after a rapid increase of the number of banks during the first years, there followed a slowing of the growth and then a stabilisation in the last years (see table). To a large extent, this was the effect of the prudent policy of the NBR, which, recovering its prerogatives of central bank, imposed stringent requirements for the registering of commercial banks. This prudent policy of NBR led to an avoidance of a chain of bankruptcies, which confronted countries such as Bulgaria or Russia, where initially the procedure of authorising new banks has been much more lax.

Historical evolution of the banks' number in Romania

Indicator	1995	1996	1997	1998
Number of Romanian banks	24	31	33	36
Number of foreign banks	7	9	10	9
Total number of banks	31	40	43	45

Source: NBR

The question is whether, given the actual conditions, the Romanian banking market is overcrowded or if there is still room for competition. At a population of 22.5 million, the ratio of two banks for each million of inhabitants is among the lowest in Central and Eastern Europe. The tendency of the last years, of reduction in the financial and banking services share in the creation of GDP, from 5 percent in 1995 to 1.2 percent in 1998, and of reduction of the banking personnel in the total employed population, from 0.8 percent in 1996 to 0.7 percent in 1998 can be attributed rather to economic recession and to solvency problems faced by some banks, than to market's saturation. The best prove for the above is presented by the following graph, indicating the ratio between internal credit (as a percentage of GDP) and per capita level of income (in 1996).^{xviii} It can be observed that in Romania the level of extend credit is extremely low even in comparison to countries from the same income bracket, such as Lithuania, Belarus, Estonia, Russia or Croatia.



To a certain extent, the insufficiency of credit stems from *macroeconomic* factors, such as the low monetisation of Romanian economy, one of the lowest in the area. Indeed, beside CEECs with a “normal” degree of monetisation (Czech Republic, where broad money represented 74% of GDP

between 1993-1997, Slovak Republic, where the same indicator was 69% and Bulgaria with 66%), there are also countries with a moderate degree of monetisation (Hungary with 45%, Poland and Slovenia with 37%) and countries with a low or very low degree of monetisation (Latvia with 30%, Croatia with 29%, Estonia with 27%, Macedonia with 25%, **Romania with 24%**, Belarus with 22%, Ukraine with 20%, Russia with 19%).^{xix}

On the other hand, the insufficiency of credit may reflect *microeconomic* deficiencies, so that commercial banks are reluctant to extend credit to an insufficiently restructured real sector. Paradoxically, foreign banks entering Central and East European markets, far from stimulating competition, are even more prudent in extending credit. As it is written in a specialised publication:^{xx}

“Western banks could be over-prudent, but what they say, in fact, is that they will not lend money to companies or persons that have less-than-Western credit standards. There aren’t many of those in Central Europe for the time being”.

Moreover, foreign banks operating in Romania exhibit a strong geographical discrepancy. While banks from Turkey, Greece, Austria, the Netherlands are relatively well represented, banks from countries with a strong tradition in this field (United Kingdom, Switzerland, Italy, Japan) are practically absent; the American and German banks being also rather symbolic. Their absence is not due to any restriction imposed by the monetary authority, but simply to the fact that the Romanian business environment doesn’t present enough opportunities, that would justify, in these banks’ opinion, their presence here on a larger scale. Under these circumstances, it is not surprising that in 1998 the five initially state-owned banks (BCR, BANCOREX, BA, BRD and CEC) continued to detain the largest share, both in the total of non-governmental credit, in total assets, and in total deposits of non-bank clients, as can be seen in the following table:

Share of the 5 state-owned commercial in total banking system

%

Indicator	Dec. 1991	Dec. 1992	Dec. 1993	Dec. 1994	Dec. 1995	Dec. 1996	Dec. 1997	Dec. 1998
- Non-governmental credit	97	94	88	81	76	76	73	68
- Total assets	97	90	85	74	73	72	68	67
- Deposits of non-bank clients	95	88	80	63	71	73	70	69

Source: NBR

The purchase, early 1999, of the controlling stock in the Romanian Bank for Development by Société Generale, as well as the merger through absorption of BANCOREX into BCR did not fundamentally alter the data of the problem, state-owned banks continuing to detain an excessively large share.^{xxi}

4.2. Presence of foreign banks-advantages and disadvantages

As shown in a previous paragraph, the presence of foreign banks, themselves in a minority, did not stimulate competition on the internal money market. On the contrary, foreign banks were among the first to profit from the market’s imperfections, asking exorbitant interest rates for buying state T-bills and limiting themselves to arbitraging, instead of crediting the economy.

Thus, the hypothesis of increased competition as a result of foreign banks' entrance onto the market, was not verified in the case of Romania, at least not until this moment. One of the explanations is that, in their vast majority, those banks didn't engage into retail and, as a result, were reluctant to develop a significant territorial network. Their desire to gain a lot from a few clients can be understood, but does not represent the way by which Western banking standards will get disseminated in Romania.

Also, foreign banks were usually reticent in acquiring large Romanian banks (with the notable exception of BRD), pointing to the incompatibility of their organisational cultures.^{xxii} It could be the case that the real problem lie in the sphere of working legislation, making it very difficult, in Romania, to fire an employee that performs unsatisfactorily. The same recommendation for a liberalisation of working contractual relations is probably welcome in other fields of activity, as well.

Another reason for which large bank privatisation didn't occur in Romania was the state's pretention (an explicit one until 1996) to use the state banks as a vehicle for its economic policy. Subsidised credits extended by BANCOREX to energy importers and by BA to farmers have constituted an essential mix of the policies of pre-1996 governments. Foreign banks, well aware of it, were also reluctant to purchase state banks with a balance sheet burdened by credits extended on non-financial criteria. Their fear was confirmed by the dramatic situation of BANCOREX, which, despite repeated injections of liquidity and transfers of debt onto the state budget, could not be saved as a going concern and was merged with BCR. As regards Banca Agricola, its restructuring started much earlier and resulted into the recovery of around 30% of its non-performing credits. It seems that a large proportion of Banca Agricola's nonperforming credits are related to a single debtor, the pig farm COMTIM, through which liquidation it is hoped to recover at least a part of the debt. In these circumstances, and through transferring to the AVAB (Banking Assets Recovery Agency) of non-performing credits, Banca Agricola has reasonable chances to be privatised by mid-2000.

It is foreseen that, through the budget, the Romanian state will have to pay the equivalent of more than \$ 2 billion (over 6 percent of GDP) only to cover the losses of BANCOREX and Banca Agricola. Although it seems excessive, this figure is nevertheless in line with similar experiences in other transition countries. The following table, taken from an IMF publication,^{xxiii} shows that a large number of countries have been or will be obliged to sacrifice large proportions of their GDP in order to counteract the negative effects of a banking crisis.

Contingent liabilities of the government connected to banking system's restructuring

Country	Minimum percentage	Maximum percentage
Czech Republic	23	35
Slovak republic	12	17
Romania	8	12
Slovenia	5	11
Poland	4	8
Latvia	4	8
Russia	4	8
Hungary	3	8

The problem in Romania's case is whether it's worthwhile having in view to keep a large state-owned bank as a "national-champion" or not. According to a ranking recently (October 1999) published by the Central European Economic Review, according to the level of assets, the Romanian Commercial Bank (BCR) ranked, at end 1998, 24th among transition countries' banks (in the same table, BRD was 43rd, BC Ion Tiriac – 85th, Bank Post – 92nd, Bank Turco-Romana – 121st, Eximbank – 130st).

The advantage for the state in having a large bank in its ownership is to be able to compete with large foreign banks, when the latter will finally decide to establish themselves in Romania. The disadvantage could consist in that being "supervised" by the state, the credit policy of such a bank could evolve in an unsatisfactory manner, needing later another massive intervention from the budget. The answer to this dilemma is not a simple one, even more so since the majority of EU countries are preaching one thing and doing another one. The French authorities' desire to have a national banking "champion", through the merger of banks such as BNP, Paribas and Société Generale. Or the action of the Portuguese authorities is a well-known, who recently prohibited the take-over of the financial group Champelimaud by a foreign bank, Banca Santander Centralo Hispano SA. Connected to this latter decision, the position of the European Commission was of contesting it, announcing Lisbon that it has one month to modify its decision or to face the European Court of Justice. In defence of its position, the Commission argued that an acquisition or a merger can only be interdicted if it can be demonstrated that it affects "legitimate national interests" including defence, public security or prudential management of the financial markets, which in the invoked example were not obviously the case.

For the Romanian authorities, the dilemma is twofold: a) is it worthwhile or not assuming the risk of keeping BCR in the state's property, neglecting the protest of financial international organisations? And b) will such a measure possibly be contested in justice in the process or after Romania's joining the EU?

Concerning the first question, the affirmative answer depends on the very prudence of the bank's management which, being exposed to a non-performing real sector, had so far an outstanding performance. *Caeteris paribus*, as the real sector will get rid of its current plagues, one would expect a diminishing of the risks related to BCR's credit portfolio. Of no lesser importance is the attitude of the state towards this bank, because through selective policies it can get into the same kind of troubles that burdened BANCOREX. For the second question, the answer is much more difficult but, at any rate, it is not an urgent one, since the time horizon in which Romania will be ready to negotiate with the EU this kind of problems is a distant one.

4.3. Freedom of entry and exit onto/from the market

Currently, in Romania there do not exist significant barriers to the entry of a banking company onto the market. The only requirements that they are supposed to fulfil are those related to the observance of the Authorisation Norms and of the Minimum Capital Norm. These were updated practically every year, in accordance to Leu's depreciation (see table) and currently require the banks to have a minimum level of subscribed and paid-in capital of Lei 100 billion, up to end-2000, which will represent around USD 4 billion by that date.

The branches and subsidiaries of foreign banks are not subject to any discrimination, the NBR requesting the supervisory informations from the home country, concerning the soundness of those banks. Although Romanian norms do not request it specifically, the NBR asks, in practice, also

informations concerning the soundness of the group to which the mother-bank belongs, in order to protect potential Romanian clients from any unpleasant surprises.

Evolution of prudential requirements concerning the minimum level of social capital

No.	Regulation	Minimum level of social capital
1.	Norms no. 58/1991 concerning the minimum capital of banking companies 29.10.1991 (Official Gazette 217/1991)	Lei 700 million
2.	Norms no. 7/1992 concerning the minimum capital of banking companies 21.08.1992 (O.G. 201/1992)	Lei 2 billion
3.	Norms no. 8/1993 concerning the minimum capital of banking companies 01.01.1994 (O.G. 310/1993)	Lei 8 billion
4.	Norms no. 5/1995 concerning the minimum capital of banking companies 23.10.1995 (O.G. 128/1995)	Lei 12 billion
5.	Norms no.1/1996 concerning the minimum capital of banking companies 23.01.1996 (O.G. 32/1996)	Lei 25 million
6.	Norms nor.8/1997 concerning the minimum capital of banking companies 20.05.1997 (O.G. 94/1997)	Lei 50 billion
7.	Norms no.4/1998 concerning the minimum capital of banking companies 29.07.1998 (O.G. 280/1998)	Lei 50 billion
8.	Norms no.5/1999 concerning the minimum capital of banking companies 15.04.1999 (O.G. 157/1999)	Lei 100 billion

If, concerning freedom of entry onto the market of commercial banks, Romanian legislation and practice are reasonably permissive, the freedom of entry of so-called ‘popular banks’ is virtually unlimited, as a result of the adoption of populist Law no.109/1996 by a Parliament in its last days which, therefore, considered it its duty to make this ‘gift’. The rapid proliferation of these new entities (by mid-1999 their number was estimated between 900 and 1200) and the fact that, by law, these so-called banks are not subject to any kind of prudential supervision, obliged the NBR to be at the origin of the initiation of the Emergency Ordinance no.114/1999 according to which creation of new such ‘banks’ was frozen, until the clarification of the status of the existing ones.

Currently, the NBR works (upon Government’s request) on a project of modification of Law 109/1996, which will make it possible to supervise these popular banks, this avoiding a new ‘Caritas’-type phenomenon, at the national level.

Concerning the barriers to exit from the market for banking companies, they were, until very recently, extremely high. Until the appearance of the new NBR Law (no. 101/1998) and of the Law of Banking Bankruptcy (no. 83/1998), the cases of withdrawal from the system of insolvent banks were tackled less than unsatisfactorily by the old NBR Statute (no. 39/1991), and by the Law of Judicial Liquidation no. 64/1995. Symptomatically, the word ‘bankruptcy’ doesn’t even appear in a

law adopted in 1995(!), whereas bankruptcy applied in such a delicate field as banking was out of the agenda, because Romanian society in its majority, politicians and even some technical experts didn't agree to the concept.^{xxiv} Thus, one can explain the stalemate of three banking companies which, despite having their licences withdrawn by the NBR, were maintained in life by courts' decisions, which interpreted the law with a total disregard for the protection of clients and creditors.

Bank Dacia Felix, for which the NBR had requested judicial liquidation, was subjected to a procedure of judicial reorganisation through a court decision that validated the restructuring plan, in spite of its contesting by the monetary authority. As a result, Bank Dacia Felix continues to exist and even to engage into inter-bank placements, with the intention to also get involved in T-bills placements (!). Its debt towards the NBR was rescheduled on a long term-basis and is not bearing any interest. Under these circumstances, Bank Dacia Felix looks 'profitable', but its 'profitability' is obtained at the expense of the main creditors (NBR, CEC). The compensation of physical persons-deponents, was done through a special credit line extended therefore by the NBR

A similar situation is to be found at Creditbank, with the proviso that, in its case, physical person clients still have to be compensated, probably from the Deposit Guarantee Fund and, if the amounts of the latter are insufficient, through a special credit line opened by the NBR.

A third example of 'zombie-bank', which is neither alive, nor dead, is represented by Columna Bank, against which there is a file, sued by CEC (its main creditor) and which is in the court for about two years. Without the fear of being mistaken, one can blame the Romanian judicial system for the aberrant character of some decisions taken in connection to the banking system (if one is to look from market economy perspective), as well as for the extremely slow pace at which issues are solved.

A much harsher legislation allowed the NBR not only to withdraw the license of Bank Albina, in the spring of 1999, but also to obtain the starting of the judiciary liquidation procedure, currently under way. Deponents – physical persons were fully compensated. In fact, deponents of other commercial banks in trouble (for instance, Bankcoop) come to ask imperatively the NBR to start the same procedure in order for them to redeem the immobilised sums.

All in all, it can be said that deponents – physical persons were not hurt in a material way by crises that beset one or the other of the commercial banks. Moreover, much improved legislation adopted in 1998 allows the NBR to intervene more authoritatively in punctual treatment of banking insolvency cases.

4.4. Consumer's protection

Banking sector is, by its nature, a very sensible one, where the access of public to data about banks is limited for prudential reasons. Under these circumstances, transparent information of the public, one of the measures for consumer's protection, takes mainly the form of monthly, quarterly and annual reports of the NBR. It is true that, in these reports, the banking sector's presentation is done in an aggregate way, but the cautious reader can find early signals of crises.

Another theoretically possible arrangement is the publication, by the Supervisory Authority (when the latter is separated from the Central Bank) of special reports – the way it is done, for instance, in Hungary. But, even in this case, dates are aggregated and not bank-specific.

A third way to inform the public is the publishing, in the commercial banks' annual reports, of their solvency indicators. Large banks with foreign capital operating in Romania practice this system,

with a good result for their credibility. Romanian banks are partly reluctant to follow this model, but might adopt it if they want to enhance their credibility.

A second means to protect the consumer is represented by early intervention by the supervisory authority (in Romania's case – by the NBR) in sanctioning risky banking practices. In countries such as Italy, all sanctions applied by the Central Bank were made public. Unfortunately, in Romania such sanctions were applied, *de facto*, only when the banks' situation was already a hopeless one, so that such publication would have, in the public's eyes, a rather negative connotation.

Finally, the last and most important way to protect the consumer is the Banking System Deposits Guarantee Fund, an institution created through Ordinance no. 39/1996 and confirmed through Law 88/1997. The peculiarities of this system are presented in detail in the sub-chapter concerning Directive 94/19 of Stage I. Even if the maximum guarantee ceiling is rather modest in comparison to the Western-European benchmark, one can state that there is enough covering, and even a slight overcovering, if taking into account that:

- a) CEC deposits are still covered 100%, irrespective of their size;
- b) Guarantees cover, in fact, more than 90 percent of total deposits of population;
- c) The peculiarity that the guarantee refers to the deposits and not to the deponent allows the latter to abuse the system, by 'splitting' large deposits into smaller ones, which would be fully compensated .

Overall, one can assess that consumer's protection in the Romanian banking system is very asymmetrical, with little emphasis put on information and a lot of emphasis put on compensation.

Chapter I: The Banking Market

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Valentin Lazea

1. Objectives and principles of European banking regulation

The Treaty establishing the European Economic Community, signed in Rome on March, 25th, 1957, put the foundation of the creation between member states of an economic space without frontiers, based on free circulation of persons, goods, services, and capitals and on equal conditions of competition. The realisation of this "Single market" is based on the adoption of some regulations of the Council or of the Commission, which aim at the harmonising of the member states' legislation.

The Agreement upon the European Single Space has enlarged the single market, starting January 1st 1994, for several EFTA countries. In parallel, the member states of the European Community have strengthened the links uniting them, through the adoption of the Treaty regarding the European Union (EU).

The fulfilment of a single banking market, starting January 1st, 1993, implied a minimal harmonisation of member states' banking regulations. To this end, a minimum basis of regulation was adopted, having as goals:

- (5) to ensure free exercising of banking activities in all member countries;
- (6) to ensure equality of competition conditions;
- (7) to avoid arbitrage in the field of banking supervision;
- (8) to ensure solid banking systems.

In order to define this minimum basis of regulation, the following principles were retained:

- f) *total freedom of capital movements within the EU*;
- g) *freedom of establishment*: any institution authorised in a member state has the right to set a branch in any other member state, without requiring the approval of the host country;
- h) *freedom to provide services*: any credit institution authorised in a member state may provide banking services for a client located in another member state without needing to detain a branch in that state;
- i) *mutual recognition of authorisations and of banking practices*: exercising the above mentioned liberties is allowed for all credit institutions which are authorised in their country of origin;
- j) *supervising by the country of origin*: the EU didn't create an European organism of banking supervision but, based on the principle of subsidiarity, left competence in this matter to the member states.

2. Directives of stage I

2.1. First Directive of banking co-ordination

The Council Directive 77/780/EEC concerning the co-ordination of laws, regulations and administrative provisions related to the starting and operating of credit institutions, was adopted on December 12, 1977 and entered into force on December 17, 1979.

The Directive has a limited area of regulation, but it represented the first step in the implementation of the present framework of Community banking regulation, establishing common rules concerning the starting and the operating of credit institutions.

This Directive introduces the principle of home country control and imposes a series of rules regarding the supervision of credit institutions. It applies to credit institutions that are defined as entities attracting reimbursable funds from the public and extending credit on their own account.

The Directive doesn't however apply to Central Banks, to institutions of postal transfers' ant to other categories of institution specifically named in its text.

The Directive sets the obligation for the credit institutions to be authorised before starting functioning. The functioning authorisation may be granted only if the following conditions are fulfilled: (1) the credit institutions dispose of adequate and permanent minimum funds; (2) the activity of the institutions is effectively managed by at least two persons (the "four eyes" principle) that have to have a good reputation and enough experience to fulfil their attributions.

At the same time, the Directive abolishes the criterion of "economic necessity" as a requirement upon which a functioning authorisation may be granted.

According to the Directive, member states may subject the branches of credit institutions that have their headquarters in another member state to the same authorising criteria that are applicable to the credit institutions set up on their territory. Also, according to the Directive, member states have full liberty in establishing the criteria of granting functioning authorisations to branches of extra-Community banks, but they may not offer more favourable terms than the ones offered to the Community credit institution's branches. Moreover, the Directive establishes the basic principles of co-operation between the supervisory authorities of member states, in special with regard to the exchange of information concerning the management and the structure of shareholders of credit institutions. The Directive introduces the obligation of professional secret for the persons hired by competent authorities. The same obligation applies to confidential informations about credit institutions, that are transmitted to competent authorities from other member states.

The Directive was largely implemented in Hungary and Poland and partially in the Czech Republic. In all these countries, the provisions concerning professional secret must be amended to became fully compatible with those of the Directive under discussion. Also, in the Czech Republic, there is a need to revise the conditions established for foreign banks in order to operate on the national market. In the majority of cases, the remaining amendments will be implemented at the moment of these countries' accession.

With regard to Romania, the vast majority of the Directive's provisions were transposed into national legislation. There still remain some differences, such as those linked to the regime applied to foreign banks' branches; the exchange of information's with the supervisory authorities of the Community countries; the maintaining of a permanent minimum level of own funds. Concerning the first issue, it must be mentioned that, according to the Directive, branches established in the same member state by a credit institution having its headquarter in another member state must be treated as a single branch. On the contrary, Romanian banking legislation treats individually each branch established on the national territory by a bank with its headquarters abroad:

As a consequence, in conformity with Romanian authorities' declarations, the provisions concerning foreign bank branches (including the Banking Law) will be amended until the end of 2000. Referring to the second aspect, it is foreseen to amend the legislation and the relevant provisions concerning foreign banks branches supervision within the same time horizon. Finally, there must be brought

corresponding amendments to the banking legislation in order to respect the Community principle of the permanence of minimum own funds, which applies to credit institutions.

2.2. Directive of the Council of April 17, 1989 concerning the own funds of the credit institutions (89/299/CEE)

The Directive concerning the own funds of credit institutions was adopted on April 17, 1989 and entered into force on January 1, 1991, together with the Directive of December 18, 1989 concerning the solvency ratio.

The Directive provides a common definition of credit institutions' "own funds" and the determining criteria of their structure. It represents a key element in creating a single market in the banking field, because the existence of adequate own funds ensures the stability of credit institutions and protects the public's savings. At the same time, through harmonising the standards relating to own funds, one can avoid the distortion of competition in the banking sector due to different national definitions and can create equal competitive conditions for banks at the Community level.

The Community definition of own funds follows to a great extent the regulations of the Bale Agreement of 1988 concerning capital standards. As a result, own funds are divided into core capital and supplementary capital.

Core capital (tier I) consists of elements pertaining to capital of the highest quality, as for instance: social capital, legal reserves and funds for general banking risks. The high quality of these elements consists of the fact that they have an internal nature and can absorb the losses. Supplementary capital (tier II) consist of reserves from revaluation, value corrections, latent reserves, titles with an undetermined value, commitments of the co-operative companies' members, subordinated debt and other financial instruments that fulfil certain conditions expressly specified in the Directive.^{xxv}

The Directive rules that member states may foresee stricter rules for their credit institutions. To this end, member states may not include certain elements in the national definition of own funds or to foresee more severe conditions to include them, to demand more important or more numerous deductions etc. It must be specified that, in conformity with the principle of mutual recognition of supervision, the member state that has foreseen stricter rules may not apply them onto credit institutions authorised in other member states, where only the Directive's provisions are applied. In the context of competition, national credit institutions will be more penalised as their own state's legislation will be more severe in defining own funds.

The main provisions of the Directive have already been implemented in Hungary, the Czech Republic, and Poland. The definition of core capital and of supplementary capital establish by relevant Magyar provisions departs in a number of ways from the Community one. At the same time, the Hungarian Banking Law foresees more numerous deductions than those established by the Directive in the computation of core capital, which leads to stricter requirements than the EU standards. This situation, in the absence of further modifications, is bound to affect the

competitiveness of Hungarian credit institutions in the post-accession period. In Poland, the differences between the Directive and relevant national provisions can be considered insignificant, being subject to complete elimination by year 2004. It is worth mentioning that, in certain respects, the solutions adopted by Polish authorities are more restrictive than the Directive's. Concerning the Czech Republic, experts consider that the provisions relating to own funds of the credit institutions correspond to the Directive's provisions.

The Directive is implemented in the Romanian legislation through Law no. 58/1998 – the Banking Law – and through NBR's Norms no. 7/1999 concerning banks' own funds. Although these regulations are relatively recent, they are not fully harmonised with the Directive's provisions.

The main differences refer to the definition and structure of own funds. In accordance to actual Romanian regulations, both own capital (which correspond to the Community's notion of basic own funds) and supplementary capital contain addition elements that are not to be found in the definition used in the Directive.^{xxvi} *Solving these differences will require amending both accounting legislation and banking legislation.* Also, Romanian provisions regarding subordinated debt are only partially harmonised with the Community ones.^{xxvii} Another difference consists in the fact that Romanian legislation does not contain provisions concerning the recognition of co-operative companies members' commitments as an element of own capital; *this last aspect will be possible to solve in the context of adopting a new framework for the credit co-operatives.* Lastly, the problem of the absence of provisions concerning the consolidated accounts will have to be solved. *To this end, it is necessary for the National Bank of Romania to issue specific norms, immediately after the Ministry of Finance will establish general rules about accounts' consolidation.*

2.3. Directive of the Council of December 18, 1989 concerning the solvency ratio of credit institutions (89/647/EEC)

The Directive concerning the solvency ratio of credit institutions was adopted on December 18, 1989 and entered into force on January 1, 1993.

The Directive has two objectives: 1) to harmonise prudential supervision rules necessary for the completion of internal market; 2) to strengthen the solvency standards of Community credit institutions in order to protect the deponents, the investors and to ensure the stability of the banking system within the EU.

The Directive rules that the solvency ratio is computed as a rate between own funds of credit institutions (the numerator) and assets and off-balance items weighted in accordance to credit risk (the denominator).

Starting January 1, 1993, credit institutions are obliged to permanently maintain the solvency ratio, as previously defined, at a level of 8%. The harmonisation being a minimal one, national authorities may fix a higher level of the solvency ratio; this supplementary constraint will only apply to those institutions under the supervision of the competent authority that has announced them. If the solvency ratio falls below 8% (or below the higher national standard), the competent banking supervision authorities must take measures to re-establish the situation. The solvency ratio must be computed on a consolidated basis, but additional unconsolidated ratios are asked for all credit institutions.

Computing the solvency ratio implies applying some technical rules that are not established in detail in the Directive. Thus, article 6 of the Directive indicates for each bilateral asset the category to which it belongs and the share that must be applied. Wishing to have a simpler method, only four shares were retained: 0%, 20%, 50% and 100%, which are attributed in accordance to the nature of the debtor, of his origin country or of the operation's nature.^{xxviii} Annexes I and II ensure a classification of the off-balance items and establish the treatment that must be applied to those items, concerning the interest rate and the exchange rate risks, while article 6(2) establish as the risk weights for off-balance assets. Annex II was replaced by Directive 96/10 of March 21, 1996, which introduced specific rules concerning contractual compensation.

