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US Securities and Exchange Commission chairman Christopher Cox recently observed at an international regulatory meeting in London that "financial transactions are crossing national boundaries faster than ever before," and that "the world's exchanges are now beginning to combine their operations in order to more closely integrate the world's capital markets". Cox concluded that national regulators "have no choice but to cooperate".

European securities regulators are responding to this environment by bulking up their enforcement muscle and bringing large enforcement cases that increasingly have the look and feel of the SEC's cases in the US markets. In the last few years, Europe has created new and far more potent securities regulatory bodies that are beginning to make their presence felt. And EU member states are implementing EU directives to achieve genuine cross-border convergence in securities regulation.

We can expect to see an ever-increasing number of cross-border enforcement investigations involving two or more national regulators, one of which will often be the SEC. As such cross-border investigations proliferate in Europe, the involvement of the traditionally aggressive SEC will influence the continuing evolution of securities enforcement in Europe, and recent developments suggest that the balance will be struck closer to the US enforcement model. As this happens, Europeans might consider responding to European investigations with approaches more often used in SEC matters, while remaining sensitive to local practices and customs. And in a cross-border enforcement world, Europeans should be mindful that what begins as a local investigation could soon morph into parallel investigations by other regulators (including the SEC), with the possibility of harsher sanctions.

Market and SRO combinations

Recently announced market and regulatory combinations will facilitate coordinated market surveillance of issuers and securities trading across multiple markets. This more effective surveillance will inevitably lead to more and better alerts to government securities regulators concerning possible illegal activity spanning jurisdictions, which will in turn yield more cross-border enforcement investigations and cases.

In late December 2006, the NYSE Group and Euronext announced that over 98% of their respective voting shareholders had approved a proposed merger that will create NYSE Euronext in the first quarter of 2007. This will bring under one roof the New York Stock Exchange, NYSE Arca (formerly the Archipelago Exchange and the Pacific Exchange), the exchanges in Amsterdam, Brussels, Paris and Portugal, and London's futures market, LIFFE. While NYSE Euronext will hold its US and European markets in separate subsidiaries, and the combination will be structured to assure "continued local regulation of the marketplace," NYSE Euronext's proposed bylaws commit it to cooperating and taking "all reasonable steps necessary to cause its agents to cooperate" both with the SEC and with European regulators.

At the same time as NYSE is combining its markets with Euronext, it will also be joining with NASD to create a new self-regulatory organization (SRO) for the US markets that will combine NASD's 2,400 regulatory staff with NYSE Regulation's 470 staff. This new unitary SRO will begin operations in the second quarter of 2007, and will facilitate sharing of enforcement information across main US markets. NASD already regulates Nasdaq, the American Stock Exchange, the International Securities Exchange and the Chicago Climate Exchange. The details of this SRO combination are still being worked out, and after public comment will require SEC approval, but the SEC's chairman has expressed his "strong support" for the regulatory combination.

Also in December 2006, Nasdaq launched a hostile takeover bid for the London Stock Exchange Group (LSE). Nasdaq already owns about 28.75% of LSE, and needs to reach just over 50% for the acceptance condition of its bid to be met. After obtaining support from only 0.6% of LSE's shareholders, Nasdaq extended its offer from January 11 to January 26 2007, and can further extend the offer to February 10 2007. Nasdaq might be forced to raise its bid to succeed, or a rival suitor might appear.

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Energized European enforcement

European regulators are bringing headline-grabbing disciplinary and enforcement actions that seek substantial financial penalties from large business and financial services entities. In just over two years, Europeans have seen the UK Financial Services Authority (FSA) fine Shell £17 million and Citigroup £13.9 million, while the Dutch public prosecutor fined Ahold €8 million – amounts previously unheard of in European securities enforcement. This trend continued during 2006, with European regulators continuing to aggressively pursue large targets and seek substantial fines across a variety of cases, often with cooperation from, or parallel to, other European regulators and/or the SEC.

Trading cases

In December 2006, French police raided the Paris headquarters of European Aeronautic Defence & Space (EADS), parent of Airbus, and the offices of its French shareholder Lagardère, as part of an insider trading investigation by two French investigating judges. The inquiry involves alleged sales by EADS insiders in March before an April announcement that Lagardère and Daimler Chrysler would each sell 7.5% interests in EADS.

The FSA fined Europe's third-largest hedge fund manager, GLG Partners, £750,000 in August 2006, and separately fined a former GLG managing director £750,000 individually, for allegedly using confidential information about a Japanese company's upcoming offering of convertible preferred shares to have a GLG fund short sell the issuer's common shares. The Japanese Securities and Exchange Surveillance Commission assisted the FSA's investigation. In an unrelated matter, in late December 2006, it was reported that the French securities regulator, Autorité des Marchés Financiers (AMF), would fine GLG Partners €1.2 million for alleged trading abuses in connection with an Alcatel convertible bond offering, and would also fine Germany's largest bank, Deutsche Bank, €300,000 for alleged technical violations. GLG said it would appeal the AMF's decision. Commentators noted that this shows that regulators across Europe are talking to each other and taking the issue