To a large extent, the provisions concerning the solvency ratio have been transposed into the national legislation in Poland, Hungary, and the Czech Republic. In Romania, most of the provisions are transposed into the legislation, the main differences which will require its amendments being the following:

- the lack of provisions concerning credit institutions that themselves are affiliated to a central institution. This aspect will be solved through modifying Law 109/1996 concerning credit co-operatives;
- the lack of provisions concerning supervision on a consolidated basis;
- the lack of provisions concerning the treatment of the off-balance positions concerning and exchange rates. For these, the NBR has asked the assistance of Banque de France, within a twinning agreement.

2.4. Directive 94/19/CE of the European Parliament and of the Council, of May 30, 1994, concerning the system for deposits guaranteeing

Deposits guaranteeing is, together with prudential regulations and Central Bank's interventions as a lender of last resort, one of the instruments that can be used to reduce or eliminate the negative effects which the bankruptcy of a credit institutions can induce upon the rest of the financial system.

The Directive 94/19/CE of the European Parliament and of the Council, of May 30, 1994, concerning the systems of deposits guaranteeing, has entered into force on July 1, 1995. The adoption of this Directive is justified by the fact that deposit guaranteeing is a central element for a single banking market and an indispensable complement of the supervisory system, by virtue of solidarity which it creates among all institutions of the same financial market in the case of one's bankruptcy. The

Directive has in view ensuring a minimum harmonised level of deposit guaranteeing, irrespective of deposits' localisation within the European Union.

The main features of Directive 94/19/CE are the following:

- each EU country must have one or several schemes of deposit guaranteeing;
- the Directive imposes the principle of mandatory participation in a system of deposits guaranteeing for every credit institution authorised within the EU. The Directive admits an exception from this principle only for credit institutions that belong to a system that protects both the credit institutions and its liquidity and solvency and only if this protection is equivalent to the one ensured by the relevant scheme(s) of that state. In this case, beside other conditions that must be fulfilled, it is necessary for the guaranteeing scheme not to represent a guarantee extended to the credit institutions by a member state or by any the local/regional authorities;
- credit institutions that are not member of a guaranteeing scheme may not attract deposits;
- the deposits' protection rests upon the modified principle of origin country;^{xxix}
- branches established by an extra-Communitarian credit institution must dispose of a guaranteeing ceiling equivalent to the one established in the Directive, otherwise these branches having to adhere to the host country's scheme;
- the minimum level of guarantees was established at EURO 20,000 (EURO 15,000 until December 31, 1999 for the member countries having already a limit smaller than EURO 20,000);
- the guarantee is given per deponent and not per deposit;
- interbank deposits, commitments of the nature of own funds and deposits arising from money laundering operations are not protected by guaranteeing schemes;
- certain deponents or deposits may be exempted or may be granted a lower level of guaranteeing;
- payment of verified liabilities should be done within three months since deposits' indisponibility; prolonging this period is allowed in exceptional circumstances;
- the Directive does not contain harmonisation features regarding the legal status of guaranteeing funds (of public or private nature) or financing mechanisms (capitalising or repartition schemes).

As it can be noticed, the EU Directive contains explicit harmonisation provisions concerning the minimum level of protection; the co-responsibility; the types of deposits which are guaranteed; the scope of the guarantee; the status of Community or extra-Community branches. As a consequence, candidate countries will have, sooner or later, to implement these provisions into their national legislation. Conversely, these countries are free to chose from a relatively wide set of options, concerning the financing mechanism and the administrative structures of the guaranteeing systems.

In the last years, a series of countries from Central and Eastern Europe have set up guaranteeing schemes, in the next chronological order: Hungary (March 1993), the Czech Republic (December 1994), Poland (February 1995), Slovakia (July 1996), Romania (August 1996). All these countries have adopted explicit systems of deposit guaranteeing. Their institutional scope and the types of guaranteed deposits differ from country to country, depending on the structure of the banking system and on the adopted philosophy of prudential regulation. For instance, Poland, the Czech Republic and Hungary guarantee the deposits of certain legal persons, while Romania and Slovakia cover only natural persons.

Regarding the maximum limits of deposits guaranteeing in the above mentioned countries, they are the following: Hungary – 1 million Forints, Poland – 5000 Euros, Czech Republic – 400 000 Korunas, Romania – 46,2 million lei (corresponding to the second semester of 1999, semestrially adjustable with the inflation index CPI), Slovakia – 30 monthly average wages for deposits placed with commercial banks and 60 monthly average wages for deposits placed with savings banks for construction. In all these countries, the guaranteeing ceiling is well below the one imposed by Community legislation, due to the much lower level of revenues as compared to the EU. Because the Community level of protection is too high, Hungary intends to ask for a transition period of five years, while Poland has decided to gradually increase the ceiling, so as to harmonise fully with the Community by January 1, 2003.

In view of EU accession, the Romanian legislative should introduce into national legislation the minimum requirements of the Directive. Hereafter are presented the main modifications needed to ensure compatibility with the European legal framework:

8. Mandatory participation of all credit institutions in a scheme of deposits guaranteeing. In this context, it should be analysed whether credit co-operatives should adhere to the existing scheme or should rather create their own scheme. Also, full harmonisation will require CEC (the Savings Bank) to renounce the state guarantee and to adhere to the scheme of deposit guaranteeing.
9. Abandoning the obligation of EU banks' branches to adhere to the Romanian system of guaranteeing.
10. Extending the guarantee of the Romanian scheme upon the deposits constituted in EU countries by Romanian banks' branches.
11. Extending the guarantee upon certain legal persons. Such a decision will however lead to higher costs for the Fund, while the restructuring process of the Romanian banking system is not over yet. As a result, this extension should be done in a wider frame of time.
12. Establishing a minimum level of protection equivalent to Euro 20000. For the Fund's resource the match its liabilities, it is advisable to have the increase of the guarantee ceiling to this level after Romania's accession into the EU. *It could be necessary to negotiate a transition period of five to ten years (similar to Hungary).*
13. Excluding from guaranteeing the deposits linked to money laundering operations.
14. The guaranteeing to be done per deponent and not (as currently) per deposit. This will reduce the Fund's liabilities.

3. Directives of stage II

3.1. Second Directive of the Council (89/646/EEC) of December 15, 1989 concerning the co-ordination of laws, regulations and administrative provision linked to the starting and operating of credit institutions, amending Directive 77/780/EEC.

The second Directive on banking co-ordination was adopted on December 15, 1989 and entered into force on January 1, 1993.

The Directive represents the main instrument for the creation of a single banking market. It founded the freedom of establishment and providing service by a credit institution within the EU, on the basis of mutual recognition of the authorisation received in another Member State where it has its headquarters. Once a credit institution has been authorised in a member state, it can establish branches or provide services in other member countries, on a transboundary basis, without the need to be authorised by the competent authority of the host country. This freedom, labelled “single European passport”, applies both to the Community banks and to the subsidiaries set in EU countries by extra-Community credit institutions. It does not apply to branches of extra-Community banks, which must obtain a functioning authorisation within each EU country of operation.

The single authorisation allows a credit institutions to perform throughout all of the EU not only “classical” banking activities, but also other financial services presented in the Annex^{xxx} to the Directive, on the condition that the concerned institution has been authorised to perform those activities in its home country. Thus, if a credit institutions provides “universal bank” services within its home country, then it can offer them in any other EU country, even if domestic credit institution are not allowed to provide such services.

From the principle of mutual recognition of authorisations follows logically the principle of prudential supervision of credit institutions by the authority of the member state that gave the authorisation (“authority of origin country”). However, the Directive stipulates that, until further co-ordination, the competent authority of the host country remains responsible for the supervision of a bank branch’s liquidity, in collaboration with the authority of the home country. Moreover, while the home country authority must take the necessary measures to stop the wrongdoings of a credit institution on the territory of another member state, the competent authority of the host country may take, in emergency cases, steps indispensable for protecting clients’ interests or adequate measures to prevent or repress on its territory acts which go against the legal dispositions it has issued for general interest purposes.

The Directive harmonises also the authorising and supervising conditions of the credit institutions’ shareholders, the minimum level of own capital and limits the non-financial participations.

A first authorisation requirement imposed by the Directive is that credit institutions dispose of an initial capital of at least ECU 5 million. Member states are free to apply higher levels of initial capital for their credit institutions. Under certain conditions and for a limited number of credit institutions (e.g., for banking co-operations), the initial minimum capital requirement may be reduced to the amount of ECU 1 million. Before the authorisation’s granting, the credit institution

must inform the competent authority about the identity of its shareholders/associates. The respective authority may refuse granting the authorisation if it is not satisfied with the quality of shareholders/associates that detain a qualified participation.^{xxx1} As to the permanence of own capital of a credit institution, the Directive foresees that this may not fall below the initial minimum capital amount from the moment of authorisation.

The Directive introduces strict requirements as to the control of capital participation in credit institutions. Beside the mandatory condition that competent authorities verify carefully the quality of shareholders which detain a qualified participation before granting an authorisation of functioning, the Directive rules that if a legal or natural person intend to acquire a qualified participation in a credit institution or intend to increase such a participation, they must first notify the competent authority which may raise objections within three months.

If the influence of shareholders/associates that detain qualified participation is detrimental to a strong and healthy management of credit institutions, the Directive establishes adequate measures for remedying this situation, such as suspending the voting rights attached to the shares detained by the said shareholders. Also, when a capital participation is obtained despite the banking supervision authorities' refusal, the Directive foresees the following sanctions: suspending of the corresponding voting rights, nullity of the given votes or the possibility to nullify them.

According to the Directive, a credit institution may not detain qualified participations that exceed 15% of its own capital in another entity, with the exception of participations in other financial institutions or in insurance companies. At the same time, the total sum of these participations may not exceed 60% of a credit institution's own capital.

The Directive's provisions have been partially implemented in Poland, Hungary and the Czech Republic. In general, banking prudential regulations in these countries impose restrictions on foreign credit institutions' free access onto the national market and do not take into account the principle of supervision's mutual recognition.

All these countries, with the exception of the Czech Republic, consider that the Community regulations concerning the single market (the principle of a single license, the principle of origin country control) can only be adopted at the moment of accession. The Czech Republic intends to transpose entirely the regulations into the national legislation before becoming an EU member.

In its turn, Romania has implemented partially the Directive's regulations. The main differences still existing are presented below:

- in order to open a branch in Romania, a foreign bank must obtain a functioning authorisation from the NBR and must have a starting capital. These requirements are not compatible with the relevant Community legislation which stipulates the freedom of establishment and does not require starting capital for branches. *These aspects may be solved through amending the banking legislation at the moment of accession;*
- Romanian regulations do not foresee the principle of permanent maintaining of minimum own capital for credit institutions;

- Romanian regulations concerning the control of capital participation for credit institutions do not establish a deadline within which competent authorities can oppose the intention of a significant acquisition, nor a maximum period for enforcing this in the case of the reduction of a significant participation;
- in the banking legislation there are missing specific regulations concerning banking mergers;
- also, there is a lack of regulations concerning the relations with the Stock Exchange, and those concerning the information exchange between the competent authorities of the state;
- as mentioned for other Directives, there is a lack of regulations concerning credit institutions affiliated to a central body (these will be corrected through the amendment of the Credit Co-operatives Law), as well as of those concerning supervision on a consolidated basis.

Solving these differences will require the amendment of the Banking Law.

3.2. The Directive concerning the supervision and the control of large credit risk (92/121/EEC)

The Council Directive concerning the supervising and the control of large exposures was adopted on December 21, 1992 and entered into force on January 31, 1994.

Monitoring and controlling large exposures represents an intrinsic part of banking supervision, because excessive concentration of credit risks vis-à-vis a client or a group of clients connected between them^{xxxii} may lead to important losses able to affect the solvency of banking institutions.

The Directive establishes the criteria for determining large exposures and fixes limits for them in relation to credit institutions' own capital, which are mandatory at the EU level.

Exposures are defined as credit risks established by the Directive concerning the solvency ratio.^{xxxiii} With regard to the definition of a large exposure, according to Directive 92/121/EEC, it represent a risk incurred by a credit institution vis-à-vis a client or a group of clients connected between them, whose value amounts to or exceeds 10 percent of its own capital. Large exposures have to be reported to supervision authorities and may not exceed 25% of own capital of the credit institution. In the case when credits are extended to persons which are linked to the credit institutions (mother-institution, own subsidiary or subsidiary of the mother-institution), the Directive establishes a stricter limit, of 20%.^{xxxiv} Beside these individual limits, the Directive introduces a ceiling to be applied to the sum of large exposures. To this end, in order to prevent the accumulation of a clustering of big exposures, the Directive forbids a credit institution to incur a total amount of large risks in excess of 800 percent of its own capital. In expressly specified cases, the Directive authorises member states to except from the limits it sets (20%, 25% or 800%) certain risks.^{xxxv} Also, the Directive asks the credit institutions to implement adequate internal procedures for identifying and accounting large exposures and sets transitory periods in order to allow the credit institutions to adapt themselves to the new limits.^{xxxvi}

The Directive's requirements have largely been transposed into national legislation in Hungary and Poland and partially in the Czech Republic. In Hungary, the requirements concerning subsidiaries and mother-companies are more restrictive than the Communitarian ones, in order to compensate for the lack of an efficient framework of consolidated supervision. In Poland, the Communitarian rules concerning large exposures of consolidated groups have not been applied yet.

In Romania, the requirements of the Directive are only partially transposed. If for some minor aspects it is enough to have secondary legislation approved by NBR's board, for other aspects it is necessary to amend the existing legislation. Such problems concern mainly the definition of such terms as "financial holding company", "financial institution", or "activity of mother-company", which may be solved only in the context of defining the supervision on a consolidated basis. At the same time, it is necessary to improve the regime of the consolidated accounts.

3.3. Council Directive (92/30/EEC) concerning the supervision of credit institutions on a consolidated basis

The Directive concerning the supervision of credit institutions on a consolidated basis was adopted on April 6, 1992, and entered into force on January 1, 1993.

Prudential supervision only makes sense when it allows the assessment of the totality of risks assumed, directly or indirectly, by a credit institution. Credit institutions are often part of a larger framework of legal persons, which form a group (at a national or supra-national level): mother-company, subsidiaries, under-subsidiaries. In this case, a credit institution must be subjected to supervision on the basis of consolidated financial statements, in other words by taking into account all risks assumed by the group.

The legal framework for introducing supervision on a consolidated basis at the Community level was created by adopting Directive 83/350/EEC on June 13, 1983. This Directive had, however, a series of deficiencies, the most important being that it foresaw consolidation only 'in downstream' and only if the mother-company was a credit institution. As a result, it was enough to place all the credit institutions of the group under the control of a holding company, to get them out of the supervision on a consolidated basis.

The new Directive (92/30/EEC) extends the obligation of supervising the banking activity on a consolidated basis to the cases when the mother-company of a group is a financial holding company, i.e. a financial institution which has at least one credit institution as a subsidiary. In the case when the mother-company of a group is a mixed activity holding company,^{xxxvii} the Directive imposes to all its subsidiaries the obligation to transmit informations to the prudential supervision authority.

Also, the Directive contains rules concerning the competent authority or authorities who will perform the supervision on a consolidated basis and establishes the consolidated methods that can be applied. An important feature of the Directive is that it allows, based on mutual agreements, to transfer the

primary supervision responsibility towards the member state in which the largest part of activity is being performed. This way, banking supervision will substantially improve.

Consolidated supervision is efficient only if it can be performed at the level of the whole group. To this end, the Directive grants the European Commission the power to negotiate agreements with extra-Community countries in order to extend consolidated supervision and exchange of confidential informations with the countries having branches on EU territory or having themselves branches of a Communitarian mother-company.

The rules of the Directive were not or were only partially implemented in countries belonging to the first wave of accession negotiations with the EU. In Poland, the banking supervision authority is entitled to exchange informations with other internal or external prudential control organisations. Also, the Banking Law requires completing the financial statements on a consolidated basis. Nevertheless, there remain numerous important differences which are planned to be solved before the moment of accession, through issuance of detailed requirements in the field of consolidated supervision. Also, in Hungary, the implementation of a consolidated supervision system for credit institutions is planned before its EU accession.

Currently, the Directive's requirements are not transposed into Romanian legislation. This situation will be solved through NBR's issuing of specific norms concerning supervision on a consolidated basis. Using this technique is, however, conditional upon the Ministry of Finance's issuing of general accounting standards concerning the consolidation of accounts.

3.4. Directive of the Council 86/635/EEC of October 8, 1986 concerning the annual accounts and the consolidated accounts of banks and other financial institutions

Accounting rules play an important role in evaluating the financial health of a credit institution. Also, the nature and the scope of informations that have been published represent a competition element. For these reasons, the Community authorities have decided to harmonise the accounting rules applicable to credit institutions even before the creation of a single banking market. The Directive of December 8, 1986 harmonises the way of balance presenting by the credit institutions through establishing a standard format, where assets and liabilities are registered in descending order of liquidity and through imposing specific requirements for some positions in the balance. Also, the Directive sets two versions for the profit and losses account (one horizontal and one vertical), together with the specific rules for certain of its elements. The harmonisation had in view by the Directive includes methods of evaluating different categories of balance and off-balance items, and also informations that must accompany the annual accounts and the conditions under which they may be published. At the same time, the Directive obliges the credit institutions to use and to publish consolidated accounts when they detain subsidiaries performing banking activities, and it establishes the way of presenting them.

The requirements of the Directive have been partially implemented in Hungary and in the Czech Republic, while Poland reported that they have been fully transposed into national legislation. In the

case of Romania, differences persist concerning the structure of the balance, the structure of off-balance accounts, of the profit and losses account and the methods of evaluation.

In order to harmonise the legislation with the European one, the Ministry of Finance has to issue new accounting norms.

3.5. The Directive of the European Parliament and of the Council 95/26/EC of June 29, 1995, amending Directives 77/780/EEC and 89/646/EEC concerning credit institutions, Directives 73/239/EEC and 89/646/EEC concerning non-life insurance, Directives 79/267/EEC and 92/96/EEC concerning life insurance, Directive 93/22/EEC concerning investment firms and Directive 85/611/EEC concerning entities for collective investment in stock, related to strengthening prudential supervision

The Directive 95/26/EEC was adopted on June 29, 1995 and entered into force on July 18, 1996.

The Directive, also called the post-BCCI Directive, sets measures to strengthen the prudential supervision of financial institutions. Its goal is to offer extra powers to the authorities in order to allow them to prevent the appearance of frauds and irregularities similar to those that led to the fall of Bank for Credit and Commerce International (BCCI). The Directive recognises that the problems experienced in the BCCI case are not only related to the banking sector and that they may appear also in the process of supervising financial groups. Thus, the Directive amends a series of Directives concerning credit institutions, insurance firms and investment companies.

The amendments introduced by the Directive refer to:

5. introducing measures to ensure the transparency of the financial group and to allow supervision authorities to efficiently supervise each financial institution member of the group;
6. introducing the requirement that the headquarters of the financial institution be located in the member state where the authorisation was issued;
7. extending the list of the organisations to which supervision authorities may communicate confidential informations; within these organisation are, *inter alia*, the authorities that supervise the liquidations or the auditors of the respective financial institutions;
8. introducing the requirement that statutory auditors immediately report to the competent authorities the irregularities they have discovered.

The post-BCCI Directive was fully implemented into the relevant Polish legislation. In the Czech Republic, the Directive was transposed to a large extent into national law, remaining to be solved aspects concerning the exchange of informations between supervision authorities and external auditors. In Hungary, only a few harmonised requirements have been so far included into the national legislation.

The Community requests concerning the strengthening of prudential supervision of financial institutions have not yet been implemented in Romania. NBR has to issue specific rules in this field.

3.6. Directive 96/10/EC of the European Parliament and of the Council, of March 21, 1996, amending the Directive 89/647/EEC concerning the recognition, by the competent authorities, of bilateral netting.

In the last years, the international fora of banking supervisors have proposed rules concerning recognition of bilateral netting. Using this technique, two credit institutions, that detain positions in opposite sense, may agree, under very strict conditions, to compensate their reciprocal debts, which will allow them to weight the risks on a net basis a not on a gross basis, when computing the solvency ratio. This situation leads to lower requirements of own capital, with corresponding impact on banking competition.

The Directive, which is in accordance with the works of banking supervision international bodies, modifies Annex II of the Directive concerning the solvency ratio. Its purpose is to allow a larger recognition of bilateral netting, at the Community's level, in order to create equal competitive conditions for both EU credit institutions, and between them and other states'. According to the Directive, national authorities are allowed to recognise not only netting through innovation, but also other types of bilateral netting, on the condition to prove the juridical validity of bilateral netting.

Due to the problems of juridical nature concerning the validity of bilateral netting contracts, none of the countries currently negotiating their accession to the EU has implemented in its national legislation the requirements of the Directive. This situation is valid also for Romania.

3.7. Directive of the Council 93/6/EEC of March 15, 1993 concerning the adequacy of own capital of investment firms and credit institutions

Directive 96/6/EEC was adopted on March 15, 1993 and entered into force on January 1, 1996.

The Directive concerning the adequacy of own capital of investment firms and credit institutions, whose enforcement is connected to Directive 93/22/EEC concerning investment services, has in view that free provision of financial services throughout the Community should be done in safety. It identifies the risk, others than the credit ones, to which are exposed banks and investment firms when performing operations on the capital market^{xxxviii} and allows applying a single rate of own capital to ensure equal competitive conditions between banks and non-bank entities that perform the same type of activity.

According to the Directive, investment firms and banks that operate on the stock exchange must divide their assets into two parts: the trading book^{xxxix} and the non-trading book.^{xl} The capital requirements for the non-trading book are computed in accordance to the Directive 89/647/EEC concerning the solvency ratio. The capital requirement for the trading book are set by the Directive 93/6/EEC based on the building block approach.^{xli} Also, the Directive includes detailed rules concerning the computation of own capital requirements both for the settlement risk, for the counterpart risk, and for the exchange risk. The Directive includes also special rules referring to the treatment of large exposures.

According to the Directive, a credit institution must permanently maintain own capital equal at least to the sum between the capital requirements for the trading book and the capital requirements for its other operations. This own capital must be defined in accordance with the Directive concerning own capital of credit institutions. However, for covering the risk existing in the trading book, the Directive allows an alternative definition which includes a third category of capital ("tier 3"), more elastic and more adapted to the market's fluctuations, constituted from short-term subordinated debt. The alternative definition allows for a substitution of the second capital category with the third one within a ceiling of 250 percent of the first level ("tier 1") of capital. Also, the profits of the current year may be considered as an element of own capital, provided these were not taken into account when computing the first two capital categories.

The Directive extends upon non-banking investment firms the dispositions of the Directive concerning the consolidated supervision of credit institutions. However, for groups that do not include a banking institution, the capital requirements may be computed on an individual basis.

Until now, Directive 93/6/CEE was partially implemented in Poland and Hungary. In the first country, a series of requirements regarding risk measurement are to be found also in the prudential requirements issued by the Central Bank. It is, however, estimated that complete transposition in the national law of this Directive will not take place before end-2000. In the second country there exist relatively recent amendments of the legislation regarding stock, as for instance defining the financial instruments included in the trading book and the requirement to daily value them at a market price. According to disposable information, regulations concerning capital requirements for the trading book have not yet been adopted. In what concerns the Czech Republic, this country has expressed its willingness to implement the Directive's rules during 1999.

The Directive 93/6/EEC was not yet implemented into Romanian legislation. Its main requirements are, however, included in the draft law concerning the stock and the regulated markets which were submitted to the Romanian Parliament.

3.8. The Directive of the Council 89/117/EEC of February 13, 1989 concerning the obligation of credit institutions' and financial institutions' branches which are located in a member-state but have the headquarter in another state, to publish annual accounts

The Directive 89/117/EEC was adopted on February 13, 1989 and entered into force on January 1, 1991.

The Directive 89/117/EEC stipulates that member-states must require the publishing of documents referring to the annual accounts^{xvii} and to the consolidated accounts, from the credit institutions' and financial institutions' branches established on their territory.

These documents must be drafted and audited in the way required by the law of the member-state where the credit institution or financial institution has its headquarters. Branches belonging to the previously mentioned institutions may not be obliged to publish annual accounts referring to their own activity. This last feature is justified by the fact that, once the Directive 86/635/EEC, concerning the consolidated accounts, was adopted, publishing of branches' annual accounts cannot offer to the public, and especially to its creditors, a clear perspective about its financial situation, because a part cannot be judged in isolation from the whole. However, taking into account the actual stage of integration, the Directive allows member states to ask, until further co-ordination, some informations regarding the branch's activity, specified in art. 2(4) of the Directive.

Regarding the branches of credit institutions and of financial institutions, having their headquarters in extra-Community countries, member-states must ask them the same informations, drafted and audited in accordance to the law of that country. Provided these documents are equivalent with those drafted in accordance to Directive 86/635/EEC and provided the condition of reciprocity for similar institutions is fulfilled in that country, the respective branches must not publish annual accounts regarding their own activities.

The requirements of this Directive are not yet transposed into Romanian banking legislation. According to art. 60 of the Banking Law 58/1998, branches of foreign banks must publish an accounting balance, stating both their own activity and that of their subordinated institutions.

3.9. The Directive of the Council 91/308/EEC concerning the prevention of utilising the financial system for money laundering

The Directive 91/308/EEC was adopted on June 10, 1991 and entered into force on January 1, 1993.

In contrast with other international Conventions that limited themselves to define in juridical terms the concept of money laundering and had a recommendation character, the Directive 91/308/EEC introduces the obligation for EU member countries to forbid and to penally incriminate the activity of money laundering. Its scope is not limited to the capital obtained from drug trafficking but extends also upon funds derived from other criminal activities. The Directive applies to credit institutions and to financial institutions. Because money laundering activities can be performed also by entities from outside the financial system (casino, wholesale retails, lawyers, notariuses), the Directive establishes that its rules may be extended by member states to other professional activities or to enterprises that perform activities liable to be used for money laundering.

The definition given by the Directive to money laundering is similar to the one that is found in the preceding Conventions, of Vienna and Strasbourg. Broadly, money laundering activity represents an

intentional act of conversion or transfer of the property obtained from a criminal activity, with the aim to hide its origin, or the assistance provided to any person in order to do this.

According to the Directive's stipulations, the financial institutions have the following duties: to identify their clients; to keep the track record of the clients and of their transactions; to pay a larger attention to transactions that might be related to money laundering; to report suspect transactions; to establish internal control procedures and personnel training programs to prevent money laundering activities.

The Directive concerning money laundering was fully implemented in Slovenia and partially in Hungary, Poland and the Czech Republic. In these last three countries, according to a relatively recent study of the Commission's Banking Consultative Committee, there still exist anonymous accounts. The Hungarian authorities have recently taken measures to abolish this type of accounts.

In Romania, the main provisions of the Directive were transposed into national legislation through Law 21/1999 concerning the prevention and the sanctioning of money laundering. *There remain still a number of differences between the Community and the Romanian laws, which will have to be eliminated in the next period. A first difference concerns the clients' identification requirements.* According to the Directive, clients have to be identified in one of the next situations: (1) when they establish a business relation with the financial institutions; (2) when the transaction exceeds EURO 15,000; and (3) when the sum of the transaction is smaller than the previously mentioned amount, but there exists a suspicion of money laundering. The Romanian Law does not, however, require identification of permanent clients for transactions below the minimum sum. By neglecting a fundamental principle of financial activity: "know your customer", financial institutions may incur direct losses because they have accepted undesirable clients or because their employee's collusion with criminals. Moreover, as a consequence of non-observance of this principle, it will be much harder for the credit institutions to identify suspect transactions. *A second difference refers to the obligation of confidentiality from the part of credit and financial institutions which, according to the Directive, may not inform their clients that informations have been given to competent authorities concerning them and that an investigation is under way.* The Romanian Law doesn't contain any article with a similar content, which will permit criminals to be always one step ahead of authorities, making the files or the money to disappear. *As a result, in order to obtain a full harmonisation with the European requirements concerning money laundering, it is necessary to have a revisal, as soon as possible, of Law 21/1999.*

4. Competition in the banking sector

The way it was set up after the 1989 revolution, the Romanian banking system consists of universal banks offering their clients, in principle, the whole gamut of banking services. Ten years after the start of transition, this feature was preserved in that there don't exist, practically, any specialised banks. For instance, the Investment Bank's successor, the Romanian Bank for Development, deals also in commercial credit extending. Also, a credit institution very narrowly specialised, the Savings Bank (CEC) has, as a result of Law 66/1996, some involvement in the crediting of economy's real sector. In principle, the similar features of the services provided by Romanian commercial banks should have stimulated competition (as they did, to a certain extent).

4.1. Historical evolution of the banking system

At the beginning of the century and between the two world wars, the Romanian banking system developed very much, at least in numerical terms. During that period, Romania could have been considered the financial centre of the Balkans, a position that offered this country a certain rent.

After the Second World War, following the Soviet model, in Romania there functioned four banks with clearly defined attributions (the National Bank of Romania, the Romanian Bank for Foreign Trade, the Bank for Agriculture and Food Industry, the Investment Bank), as well as a credit institution for the population (the Saving Bank). During this period there couldn't have been any competition within the banking system, even more so since the foreign banks' presence was a purely symbolic one, leading to the worsening of professionalism and of the banking services' quality.

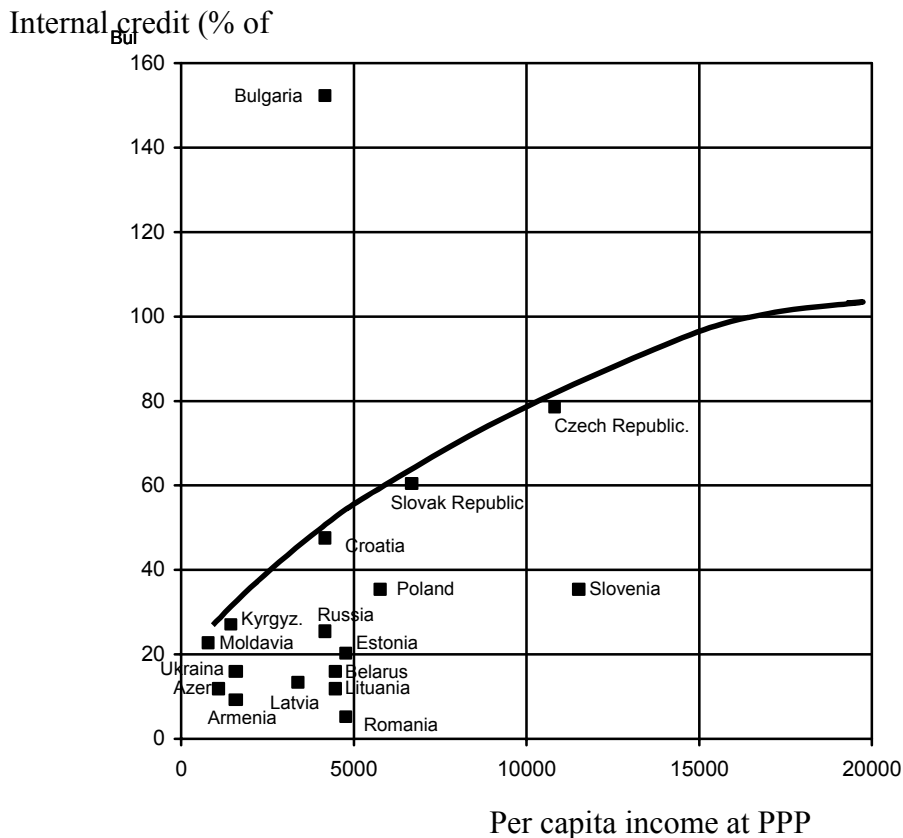
In the last decade, after a rapid increase of the number of banks during the first years, there followed a slowing of the growth and then a stabilisation in the last years (see table). To a large extent, this was the effect of the prudent policy of the NBR, which, recovering its prerogatives of central bank, imposed stringent requirements for the registering of commercial banks. This prudent policy of NBR led to an avoidance of a chain of bankruptcies, which confronted countries such as Bulgaria or Russia, where initially the procedure of authorising new banks has been much more lax.

Historical evolution of the banks' number in Romania

Indicator	1995	1996	1997	1998
Number of Romanian banks	24	31	33	36
Number of foreign banks	7	9	10	9
Total number of banks	31	40	43	45

Source: NBR

The question is whether, given the actual conditions, the Romanian banking market is overcrowded or if there is still room for competition. At a population of 22.5 million, the ratio of two banks for each million of inhabitants is among the lowest in Central and Eastern Europe. The tendency of the last years, of reduction in the financial and banking services share in the creation of GDP, from 5 percent in 1995 to 1.2 percent in 1998, and of reduction of the banking personnel in the total employed population, from 0.8 percent in 1996 to 0.7 percent in 1998 can be attributed rather to economic recession and to solvency problems faced by some banks, than to market's saturation. The best prove for the above is presented by the following graph, indicating the ratio between internal credit (as a percentage of GDP) and per capita level of income (in 1996).^{xliii} It can be observed that in Romania the level of extend credit is extremely low even in comparison to countries from the same income bracket, such as Lithuania, Belarus, Estonia, Russia or Croatia.



To a certain extent, the insufficiency of credit stems from *macroeconomic* factors, such as the low monetisation of Romanian economy, one of the lowest in the area. Indeed, beside CEECs with a “normal” degree of monetisation (Czech Republic, where broad money represented 74% of GDP between 1993-1997, Slovak Republic, where the same indicator was 69% and Bulgaria with 66%), there are also countries with a moderate degree of monetisation (Hungary with 45%, Poland and Slovenia with 37%) and countries with a low or very low degree of monetisation (Latvia with 30%, Croatia with 29%, Estonia with 27%, Macedonia with 25%, **Romania with 24%**, Belarus with 22%, Ukraine with 20%, Russia with 19%).^{xliii}

On the other hand, the insufficiency of credit may reflect *microeconomic* deficiencies, so that commercial banks are reluctant to extend credit to an insufficiently restructured real sector. Paradoxically, foreign banks entering Central and East European markets, far from stimulating competition, are even more prudent in extending credit. As it is written in a specialised publication:^{xliv}

“Western banks could be over-prudent, but what they say, in fact, is that they will not lend money to companies or persons that have less-than-Western credit standards. There aren’t many of those in Central Europe for the time being”.

Moreover, foreign banks operating in Romania exhibit a strong geographical discrepancy. While banks from Turkey, Greece, Austria, the Netherlands are relatively well represented, banks from countries with a strong tradition in this field (United Kingdom, Switzerland, Italy, Japan) are practically absent; the American and German banks being also rather symbolic. Their absence is not due to any restriction imposed by the monetary authority, but simply to the fact that the Romanian business environment doesn’t present enough opportunities, that would justify, in these banks’ opinion, their presence here on a larger scale. Under these circumstances, it is not surprising that in

1998 the five initially state-owned banks (BCR, BANCOREX, BA, BRD and CEC) continued to detain the largest share, both in the total of non-governmental credit, in total assets, and in total deposits of non-bank clients, as can be seen in the following table:

Share of the 5 state-owned commercial in total banking system

%

Indicator	Dec. 1991	Dec. 1992	Dec. 1993	Dec. 1994	Dec. 1995	Dec. 1996	Dec. 1997	Dec. 1998
- Non-governmental credit	97	94	88	81	76	76	73	68
- Total assets	97	90	85	74	73	72	68	67
- Deposits of non-bank clients	95	88	80	63	71	73	70	69

Source: NBR

The purchase, early 1999, of the controlling stock in the Romanian Bank for Development by Société Generale, as well as the merger through absorption of BANCOREX into BCR did not fundamentally alter the data of the problem, state-owned banks continuing to detain an excessively large share.^{xlv}

4.2. Presence of foreign banks-advantages and disadvantages

As shown in a previous paragraph, the presence of foreign banks, themselves in a minority, did not stimulate competition on the internal money market. On the contrary, foreign banks were among the first to profit from the market's imperfections, asking exorbitant interest rates for buying state T-bills and limiting themselves to arbitraging, instead of crediting the economy.

Thus, the hypothesis of increased competition as a result of foreign banks' entrance onto the market, was not verified in the case of Romania, at least not until this moment. One of the explanations is that, in their vast majority, those banks didn't engage into retail and, as a result, were reluctant to develop a significant territorial network. Their desire to gain a lot from a few clients can be understood, but does not represent the way by which Western banking standards will get disseminated in Romania.

Also, foreign banks were usually reticent in acquiring large Romanian banks (with the notable exception of BRD), pointing to the incompatibility of their organisational cultures.^{xlvi} It could be the case that the real problem lie in the sphere of working legislation, making it very difficult, in Romania, to fire an employee that performs unsatisfactorily. The same recommendation for a liberalisation of working contractual relations is probably welcome in other fields of activity, as well.

Another reason for which large bank privatisation didn't occur in Romania was the state's pretention (an explicit one until 1996) to use the state banks as a vehicle for its economic policy. Subsidised credits extended by BANCOREX to energy importers and by BA to farmers have constituted an essential mix of the policies of pre-1996 governments. Foreign banks, well aware of it, were also reluctant to purchase state banks with a balance sheet burdened by credits extended on non-financial criteria. Their fear was confirmed by the dramatic situation of BANCOREX, which, despite repeated injections of liquidity and transfers of debt onto the state budget, could not be saved as a going concern and was merged with BCR. As regards Banca Agricola, its restructuring started much earlier and resulted into the recovery of around 30% of its non-performing credits. It seems that a large proportion of Banca Agricola's nonperforming credits are related to a single debtor, the pig farm COMTIM, through which liquidation it is hoped to recover at least a part of the debt. In these

circumstances, and through transferring to the AVAB (Banking Assets Recovery Agency) of non-performing credits, Banca Agricola has reasonable chances to be privatised by mid-2000.

It is foreseen that, through the budget, the Romanian state will have to pay the equivalent of more than \$ 2 billion (over 6 percent of GDP) only to cover the losses of BANCOREX and Banca Agricola. Although it seems excessive, this figure is nevertheless in line with similar experiences in other transition countries. The following table, taken from an IMF publication,^{xlvii} shows that a large number of countries have been or will be obliged to sacrifice large proportions of their GDP in order to counteract the negative effects of a banking crisis.

Contingent liabilities of the government connected to banking system's restructuring

Country	Minimum percentage	Maximum percentage
Czech Republic	23	35
Slovak republic	12	17
Romania	8	12
Slovenia	5	11
Poland	4	8
Latvia	4	8
Russia	4	8
Hungary	3	8

The problem in Romania's case is whether it's worthwhile having in view to keep a large state-owned bank as a "national-champion" or not. According to a ranking recently (October 1999) published by the Central European Economic Review, according to the level of assets, the Romanian Commercial Bank (BCR) ranked, at end 1998, 24th among transition countries' banks (in the same table, BRD was 43rd, BC Ion Tiriuc – 85th, Bank Post – 92nd, Bank Turco-Romana – 121st, Eximbank – 130st).

The advantage for the state in having a large bank in its ownership is to be able to compete with large foreign banks, when the latter will finally decide to establish themselves in Romania. The disadvantage could consist in that being "supervised" by the state, the credit policy of such a bank could evolve in an unsatisfactory manner, needing later another massive intervention from the budget. The answer to this dilemma is not a simple one, even more so since the majority of EU countries are preaching one thing and doing another one. The French authorities' desire to have a national banking "champion", through the merger of banks such as BNP, Paribas and Société Generale. Or the action of the Portuguese authorities is a well-known, who recently prohibited the take-over of the financial group Champelimaud by a foreign bank, Banca Santander Centralo Hispano SA. Connected to this latter decision, the position of the European Commission was of contesting it, announcing Lisbon that it has one month to modify its decision or to face the European Court of Justice. In defence of its position, the Commission argued that an acquisition or a merger can only be interdicted if it can be demonstrated that it affects "legitimate national interests" including defence, public security or prudential management of the financial markets, which in the invoked example were not obviously the case.

For the Romanian authorities, the dilemma is twofold: a) is it worthwhile or not assuming the risk of keeping BCR in the state's property, neglecting the protest of financial international organisations? And b) will such a measure possibly be contested in justice in the process or after Romania's joining the EU?

Concerning the first question, the affirmative answer depends on the very prudence of the bank's management which, being exposed to a non-performing real sector, had so far an outstanding performance. *Caeteris paribus*, as the real sector will get rid of its current plagues, one would expect a diminishing of the risks related to BCR's credit portfolio. Of no lesser importance is the attitude of the state towards this bank, because through selective policies it can get into the same kind of troubles that burdened BANCOREX. For the second question, the answer is much more difficult but, at any rate, it is not an urgent one, since the time horizon in which Romania will be ready to negotiate with the EU this kind of problems is a distant one.

4.3. Freedom of entry and exit onto/from the market

Currently, in Romania there do not exist significant barriers to the entry of a banking company onto the market. The only requirements that they are supposed to fulfil are those related to the observance of the Authorisation Norms and of the Minimum Capital Norm. These were updated practically every year, in accordance to Leu's depreciation (see table) and currently require the banks to have a minimum level of subscribed and paid-in capital of Lei 100 billion, up to end-2000, which will represent around USD 4 billion by that date.

The branches and subsidiaries of foreign banks are not subject to any discrimination, the NBR requesting the supervisory informations from the home country, concerning the soundness of those banks. Although Romanian norms do not request it specifically, the NBR asks, in practice, also informations concerning the soundness of the group to which the mother-bank belongs, in order to protect potential Romanian clients from any unpleasant surprises.

Evolution of prudential requirements concerning the minimum level of social capital

No.	Regulation	Minimum level of social capital
1.	Norms no. 58/1991 concerning the minimum capital of banking companies 29.10.1991 (Official Gazette 217/1991)	Lei 700 million
2.	Norms no. 7/1992 concerning the minimum capital of banking companies 21.08.1992 (O.G. 201/1992)	Lei 2 billion
3.	Norms no. 8/1993 concerning the minimum capital of banking companies 01.01.1994 (O.G. 310/1993)	Lei 8 billion
4.	Norms no. 5/1995 concerning the minimum capital of banking companies 23.10.1995 (O.G. 128/1995)	Lei 12 billion
5.	Norms no.1/1996 concerning the minimum capital of banking companies 23.01.1996 (O.G. 32/1996)	Lei 25 million
6.	Norms nor.8/1997 concerning the minimum capital of banking companies	Lei 50 billion

	20.05.1997 (O.G. 94/1997)	
7.	Norms no.4/1998 concerning the minimum capital of banking companies 29.07.1998 (O.G. 280/1998)	Lei 50 billion
8.	Norms no.5/1999 concerning the minimum capital of banking companies 15.04.1999 (O.G. 157/1999)	Lei 100 billion

If, concerning freedom of entry onto the market of commercial banks, Romanian legislation and practice are reasonably permissive, the freedom of entry of so-called ‘popular banks’ is virtually unlimited, as a result of the adoption of populist Law no.109/1996 by a Parliament in its last days which, therefore, considered it its duty to make this ‘gift’. The rapid proliferation of these new entities (by mid-1999 their number was estimated between 900 and 1200) and the fact that, by law, these so-called banks are not subject to any kind of prudential supervision, obliged the NBR to be at the origin of the initiation of the Emergency Ordinance no.114/1999 according to which creation of new such ‘banks’ was frozen, until the clarification of the status of the existing ones.

Currently, the NBR works (upon Government’s request) on a project of modification of Law 109/1996, which will make it possible to supervise these popular banks, this avoiding a new ‘Caritas’-type phenomenon, at the national level.

Concerning the barriers to exit from the market for banking companies, they were, until very recently, extremely high. Until the appearance of the new NBR Law (no. 101/1998) and of the Law of Banking Bankruptcy (no. 83/1998), the cases of withdrawal from the system of insolvent banks were tackled less than unsatisfactorily by the old NBR Statute (no. 39/1991), and by the Law of Judicial Liquidation no. 64/1995. Symptomatically, the word ‘bankruptcy’ doesn’t even appear in a law adopted in 1995(!), whereas bankruptcy applied in such a delicate field as banking was out of the agenda, because Romanian society in its majority, politicians and even some technical experts didn’t agree to the concept.^{xlvi} Thus, one can explain the stalemate of three banking companies which, despite having their licences withdrawn by the NBR, were maintained in life by courts’ decisions, which interpreted the law with a total disregard for the protection of clients and creditors.

Bank Dacia Felix, for which the NBR had requested judicial liquidation, was subjected to a procedure of judicial reorganisation through a court decision that validated the restructuring plan, in spite of its contesting by the monetary authority. As a result, Bank Dacia Felix continues to exist and even to engage into inter-bank placements, with the intention to also get involved in T-bills placements (!). Its debt towards the NBR was rescheduled on a long term-basis and is not bearing any interest. Under these circumstances, Bank Dacia Felix looks ‘profitable’, but its ‘profitability’ is obtained at the expense of the main creditors (NBR, CEC). The compensation of physical persons-deponents, was done through a special credit line extended therefore by the NBR

A similar situation is to be found at Creditbank, with the proviso that, in its case, physical person clients still have to be compensated, probably from the Deposit Guarantee Fund and, if the amounts of the latter are insufficient, through a special credit line opened by the NBR.

A third example of ‘zombie-bank’, which is neither alive, nor dead, is represented by Columna Bank, against which there is a file, sued by CEC (its main creditor) and which is in the court for about two years. Without the fear of being mistaken, one can blame the Romanian judicial system for the aberrant character of some decisions taken in connection to the banking system (if one is to look from market economy perspective), as well as for the extremely slow pace at which issues are solved.

A much harsher legislation allowed the NBR not only to withdraw the license of Bank Albina, in the spring of 1999, but also to obtain the starting of the judiciary liquidation procedure, currently under way. Deponents – physical persons were fully compensated. In fact, deponents of other commercial banks in trouble (for instance, Bankcoop) come to ask imperatively the NBR to start the same procedure in order for them to redeem the immobilised sums.

All in all, it can be said that deponents – physical persons were not hurt in a material way by crises that beset one or the other of the commercial banks. Moreover, much improved legislation adopted in 1998 allows the NBR to intervene more authoritatively in punctual treatment of banking insolvency cases.

4.4. Consumer's protection

Banking sector is, by its nature, a very sensible one, where the access of public to data about banks is limited for prudential reasons. Under these circumstances, transparent information of the public, one of the measures for consumer's protection, takes mainly the form of monthly, quarterly and annual reports of the NBR. It is true that, in these reports, the banking sector's presentation is done in an aggregate way, but the cautions reader can find early signals of crises.

Another theoretically possible arrangement is the publication, by the Supervisory Authority (when the latter is separated from the Central Bank) of special reports – the way it is done, for instance, in Hungary. But, even in this case, dates are aggregated and not bank-specific.

A third way to inform the public is the publishing, in the commercial banks' annual reports, of their solvency indicators. Large banks with foreign capital operating in Romania practice this system, with a good result for their credibility. Romanian banks are partly reluctant to follow this model, but might adopt it if they want to enhance their credibility.

A second means to protect the consumer is represented by early intervention by the supervisory authority (in Romania's case – by the NBR) in sanctioning risky banking practices. In countries such as Italy, all sanctions applied by the Central Bank were made public. Unfortunately, in Romania such sanctions were applied, *de facto*, only when the banks' situation was already a hopeless one, so that such publication would have, in the public's eyes, a rather negative connotation.

Finally, the last and most important way to protect the consumer is the Banking System Deposits Guarantee Fund, an institution created through Ordinance no. 39/1996 and confirmed through Law 88/1997. The peculiarities of this system are presented in detail in the sub-chapter concerning Directive 94/19 of Stage I. Even if the maximum guarantee ceiling is rather modest in comparison to the Western-European benchmark, one can state that there is enough covering, and even a slight overcovering, if taking into account that:

- d) CEC deposits are still covered 100%, irrespective of their size;
- e) Guarantees cover, in fact, more than 90 percent of total deposits of population;
- f) The peculiarity that the guarantee refers to the deposits and not to the deponent allows the latter to abuse the system, by 'splitting' large deposits into smaller ones, which would be fully compensated .

Overall, one can assess that consumer's protection in the Romanian banking system is very asymmetrical, with little emphasis put on information and a lot of emphasis put on compensation.

ⁱ The sum of own funds of a credit institution is obtained by adding the above mentioned elements, respecting some limits and deductions as prescribed by the Directive. In order to maintain the low-quality capital at a lower level, supplementary own funds may not exceed 100% of base own funds, whereas some of their constitutive elements may not exceed 50% of base own funds.

ⁱⁱ Beside the elements nominated in the Directive, Romanian regulations also include in own capital definition the following elements: fund of corporal immobilisation; fund for increase of own sources of financing that are defined in the national accounting legislation; and reserves from exchange rate influences and from patrimonial reevaluation that are defined in the Banking Law. Also, in the structure of supplementary capital are included subsidies for investment.

ⁱⁱⁱ The differences consist in that subordinated debt does not include preferential cumulative shares with fixed maturity and in case of reimbursement no approval by the competent authority is needed.

^{iv} According to the first criterion, among the debtors there will be central administrations, central banks, supranational organisations, multilateral development banks, regional or local administrations, credit institutions, non-banking debtors. According to the second criterion (home country of the debtor), countries are divided into two zones: zone A and zone B. Countries of zone A are all EU member states, all OECD states and all countries that have concluded special lending arrangements with the IMF. The classification retained by the Directive combines these two criteria: for instance, a receivable from a regional administration from zone A has not the same ratio (20%) as a receivable from a regional administration from zone B (100%). Regarding the nature of the operation, the Directive requires, for example, a 50% ratio for credit guaranteed by a mortgage on an occupied or rented building and a 100% ratio for a credit extended to the private sector.

^v The principle of origin country requires the systems for deposit guaranteeing set up and officially recognised in a member state to guarantee also the deponents of branches created by that country's credit institutions in other countries. Because implementing this principle in its purest form would have led to the coexistence, in members states, of several systems for deposit guaranteeing, which would have offered different levels of protection and, therefore, would have exposed banks to distortions, the Directive requires two additional rules. The first, called the 'non-export' clause, stipulates that the level of protection offered by home-country scheme to branches of other member states should not be higher than the one offered by the similar schemes in those other countries. The second, called 'top-up provision', allows branches that enjoy a lower protection than in their home countries' scheme, to adhere to the latter, in order to obtain a guarantee offsetting the competitive disadvantage.

^{vi} Activities that benefit from mutual recognition are the following:

1. attraction of deposits or other reimbursable funds;
2. loans (including, especially: consumer loan, mortgage loan, factoring, financing of trade transactions);
3. leasing
4. payment operations;
5. issuing and managing means of payment (credit cards, travel checks);
6. guaranteeing;
7. transactions in own name or in the client's name with/on:
 - a) monetary market instruments;
 - b) forex market;
 - c) futures and options;
 - d) instruments related to forex or to interest rates;
 - e) shares.
8. participations in shares issuing and services connected to them;
9. assisting enterprises in capital structure, in industrial strategy and connected problems, assistance and services in the fields of mergers and buy-backs of enterprises;
10. intermediation on interbank market;
11. portfolio management;
12. shares administration;
13. commercial informations;
14. renting of safety boxes.

^{vii} A qualified participation is defined by the Directive as ‘detaining within an institution, directly or indirectly, of at least 10% of capital or voting rights, or any other possibility to exert an important influence upon the management of that institution’.

^{viii} According to the Directive, connected clients mean:

- either two natural or legal persons, which constitute, unless otherwise proven, an entity as far as risk is concerned, because one of them detains control power upon the other one;
- or two (or more) natural or legal persons, between which there exists no control link in the sense previously defined, but which must be considered as an entity as far as risk is concerned, because the links between them are such that, if any of them is confronted with financial problems, it is probable that the other ones will also be confronted with such problems.

^{ix} Because the objective of Directive 91/121/CEE is to limit the potential loss which a credit institution could incur due to its excessive exposure to a debtor or to a group of connected debtors, such risk ratios are not generally applied. As a result, risks are computed at their nominal value. The Directive leaves, however, member states the possibility to derogate, partially or totally, from this principle, when the risk of obligations non-execution is very limited.

^x Member States may to not solicit the application of the 20% limit, if they apply a particular control upon the mentioned risk. The presumption of a higher risk when the credit is extended to connected persons does not apply when the risk is assumed towards entities that enter the consolidation range of the credit institution, because consolidated supervision allows member states to exonerate, partially or totally, credit institutions from limit applying, including the 800% limit, which is the limit of cumulative large risks.

^{xi} The Directive authorises member states to except from the limits it foresees (20%, 25% or 800%) certain risks which are listed in art.4(7). These risks are mostly (but not totally) the ones that enjoy a 0% share in the computation: receivables from central administrations or Central banks of zone A and from the Community, receivables guaranteed by a deposit in cash placed with the lender, receivables guaranteed by central administrations of zone B but financed in the lender’s currency etc.

^{xii} Credit institutions that detain, at the date of Directive’s publishing risk exposures above and beyond the limits established hitherto, will enjoy a transitory period in order to adapt themselves to the stricter limits. This period will last, at the very latest, until Dec.31, 2001. A supplementary exoneration is foreseen for smaller banks (own funds of less than EURO 7 million), which have the right to a supplementary period of 5 years in order to adjust their exposures to the Community levels (that is to say, until Dec. 31,2006).

The risks with a longer maturity for which credit institutions are obliged to observe the contractual terms may be maintained until maturity.

^{xiii} A joint (mixed) company is defined by the Directive as: ‘a mother-company, other than a financial or credit institution, whose subsidiaries include at least a credit institution’.

^{xiv} The risks connected to market activities identified by the Directive are the following: exchange risk, position risk (which, in its turn, includes interest rate risk and price volatility risk) and settlement/delivering risk.

^{xv} The negotiation portfolio includes positions in financial instruments (shares or debt instruments) which are detained in order to be resold for a short-term profit, due to favourable movements in their price.

^{xvi} According to this method, for the computation of capital requirements corresponding to positions in shares or in debt instruments, a distinction is made between general risk and specific risk. General risk is linked to the general movement of the market, independent from the issuer, while specific risk is linked to the issuer or to the stock itself. In the first case, capital requirements are computed in relation to the net value of the portfolio, while in the second case, in relation to the gross value of the portfolio.

^{xvii} The documents required are the following: annual accounts, consolidated accounts, annual report, consolidated annual report, opinions of persons responsible with external audit of annual and consolidated accounts.

^{xviii} ‘Transition Report 1998. Financial Sector in Transition’, EBRD, April 1999.

^{xix} If the weak monetisation of economy is, clearly, a symptom of poor macroeconomic performances, it is also true that a high monetisation may be accompanied by a poor quality of credit, which in the event leads to a chain of bankruptcies in

the banking system (the Bulgarian case, 1997-1998) or to massive budgetary injections to save it (the Czech and Slovak cases of the same period).

^{xx} ‘Hollow roar: a Survey of Banking’, in Business Central Europe, October 1999.

^{xxi} It is worthwhile to signal the tendency, in all the important banking systems (with the exception of the British one), of increased concentration between 1990 and 1997. Thus, the share of the major five banks in banks’ total detained assets increased from 70 to 90% in Sweden, from 72 to 78% in the Netherlands, from 50 to 55% in France, from 40 to 45% in Spain, from 25 to 28% in Italy etc. Japan and the USA witness also a similar process (‘The Business of Banking’, in The Economist, Oct. 30,1999).

^{xxii} Despite this, even in the case of the RDB anecdotal evidence shows that organisational culture’s transplantation was not performed, as one would expect, by sending Romanian personnel for training to the West, but merely by bringing French managers to key positions, virtually ‘doubling’ the bank’s management.

^{xxiii} Hana Polackova, ‘Contingent Government Liabilities – A Hidden Fiscal Risk’, in Finance Development, March 1999.

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^{xxvi} Beside the elements nominated in the Directive, Romanian regulations also include in own capital definition the following elements: fund of corporal immobilisation; fund for increase of own sources of financing that are defined in the national accounting legislation; and reserves from exchange rate influences and from patrimonial reevaluation that are defined in the Banking Law. Also, in the structure of supplementary capital are included subsidies for investment.

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^{xxix} The principle of origin country requires the systems for deposit guaranteeing set up and officially recognised in a member state to guarantee also the deponents of branches created by that country’s credit institutions in other countries. Because implementing this principle in its purest form would have led to the coexistence, in members states, of several systems for deposit guaranteeing, which would have offered different levels of protection and, therefore, would have exposed banks to distortions, the Directive requires two additional rules. The first, called the ‘non-export’ clause, stipulates that the level of protection offered by home-country scheme to branches of other member states should not be higher than the one offered by the similar schemes in those other countries. The second, called ‘top-up provision’, allows branches that enjoy a lower protection than in their home countries’ scheme, to adhere to the latter, in order to obtain a guarantee offsetting the competitive disadvantage.

^{xxx} Activities that benefit from mutual recognition are the following:

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17. leasing
 18. payment operations;
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 21. transactions in own name or in the client's name with/on:
 - f) monetary market instruments;
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 22. participations in shares issuing and services connected to them;
 23. assisting enterprises in capital structure, in industrial strategy and connected problems, assistance and services in the fields of mergers and buy-backs of enterprises;
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^{xxxviii} Because the objective of Directive 91/121/CEE is to limit the potential loss which a credit institution could incur due to its excessive exposure to a debtor or to a group of connected debtors, such risk ratios are not generally applied. As a result, risks are computed at their nominal value. The Directive leaves, however, member states the possibility to derogate, partially or totally, from this principle, when the risk of obligations non-execution is very limited.

^{xxxix} Member States may to not solicit the application of the 20% limit, if they apply a particular control upon the mentioned risk. The presumption of a higher risk when the credit is extended to connected persons does not apply when the risk is assumed towards entities that enter the consolidation range of the credit institution, because consolidated supervision allows member states to exonerate, partially or totally, credit institutions from limit applying, including the 800% limit, which is the limit of cumulative large risks.

^{xl} The Directive authorises member states to except from the limits it foresees (20%, 25% or 800%) certain risks which are listed in art.4(7). These risks are mostly (but not totally) the ones that enjoy a 0% share in the computation: receivables from central administrations or Central banks of zone A and from the Community, receivables guaranteed by a deposit in cash placed with the lender, receivables guaranteed by central administrations of zone B but financed in the lender's currency etc.

^{xli} Credit institutions that detain, at the date of Directive's publishing risk exposures above and beyond the limits established hitherto, will enjoy a transitory period in order to adapt themselves to the stricter limits. This period will last, at the very latest, until Dec.31, 2001. A supplementary exoneration is foreseen for smaller banks (own funds of less than EURO 7 million), which have the right to a supplementary period of 5 years in order to adjust their exposures to the Community levels (that is to say, until Dec. 31,2006).

The risks with a longer maturity for which credit institutions are obliged to observe the contractual terms may be maintained until maturity.

^{xlii} A joint (mixed) company is defined by the Directive as: 'a mother-company, other than a financial or credit institution, whose subsidiaries include at least a credit institution'.

^{xxxviii} The risks connected to market activities identified by the Directive are the following: exchange risk, position risk (which, in its turn, includes interest rate risk and price volatility risk) and settlement/delivering risk.

^{xxxix} The negotiation portfolio includes positions in financial instruments (shares or debt instruments) which are detained in order to be resold for a short-term profit, due to favourable movements in their price.

^{xl} According to this method, for the computation of capital requirements corresponding to positions in shares or in debt instruments, a distinction is made between general risk and specific risk. General risk is linked to the general movement of the market, independent from the issuer, while specific risk is linked to the issuer or to the stock itself. In the first case, capital requirements are computed in relation to the net value of the portfolio, while in the second case, in relation to the gross value of the portfolio.

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^{xliii} If the weak monetisation of economy is, clearly, a symptom of poor macroeconomic performances, it is also true that a high monetisation may be accompanied by a poor quality of credit, which in the event leads to a chain of bankruptcies in the banking system (the Bulgarian case, 1997-1998) or to massive budgetary injections to save it (the Czech and Slovak cases of the same period).

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^{xlv} It is worthwhile to signal the tendency, in all the important banking systems (with the exception of the British one), of increased concentration between 1990 and 1997. Thus, the share of the major five banks in banks' total detained assets increased from 70 to 90% in Sweden, from 72 to 78% in the Netherlands, from 50 to 55% in France, from 40 to 45% in Spain, from 25 to 28% in Italy etc. Japan and the USA witness also a similar process ('The Business of Banking', in The Economist, Oct. 30, 1999).

^{xlvi} Despite this, even in the case of the RDB anecdotal evidence shows that organisational culture's transplantation was not performed, as one would expect, by sending Romanian personnel for training to the West, but merely by bringing French managers to key positions, virtually 'doubling' the bank's management.

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^{xlviii} A revealing anecdote said that a judge, having to decide upon a bank's liquidation, justified his negative resolution through the parallel with a human being, for which death penalty has been abolished.

Chapter II: Capital Markets

Cristian Donovici

Development of Romanian capital markets was accomplished upon the provisions of Law no. 52/1994 on securities and stock exchanges and Government Ordinance No. 24/1993, approved through the Law no. 83/1994, concerning establishment and functioning of open-end investment funds and investment societies as financial intermediation institutions. These laws sustained establishment and function of the capital market institutions.^{xlvi}

Considering that, for almost fifty years, Romanian had no capital market the process for developing of such a market has been started from nothing, benefiting of no experience in this field, but without any negative “heritage” like the banking and insurance systems registered and which must undergo restructure and privatization.

Development of the Romanian capital market aimed the creation of a market where either Romanian and foreign investors benefit of the regulations and specific capital markets’ institution functioning in advanced countries.

Romanian capital market fulfils an important function in the process of property restructure when the State Ownership Fund has successfully used the RASDAQ market and Bucharest Stock Exchange to sale shares from its portfolio.

Romania tried out to build the capital market applying the experience and practice from advanced countries, benefiting of a strong support coming from the part of organizations and Occidental States, as follows:

- The United States of America, through the intermediary of the United States Agency for International Development (USAID) provided an important technical assistance in emerging the RASDAQ market – market the pattern of which is NASDAQ market -, it provided, also, assistance for the National Union of Collective Investment Schemes and Romanian National Securities Commission;
- Canada, assistance for the Bucharest Stock Exchange and Romanian National Securities Commission;
- The United Kingdom, assistance for Bucharest Stock Exchange and Romanian National Securities Commission;
- The European Union, assistance through the agency of Phare program for Romanian National Securities Commission used for drafting the Law on securities and regulated markets and Law concerning undertakings for collectives investments in transferable securities in line with the provisions of European directives. These drafts were submitted to the Romanian Parliament in September 1998 in order to be scrutinized and approved.

Considering the European accession process for Romania, and the need for legal harmonization, the bills of the Law on securities and regulated markets and Law coordinating undertakings for collective investments in transferable securities were drafted, benefiting of the Phare assistance provided by the European Union, and submitted to the Romanian Parliament in the fall of 1998. Drafting the bills in close relation with the European directives were taken in national legal framework the European principles either regulated aspects which are not finding in existing

regulations like insider dealing, compensation schemes essential to cover investors' losses resulting from securities companies' misconduct, free movement of services principle. The motivation residing in provisions of these bills is represented by the increased transparency and investors' confidence in market operations^{xlviii}.

On the list of legislative priorities the Government has 19 bills which harmonize to the European Directives important sectors of activity in Romania, capital markets' laws being one of these. Although, according with the time periods mentioned in the National Program for Accession of Romania, adoption of these laws is scheduled by the end of the year, the Romanian Parliament has not scrutinized them by now.

Regarding the capital markets situation within the candidate countries with transition economy, the following aspects can be revealed:

- The capital markets represent a brand new segment of financial sector, therefore, in contrast with banking and insurance segments, is not burden by the inheritance coming from the times preceding transition period;
- The capital markets registered an important development along the transition period:
 - the activity of stock exchanges has grown rapidly from the point of view of market capitalization and trading volume,
 - capital markets regulations has been done from the very beginning in relation with the European Union legislation; in some of the more advanced countries the listing requirements are similar with the one required at the European level, regulations on insider dealing exist, activities addressing information on major holdings are, also, regulated and legislation concerning taking over activities is alike;
- In spite of sustainable growth, the capital markets are in incipient stage, which is confirmed by the (1) presence of institutional investors (insurance companies, pension funds, mutual funds), (2) market size (they remain, however, small from the point of view of capitalization, range of instruments);
- Market development has been accomplished, mainly, in relation with privatization programs, these becoming an instrument for ownership restructure than an instrument for companies' financing through the intermediary of primary market;
- A growing demand for listed shares coming from the foreign investors;
- Capital markets' characteristic is a high degree of fragmentation, increased volatility of prices and low transparency of trading (therefore disclosure activity concerning listed companies must be improved);
- Important weakness relative to regulation and enforcement, reflecting a market where interventions and political interests prevail;
- Weakness in market supervision, limited independence and weak supervision capacity (lack of the human resources and experience) of the institutions responsible for market surveillance.

Main objectives that must be attained by the countries in transition which candidate to the European Union in order to develop their capital markets are:

- Develop and maintain a stable macro-economic environment accompanied by fiscal and monetary politics, and a currency regime capable to encourage capital markets activity in order to fulfill their role in financing the economy;
- Improvement the capital markets infrastructure through
 - improvement of accounting, reporting and disclosure norms,
 - simplification of listing requirements,

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- clear procedure for clearing and settlement activities,
 - secure information technology, capable to process important volume of information at low costs;
 - Strict enforcement of legislation;
 - Strengthen the supervision capacity of the competent authorities:
 - strengthen institutional capacity from the point of view of personnel number and experience,
 - enlarge the co-operation with supervision authorities of other segments from financial sector;
 - Harmonization of legal framework to the European Directives in the field of capital markets.

HARMONIZATION OF THE ROMANIAN LEGAL FRAMEWORK WITH THE EUROPEAN DIRECTIVES IN THE FIELD OF CAPITAL MARKETS

The objective of European directives in the field of capital markets, similar with the other two segments of financial sector – the banking and insurance one – resides in development of the integrated European capital markets.

In this regard, three are the fundamental principals for development of the capital market, as follows:

- harmonization of licensing requirements and prudential standards,
- home country control,
- mutual recognition of surveillance standards.

European legislation in the field of capital markets has been adopted starting with 1997, consisting in:

- legislation concerning transferable securities, and
- legislation concerning undertakings for collective investments in transferable securities.

Following we shall present the conditions concerning absorption of the European directives within the two drafts forward to the Romanian Parliament for scrutiny and adoption in the fall of 1998. Considering that negotiation for accession will be based on the harmonized laws not on drafts, and knowing that drafts of Law on securities and regulated markets and Law concerning undertakings for collectives investments in transferable securities submitted to the Romanian Parliament were not scrutinized and approved yet, the *acquis communautaire* in the field of capital markets cannot consider as absorbed. To accomplish this objective the two drafts must be scrutinized and approved.

In order to enforce the directives the European Commission emphasizes the necessity of *the national competent authority*.

The appropriate enforcement of laws and regulations in the field of capital markets, especially for countries with transition economy, like the candidate countries, where negative phenomenon – pressures determined by political and economical interests, market abuses of the intermediaries etc. – become manifest stronger comparative to advanced economies with culture in the field of capital markets and which are likely to affect the investors' confidence impose the existence of an autonomous body responsible for regulation, surveillance and control of the capital markets less exposed to external influences.

In Romania this body is represented by the Romanian National Securities Commission, which is an autonomous institution accountable to the Romanian Parliament. In Hungary and Poland this institution are independent also, as long as in Czech Republic this institution was under the authority of the Ministry of Finance until the end of 1998.

1. Stage I Directives

1.1. Council Directive 89/298 of 17 April 1989 coordinating the requirements of the drawing-up, scrutiny and distribution of the prospectus to be published when transferable securities are offered to the public

THE SECURITIES OFFERED TO THE PUBLIC FOR THE VERY FIRST IN A MEMBER STATE, WHICH ARE NOT LISTED TO A STOCK EXCHANGE WITHIN THAT MEMBER STATE ARE SUBJECT OF DIRECTIVE 89/298/EEC COORDINATING THE REQUIREMENTS OF THE DRAWING-UP, SCRUTINY AND DISTRIBUTION OF THE PROSPECTUS TO BE PUBLISHED WHEN TRANSFERABLE SECURITIES ARE OFFERED TO THE PUBLIC^{xlvi}.

THE ADOPTION OF DIRECTIVE WAS BASED ON THE FOLLOWING MOTIVATIONS:

- RISKS INVOLVED BY THE INVESTMENT IN TRANSFERABLE SECURITIES, LIKE ANY OTHER FORMS OF INVESTMENT, IMPOSE, IN ORDER TO PROVIDE THE INVESTORS' PROTECTION, THE POSSIBILITY FOR THESE TO MAKE A CORRECT ASSESSMENT OF SUCH RISKS SO AS TO BE ABLE TO TAKE INVESTMENT DECISION IN FULL KNOWLEDGE OF THE FACTS.
- TO PROVIDE INVESTORS PROTECTION ALL APPROPRIATE INFORMATION MUST BE DISCLOSED IN REGARD WITH TRANSFERABLE SECURITIES AND ISSUERS THIS ACTIVITY REPRESENTING IN THE SAME TIME A MODALITY TO INCREASE THE CONFIDENCE N TRANSFERABLE SECURITIES, CONTRIBUTING TO SMOOTH FUNCTIONING AND DEVELOPMENT OF THE CAPITAL MARKETS.
 - PROMOTION OF THE INTER-PENETRATION BETWEEN THE EUROPEAN NATIONAL CAPITAL MARKETS AND FORMATION OF A GENUINE EUROPEAN CAPITAL MARKET IMPOSED THE ADOPTION OF A COORDINATED POLITICS TO THE LEVEL OF THE EUROPEAN UNION RELATIVE TO INVESTORS' PROTECTION AND INFORMATION TO BE DISCLOSED REGARDING TRANSFERABLE SECURITIES OFFERED TO THE PUBLIC.^{xlvi}

FOR THE PUBLIC OFFERS DESTINED TO BE ADMITTED TO OFFICIAL STOCK EXCHANGE LISTING, THE DEGREE OF CO-ORDINATION BETWEEN THE MEMBER STATES ALLOWS THAT A PROSPECTUS FOR PUBLIC OFFER APPROVED BY THE COMPETENT AUTHORITY OF A MEMBER STATE TO USE THE SAME PROSPECTUS IN CARRYING OUT A PUBLIC OFFER FOR THE SAME TRANSFERABLE SECURITIES WITHIN A THIRD MEMBER STATE UPON THE MUTUAL RECOGNITION.

THE MUTUAL RECOGNITION MUST BE APPLIED IN THE CASE OF PROSPECTUS FOR PUBLIC OFFER WHICH COMPLIES WITH DIRECTIVE 80/390/EEC COORDINATING THE REQUIREMENTS FOR THE DRAWING UP, SCRUTINY AND DISTRIBUTION OF THE LISTING PARTICULARS TO BE PUBLISHED FOR THE ADMISSION OF SECURITIES TO OFFICIAL STOCK EXCHANGE LISTING, WHICH WAS APPROVED BY THE COMPETENT AUTHORITIES, EVEN IN THE ABSENCE OF AN OFFICIAL APPLICATION FOR ADMITTANCE TO OFFICIAL STOCK EXCHANGE LISTING.

DIRECTIVE 89/298/EEC AIMS. THAT ON THE GROUND OF THE AGREEMENTS SIGNED BETWEEN COMMUNITY AND THIRD COUNTRIES, TO PROMOTE THE MUTUAL RECOGNITION OF THE PROSPECTUS FOR PUBLIC OFFERS FOR TRANSFERABLE SECURITIES.

THE DIRECTIVE PROVIDES THE OBLIGATION FOR DRAWING UP AND DISTRIBUTION TO THE PUBLIC BY THE SECURITIES OFFERER OF PROSPECTUS IN CASE OF A PUBLIC OFFER FOR TRANSFERABLE SECURITIES, NO MATTER THOSE SECURITIES WILL BE OR NOT LISTED.

THIS PROSPECT FOR PUBLIC OFFER IS SUBJECT OF APPROVAL FROM THE PART OF
THE COMPETENT AUTHORITY.^{xlviii}

THE DIRECTIVE INCLUDES PROVISIONS ADDRESSING CO-OPERATION BETWEEN
THE MEMBER STATES, MUTUAL RECOGNITION AND NEGOTIATION WITH NON-
MEMBER STATES.

THE CO-OPERATION BETWEEN THE MEMBER STATES TAKES PLACE UPON
DESIGNATION BY THESE OF THE COMPETENT AUTHORITIES, AUTHORITIES, WHICH
ARE EMPOWERED WITH APPROPRIATE COMPETENCE.

THE MEMBER STATES SHALL INFORM THE COMMISSION IN CONCERN ON THE
APPOINTMENT OF THE NATIONAL COMPETENT AUTHORITIES, AND THIS SHALL
INFORM ON ITS TURN THE OTHER MEMBER STATES.

THE COMMUNITY MAY, UPON THE AGREEMENTS SIGNED WITH ONE OR MANY
OTHER NON-MEMBER STATES TO RECOGNIZE, ON THE BASE OF RECIPROCITY, THE
PROSPECTUS FOR PUBLIC OFFER DRAWN UP AND APPROVED ACCORDINGLY THE
NON-MEMBER STATE'S OR STATES' REGULATIONS, IN COMPLIANCE WITH
DIRECTIVE'S REQUIREMENTS, PROVIDING THAT THE RESPECTIVE REGULATIONS
CONFERS AN EQUIVALENT LEVEL OF PROTECTION LIKE DIRECTIVE 89/298/EEC FOR
INVESTORS, EVEN THESE REGULATIONS DIFFER FROM THE DIRECTIVE.

WITH REGARDS TO ROMANIA, LAW NO. 52/1994 ON SECURITIES AND STOCK
EXCHANGES REGULATES THE PUBLIC OFFER OR TRANSFERABLE SECURITIES,
WHICH ON RNSC HAS ISSUED THE REGULATION NO. 6/1995 CONCERNING THE
PUBLIC OFFER FOR TRANSFERABLE SECURITIES.

THE DRAFT OF THE LAW ON SECURITIES AND REGULATED MARKETS SUBMITTED TO
THE ROMANIAN PARLIAMENT IN THE FALL OF 1998 FOR SCRUTINIZE AND
ADOPTION EMBODIES A CHAPTER DEDICATED TO THE PUBLIC OFFER FOR
TRANSFERABLE SECURITIES.

CHAPTER III OF THE DRAFT, TITLED "PUBLIC OFFER FOR TRANSFERABLE
SECURITIES," INCLUDES THE MINIMAL PROVISIONS ADDRESSING THE PROCESS OF
PUBLIC OFFERS PROVIDED BY DIRECTIVE 89/298/EEC.

THE DRAFT APPROXIMATES THE MINIMUM NUMBER OF PERSONS WHICH MUST
RECEIVE THE PUBLIC OFFER, THE CONTENTS OF THE PROSPECTUS, APPLICATIONS
FOR LICENSING THE PUBLIC OFFER, MINIMUM PUBLICITY FOR PROSPECTUS, REGIME
OF THE PROSPECTUS RELATIVE TO THE ALTERATIONS IN THE PUBLIC OFFER.
REGARDING THE RANGE OF PUBLIC OFFERS EXCEPTED FROM THE PROSPECTUS
REQUIREMENTS, THE MINIMUM INFORMATION FOR LICENSING AND FOR
EXEMPTION AND THE PRESENTATION FOR VARIOUS CLASS OF OFFERS, ALONG
WITH THE PROCEDURES FOR LICENSING AND EXEMPTION SHALL BE SUBJECT OF
RNSC REGULATION IN CLOSE CONSIDERATION WITH THE PROVISIONS OF
DIRECTIVE 89/298/EEC.^{xlviii} IN ORDER TO DRAFT THE REGULATIONS ON PUBLIC
OFFER THE COMPETENT DEPARTMENTS OF RNSC WERE DIRECTED TO A CLOSE
CONSIDERATION OF EUROPEAN DIRECTIVES.

1.2. Commission Directive 79/279/EEC of 5 March 1979 coordinating the conditions for the admission of securities to official stock exchange listing^{xlviii}

THE PURPOSE OF THIS DIRECTIVE IS TO CREATE UNIFORM CONDITIONS WITH
REGARD THE ADMITTANCE OF SECURITIES TO OFFICIAL STOCK EXCHANGE
LISTING, IN ORDER TO PROVIDE AN EQUIVALENT DEGREE OF PROTECTION FOR

INVESTORS IN CONCERN WITH THE TRANSFERABLE SECURITIES ADMITTED TO OFFICIAL STOCK EXCHANGE LISTING OPERATING WITHIN THE MEMBER STATES. IN ADDITION, THE DIRECTIVE, UPON CREATION OF UNIFORM NORMS, FACILITATES THE ADMITTANCE OF TRANSFERABLE SECURITIES TO OFFICIAL STOCK EXCHANGE LISTING TO ANY STOCK EXCHANGE OPERATING WITHIN THE MEMBER STATES. MOREOVER A CLOSER INTER-PENETRATION BETWEEN THE NATIONAL CAPITAL MARKETS IS ACCOMPLISHED WHAT WILL DETERMINE THE ESTABLISHMENT OF THE SINGLE CAPITAL MARKET.

THE PROVISIONS OF DIRECTIVE ARE LIKELY BE ENFORCED, NO MATTER OF THE LEGAL FORM OF THE ISSUER, ALSO THE TRANSFERABLE SECURITIES ISSUED BY THE NON-MEMBER STATES OR THEIR LOCAL OR REGIONAL AUTHORITIES OR TO THE ONE ISSUED BY THE INTERNATIONAL PUBLIC ORGANISMS^{xlviii}.

IN REACH OF THE SECTION II, TITLED “COMPETENT AUTHORITIES FOR ADMITTANCE OF TRANSFERABLE SECURITIES TO OFFICIAL STOCK EXCHANGE LISTING,” ART. 9 THE MEMBER STATES OBLIGATION TO EMPOWER THE COMPETENT AUTHORITIES IS STIPULATED. IN REACH OF THIS SECTION IS ALSO STIPULATED THE RIGHT OF THE COMPETENT AUTHORITY TO TURN DOWN AN APPLICATION FOR OFFICIAL LISTING, WHEN, IN ITS OPINION, IT IS CONSIDERED THAT THE ISSUER SITUATION IS LIKELY TO AFFECT THE INVESTORS INTERESTS.

FOR A TRANSFERABLE SECURITIES THAT ALREADY HAVE BEEN LISTED IN A MEMBER STATE WHERE THE ISSUER FAILED TO FULFIL ITS OBLIGATIONS CONSEQUENT TO OFFICIAL LISTING, THE COMPETENT AUTHORITY OF THAT STATE WHERE ISSUER APPLIES FOR ADMITTANCE TO OFFICIAL LISTING MAY TURN DOWN THE LISTING APPLICATION.

ISSUERS THE SECURITIES OF WHICH WERE ADMITTED TO OFFICIAL STOCK EXCHANGE LISTING MUST DISCLOSE TO THE COMPETENT AUTHORITIES THE REQUESTED INFORMATION IN ORDER TO PROVIDE THE INVESTORS PROTECTION AND SMOOTH FUNCTIONING OF THE MARKET. THE COMPETENT AUTHORITY MAY SOLICIT THE ISSUER TO PUBLISH THE REQUESTED INFORMATION FOR THE INVESTORS’ PROTECTION AND SMOOTH FUNCTIONING OF THE MARKET. WHEN THE ISSUER FAILS TO PUBLISH THE INFORMATION THE COMPETENT AUTHORITY MAY PUBLISH THE INFORMATION ITSELF, AFTER THE ISSUER HEARING.

CONSIDERING THE SAME REASONS – INVESTOR’S PROTECTION AND SMOOTH FUNCTIONING OF THE MARKET – THE COMPETENT AUTHORITY MAY DECIDE FOR TRANSFERABLE SECURITIES ALREADY LISTED THE SUSPENSION FROM THE TRADING ACTIVITY.

ACCORDING WITH DIRECTIVE’S PROVISIONS, THE INFORMATION TO BE DISCLOSED BY THE ISSUER MUST BE PUBLISHED IN ONE OR MANY COMMUNITY WIDE NEWSPAPERS AND SIMULTANEOUSLY DISCLOSE TO THE COMPETENT AUTHORITY. THE COMPETENT AUTHORITIES OF THE MEMBER STATES SHALL CO-OPERATE AND SHALL EXCHANGE INFORMATION WHENEVER NECESSARY ON PURPOSE TO FULFIL THEIR ASSIGNMENTS LAID DOWN WITHIN DIRECTIVE AND FOR EXPEDITIOUS SETTLEMENT OF THE LISTING APPLICATIONS.

ON THE ROMANIAN CAPITAL MARKET THE LISTING REQUIREMENTS ARE REGULATED UPON THE LAW NO. 52/1994 ON SECURITIES AND REGULATED MARKETS AND THE BUCHAREST STOCK EXCHANGE REGULATIONS APPROVED BY RNSC.

IN HUNGARY, CZECH REPUBLIC AND POLAND THERE ARE IN FORCE SIMILARLY REGULATIONS WITH THE EUROPEAN DIRECTIVES RELATIVE TO THE LISTING REQUIREMENTS.

THE CHAPTER V, SECTION 3RD, TITLED “OFFICIAL LISTING FOR TRANSFERABLE SECURITIES”, IN DRAFT OF THE LAW ON SECURITIES AND REGULATED MARKETS PROVIDES THAT TRANSFERABLE SECURITIES ADMITTED FOR TRADING ARE TRANSFERABLE SECURITIES ADMITTED FOR OFFICIAL LISTING ON THE BUCHAREST STOCK EXCHANGE OR RASDAQ MARKET ONLY, EXCEPTING THE TRADING DISPOSE UPON RNSC REGULATION OR COURT DECISION.

THE CHAPTER CALLED “OFFICIAL LISTING FOR TRANSFERABLE SECURITIES” FROM THE DRAFT WAS ELABORATED IN CONSIDERATION WITH THE PROVISIONS OF DIRECTIVE 79/279/EEC. THE REQUIREMENTS FOR ADMISSION OF TRANSFERABLE SECURITIES TO OFFICIAL STOCK EXCHANGE LISTING AND THE INFORMATION TO BE DISCLOSED BY THE ISSUERS OF SUCH SECURITIES, COVERED BY THE ANNEXES OF THE DIRECTIVE 79/279/EEC, WILL BE ESTABLISHED UPON REGULATIONS ISSUED BY RNSC. INFORMATION DISCLOSED WITHIN ANY PROSPECTS FOR ADMITTANCE TO OFFICIAL LISTING SHALL BE PROVIDED TO THE PUBLIC AND PUBLISHED IN A NATIONWIDE NEWSPAPER AT LEAST, ACCORDING WITH THE REGULATIONS OF RNSC.

1.3. Council Directive 88/627/EEC of 12 December on the information to be published when a major holding in a listed company is acquired or disposed of

THE ADOPTION OF DIRECTIVE WAS BASED ON THE FOLLOWING REASONS:

- INVESTORS PROTECTION,
- ACHIEVEMENT OF A HIGHER INTER-PENETRATION BETWEEN THE CAPITAL MARKETS OF THE MEMBER STATES TOWARDS CREATION OF THE SINGLE EUROPEAN CAPITAL MARKET,
- THE NEEDS FOR DISCLOSURE TO THE INVESTORS IN REGARD WITH THE MAJOR HOLDINGS AND THE CHANGES REGARDING THE MAJOR HOLDINGS FOR THE COMPANIES OPERATING WITHIN THE EUROPEAN UNION AND LISTED ON A STOCK EXCHANGE FUNCTIONING IN REACH OF THE EUROPEAN UNION,
 - THE FACT THAT, THE COMPANIES CAN INFORM THE PUBLIC ON CHANGES REGARDING THE MAJOR HOLDINGS ONLY IN CASE WHEN THE COMPANIES WERE ACKNOWLEDGED BY THE RESPECTIVE HOLDERS,
 - THE FACT THAT THE GREAT PART OF THE MEMBER STATES WERE NOT PROVIDING SUCH REQUIREMENTS, AND IN CASE OF EXISTENCE OF SUCH REQUIREMENTS THE DIFFERENCES WERE APPRECIABLE FROM STATE TO STATE.
- ARE SUBJECT OF THE DIRECTIVE ANY INDIVIDUAL OR LEGAL ENTITY SET UP ACCORDING WITH THE PUBLIC OR PRIVATE LAW WHICH ARE ACQUIRE OR DISPOSE OF DIRECTLY OR THROUGH THE AGENCY OF BROKERS HOLDINGS IN THE LISTED COMPANIES OFFICIALLY QUOTED ON A STOCK EXCHANGE AND WHICH ARE REACHING, EXCEEDING OR FALLING UNDER 10%, 20%, 1/3, 50% OR 2/3 FROM THE VOTING RIGHTS. THESE ARE OBLIGED THAT WITHIN SEVEN CALENDAR DAYS TO INFORM THE COMPANY AND THE COMPETENT AUTHORITY IN CONCERN WITH THE VOTING RIGHTS’ PROPORTION WHICH THEY ARE HOLDING.^{xlvi}

THE MEMBER STATES MAY DECIDE THAT LISTED COMPANIES TO INFORM ON THE PROPORTION OF THE CAPITAL HELD BY AN INDIVIDUAL OR A LEGAL ENTITY. THE COMPETENT AUTHORITY MAY EXCEPT FROM THE OBLIGATION FOR DISCLOSURE IN

REGARD WITH THE ACQUISITION OR SELLING OF A MAJOR HOLDING IN CASE OF A SECURITIES COMPANY ACTING IN POSITION OF DEALER ON THE CAPITAL MARKET, IF THE SECURITIES COMPANY ACQUIRING OR DISPOSING OF ON PURPOSE OF PRACTICING THE DEALER ACTIVITY, AND THE RESPECTIVE HOLDINGS ARE NOT USED TO INTERFERE IN THE ISSUERS MANAGEMENT. IN CASE OF ROMANIA, ACCORDING WITH THE REGULATION CONCERNING SECURITIES INTERMEDIATION ISSUED BY RNSC, THE DEALER IS A SECURITIES INTERMEDIARY, ESTABLISHED AS A ROMANIAN LEGAL ENTITY LICENSED BY RNSC TO PRACTICE SECURITIES INTERMEDIATION ON PROFESSIONAL BASIS, AS AN ACT OF COMMERCE, ON ITS OWN ACCOUNT.

A LISTED COMPANY WHICH IS ACKNOWLEDGED IN WRITTEN IN CONCERN WITH A MAJOR HOLDING IN ITS SHARE CAPITAL IS OBLIGED TO MAKE PUBLIC, WITHIN ALL THE MEMBER STATES WHERE THE COMPANY IS LISTED, THIS INFORMATION AS SOON AS POSSIBLE, BUT NO LATER THAN NINE CALENDAR DAYS, THROUGH THE AGENCY OF ONE OR MANY COMMUNITY WIDE NEWSPAPER.

A MEMBER STATE MAY DECIDE THAT THE DISTRIBUTION TO THE PUBLIC TO BE DONE BY THE COMPETENT AUTHORITY OR BY THE COMPETENT AUTHORITY AND THE RESPECTIVE ISSUER.

THE COMPETENT AUTHORITY MAY DECIDE, EXCEPTIONALLY, TO EXCEPT THE ISSUER FROM PUBLISHING THE INFORMATION WHEN CONSIDERS THAT PUBLICATION OF SUCH INFORMATION IS DETRIMENTAL FOR THE ISSUER, BUT PROVIDING THAT THE EXEMPTION IS NOT LIKELY TO AFFECT INVESTORS PROTECTION.

IN ORDER TO PROVIDE THE DIRECTIVE'S APPLICATION THE MEMBER STATES MUST DESIGNATES THE COMPETENT AUTHORITY OR AUTHORITIES APPROPRIATELY EMPOWERED TO FULFIL ITS ASSIGNMENTS AND THAT WILL CO-OPERATE WHENEVER NECESSARY TO ACHIEVE THESE ASSIGNMENTS, UNDER THE BOUNDING OF PROFESSIONAL SECRECY.

LAW NO. 52/1994 AND REGULATION NO. 2/1996 OF RNSC COORDINATING CONTINUOS DISCLOSURE OF SECURITIES ISSUER PROVIDE NORMS ON THE INFORMATION TO BE DISCLOSED WHEN ACQUIRE OR DISPOSE OF MAJOR HOLDINGS WITHIN PUBLICLY OWNED COMPANIES. EACH PERSON ACQUIRING OR HOLDING, ON ITS OWN OR IN RELATION WITH THIRD PARTIES, SHARES OR TRANSFERABLE SECURITIES GIVING RIGHT TO SUCH SHARES REPRESENTING 5% OR MORE FROM THE VOTING RIGHTS SHALL INFORM RNSC AND, IN CASE OF SHARES ISSUED BY PUBLICLY OWNED COMPANIES LISTED ON A STOCK EXCHANGE, SHALL INFORM THE STOCK EXCHANGE TOO WITHIN TWO DAY SINCE THE TRADING DATE.

THE PUBLICLY OWNED COMPANIES SHALL DRAW UP, SUBMIT, DISTRIBUTE AND PUBLISH IN AT LEAST ONE NATIONWIDE NEWSPAPER A CURRENT REPORT IN CASE OF CHANGES CONCERNING THE CONTROL OVER COMPANY. THIS INFORMATION SHALL BE PUBLISHED WITHIN MAXIMUM 15 DAYS SINCE THE EVENT DATE.

PROVISIONS CONCERNING DISCLOSURE ARE ENFORCED IN HUNGARY, CZECH REPUBLIC AND POLAND, EVEN IF RELATIVE DIFFERENT BY THE EUROPEAN DIRECTIVES IN REGARD WITH THE HOLDING LIMITS.

THE DRAFT ON SECURITIES AND REGULATED MARKETS HAS INCLUDED IN CHAPTER VI, "INVESTORS PROTECTION"^{xxlviii}, THE DIRECTIVE'S 88/628/EEC PROVISIONS, *FOLLOWING THAT UPON ITS REGULATIONS THE RNSC TO WATCH OVER THE COMPLIANCE OF THE DISCLOSURE AND PUBLICITY REQUIREMENTS. ACCORDING TO THE DRAFT, THE REGULATED PERSON^{chiii} SHALL INFORM RNSC AS SOON AS POSSIBLE*

IN REGARD WITH ANY ACQUISITION OR SELLING OF HOLDINGS FROM ITS CAPITAL WHICH IS LIKELY TO EXCEED OR FALL UNDER 10%, 20%, 33%, 50% AND 66%.

1.4. Council Directive 89/592/EEC of 13 November 1989 coordinating regulations on insider dealing^{xlviii}

THE ADOPTION OF THIS DIRECTIVE WAS BASED ON THE FOLLOWING CONSIDERATIONS:^{xlviii}.

- THE SECONDARY MARKET FOR TRANSFERABLE SECURITIES PLAY AN IMPORTANT ROLE IN FINANCING THE COMPANIES;
 - TO FULFIL ITS ROLE IN FINANCING THE COMPANIES IT IS IMPORTANT TO PROVIDE ALL THE APPROPRIATE MEASURES FOR THE SMOOTH FUNCTIONING OF THE MARKET, THE EFFECTIVE FUNCTIONING GO THE MARKET DEPENDING ON THE INVESTORS CONFIDENCE;
 - AN IMPORTANT PLACE IN THE RANGE OF THE FACTORS OF WHICH INVESTORS CONFIDENCE DEPEND ON IS OCCUPIED BY THE INVESTORS' ASSURANCE THAT THEY ARE PLACED ON AN EQUAL FOOTING AND THEY WILL BE PROTECTED AGAINST THE IMPROPER USE OF INSIDE INFORMATION;
 - DUE TO THE REASONS MENTIONED BEFORE THE MEASURES AGAINST INSIDER DEALING ACTIVITIES ARE NEEDED, AND BECAUSE THE LACK FOR SUCH MEASURES IN SOME MEMBER STATES AND OF THE CONSIDERABLE DIFFERENCES REGARDING SUCH MEASURES BETWEEN OTHER MEMBER STATES, ADOPTION OF COORDINATED REGULATIONS IN THIS FIELD IS REQUIRED AT THE LEVEL OF THE EUROPEAN UNION;
 - THE ADVANTAGE OF COORDINATED REGULATIONS AT THE LEVEL OF EUROPEAN UNION CONSISTS IN THE FACT THAT CREATES THE POSSIBILITY FOR STRUGGLE AGAINST INSIDER DEALING ACTIVITIES IN CROSS BORDER TRADING, ON THE GROUND OF CO-OPERATION BETWEEN THE COMPETENT AUTHORITIES OF THE MEMBER STATES.
 - THE DIRECTIVE STIPULATES THE OBLIGATION OF CO-OPERATION BETWEEN THE MEMBER STATES WHENEVER NECESSARY ON PURPOSE TO FULFIL THEIR ASSIGNMENTS.
 - THE EXCHANGE OF INFORMATION ACTIVITY BETWEEN THE COMPETENT AUTHORITY OF THE MEMBER STATES, WHICH ADDRESS THE INSIDER DEALING CASES, IS FOLLOWING UNDER THE PROFESSIONAL SECRECY BOUNDING.
 - THE COMPETENT AUTHORITIES MAY REFUSE AN INFORMATION REQUEST WITHIN A CASE OF INSIDER DEALING WHEN;
 - COMMUNICATION OF SUCH INFORMATION IS LIKELY TO AFFECT THE SOVEREIGNTY, SECURITY OR THE PUBLIC POLICY OF THE STATE;
 - THE JUDICIAL PROCEDURE HAS ALREADY BEEN INITIATED AGAINST THE PERSON SUBJECT TO THE INFORMATION REQUEST.
- THE EUROPEAN UNION MAY SIGN AGREEMENTS CONCERNING INSIDER-DEALING ACTIVITIES WITH NON-MEMBER STATES.

THE PROCEDURES AGAINST INSIDER DEALING ACTIVITIES HAS BEEN LAID DOWN SINCE 1990-1992 WITHIN THE LEGAL FRAMEWORK OF HUNGARY, CZECH REPUBLIC AND POLAND, WHILE IN ROMANIAN SUCH PROCEDURES ARE PROVIDED BY THE DRAFT ON SECURITIES AND REGULATED MARKETS.

IN CHAPTER VI, "INVESTORS PROTECTION" FROM THE DRAFT ON SECURITIES AND REGULATED MARKETS ARE BROUGHT TOGETHER PROVISIONS OF DIRECTIVE 89/592/EEC COORDINATING REGULATIONS ON INSIDER DEALING. ARTICLE 64 STIPULATES THE INVESTORS' RIGHT FOR ACCESS TO SECURE, CORRECT, SUFFICIENT AND SIGNIFICANT INFORMATION DISCLOSED IN DUE TIME IN CONCERN WITH TRANSFERABLE SECURITIES, ISSUERS, GENERAL ASSEMBLIES AND DECISIONS ADOPTED, AND THE MARKET ACTIVITY OF THE ISSUER. THE ISSUERS OF TRANSFERABLE SECURITIES PUBLICLY OFFERED, REGISTERED WITH SECURITIES REGISTRATION OFFICE FROM RNSC ARE KEPT TO IMMEDIATELY INFORM INVESTORS IN WHEN SIGNIFICANT EVENTS COME UP.^{xlviii} WHEN THE DISCLOSURE CANNOT BE MADE IMMEDIATELY WITHOUT THE RISK OF A NEGATIVE IMPACT FOR THE ISSUER, RNSC SHALL INFORM AND TAKE MEASURES ON PURPOSE TO MAINTAIN ON ORDAINED MARKET FOR RESPECTIVE TRANSFERABLE SECURITIES, OR TO SUSPEND THE NEGOTIATION UNTIL DISCLOSURE CAN BE EFFECTED. THE RULES TO BE FOLLOWED FOR DISCLOSURE SHALL BE ESTABLISHED BY RNSC. UNTIL DISCLOSURE MOMENT THESE INFORMATION ARE CONSIDERED TO BE PRIVILEGED. THE DRAFT DEFINES IN ART. 2, PAR. Q) AND R) THE CONFIDENTIAL AND PRIVILEGED INFORMATION.^{xlviii} A PERSON WITHIN THE NORMAL FRAMEWORK OF ITS ACTIVITY OR ITS DUTIES MAY DO DISCLOSURE OF THE PRIVILEGED INFORMATION. RNSC SHALL ISSUE REGULATIONS ADDRESSING THE PROCEDURE FOR ENFORCEMENT THE INTERDICTIONS ON ILLEGAL USING OF THE CONFIDENTIAL AND/OR PRIVILEGED INFORMATION. ACCORDING WITH THE DRAFT ON SECURITIES AND REGULATED MARKETS, INFRINGEMENT OF THESE PROVISIONS SHALL CONSTITUTE CRIMINAL OFFENSE AND WILL BE SANCTION UNDER THE PENAL CODE. THE PENALTIES TO BE ENFORCED AND THEIR LEVEL SHALL BE ESTABLISHED BY RNSC UPON REGULATIONS.

1.5. Council Directive 85/611/EEC of 20 December 1985 on the coordinating of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)^{xlviii}

- THE ARGUMENTS IN ADOPTION OF THE DIRECTIVE ARE AS FOLLOWS:
- TO ELIMINATE THE APPRECIABLE DIFFERENCES EXISTING BETWEEN THE LAWS AND REGULATIONS WITHIN THE MEMBER STATES, ESPECIALLY REGARDING THE OBLIGATIONS OF CORRESPONDING ORGANISMS AND THEIR CONTROL, DIFFERENCES LIKELY TO AFFECT THE COMPETITION IN THE FIELD OF UNDERTAKINGS FOR COLLECTIVE INVESTMENT IN TRANSFERABLE SECURITIES IN INTERIOR OF THE EUROPEAN UNION DUE TO THE LACK OF EQUIVALENT PROTECTION FOR INVESTORS IN THE MEMBER STATES, UPON A COORDINATED POLITIC IN THIS FIELD CAPABLE TO ALLOW THE ACCESS OF UCITS COMING FROM A MEMBER STATE ON THE CAPITAL MARKETS FROM OTHER MEMBER STATES.
 - THROUGH THE INTERMEDIARY OF A COORDINATED POLITIC IS INTENDED REMOVAL OF RESTRICTION AFFECTING THE FREE MOVEMENT OF THE UNITS ISSUED BY THE UCITS FROM EUROPEAN UNION, WHICH IS LIKELY TO SUPPORT THE EMERGING THE SINGLE EUROPEAN CAPITAL MARKET;
 - DUE TO ABOVE MENTION IT IS NECESSARY THE ESTABLISHMENT OF COMMON REGULATIONS CONCERNING THE LICENSING, SUPERVISION, STRUCTURE,

ACTIVITIES AND INFORMATION TO BE DISCLOSED BY THE UCITS FROM THE MEMBER STATES OF EUROPEAN UNION;

– DIRECTIVE IMPLEMENTATION AT THE LEVEL OF EUROPEAN UNION CONFERS ENOUGH GUARANTEES TO ALLOW A UCITS SITUATED IN A MEMBER STATE TO MARKET ITS UNITS IN ANOTHER MEMBER STATE WITHOUT THE OBLIGATION TO MAKE THE UCITS SUBJECT OF DIFFERENT REGULATIONS. THE UCITS OF A MEMBER STATE WHICH SELL THEIR UNITS IN ANOTHER MEMBER STATE MUST UNDERTAKE ALL APPROPRIATE STEPS TO PROVIDE THAT THE UNITS HOLDERS CAN EXERCISE FINANCIAL RIGHTS WITHOUT ANY DIFFICULTY AND THEY HAVE ACCESS TO INFORMATION.

THE COMPETENT AUTHORITIES OF THE MEMBER STATES SHALL CO-OPERATE IN ORDER TO FULFIL THEIR ASSIGNMENTS AND PROVIDING THAT THEIR EMPLOYEES ARE SUBJECT TO PROFESSIONAL SECRECY OBLIGATION.

THE DIRECTIVE'S PRINCIPALS WERE SIMILARLY ADOPTED IN THE LEGAL FRAMEWORK OF HUNGARY, CZECH REPUBLIC, SLOVAKIAN REPUBLIC AND POLAND, WHILE IN ROMANIA THE INVESTMENT FUNDS ARE REGULATED FOR THE TIME BEING UPON GOVERNMENT ORDINANCE NO. 24/1993, APPROVED THROUGH THE LAW NO. 83/1994, CONCERNING THE ESTABLISHMENT AND FUNCTIONING OF THE OPEN-END INVESTMENT FUNDS AND FINANCIAL INVESTMENT SOCIETIES AS FINANCIAL INTERMEDIATION INSTITUTIONS.

THE DIRECTIVE'S 85/611/EEC PROVISIONS WILL BE REFLECTED IN ROMANIAN LEGISLATION BY THE LAW CONCERNING UNDERTAKINGS FOR COLLECTIVE INVESTMENTS IN TRANSFERABLE SECURITIES THE DRAFT OF WHICH HAS BEEN SUBMITTED TO THE ROMANIAN PARLIAMENT TOGETHER WITH THE DRAFT ON SECURITIES AND REGULATED MARKETS FOR SCRUTINY AND APPROVAL IN THE FALL OF 1998.

THE DRAFT REGULATES ESTABLISHMENT, STRUCTURE, AND ACTIVITIES OF UCITS TOGETHER WITH SUBSEQUENT ENTITIES IN ORDER TO STIMULATE COLLECTION OF THE SPREAD SAVINGS AND THEIR INVESTMENT IN CONDITION OF APPROPRIATE PROTECTION FOR INVESTORS.

THE UCITS, ACCORDING WITH THE DRAFT PROVISION, MEANS THAT KIND OF COLLECTIVE INVESTMENT IN TRANSFERABLE SECURITIES WHICH IS ESTABLISHED ON PUBLIC SUBSCRIPTION FOR UNITS ON THE GROUND OF A PUBLIC OFFER LICENSED AND REGULATED BY THE LAW.

THE UCITS ARE LICENSED BY RNSC UNDER FOLLOWING CLASSIFICATION: OPEN-END INVESTMENT FUND, CLOSE-END INVESTMENT FUND, MUTUAL FUND, INVESTMENT FUND, INVESTMENT SOCIETY WITH VARIABLE CAPITAL, INVESTMENT SOCIETY WITH FIX CAPITAL, FINANCIAL INVESTMENT SOCIETY.

THE UCITS RE-UNITE THE TOTALITY OF PECUNIARY CONTRIBUTION TO THE ORGANISM, RESULTED FROM SUBSCRIPTION OF THE UNITS UPON A PUBLIC OFFER FOR UNITS OF PARTICIPATION WHICH REPRESENT BOTH THE OWNERSHIP RIGHTS AT THAT ORGANISM, AND THE ASSETS PURCHASED AS RESULT OF INVESTMENT OF SUCH RESOURCES IN THE FORM OF A DIVERSIFIED PORTFOLIO FOR TRANSFERABLE SECURITIES.

LIKEWISE FOR DIRECTIVE 85/611/EEC IS PROVIDED THE EXISTENCE OF THE ASSET MANAGEMENT COMPANY FOR UCITS AND THE DEPOSITORY COMPANY WITH SIMILAR FUNCTIONS AS SET OUT IN DIRECTIVE. LIKE IN DIRECTIVE 85/611/EEC IS STIPULATED SAME THE DRAFT PROVIDES THE LICENSING REQUIREMENTS AND THE ASSIGNMENTS OF THE ASSET MANAGEMENT COMPANIES AND FOR DEPOSITORY

COMPANIES. IN ORDER TO PROVIDE THE TRANSPARENCE IN UCITS ACTIVITY, IT WAS PROVIDED IN THE DRAFT REQUIREMENTS ADDRESSING THE INITIATIVE AND PROCESS OF THE PUBLIC OFFERS FOR PARTICIPATION UNITS IN SUCH AN ORGANISM, DISCLOSURE TO BE DONE TO THE RNSC AND PUBLIC, AND THE RULES CONCERNING THE RISK SPREADING.^{xlvi}

IN ADDITION OF THE PRUDENTIAL NORMS FOR UCITS INVESTMENTS AND OF SPECIFIC MODALITY OF ORGANIZATION STRUCTURE, WHICH IN A CERTAIN MEASURE WERE PRESENT IN EXISTING LEGAL FRAMEWORK, THE DRAFT PROVIDES THE OPPORTUNITY FOR NEW TYPE OF INVESTMENT FUNDS.

2. Stage II Directives

2.1. Council Directive 93/6/EEC of 15 March 1990 on the capital adequacy of investment firms and credit institutions

TOGETHER WITH DIRECTIVE 93/22/EEC – DIRECTIVE 93/22/EEC THE MAIN OBJECTIVE OF WHICH IS ALLOW THE INVESTMENT FIRMS LICENSED BY THE COMPETENT AUTHORITIES OF THE HOME MEMBER STATES AND SUPERVISED BY THESE TO ESTABLISH SUBSIDIARIES AND TO PROVIDE INVESTMENT SERVICES IN OTHER MEMBER STATES -, DIRECTIVE 93/6/EEC INTEND TO ACCOMPLISH THE FULLY RECOGNITION, ON MUTUAL BASIS OF INVESTMENT FIRMS FROM THE EUROPEAN UNION.

DIRECTIVE 93/6/EEC INTEND TO ESTABLISH A COMMON FRAMEWORK RELATIVE TO THE OWN FUNDS OF INVESTMENTS FIRMS, AMOUNTS REPRESENTING INITIAL CAPITAL, RISK MONITOR THESE ASPECTS REPRESENTING ESSENTIAL MATTERS WHICH MUST BE SETTLED FOR APPROPRIATE FUNCTIONING OF THE INTERNAL MARKET IN FINANCIAL SECTOR.

IS CONSIDERED AS APPROPRIATE THE ESTABLISHMENT OF DIFFERENT VALUES REPRESENTING INITIAL CAPITAL OF INVESTMENT FIRMS, ACCORDINGLY TO THE RANGE OF ACTIVITIES WHICH OF THE COMPANIES ARE LICENSED TO PROVIDE, THE DIRECTIVE BEING APPRECIATED AS PART OF THE INTERNATIONAL EFFORT TOWARDS ALIGNMENT OF THE REGULATIONS ON THE SUPERVISION OF INVESTMENT FIRMS AND CREDIT INSTITUTION (FROM NOW ON CALLED INSTITUTIONS). THUS, THE ESTABLISHMENT OF BASIC COMMON STANDARDS WITH REGARD TO THE OWN FUNDS OF THESE INSTITUTIONS REPRESENTS THE MAIN FEATURE OF THE INVESTMENT SECTOR WITHIN THE INTERNAL MARKET, THE OWN FUND PROVIDING THE CONTINUITY OF THE INSTITUTIONS' ACTIVITY AND INVESTORS PROTECTION, IN ADDITION WITH A EQUIVALENT TREATMENT BETWEEN THE COMPETING INSTITUTIONS.

THE MARKET AND PORTFOLIO RISKS, THE ONE RELATED TO THE SETTLEMENT ACTIVITIES AND THE CURRENCY RISK IMPOSE DEVELOPMENT OF THE STANDARDS AND SUPERVISION FRAMEWORK FOR INSTITUTIONS INVOLVED IN PROVIDING INVESTMENT SERVICES.^{xlvi}

THE PURPOSE OF DIRECTIVE IS TO ESTABLISH A COMMON FRAMEWORK OF ACTIVITY FOR THE MEMBER STATE IN CONCERN WITH THE MONITORING AND CONTROL OF RISK EXPOSURE IN CASE OF INVESTMENT FIRMS, ALONG WITH THE POSSIBILITY TO ACCOMPLISH OF PROSPECTIVE TECHNICAL ALTERATION DUE TO EVOLUTIONS IN FINANCIAL SECTORS.

THE PROVISIONS OF DIRECTIVE 93/6/EEC ON THE CAPITAL ADEQUACY OF INVESTMENT FIRMS AND CREDIT INSTITUTIONS ARE ASSIMILATED IN THE DRAFT OF SECURITIES AND REGULATED MARKETS, CHAPTER IV, "INVESTMENT SERVICES". THE LICENSING IS RELATED WITH COMPLIANCE OF MINIMUM REQUIREMENTS SET OUT BY RNSC THROUGH REGULATIONS ISSUED UPON THE NEW LAW.^{xlviii} AT THE LEVEL OF THE EUROPEAN UNION THE INITIAL CAPITAL FOR INVESTMENT FIRMS IMPOSED UPON DIRECTIVE 93/6/EEC, ACCORDING WITH RANGE OF INVESTMENT SERVICES PROVIDED, VARY FROM EURO 50,000 TO 730,000. IN ROMANIA THE LIMITS VARY AT THE MOMENT BETWEEN ROL 300,000,000 TO 1,800,000,000 (AT THE EXCHANGE RATE OF ABOUT 17,000 ROL/EURO, THE ROMANIAN INVESTMENT FIRMS' CAPITAL IS SITUATED BETWEEN EURO 18,000 TO 106,000).

RNSC STIPULATES ALIGNMENT FOR THE QUOTES OF INITIAL CAPITAL TO THE MINIMUM REQUIREMENTS OF DIRECTIVE 93/6/EEC. THE PROCESS OF ALIGNMENT SHALL BE ACCOMPLISHED TAKING IN CONSIDERATION THE EVOLUTION OF THE ROMANIAN CAPITAL MARKET. THE LAST ALTERATION OF THE MINIMUM REQUIREMENTS FOR INITIAL CAPITAL TOOK PLACE IN 1998 WHEN THE CAPITAL LIMITS WERE THREE TIMES INCREASED, THE LICENSE FOR SECURITIES COMPANIES THE CAPITAL OF WHICH WAS NOT ALIGNED TO THE NEW REQUIREMENT WAS ADJUSTED IN CONCERN WITH THE RANGE OF SECURITIES SERVICES PROVIDED, OR IN CASE OF SECURITIES FIRM FALLING UNDER THE LIMIT OF ROL 300,000 THE LICENSE WAS SUSPENDED. AT THE MOMENT, ON THE ROMANIAN CAPITAL MARKET THE NUMBER OF SECURITIES FIRMS, OUT OF THE TOTAL OF 170 MEMBERS OF THE NATIONAL ASSOCIATION OF SECURITIES DEALERS, THE CAPITAL OF WHICH EXCEED THE MINIMUM LIMIT OF EURO 50,000 IMPOSED BY THE EUROPEAN DIRECTIVE IS ABOUT 110, A ROMANIAN SECURITIES COMPANY EXCEEDING THE SUPERIOR LIMIT OF EURO 730,000 (WITH A CAPITAL OF AROUND EURO 4,700,000).

IN HUNGARY, CZECH REPUBLIC, AND POLAND, ALTHOUGH THE CAPITAL LIMITS ARE NOT INTEGRATED WITH THE EUROPEAN REQUIREMENTS, THE EXISTING LIMITS ARE SUPERIOR TO THE ROMANIAN LIMITS. THUS, THE MINIMUM REQUIREMENTS FOR A SECURITIES COMPANY PROVIDING THE WHOLE RANGE OF INVESTMENT SERVICES IS SITUATED BETWEEN EURO 300,000 TO 400,000. THIS FACT IS A CONSEQUENCE OF THE BETTER RESULTS OBTAINED BY THE NATIONAL ECONOMIES IN THESE COUNTRIES, HAVING A POSITIVE INFLUENCE AT THE LEVEL OF THE CAPITAL MARKETS.

2.2. Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field

THE FIRMS PROVIDING INVESTMENT SERVICES ENCOUNTERED WITHIN DIRECTIVE MUST BE SUBJECTS OF LICENSING IN MEMBER STATES THEY ARE COMING ON PURPOSE TO ENSURE INVESTOR'S PROTECTION AND STABILITY OF THE INVESTMENT SECTOR.

THIS DIRECTIVE REPRESENTS AN IMPORTANT INSTRUMENT TO ACCOMPLISH INTERNAL MARKET BOTH FROM THE POINT OF VIEW OF THE SETTLEMENT RIGHT AND THE FREE MOVEMENT OF SERVICES IN THE FIELD OF CAPITAL MARKETS. DIRECTIVE INTENDS TO ACCOMPLISH THE HARMONIZATION ONLY IN REGARD WITH ESSENTIAL REQUIREMENTS, NECESSARY AND SUFFICIENT TO SECURE THE MUTUAL RECOGNITION OF AUTHORIZATION AND PRUDENTIAL SUPERVISION SYSTEMS, MAKING POSSIBLE THE GRANT OF A SINGLE AUTHORIZATION VALID THROUGHOUT THE EUROPEAN UNION, IN CONDITION OF APPLICATION THE HOME

COUNTRY CONTROL PRINCIPLE. THE SECURITIES FIRMS, UPON THE LICENSE GRANTED IN THE HOME COUNTRY, CAN PROVIDE INVESTMENT SERVICES THROUGHOUT THE EUROPEAN UNION THROUGH THE INTERMEDIARY OF SUBSIDIARIES OR UNDER THE PRINCIPAL OF FREE MOVEMENT OF SERVICES. THE PRINCIPALS OF MUTUAL RECOGNITION AND HOME COUNTRY CONTROL IMPOSE THAT THE COMPETENT AUTHORITIES OF THE HOME MEMBER STATE TO REFUSE A LICENSING APPLICATION OR TO WITHDRAW THE LICENSE OF SECURITIES FIRMS IN THAT CASES WHERE CONDITIONS, LIKE THE OPERATION PROGRAMS, GEOGRAPHICAL DISTRIBUTION OF THE ACTIVITIES CARRIED OUT CLEARLY INDICATE THAT SECURITIES FIRMS CHOOSE THE LEGAL SYSTEM OF A MEMBER STATE IN ORDER TO ELUDE THE STRICTER REGULATIONS IN FORCE IN ANOTHER MEMBER STATE WHERE THE SECURITIES FIRMS INTEND TO CARRY ON THE MOST OF THE THEIR OPERATIONS.

ANOTHER PRINCIPAL OF THE DIRECTIVE ADDRESSES INVESTORS' PROTECTION UPON SECURING INTERNAL SUPERVISION FOR EACH SECURITIES COMPANY. IN ORDER TO PROVIDE INVESTORS PROTECTION THEIR ASSETS SHALL BE HELD SEPARATELY OF THE SECURITIES FIRM'S ASSETS. THE MEMBER STATES MAY, GENERALLY, ESTABLISH STRICTER REGULATIONS THEN THE DIRECTIVE'S ONE, ESPECIALLY IN CONCERN WITH THE LICENSING REQUIREMENTS, PRUDENTIAL REGULATIONS AND REPORTING.

THE SUBSIDIARIES OF INVESTMENT FIRMS FROM THIRD COUNTRIES SHALL BE SUBJECT OF THE SAME LICENSING PROCEDURES ALIKE UNTIL DIRECTIVE'S ENACTMENT. THE LICENSING OF INVESTMENT FIRMS' SUBSIDIARIES FROM THIRD COUNTRIES SHALL BE SUBJECT OF LICENSING PROCEDURES LIKELY TO PROVIDE THE RECIPROCITY FOR INVESTMENT FIRMS FROM EUROPEAN UNION PROVIDING INVESTMENT SERVICES IN THIRD COUNTRIES.

EACH MEMBER STATE MUST, CONSEQUENT OF DIRECTIVE ENACTMENT, PROVIDE THAT WITHIN ITS TERRITORY ALL LICENSED INVESTMENT FIRMS IN ANY MEMBER STATE BENEFIT OF EQUAL OPPORTUNITIES IN CONCERN WITH THE ACCESS TO THE REGULATED MARKETS OF TRANSFERABLE SECURITIES.

UPON DIRECTIVE'S ADOPTION CREDIT INSTITUTIONS ARE GRANTED WITH THE RIGHT OF DIRECT ACCESS ON THE CAPITAL MARKETS WITHOUT THE NECESSITY TO ESTABLISH SPECIALIZED BRANCHES.

THE DRAFT ON SECURITIES AND REGULATED MARKET'S TAKE IN CONSIDERATION DIRECTIVE'S 93/22/EEC PROVISIONS WITHIN THE CHAPTER IV TITLED "INVESTMENT SERVICES."

ACCORDING WITH THE DRAFT, FINANCIAL INSTRUMENT INTERMEDIATION IS CARRIED OUT BY SECURITIES FIRMS IN CONFORMITY WITH THE LICENSE AND UNDER RNSC SUPERVISION, THE SECURITIES FIRMS HAVING THE OBLIGATION TO ALIGN TO THE NORMS CONCERNING PROFESSIONAL CONDUCT TOGETHER WITH OTHER APPLICABLE PROVISIONS ESTABLISHED UNDER THIS DRAFT AND WITHIN RNSC REGULATIONS.

TO OBTAIN THE LICENSE FOR FINANCIAL INTERMEDIATION, THE INTERMEDIATION INSTITUTIONS WHICH ARE NOT BANKS, CANNOT HAVE OTHER OBJECT OF ACTIVITY OTHER THAN FINANCIAL INTERMEDIATION. THE DRAFT STIPULATES THAT, RNSC MAY LICENSE ROMANIAN LEGAL ENTITIES ONLY TO PROVIDE INVESTMENT SERVICES. IN ROMANIA. CONSIDERING THAT,

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- ON THE ONE HAND, THE ACCESSION PROCESS OF ROMANIA TO THE EUROPEAN UNION, WHICH INVOLVES, INTER ALIA, FREE ACCESS ON THE MARKET FOR COMMUNITY'S INVESTMENT FIRMS AND VICE VERSA IN THE MOMENT OF ACCESSION ACCORDING TO THE PRINCIPLE OF FREE MOVEMENT OF SERVICES,
 - ON THE OTHER HAND, IN THIS MOMENT ROMANIA IS NOT MEMBER OF THE EUROPEAN UNION, CONSEQUENTLY THE FREE MOVEMENT OF SERVICE PRINCIPLE IS NOT FUNCTIONING,

IT IS PROVIDED IN THE DRAFT ON SECURITIES AND REGULATED MARKETS THE POSSIBILITY THAT, RNSC, UPON REGULATIONS ISSUED, TO SPECIFY ANY PERSON OR ACTIVITY, WHICH MAY BE EXEMPTED FROM THE LICENSING PROCESS. THUS, IN CASE OF FINANCIAL INTERMEDIARIES FROM THIRD COUNTRIES, IN ORDER TO BE ABLE TO BENEFIT OF THE EXEMPTION RIGHT, SHALL BE EXAMINE, ON BILATERAL BASIS, THE PROVISIONS OF THE LEGISLATION ADDRESSING INVESTMENT SERVICES IN THE THIRD COUNTRY AND ROMANIA ON PURPOSE TO ASSURE IN CONCERN WITH PRUDENTIAL NORMS AND INVESTORS PROTECTION.

IT IS ALSO STIPULATED THAT EVERY TRADING OR OPERATION WITH FINICAL INSTRUMENTS CARRIED OUT BY A SECURITIES COMPANY EXEMPTED FROM THE LICENSING PROCEDURES BY RNSC IT IS CONSIDERED AS AN ACT OF COMMERCE AND GIVES BIRTH TO A VALID OBLIGATION WHICH OF THE GAME EXEMPTION CANNOT BE OPPOSED TO.

IN HUNGARY, CZECH REPUBLIC AND POLAND, THE APPLICABLE REGIME RELATIVE TO FOREIGN INVESTMENT FIRMS WILLING TO PROVIDE SERVICES ON THE CAPITAL MARKETS IS EQUIVALENT WITH THE REGIME APPLICABLE TO DOMESTIC INVESTMENT FIRMS.

REGARDING THE DIRECT ACCESS OF BANKS ON SECURITIES MARKET, THE DRAFT STIPULATES THAT, NO BANKING COMPANY CAN SOLICIT LICENSE FROM RNSC WITHOUT NBR AGREEMENT. RNSC SHALL BE EMPOWERED WITH THE SAME SUPERVISION AND CONTROL COMPETENCE RELATIVE TO THE BANKING COMPANIES' ACTIVITIES ON THE CAPITAL MARKET AS IT IS IN RELATION WITH SECURITIES COMPANIES.

THE POSSIBILITY OF FREE ACCESS FOR BANKS ON THE ROMANIAN CAPITAL MARKET COULD DETERMINE AN INCREASE RELATIVE TO THE RISK DEGREE OF THE MARKET, UNDER THE FOLLOWING CIRCUMSTANCES:

- ROMANIAN BANKS DO NOT POSSESS THE MATURITY, EXPERIENCE AND TRADITION NEEDED FOR DIRECT ACCESS ON THE CAPITAL MARKET;
- ROMANIAN BANKS ENCOUNTER DIFFICULTIES IN THEIR OWN ACTIVITIES IN THE BANKING FIELD, INVOLVEMENT OF BANKS LIABLE TO BANKRUPTCY IS LIKELY TO AFFECT THE SMOOTH FUNCTIONING OF THE MARKET;
- THROUGH THE CONCENTRATION OF THE FINANCIAL POWER WITHIN FEW BANKS, UNDER THE CIRCUMSTANCES OF ROMANIAN SOCIETY, IS LIKELY TO DETERMINE POLITICAL STRUGGLES ON THE MARKET WHENEVER THE ADMINISTRATION OF ONE OR ANOTHER BANK IS APPOINTED;
- THE BANKS WILL NOT ENCOURAGE THE CAPITAL MARKET – CREDIT POLITIC DISPROVING THE RISKS OF THE CAPITAL MARKETS, UNLESS ON ITSELF SPECULATION PURPOSES.

IN CONCLUSION, THE ELABORATION OF THE TWO DRAFTS AS DESCRIBED HAS BEEN ACCOMPLISHED NOT ONLY IN RESPECT WITH THE PROVISIONS STIPULATED WITHIN THE EUROPEAN DIRECTIVES IN THE FIELD OF CAPITAL MARKETS, BUT IT WAS

INTENDED THAT THE NORMS STIPULATED WITHIN THE DRAFTS TO SECURE TRANSPARENCE ON THE CAPITAL MARKET AND INVESTORS PROTECTION. AS MENTIONED, QUESTIONS ARISE IN REGARD WITH THE IMPACT OF THE BANKS DIRECT ACCESS OVER THE CAPITAL MARKET UNDER THE CIRCUMSTANCE DETERMINED BY THE LACK OF EXPERIENCE AND TRADITION, AND THE BANKING SYSTEM DISABILITIES.

3. Specific features of the romanian capital market

3.1. Historical development of the securities companies

In 1995 at Bucharest it is inaugurated the first Romanian regulated capital market, after almost fifty years of absence of any activity on the capital market. This first capital market was the Bucharest Stock Exchange. The number of securities companies that are members of the Bucharest Stock Exchange was estimated at almost 30 in 1995 and 170 at the moment.

Next year, thanks to the important assistance program provided by the United States America was founded, following the example of NASDAQ market, the RASDAQ market, on which was prepared for trading the shares resulted from the Mass Privatization Process.

1. *Between 1996 and the middle of 1997*, the Romanian capital market was having a full swing. In this period the United States Agency for International Development (USAID) was providing assistance for RASDAQ market organization and for securities companies (there were almost 40-50 securities companies selected for getting assistance; the criteria for getting this assistance was to be authorized by Romanian National Securities Commission), and also was founded the National Association of the Securities Companies (NASD).

In this period were founded many securities companies in the purpose of trading the certificates from Mass Privatization Process. Most of these securities companies were having Romanian capital, but also were founded foreign capital securities companies. These last securities companies were having foreign shareholders from financial field, which provided the know-how in their companies together with the invested capital.

2. *Between the second half of the 1997 and the first one of the 1998*, because of the upsurge of the market in the first period, characterized by high prices of shares and the presence of the institutional investor, were founded more securities companies, exceeding 200 companies at the moment. It is the period when important foreign investment firms appear on the capital market, especially the investment banks.

3. *From the second half of 1998 till now, the decline of the 1997 autumn increased*, the securities companies were seeing for themselves about this decline, at least on a short term and concerning that the shares prices is not reversible, which determined many securities companies to preserve themselves in expectation of better times, and other securities companies to be eliminated or to be sold by their shareholders. Also, at the beginning of 1998 was coming into force the Regulation no. 3 of the Romanian National Securities Commission concerning the intermediation of securities, which established new capital requirements for securities companies, which should be respected since first half of the 1998. This fact, necessary not only for the gradual alignment of the capital market requirements with the Europeans standards, but also for the health of the capital market, determined the decrease of the securities companies number. In this period important securities companies with foreign capital are getting along, and because of the support provided by the investment banks they provided investment services for the banks foreign customers in Romania.

Also, now it is the moment when the simple purchasing of shares process on the capital market turn into a capital concentration one, the number of public offers for shares acquisition is growing up, same as splitting, mergers, capital raising, and firms' privatization on the capital market emphasized.

At the moment there are almost 170 securities companies, having Romanian or foreign capital, on the Romanian capital market, out of which almost 130 are active. Having regard on the "1998 TOP" of the securities companies, on RASDAQ, according with the criteria of trading amount settled by the National Corporation for Clearing, Settlement and Depository (excepting cross-transactions), the first 10 securities companies of the 204 existing at that moment were accomplished 70% of the transactions on RASDAQ market, and the first 3 companies of these were accomplished 10%. In a descending order, those securities companies were:

1. Unicapital-12,7908%;
2. Active International-10,3075%;
3. Capital Securities-7,5709%;
4. Vanguard-5,3943%;
5. Gelsor-4,5841%;
6. Global Valori Mobiliare-4,4813%;
7. Bucharest Investment Group-2,5700%;
8. Creditanstalt Securities-2,2491%;
9. Monynvest-1,8568%;
10. Trend-1,8019%.

It is estimated that on the market do exist several categories of securities companies, as follows:

- Important securities companies, which are claimed to be rising on the legality edge;
- Important securities companies, which were constantly developing, gaining important incomes, but small profits;
- Small securities companies, created for speculative operation, undertaking, generally, the most of the law infringements;
- Small securities company which were always respecting regulations and acting in line with the legal provisions.

Concerning the number of securities companies which are members of the Bucharest Stock Exchange, these has been developed between 1995 and first semester of the 1999, as follows:

- 1995: 38 securities companies;
- 1996: 62 securities companies;
- 1997: 107 securities companies;
- 1998: 173 securities companies,
- first semester of 1999: 174 securities companies.

3.2. The state of the capital market

At the moment, the Romanian capital market, like the entire economy, is facing with a difficult situation. On purpose to identify the causes that determined the negative evolutions registered on the capital market and finding straightening solution, the Romanian National Securities Commission has undertaken in 1998 a consultation among the securities companies (especially those witch owns an important piece in the market activity or those which have foreign or banking capital).

Two major causes, affecting the capital market and the national economy, where standing out as producing these developments, as follow:

A. External causes

1. The world concourse of events (the collapse of the Asian stock exchanges occurred in the second half of the 1997) which was reflected in the changes relative to the strategies and reorganization of the institutional investors portfolios on most of the capital markets in the world.
2. The economical depression from Russia and the effects of an inappropriate banking system in the Czech Republic, have induced the distrust to the foreign investors concerning the capital markets in the region.

These two shocks were seriously affected the emergent markets, investors trust and determined, together with the interest rates decrease process within the Western Europe, the orientation of the capital flows towards developed markets.

3. The studies published during 1998 emphasized that the long-term incomes on the emerging capital markets associated with the investments risks do not justify investments on these markets, comparing with developed markets.

B. Internal causes

These causes have a complex nature and they come from political, legislative, economical, reorganization and privatization fields, as follow:

1. The insecure political climate and the excessive time lost because of the political crisis have negatively influenced the investor's decisions concerning entering on the market.
2. The positive feeling created at the end of the 1996, because of the electoral changes, has disappeared at the middle of 1997, according as the pace of reform decrease.
3. The legislation concerning privatization and direct investments was over and over modified, and the absence of a stable legal framework in this field determined the investors' reticence.
4. The absence of an appropriate accounting standards, compatible with the West-European standards is limiting the visibility and the attractiveness of the Romanian companies in the eyes of the foreign investors.

The incompatibility existing between the Romanian accounting system and the West-European one determined the majority of the issuers, once they have been audited in the International Accounting System' standards, to report losses, even if the Romanian Accounting Standards have registered profit.

5. The restrictive taxes system and the accounting system which are not complying with the inflationary environment determined the companies de-capitalization.
6. The restrictive interest rate policy determines the absence of credits for companies.
7. The corporate decline of the national economy (industry, constructions, services, exports etc.).
8. The slow privatization, with syncope, the generalized disuse of the capital market for the purpose of sustaining of privatization process (which should secure a fast and transparent privatization), the delay in bringing on the privatization agenda the important industrial companies and the regie autonom lost the investors trust.
9. The absence of an appropriate management at the companies, which should be interested in increasing of the market value for its shares a measure of its self- performance and characterized by the:
 - Concentration on production and less on the selling;
 - An insufficient costs control;
 - The absence of transparency in relation with the shareholders.
10. The absence of the state bonds on the capital market.
11. The disuse by the listed companies' management of the main function of the capital market: the financing function.

Consequence to the consultation of securities companies by Romanian National Securities Commission, has resulted the following potential solutions for clearing and sudden change of the capital market situation and for its using as a lever for the economical development:

1. The setting up of a stable legislative framework, coherent and attractive for all the participants on the Romanian capital market activity.

A firm legislation and the reform commitment should attract the investments.

The legislation concerning privatization should be brought in a final form and applied in the same form without exceptions.

2. Promoting and popularization of the capital market functions at the beneficiaries' level, as well at the different decision levels of the public administration, as following:
 - Primary market;
 - Secondary market;
 - A standard for the national economy.

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3. Development of the legislation concerning pension funds.
 4. Strict application of the requirements concerning disclosure activity.
 5. Alignment of the accounting standards at the Western-European norms.
 6. Application of a tax policy which is likely to sustain the corporate development of the economy.

3.3. The discharging and entering costs on the Romanian capital market

The discharging and entering costs on the Romanian capital market for a securities are not high, consisting in the costs of setting up of a company as a joint-stock company, the authorization charge being paid to the Romanian National Securities Commission, the charge that varying between ROL 3 and 18 millions, depending on types of the investment services which will be performed, the tax to the National Association of Securities Dealers, the Bucharest Stock Exchange, the National Corporation for Clearing, Settlement and Depository and the endowment costs.

Starting with the end of 1998, the National Association of Securities Dealers is collecting a US \$ 25,000 due from the companies which will be members of National Association of Securities Dealers. The reason of collecting this due comes from the fact that the capital market systems on which the company that will operate was developed on the efforts and the investments made along the time by the present members of the National Association of Securities Dealers. Till now, this due was paid only by two securities companies, because a lot of persons who wanted to involve itself in securities intermediation where taking over from the former shareholders the holdings in already existing securities companies, so the securities companies number was maintained relatively constant.

Same as the entering costs, the discharging costs are low, corresponding with those for the rubbing out of a company.

3.4. Foreign securities companies, yes or no?

Are securities companies interesting for Romanian capital market? Yes, as long as these are capable to bring new investors, other way these companies are only reducing the portfolios of the existing securities companies, considering that on the Romanian capital market operates, at the moment, almost 170 securities companies, and the sums invested on the market are low. Either now or in the future, there won't be any discrimination between the present companies and those that will enter on the market, no matter if they have Romanian or foreign capital, the success of each securities company depending on its own market policies.

Concerning the results of the important investment banks operating on the Romanian financial market, it is considered that the results of some of this are not always comparable with their reputation. It is also considered that the reasons of these results reside in:

- the training of their staff for sophisticated markets which are not operating at the moment in Romania, the operating Romanian market being less interesting for these investment banks;

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- the lack of interest about the Romanian capital market, their interest being captured by the privatization process and significant transfer of stakes. Thus, the State Ownership Fund uses investment banks in the privatization process counting on their reputation, the success of the privatization being many times under the expectation, sometimes even the foreign customers involved in the privatization process being dissatisfied.

3.5. The investors protection

The Romanian capital market possesses, under the conditions of adoption of the two drafts drawn up by the Romanian National Securities Commission, of an up-to-date legislative framework, which complies with the requirements existing in the countries with experience and tradition in this field, and also possesses the institutions necessary for applying these regulations on the purpose of securing the capital market transparency and investors protection.

The absence of tradition regarding capital market activity, individual and group interests resulted especially from the property reorganization process as result of privatization privatization, the inadequate mentalities that appear in the management of the publicly owned companies in their relationship with shareholders and the fact that the shareholders of the publicly owned companies resulted from the Mass Privatization Process is too much dispersed and do not have the appropriate education of a genuine investor, all that determined on the Romanian capital market, same as on all the similar capital markets in the region, the emergence of the shareholders' rights infringement.

Between January first, 1999 and August 30, 1999, Romanian National Securities Commission applied the following penalties:

- 13 securities companies penalized with minor offence fine, amounting ROL 481 million;
- 16 securities companies penalized with the license suspension for time periods between 30 and 90 days;
- 14 securities companies penalized with the license withdrawal;
- 4 agents penalized with minor offence fine, in sums between 1 and 10 million lei;
- 5 agents penalized with the license suspension for 90 days;
- 9 agents penalized with license withdrawal and the interdiction of securities intermediation for 5 years;
- 6 securities companies chairmen penalized with minor offence fine, in sums between 1 and 10 million lei;
- 4 representatives of the Compliance with Legal Provisions Offices penalized with minor offence fine, in sums between 1 and 5 million lei;
- 3 securities companies Administration Boards penalized with fine or final interdiction in practicing any kind of activity on the capital market;
- 5 securities companies chairmen penalized with interdiction of any activity on the capital market, for periods between 3 and 5 years;
- the Administration Boards of publicly owned companies were also penalized;
- the fraudulent transactions and public offers for buying/selling and private investments which do not respected the Romanian National Securities Commission regulations were cancelled.

3.6. The investors' protection in their relationship with the securities companies and concerning trading settlement within the Bucharest Stock Exchange and RASDAQ market.

According with Regulation No. 3/1998 provisions concerning the licensing and practice of the securities intermediation that was setting up by Romanian National Securities Commission, the securities company's customer should have access to the general information about the securities company regarding: the activities which of the securities company is licensed to practice, the fees and other expenditures concerning the services the company offers to the customer, the most recent annual or/and half-yearly balance sheet, the head which from the client should get the information about its accounts or that related to the securities company. The changes related to the fees and other expenditures must be communicated to the customer within maximum 5 days.

Before trading securities for its own interest or for a relevant shareholder, a member of the Administration Board or for an employee of the securities company, the securities company must execute the orders received from the customers for these securities at the same price or at a better price, in case of a limit order.

The agent of the securities company must inform the company's top-management about any of its customer's complain concerning its activity. The Securities Company should keep an evidence for all these complains, so that the evidence could be presented at any moment to the Romanian National Securities Commission.

The publicity made by the securities company will respect the full name of the company, the registered office's address, phone and fax numbers.

Publicity made by the securities company should not contain false information or information likely to mislead the public and also should not give any guarantees to the investors concerning the investment's performance.

The securities company's publicity must be approved by the Office for Legal Compliance of the securities company, and this can be suspended by the Romanian National Securities Commission or by the Self-Regulation Body if do not comply with law, the RNSC or the Self-Regulation Body' rules.

The securities company must keep at its office the copies of all publicity materials for a two years period since their appearance and must present these to the RNSC or to the Self-Regulation Body whenever requested.

At BSE and RASDAQ (inside the National Corporation for Clearing, Settlement and Depository) were constituted funds in order to secure the resources for the efficient function of the transactions settlement mechanism.

At BSE the fund is setting up upon opening an account at a banking company, which is managed by BSE. The fund is constituted from the contributions of the Stock Exchange Association' members and from contributions of the custodian companies authorized by BSE.

The fund may be used only when there are no reserves on the settlement account of the securities companies or custodian companies.

Using sums from the Fund determine the suspension from trading of that securities company or from settlement of that custodian company, till the extinction of the liability of this one at the fund.

The debtor securities company or the debtor custodian company that determine the using funds resources by BSE for completing the settlement process shall reimburse in 48 hours the sums used this way.

On RASDAQ, each direct user of the National Corporation for Clearing, Settlement and Depository will constitute a deposit at the Compensation Scheme of the National Corporation for Clearing, Settlement, and Depository, which will be managed by this.

The National Corporation set up the minimum level of the obligatory deposit constituted at the fund for Clearing, Settlement, and Depository according with one or more formulas settled by the Administration Board.

The debiting of the fund user directly by the National Corporation for Clearing, Settlement, and Depository will be limited to the redeeming of losses and /or damages linked by the objective's performance of the National Corporation for Clearing, Settlement, and Depository.

When the fund is used for covering a loss or damage, the National Corporation for Clearing, Settlement and Depository will directly inform and immediately each user and the RNSC on the sum used and the reasons justifying this measure.

3.7. The relationship with the international organizations and other states authorities in the capital markets field

On purpose of promoting its regulatory, supervision and control mission, considering the markets globalization process, the Romanian National Securities Commission attends, subject to the availability of resources, the activities of the international organization in the field of capital markets. Beginning with 1999, RNSC became a member of the International Organizations of Securities Commissions (IOSCO) the head office of which is located in Montreal. The organization, structured in committees and work groups, contemplate the settlement of some problems concerning the capital markets regulation and supervision, problems which present a general or regional interest. Thus, the Regional European Committee of IOSCO, which is composed of the European Union States and also of the candidate States to the European accession and which presidency is owned at the moment by the Polish Securities Commission, also plan the settlement of certain problems concerning the implementation of the European Directives. Also, inside IOSCO where signed Memorandum Agreements with the similar institutions of Canada, Moldavian Republic and Greece.

In June 1999, in Bulgaria, under the aegis of IOSCO and with participation of the representatives of the European Union and the United States of America took place the First Reunion of the Regulation Authorities of Capital Markets from South Eastern Europe. With this occasion, States from the South Eastern Europe, both members of the European Union and candidate countries, decided to co-operate in the field of harmonization of the capital markets regulations.

At the end of November 1998, RNSC and Capital Market Commission of the Hellenic Republic signed at Bucharest a Memorandum of Understanding concerning co-operation and exchange of information. As a result of this close co-operation it was decided to start a bilateral assistance program where, along a six-month period, experts of the two commissions will attend training sessions inside the relevant commissions. Also, has been granted the financing of this program by TAIEX Office from the European Union.

3.8. Priorities in the field of capital market for accession to the European Union

The short-term priorities, within the years 2000 limit, included in the Accession Partnership-1999 with concern to the Romanian capital market refer to: (I). Adoption of the drafts of the Law on securities regulated markets and Law concerning Undertakings for Collective Investments in Transferable Securities and (II). strengthening the supervision capacity.

I. As far as concern the adoption of the two laws, as mentioned before, RNSC elaborated, in close relation with the European Directives the projects and submitted them to the Romanian Parliament for scrutiny and adoption in September 1998. *Compliance with the reference date for this priority imposes the adoption by the Romanian Parliament of the drafts until the end of 1999.*

II. Concerning the strengthening of the supervision capacity of RNSC, such objective imposes the existence besides the appropriate institutions and regulations of the qualified human resources also. Besides the lack of experience due to the absence of capital markets for almost fifty years, the personal turnover and the lack of equipment affected too. As far as concern the personal turnover, this was removed after the RNSC became self-financed from extra-budgetary resources collected from the capital market activities, starting with April 1999. Moreover, it was realized the increasing of staff number, the volume of which, in the Control Department, has been doubled. Simultaneously, upon the Regulation No. 4 of RNSC, has been set up within RNSC the organizational structure of the capital market Supervision Office, which must supervise in due time the activities of the two regulated capital markets in order to prevent market manipulation and to administer the market risks. At the moment, the adequate software needed for the supervision activity is in process of designing, following that the Supervision Office to commence into force. These things became possible through a better remuneration policy. Strengthening the expertise in control activity reflected in improvement of the control capacity over the capital market will reflect the effects of the staff turnover stabilization and the new recruitment. The higher financial resources due to self-financing afforded the procurement of new equipment. To preserve the extinction of the short-term results on medium and long-term, RNSC should be granted with an appropriate building office.

NOTE

Chapter III: Insurance Market

Karina Rosu

1. Romanian Insurance Legislation

Insurance activity is currently regulated in Romania by two laws and a number of Government ordinances. The latter ones refer mainly to the organisation and activity of the Supervision Office of the Insurance and Reinsurance Activity (SOIRA - OSAAR).

- Law 47 of July 16th 1991 on the establishment, organization and functioning of insurance companies
This law defines the types of companies that can offer services in the insurance market (insurance companies, reinsurance companies, intermediaries, representative offices of foreign insurers), the criteria that they have to follow in order to obtain the licence from SOIRA, the lines of insurance underwritten in Romania (9 lines of general insurance and 1 line of life insurance), the current activity rules – minimum capital requirements, technical reserves, maximum underwritten premium volume, premium rates, reporting requirements. The minimum subscribed capital is set to ROL 25 million per line of business and the maximum volume of written premiums (after deducting the premiums ceded to reinsurers) should not be higher than 5 times the paid capital plus the capital reserves.
- Law 136 of December 30th 1995 on insurance and reinsurance in Romania. The provisions of this law refer to:
 - the types of insurance (compulsory and facultative)
 - insurance contracts: conclusion, provisions, the rights and obligations of the insureds and of the insurers
 - specific provisions for material damage insurance, personal insurance, third party liability insurance, reinsurance
 - set up and administration of : Insureds protection fund and Traffic accident victims' protection fund.
- Government ordinance no 674 of August 23rd 1991 on the attributions of SOIRA
This ordinance sets the attributions of SOIRA, created in the Ministry of Finance, and the ways it can act for regulating the Romanian insurance market. Some of SOIRA's attributions are: licencing insurance companies, granting special licences for insurance companies to write certain classes of business (at this moment, special licences are necessary for compulsory motor third party liability insurance and financial risks insurance), creation of norms and regulations on the solvency margin, approval of increase/ reductions in capital, portfolio transfers, mergers, etc. SOIRA has the right to limit or prohibit the operations of a company in the insurance sector and, where necessary, it can ask for a company to be declared bankrupt.

A new insurance law on the licencing and activity of insurance companies and insurance intermediaries is currently being discussed in the Parliament. This law will repeal and replace Law 47/1991 and the Government Ordinance that define SOIRA's attributions. The was adopted by the

Senate in October 1998 and by the Chamber of Deputies in December 1999 and is currently going to be discussed by the mediation commission.

One of the most important characteristics of this law is its flexibility, a large number of its provisions being set or updated by regulations issued by the insurance supervision authority (ex: the classes/lines of insurance, minimum capital requirements, solvency margin, technical and mathematical reserves calculation procedures).

1.1. European Union insurance legislation

The Treaty of Rome laid down a 12 years timetable for the introduction of freedom of establishment and freedom of service for insurance. The initial timetable provided the creation of the freedom of establishment and services for reinsurance by the end of 1963 and of the freedom of establishment and services for non-life and life insurance by the end of 1969.

This initial timetable slipped. Although for reinsurance there have been no major difficulties due to their international nature, the wide variety of practices and regulations for direct insurance meant that the directives needed to implement freedom of establishment and freedom of services have been implemented gradually, up to 1994.

Three main stages can be identified in the EU insurance legislation:

- First Generation Directives for life and non-life insurance which brought freedom of establishment. By the enactment of these directives, an insurance company from an EU country can be established in a different EU country in the same conditions as the local insurers (Art. 52 of the Treaty of Rome)
- The Second Generation Directives for life and non-life insurance represent an intermediate stage towards freedom of services. These Directives allow freedom of service for certain types of clients considered to be well informed enough not to need special protection from the insurance supervision authorities.
- The third generation Directives for life and non-life insurance completed the single insurance market and introduce a single licence for insurers and home country supervision. The introduction of home country supervision and of a single licence means that, once an insurer is licenced in one member state, this insurer can create representative offices or offer cross-border insurance services in any other member state.

In addition to these three generations, there are a number of Directives that regulate specific insurance classes (ex: motor insurance), reinsurance, insurance accounting, insurance intermediaries.

2. First Generation Directives

Need:

When an insurance company from an UE member state wished to establish itself in another member state, it was obliged to adhere to the insurance legislation and regulations of that state. These regulations differed considerably from one country to another. It was necessary therefore, as a prerequisite for freedom of establishment, to achieve a certain harmonisation in the systems of control in the member countries.

2.1. First Council Directive (73/239/EEC) of 24 July 1973 on the co-ordination of laws, regulations and administration provisions relating to the undertaking and pursuit of the business of direct insurance other than life insurance

Objective:

The Directive harmonises the insurance supervision systems and the access conditions for direct non-life insurance.

Content:

The Directive harmonises the access conditions and the practice of direct non-life insurance. It ensures that the setting up of an insurance company (a subsidiary with legal personality) or of an agency without legal personality, are subject to administrative approval in each member state.^{xlviii}

This approval is granted based on similar financial and legal criteria in each country. The aim is to guarantee equality of treatment between national companies and companies from other member countries and to obtain an adequate protection of the insureds and of third parties through an adequate supervision of the insurance market.

Harmonisation applies to conditions of access, the administrative approval required and, more particularly, to financial conditions that have to be met by an insurance company.

The Directive contains also provisions referring to insurance companies from countries that are not members of the EU and permits agreements with these third countries on condition of reciprocity.

Current stage of the implementation of the directive in Romania

The provision of this Directive are partially implemented by Law 47/1991. The draft new insurance law will achieve a better compliance with the EU legislation.

At this moment, the most important provision of the Directive that can be found in the Romanian legislation is the need to obtain a prior approval for the pursuit of insurance business in Romania. The licencing conditions are, however, very different from those applied in the EU, both as regard to the required documentation and to the minimum capital requirements and to the calculation of reserves.

A number of the provisions of the EU directive that will be harmonised by the new insurance law are mentioned bellow:

- freedom of establishment is guaranteed for foreign insurers in Romania, the same authorisation procedures will apply to foreign insurers and to Romanian insurers.
- the licence is granted based on a scheme of operations and on a appropriate reinsurance plan.^{xlviii}
- limitation of the activities of insurance companies to the pursuit of insurance business
- minimum capital requirements (equivalent to the guarantee fund mentioned in art. 17(2) of the Directive) close with those set by the Directive^{xlviii}
- introducing the idea of solvency margin and its calculation based on standards similar with those applied in the EU^{xlviii}
- detailed provisions regarding the technical reserves and their calculation based on EU standards

A number of other provisions of the Directives will not be harmonised for the time being but, due the flexibility of the new law, these provisions can be harmonised as the Romanian insurance market develops. An example is the EU classification of insurance business in 17 classes as opposed to the 9 classes used in Romania. Harmonisation was not considered to be necessary for the moment because a number of the insurance classes are not written in Romania now, the market being still

unsophisticated. Introducing 17 classes of insurance could lead to unwanted administrative difficulties for the insurers.

Due to the lack of specific accounting rules for insurance, the calculation rules for reserves will not be applied from the moment the law comes into force. In order to use these new rules, the insurance supervisions authority and the Ministry of Finance will have to create special accounting regulations for insurance that will take into account the particularities of this activity. The draft insurance law provides that specialised accounting procedures will be finalised in 6 months time from the moment the law comes into force.

Current stage of the implementation of the directive in other countries from Central and Eastern Europe

Poland:

- Insurance supervision is undertaken by the State Insurance Supervision Office (PUNU) together with the Ministry of Finance. The Ministry of Finance grants licences and has legislative powers while PUNU examines insurers solvency, advise on measures to be taken in insolvency cases and impose sanctions
- Foreign insurers can establish 100% foreign capital companies but only insurers originating from countries that allow licencing of Polish insurers will be granted a licence
- Technical reserves are regulated in detail
- Solvency margin requirements are in accordance with the EU Directive
- Specific insurance accounting regulations exists

Hungary:

- Insurance supervision is undertaken by the Insurance Supervision Authority (Allami Biztosításhelygyelet - ABIF). The new insurance law for January 1996 increases the powers of the supervision authority.
- The new insurance law is based on the insurance legislation from United Kingdom and Germany and has as objective total harmonisation with EU requirements in the near future.
- The licencing procedures takes around 3 months
- The Hungarian insurance market is dominated by foreign insurers, companies with 100% foreign capital can be established
- Technical reserves are calculated according to EU standards
- Minimum capital is of approximately USD 500,000
- Non-life insurance classes (18) are similar with those of the First Non-life EU Directive

The Czech Republic:

- Insurance supervision is undertaken by the Ministry of Finance.
- All insurers have to have a licence
- The licencing procedures takes around 3 months
- Companies with 100% foreign capital can be established
- Technical reserves are calculated according to EU standards
- Solvency margin requirements are in accordance with the EU Directive

2.2. First Council Directive (79/267/EEC) of 13 March 1979 on the co-ordination of laws, regulations and administration provisions relating to the undertaking and pursuit of the business of direct life insurance

Objective:

The Directive has the same objectives as the First Non-life Directive but it applies to life insurance

Contents:

The provisions of this Directive are similar with those of the First Non-life Directive. An important additional provision is that contained in art. 13 of the Directive that forbids newly created insurance companies to write both life and non-life insurance in the same company. This requirement has appeared due to the important differences between the principles of life and non-life insurance and especially due to the need to protect the reserves for life insurance. These reserves are medium and long term reserves and they have to be available in 10 or 20 years time for the payment of claims. For the insurance companies that were already writing life and non-life insurance in the same company (composite insurers), separate accounting for life and non-life activities is required.

Current stage of the implementation of the directive in Romania

The level of implementation of this Directive is similar with that of the First Non-life Directive except for the fact that an insurance company can write, in Romania, both life and non-life business. This will also be the case after the enactment of the new insurance that will maintain the requirement of separate accounting for life and non-life business that exists not in the insurance legislation. In practice, however, Romanian insurers are specialised either in life or in non-life insurance or write their life business through a subsidiary (the exception being ASIROM). Harmonisation of the requirement to write life and non-life business by separate companies is no longer necessary, this requirement being eliminated by the Third Generation Directives.

Current stage of the implementation of the directive in other countries from Central and Eastern Europe

Hungary:

- An insurance company cannot write both life and non-life insurance except for reinsurance for these types of business and for accident insurance if included in life insurance policies.
- Insurance companies that were writing both life and non-life business when the insurance law came into force in 1995 were able to continue to write both types of business as long as they were applying solvency margin requirements

The Czech Republic:

- An insurance company can write both life and non-life insurance

Poland:

- An insurance company cannot write both life and non-life insurance

Conclusions

Based on the above comments, we can see that the coming into force of the new insurance law will achieve an increased harmonisation with the provisions of the First Generation Directives. The remaining differences will be harmonised in the short and medium term (1 to 5 years), especially through regulations issued by the insurance supervision commission. *We have, however, to remember that the new insurance law will be fully applied in practice only when a special accounting system for insurance companies will exist. The creation of this system has to be one of the priorities of the accounting system reform in Romania.*

3. Second Generation Directives

Need:

Freedom of establishment, by itself, was not sufficient to create a single market in insurance insofar as the sale of insurance products in another member state remained subject to the requirement to have an establishment in that state. In 1986, a decision of the Court of Justice of the European Communities states that the requirement for an insurer to be established in a EC country in order to be able to offer insurance services for risks located in that country is against the principle of freedom of services of the Treaty of Rome. These restrictions are only justified where factors of general interest, such as consumer protection, require it. The same decision states that, in certain cases, no special consumer protection is needed (either because of the type of the insured risk or to the type of consumer). For these cases, an increased liberalisation of the insurance market is needed. This decision had an important influence on the Second Generation Insurance Directives.

3.1. Second Council Directive (88/357/EEC) of 22 June 1988 on the co-ordination of laws, regulations and administration provisions relating to the undertaking and pursuit of the business of direct insurance other than life insurance and laying down provisions to facilitate the effective exercise of freedom to provide services and amending directive 73/239/EEC

Objective:

The second non-life directive introduced provisions to allow freedom of services for non-life risks where no specific consumer protection is required.

Content:

The risks covered by non-life insurance are divided in two categories according to the degree of consumer protection needed. The first category, the yes called "large risks" is defined in terms of the nature and importance of the insurance buyer and the nature of risk. This category includes all transport risks, credit and suretyship risks for professional clients from the industrial and commercial sector where these risks relate to their activity, fire risks and natural perils risks where the policyholders exceeds the numerical limits of at least two out of the following three criteria: total balance sheet of EURO 6.2 million; net turnover of EURO 12.8 million and 250 employees. For the insurance of these risks, only the supervisory control of the country of the insurer's origin applies. For these large risks, freedom of services is actually implemented. For all other types of risks (the yes-called "mass risks"), risk home country control is still applied.

Current stage of the implementation of the directive in Romania

The provisions of this Directive are not implemented as such in the Romanian legislation and will not be implemented by the new insurance law due to their transitional character.

Taking into account the fact, for large risks similar with those defined by the directive, the capacity of the Romanian insurance market is too small, these risks are usually reinsured in the international markets in a very large percentage (more than 90%). A case where insurances can be concluded directly with foreign insurers is the case where the specific cover is not available in the Romanian market.

Current stage of the implementation of the directive in other countries from Central and Eastern Europe

The other countries from Central and Eastern Europe do not apply the provisions of this Directive either. Where, as in the case of Romania, certain classes or types of insurance are not available in the local market, they can be bought from foreign insurers.

3.2. Second Council Directive (90/619/EEC) of 8 November 1990 on the co-ordination of laws, regulations and administration provisions relating to the undertaking and pursuit of the business of direct life insurance and laying down provisions to facilitate the effective exercise of freedom to provide services and amending directive 79/267/EEC

Objective:

The second non-life directive introduced provisions to allow freedom of services for life risks where no specific consumer protection is required.

Content:

The quantitative criteria applied for general insurance cannot be applied for life insurance. The directive, instead, makes a distinction between contracts which are under-written at the initiative of the policyholder (passive freedom of services) and contracts actively sought by the insurer (active freedom of services). For the first type of contracts, the policyholder has taken the initiative in seeking to enter into a contract with the insurance undertaking. The directive assumes that the policyholder forgoes the protection provided by the insurance supervision authority from his home country. These contracts can be concluded directly or through an insurance broker or agent from a foreign country or from the country of origin of the insured. In all these cases, the insured will have to acknowledge formally the fact that he is removing himself from the protection of his national law. The insured has the right to cancel the policy within 14 to 30 days from the conclusion of the contract.

Current stage of the implementation of the directive in Romania

The provisions of this Directive are not implemented as such in the Romanian legislation and will not be implemented by the new insurance law due to their transitional character.

Current stage of the implementation of the directive in other countries from Central and Eastern Europe

The other countries from Central and Eastern Europe do not apply the provisions of this Directive either.

Conclusions

The Second Generation Directives are transitional directives, making a connection between the freedom of establishment and the total freedom of services. Their implementation in Romania is not necessary, total freedom of services is going to be implemented for all types of insurance risks when the insurance market and the insurance consumers in Romania will reach the appropriate development level.

4. Third Generation Directives

Need:

The main objective laid down by the White Paper in the completion of the internal market is the mutual recognition of the control legislation of the different countries and, therefore, the application of the control system of the insurer's country of origin ("home country control"). A further objective is the introduction of the "single licence". The intention is to establish a single system of authorisation and control which allows insurance undertakings having their head office in one member state, to open branches and provide insurance services freely, throughout Europe, under the control only of the Member state where their head office is based. The third generation directives, known also as framework directives, achieve these objectives.

4.1. Third Council Directive (92/49/EEC) of 18 June 1992 on the co-ordination of laws, regulations and administration provisions relating to the undertaking and pursuit of the business of direct insurance other than life insurance and amending directives 73/239/EEC and 88/357/EEC.

Objective:

This directive introduces provisions that allow freedom of services for general insurance by applying the principle of home country control of insurers.

Content:

In all member states, access to transact direct insurance is made subject to the granting of a prior authorisation, obtained from the authorities of the member state in which the head office of the insurance undertaking is situated. After the implementation of the provisions of this directive, the licence granted in a member state is valid for the entire EU ("single licence"). This licence allows an insurer to carry on insurance activity either through agencies or directly. Licence granting conditions regarding technical reserves, admissible assets, insurance conditions and insurance premiums are harmonised for the member states. The provisions of this directive should have been implemented in the national legislation of the member states between July 1992 and December 1994. These national measures had to be applied by July 1st 1994. Longer transitional periods were allowed for Spain, Greece and Portugal.

Current stage of the implementation of the directive in Romania

The provisions of this Directive regarding the single licence are not implemented as such in the Romanian legislation and there are probably not going to be implemented before Romania joins the EU.

The requirements of the draft insurance law regarding the licencing conditions are in accordance with the provisions of the directive. In order to obtain a licence, an insurer should submit a business plan containing the description of the type of business underwritten, reinsurance principles followed, minimum capital, estimated premiums and claims and significant shareholders. The provisions regarding the technical reserves and those on assets and asset diversification will be implemented through regulations issued by the insurance supervisory authority.

Current stage of the implementation of the directive in other countries from Central and Eastern Europe

Freedom of services is not allowed in Hungary, The Czech Republic or Poland for the classes of business that are available on the local market. In The Czech Republic, a fine of USD 4 million is applicable for insurances concluded with foreign insurers in breach of this provision. The provisions regarding the licencing and functioning of insurance companies are similar with those set by the directive.

4.2. Third Council Directive (92/96/EEC) of 10 November 1992 on the co-ordination of laws, regulations and administration provisions relating to the undertaking and pursuit of the business of direct life insurance amending directives 79/267/EEC and 90/619/EEC

Objective:

The provisions of this directive allow freedom of services for life insurance based on a single licence granted to the insurer in his home country.

Content:

This directive has the same main provisions as the third non-life directive: a licence granted in one member state allows the insurer to offer life insurance services in any other member state. Uniform criteria are applied for obtaining this licence. No prior notification and approval of the insurance terms and conditions is necessary. This directive abolishes the interdiction regarding the creation of composite insurers set by the first life directive but keeps the requirement for separate management and administration for life and non-life business.

Current stage of the implementation of the directive in Romania

Except for the provisions regarding the single licence, the other provisions of this directive will be implemented by the new insurance law and by the regulations issued by the insurance supervision authority.

The draft insurance law requires separate accounting for life and non-life business.

Current stage of the implementation of the directive in other countries from Central and Eastern Europe

Freedom of services for life business is not allowed in other countries of Central and Eastern Europe.

Conclusions

Harmonisation of the provisions of the third generation insurance directives is not considered as a priority for the insurance market in Romania. The same situation is present in other Central and Eastern European countries. The single licence principle will have to be discussed again when negotiations for joining the EU will reach a more advanced stage. This will allow, in the mean time, the development of the local insurance market and the creation of a stronger insurance supervision authority. An essential requirement for the application of the freedom of services principle is the existence of a strong and competent insurance supervision authority, able to co-operate as equals, with the authorities from the other states. Training programs for the personnel of SOIRA have been organised. New training modules, financed by Know How Fund and Phare, will be organised for the team of the new Insurance Supervisions Commission.

The recommendations made by the European Commission regarding the adoption of the acquis request that Romania implements the principle of the single licence. We have to remember, however, that transitional periods of up to 5 years were granted for other countries that were already members of the EU because their insurance markets were not developed enough. This is why, at this stage, the priority for Romania should be the adoption of the new insurance law that will achieve an increased, even though only partial, harmonisation with the EU directives. Once this law comes into force, the insurers will work following similar rules with those applied in EU countries and will therefore be better prepared to take part in a fair competition when the complete liberalisation of the market is achieved. This transitional period is also important for the development of the competencies of the Insurance Supervision Commission.

5. Other insurance directives

Reinsurance:

Directive 64/225/EEC on the freedom of establishment and freedom of services for reinsurance and retrocession has eliminated the restrictions based on nationality for reinsurance services. If a company also writes direct insurance business this side of its activity is excluded from the provisions of the directive.

This directive is not implemented in the Romanian legislation. Law 136/1995 has even a provision that prohibits Romanian insurers to offer the risks to foreign reinsurers without searching first for reinsurance on the local market. This restriction will not be changed by the new insurance law.

This provision is not, however, applied de facto as the capacity of the Romanian reinsurance market is extremely low. A problem can arise, from the competition point of view, if a local reinsurer is created (there were such initiatives in the last couple of years, none of them finalised yet).

One argument against the existence of this provision in the Romanian law is the principle of reinsurance in itself. Reinsurance has the aim of spreading the risk as much as possible, offering increased protection as no insurance company is strong enough to bear the consequences of an important disaster. By retaining a large proportion of the risk in the Romanian market, the probability of financial problems arising for Romanian insurers and reinsurers is increased.

Certain limitations exist also in Poland regarding reinsurance ceding to foreign reinsurers (no more than 25% of the total premium to be ceded to reinsurers from a specific country, no more than 15% of the total premium to be ceded to one reinsurer).

Accounting for insurance

The role of the 91/674/EEC Directive of 19 December 1991 regarding the accounting systems for insurers is to set a standard for the contents and the structure of the balance sheet of an insurer. By these comparisons among companies in different countries become possible.

The Directive establishes a precise format in which the profit and loss account must be presented. The Directive contains particular provisions for certain entries in the profit and loss accounts.^{xlviii} The Directive gives also evaluation rules and provides for certain obligations regarding the contents of the notes on the accounts.

This Directive has not been implemented in the Romanian legislation and no special accounting rules are being applied for insurance. The Romanian insurers use the same type of accounts any other general trade company uses, and no particular accounts are used to denominate specifically the transactions for insurance. The provisions of the draft insurance Law referring to reserves and accounting are harmonized with the EU Directives but cannot be applied before specific accounts are designed for insurance. The Article 45 of the draft Law states that “Within 16 months from the enforcement of the Law, the Insurance Supervisory Commission shall design a specific system of accounting for insurance and shall develop the appropriate methodology for insurance accounting, subject to prior approval from the Ministry of Finance”. In view of the fact that any new system of accounts needs prior approval from the Ministry of Finance, we find important to stress that for the implementation of the new insurance Law the design of an insurance specific system of accounts is essential. Without such a system of accounts the application of the legal provisions regarding the reserves and the solvency margin is not possible.

In Poland there are in force detailed legal provisions regarding the accounts for insurance companies and insurance specific profit and loss accounts have been implemented since 1/1/1996. Insurers have to file detailed annual reports and quarterly reports with the insurance supervision authority. No insurance specific accounting rules are applied in the Czech Republic.

Insurance Intermediaries

Community regulations for insurance intermediaries are to be found in the Directive 77/92/EEC of 13 December 1976 and the European Commission Recommendation of 18 December 1991.

The Directive 77/92/EEC regulates the professional activity of insurance brokers and insurance agents. There are standards set in the Directive regarding trade and professional knowledge an insurance broker or an insurance agent must have to be allowed to practice. The professional qualifications corresponding to those standards are recognized in all EU states, allowing thus, theoretically, the freedom of services in this field. In practice, the member states might require though the obligatory licensing of intermediaries, existence of a professional liability insurance, participation to a common guarantee fund, etc.

In view of the essential role played by insurance intermediaries in developing a common market in insurance, one feels a need for a more restrictive and unique regulation of all insurance intermediaries (not limited to insurance brokers and insurance agents). The goal of the Recommendation of the European Union of 18 December 1991 is to achieve a stronger consumer protection, to facilitate the freedom of services and the freedom of establishment as well as to ensure

correct competition among all intermediaries. This Recommendation applies to all insurance intermediaries, regardless if they are brokers, agents or consultants . The main elements are: compulsory registration of the intermediaries in their country of origin, minimal professional qualification and maintaining a professional liability insurance.

Currently the Romanian insurance legislation does not make a difference between insurance brokers (independent intermediaries) and insurance agents, the activity of intermediaries (identified in the Law 47/1991 as "agencies for mediation of insurance") and their activity is not regulated in detail. The draft insurance legislation makes a difference between brokers and insurance agents and asks for the former to obey similar standards to those applied in the EU (insurance brokers must be licensed by the insurance supervisory authority, to deal exclusively in insurance broking and to maintain professional liability insurance).

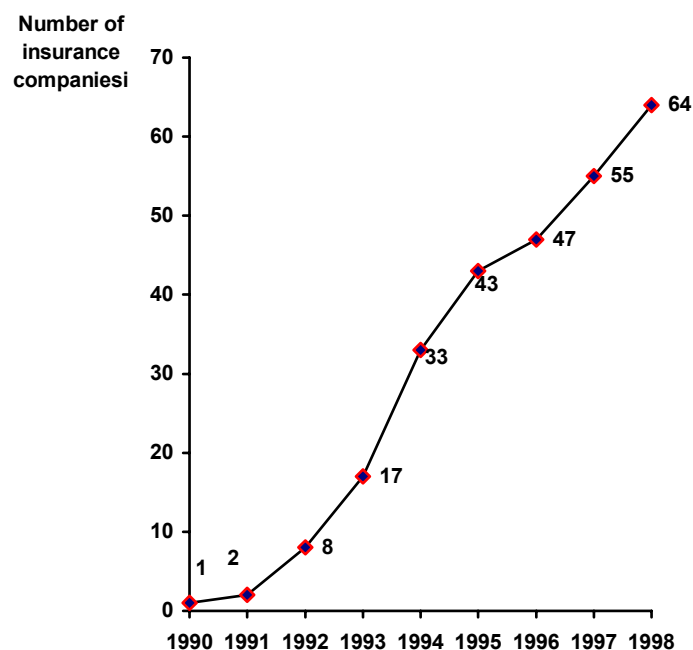
In Poland the law makes distinction between insurance brokers and insurance agents, both types of agents being authorized by the Insurance Supervisory Authority and required to have adequate professional training. Insurance brokers are required to maintain professional liability insurance. In Hungary the conditions are similar and, in addition, the category of "insurance consultants" is identified distinctly. In Czech Republic insurance intermediaries are subject to very limited regulation, the only requirement being for foreign brokers to obtain license from the supervisory authority. New legislation for this area is expected to be developed soon.

6. Structure and development of the romanian insurance market

The current stage of development of the insurance market in Romania is best illustrated by its share in GDP for 1997 and 1998 – as low as 0.52% respectively 0.71% - and by the figure for premium income per inhabitant which was only USD 8.23 and USD 9.80 respectively. These figures are even more relevant if compared with the insurance premium per capita in SUA - USD 2,374 and Japan - USD 5,088. The average insurance premium per capita in Eastern Europe in 1998 was USD 45,60.

At this moment, it is estimated that only 10-15% of the insurable values are actually insured making the market a very attractive one, with an important growth potential.

The market has developed from a single insurer in 1990 (the state owned insurance company ADAS) to over 60 insurers in 1998. Out of these, however, 13 companies had no activity in 1998. The number of insurance intermediaries is over 500.



The total capital subscribed at the end of 1998 was of about 405 billion lei (approx. 45 million USD), very low compared with the standards applied in other countries.

The type of ownership of the insurance companies is varied, ranging from companies where the state is the main shareholder (ASTRA, EXIMBANK) to entirely private companies. The foreign insurers present in the market through Romanian registered companies are: AIG (SUA), Generali (Italy), Interamerican (UAP), Nederlanden (ING Barings – The Netherlands) and, very recently, CGU (UK). Foreign capital represents approximately 38% of the total capital of insurance companies in the market.

One of the most important developments in the market in 1998 was the privatisation of ASIROM S.A., the largest Romanian insurer based on the volume of paid premiums. The privatisation was done by way of an increase of capital from ROL 11,6 billion to ROL 29 billion, the share owned by the State Ownership Fund being reduced to 26%. The privatisation has generated a number of controversies, as the conditions imposed for the private placement by the CNVM were not followed (for this reason CNVM has informed the General State Prosecutor) and the selection criteria of the investors were not made public. One of the investors is Banca Agricola, a state owned company.

The privatisation of ASTRA S.A., the second largest insurer in the market was planned for 1999 but, up to now, there are no signs that it is actually going to happen.

Some of the international insurance brokers present in the Romanian market are AON, Gras Savoye, J&H Marsh & McLennan.

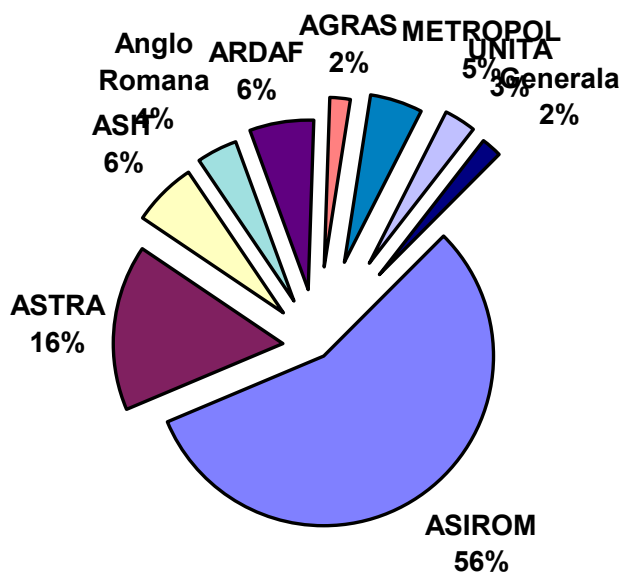
The market entry costs can be considered as being very low, the minimum subscribed capital being of ROL 25 million / line of insurance. This capital was set by Law 47/1991 and has decreased, in real terms, from approximately USD 100.000 in 1991 to only USD 1.500 in 1999.

The market exit costs are those linked with the administration of the portfolio of policies in force. For the general (non-life) insurance companies, the period up to the expiry of the existing policies is

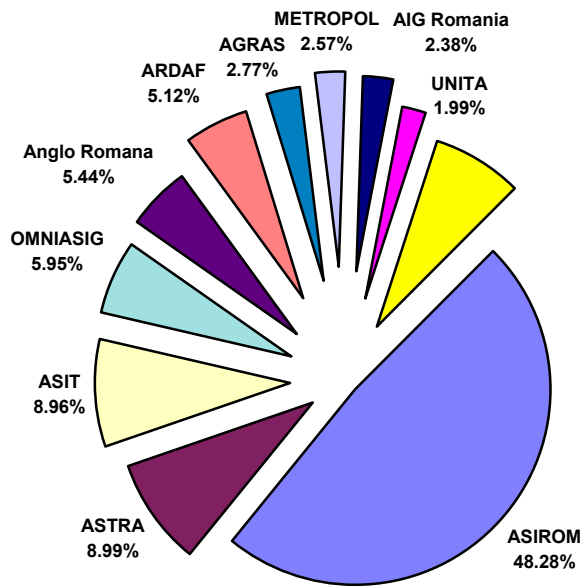
of maximum one year, this type of insurance being usually valid for 12 months. For life insurance companies, the policies are usually valid for at least 5 years, making the exit from the market more difficult for life insurers. A way of leaving the market is by portfolio transfer that, according to Government Ordinance 574/1991 has to be approved the the Supervisory Office for Insurance and Reinsurance.

As far as the market concentration is concerned, ASIROM still has a significant percentage of the market in terms of annual paid premiums for life and non-life insurance but this percentage is continuously decreasing as we can see from the graphs bellow.

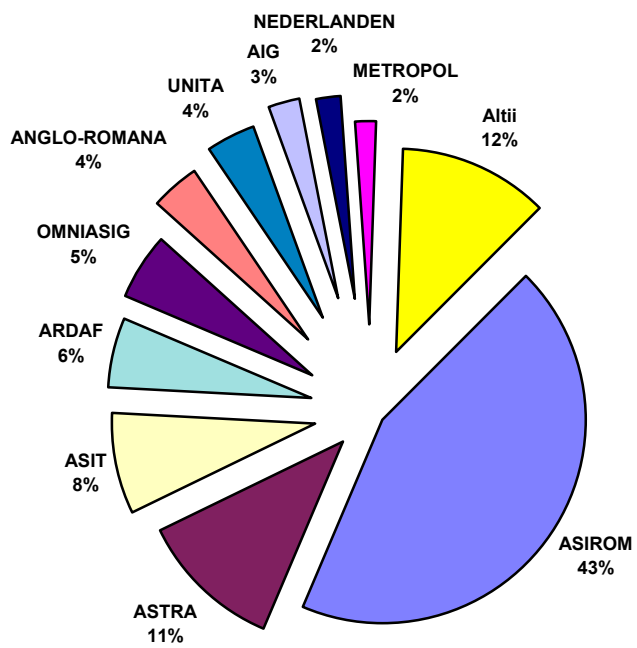
Structure of the insurance market in 1996



Structure of the insurance market in 1997

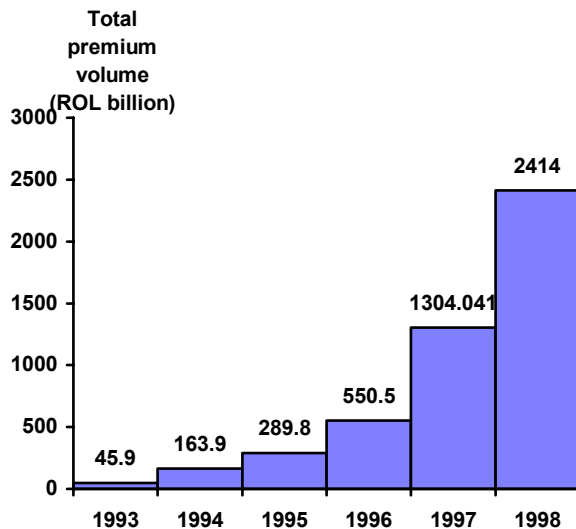


Structure of the insurance market in 1998



The total premium volume was of ROL 1,304 billion in 1997 and of ROL 2,414 billion in 1998, an increase in real terms after discounting for inflation.

The evolution of the total premium volume for life and non-life insurance during the past 6 years is presented below:



7. Methods of foreign insurer involvement in the local insurance market

- Establishment of an insurance company
- Establishment of a subsidiary
- Establishment of a branch office
- Establishment of a representative office

The entry in the insurance market by way of a locally registered company can raise a number of issues for the foreign insurers.

The first problem can be the interdiction of the access of foreign insurers in a particular insurance market because of a desire to protect the local insurance industry. This interdiction can be total or partial, in the latter case, foreign insurers having access to the market by forming joint ventures with local partners. This latter case is the case of Romania where, art.2 of Law 47/1991 states that “the establishment of insurance companies with foreign participation can be done only in association with legal or private Romanian persons”. The minimum participation share of Romanian partners is not, however, set by law (this is the reason why, in Romania, there are companies with 99,9% foreign capital and only 0,1% Romanian capital). This constraint is no longer present in the new draft insurance law, foreign insurers being allowed to set up subsidiaries (these are registered as Romanian legal entities) or representative offices (foreign legal entities).

One other problem can be discrimination against foreign owned insurance companies, these companies being denied the right to write certain lines of insurance or the insureds receiving certain incentives in order to use a local insurer. These problems do not appear in Romania now and will not appear after the coming into force of the new insurance law.

Lack of transparency in market access or competitive rules can also create a disadvantage for foreign insurers.

- Cross-border insurance trade
 - Pure cross-border insurance trade – the insured buys the insurance policy from an insurer registered in a different country, this policy being bought either as an own initiative of the insured or being offered by direct sales, through brokers or agents.
 - Own-initiative cross-border insurance: the insured is the one who contacts the insurer first. Corporations usually use this type of insurance.

The existence of cross-border freedom has the advantage of promoting competition and of increasing, as a consequence, the quality of services offered to the insureds. There are, however, a number of reasons to limit or to forbid totally cross-border insurance. The first reason is that foreign insurers will not invest in the country of origin of the insured risks and will not contribute to its economic development. Further more, the foreign insurers will not contribute, by way of know-how transfer to the development of the insurance industry in the home country

An other reason for not allowing cross-border insurance trade is the wish of governments/ supervisory authorities to protect ill-informed consumers. One condition for perfect competition in a market is the perfect information of consumers. This is, however, very hard to achieve, especially for an intangible product as insurance. Taking into account the important social protection function played by insurance, the governments prefer to have a tighter control over the companies offering insurance in the local market. These same reasons do not apply in the same degree for large companies that buy insurance. It is understood that these companies have access to information and can decide on the quality of the contracts they are entering into. This is why, cross-border insurance contracts where the clients are large companies are usually permitted.

As far as reinsurance is concerned, in most cases they are bought in the international market, being considered that insurers, as professionals, do not need the protection of the governments/ supervisory authorities. This is usually an advantage for the clients of the insurance companies, the use of international reinsurers leading to a better spread of the risk.

In Romania, at this moment, cross-border insurance is not allowed. Article 7 of Law 136/1995 stating that “legal or private Romanian persons have to buy insurance from Romanian registered insurance companies”. The same article has, however, an exception: the case where the type/ class of insurance sought by the client is not available from local insurers. This exception is used quite frequently because a number of sophisticated insurance products are not available in the Romanian market. An other way frequently used in the market in order to avoid this interdiction is “fronting” where, a Romanian insurer issues the local insurance policy and reinsures the risk 100% with a foreign insurer.

Law 136/1995 imposes also a restriction for reinsurance, stating in article 6 that “reinsurance ceding to the international market can be done only if the risks cannot be placed in the local market”. Taking into account the law capitalisation level of the Romanian insurance market, this interdiction is only formal. Lately, there was an intention to form a properly capitalised local reinsurance company with the participation of local insurance companies and of a large international reinsurer. The level of capital required in order that this reinsurer is comparable with other international reinsurers is so high that this initiative was not finalised

7.1. Arguments favoring greater foreign participation

- Improvement of customer service

Due to the increase in competition following the entry of foreign insurers in the market, the insurers will have greater motivation to introduce new products and to offer better quality service. Competition usually leads to a decrease in price. This same effect results also from increased competition between local insurers, this phenomenon being observed already in the Romanian market.

- Increased domestic savings

By bringing insurance products with a significant savings component (ex: life insurance products, private pensions plans administered by insurance companies), consumers will have access to new savings products, more flexible and more suitable for their needs than products offered by banks. Usually, foreign insurers, based on their experience in other countries bring these sophisticated insurance products into the market.

- Transfer of technological and managerial know-how

This is one of the main arguments in favour of opening the insurance market to foreign insurers. This is also the argument that has the most solid backing. In a developing insurance market as Romania, the know-how transfer by foreign insurers is essential, setting a reference for local insurers. This transfer is also done by reinsurers and international insurance brokers.

- Access to additional financial resources

The entry of a foreign insurer by setting up an insurance company will bring an important level of investment because this insurer will have to invest the capital and the reserves in the local economy. Life insurance companies are those that have medium and long-term investments, non-life insurers needing more liquid ways to invest their reserves.

- Improvement in the quality of insurance supervision and regulation

Liberalisation of insurance markets (and acceptance of foreign insurer involvement) creates the need of a more detailed and efficient supervision of these markets. The supervision and regulation authorities will have to adapt frequently the laws and regulations of the market and, usually, they will be able to rely on the experience regarding insurance regulation that foreign insurers can bring from their home country.

7.2. Arguments against greater foreign participation

- Foreign insurers will dominate the domestic market

Due to their access to more advanced technologies, to larger capital resources and mostly due to a better spread of their risks, foreign insurers can offer lower prices than those available in the local

insurance market. Foreign insurers can afford, due to their greater financial strength, dumping practices in order to gain market share. The peril of foreign insurers domination is probably real in the case of cross-border insurance but less apparent in the case of establishment insurance where the foreign insurers will have to follow the rules governing the local market.

- Capital exports will increase

For cross-border insurance, the insurance premiums will leave the country of the insured risk and, in the long term, these financial outflows will be higher than the financial inflows represented by the claim payments. Even when a local insurance company is created, this company will probably reinsure a large proportion of its risks to the mother company, abroad. There are also advantages in the capital exports, namely a better dispersion of the risk in the international reinsurance markets.

- Macro-economic and insurance supervision reforms are still needed.

One of the recommendations made by the International Monetary Fund to developing countries is that capital markets liberalisation should be made only when macro-economic stability has been reached and the local financial system is strong enough, with adequate supervision systems in place. As far as the insurance supervision system is concerned, the existence of a strong and well trained insurance supervision authority is essential before opening the market to foreign insurers, especially for cross-border business. In the absence of adequate supervision and of a good co-operation with the insurance supervisory bodies from the other countries, especially if consumers/ insurance buyers are ill-informed and have little knowledge about insurance products and about the quality of the insurance providers, fraud attempts will certainly exist. Insurance being a product where the price (the premium) is paid at the beginning and the benefit (the claim payment) is received at a latter date, it is very easy for a fraudulent insurer to disappear after receiving the premium without paying the claims. This is even easier for a foreign insurer without a permanent presence in the country. Similar cases have been reported in Romania for personal accident insurance and they can only lead to a decrease in the trust consumers have in the insurance industry, even though most players in the market are honest. If the foreign insurers set up an insurance company, the insurance supervision authority will control this company in the same way as local insurers.

As a conclusion, we can say that, taking into account the development stage of the Romanian insurance market, the fact that local insurers are in a process of growth and the fact that, for the time being, insurance market supervision needs improvement, the best solution would be the involvement of foreign insurers by way of setting up local insurance companies. In this way, we will take advantage of the benefits of their entrance in the market (know-how transfer, access to higher financial resources, improvement of the quality of insurance supervision) without being exposed to the disadvantages (fraud, unfair market domination)

8. Consumer protection

In Romania, insurance market supervision is performed by the Supervision Office of the Insurance and Reinsurance Activity (SOIRA - OSAAR), part of the Ministry of Finance. SOIRA was created by Law 47/1991 and has, according to art. 23 of this law, as main attributions the supervision of the

way legal requirements for insurance activity are followed in order to prevent insurer insolvency and to protect the rights of the insureds.

Specific attributions of SOIRA were set by two Government Ordinances - HG 574/1991 and HG 789/1993. Some of these attributions are: receiving and solving complaints against insurance companies; taking measures for the protection of the insureds and of those that receive services from insurance companies, administration of the insureds' protection fund.

The main sanction that can be applied by SOIRA is the interdiction or limitation of insurers activity. If required, SOIRA can request in court the liquidation/ bankruptcy of insurance companies.

Intervention power of SOIRA is, however, limited due to the absence of specific control attributions and due the fact that insurance legislation does not currently define "solvency" from the insurance perspective. SOIRA has to rely on the control functions of other bodies and can use only the criteria that apply to all other commercial companies and that cannot prevent the insolvency of an insurer. The control criteria used by other control bodies are not always suited for insurance and are not always in the best interest of the insureds (ex: insurers can have difficulties in setting aside the appropriate claims reserves, this being interpreted sometimes as attempts to reduce tax liabilities, reserves being tax deductible).

Control attribution of the Insurance Supervision Commission (ISC) that will take over SOIRA attributions according to the draft insurance law, are much wider, allowing ISC to actually control insurance companies. The draft insurance law gives ISC the power to control insurers and insurance brokers. ISC can apply preventive measures in order to improve the activity and financial status of an insurer by limiting or (temporarily) stopping some of its activities. If there are no results after these initial measures, ISC can nominate a special administrator of the insurance company.

The sanctions that can be applied by ISC are: written notifications, limitation of the activity, fines between ROL 5 million and ROL 50 million for insurers and between ROL 1 and 5 million for insurance brokers, interdiction of activity for one or more classes of insurance, withdraw of the licence. Practicing insurance without a licence from ISC is considered to be a criminal offence and the sanction applied can be imprisonment for up to 3 years or fines between ROL 50 million and 100 million.

Law 136/1995 has created two funds for consumer protection: Insureds protection fund and Traffic accident victims' protection fund. In case an insurance company goes bankrupt, claims will be paid from the Insureds protection fund. This fund is administered by SOIRA and is built of annual contributions from insurers. The value of these contributions is set by SOIRA and is currently 0,5% of the paid insurance premiums. Traffic accidents victims protection fund is administered by the Bureau of Motor insurers (association of the insurers that write motor business), is build from a levy on compulsory motor third party liability insurance and will reimburse victims of hit and run traffic accidents.

Information on the companies writing insurance business in Romania is not easily accessible to the public. SOIRA publishes an annual report on the insurance market and the supervision activity but this report is only available to the public from the excerpts published by the mass media. At the time the report becomes public (around the month of October each year), the information contained in the report is already out of date. The draft insurance law states that ISC will publish at least once a year,

in a public media, an updated list of licensed insurers and all other information it considers important for consumer protection.

An other angle of consumer protection is insurance placement through insurance intermediaries that know the local and international insurance markets. Insurance brokers will usually have internal systems for the evaluation of insurance companies' solvency and quality of service and will recommend to their clients only those insurers that have enough guarantees. As a consequence arises the question of insurance brokers' control. This will be done only after the coming in to force of the new insurance law. In this law, the status of brokers is defined and they will be controlled by ISC.

In other countries, the professional associations of insurers and insurance intermediaries play a very important role in consumer protection. These associations have their own codes of practice. These are self-imposed service standards and are followed by all the members of the association. In Romania, the role of the Association of Insurance and Reinsurance Companies (UNSAR), the association that includes the largest insurers in the market, can be much more important. UNSAR members can create and follow procedures and rules that will result in better consumer protection. At this moment, discussions for the setting up of an intermediaries association are under way. This association will include the most important insurance intermediaries in the market and will have an important role the imposing standards for their services.

Note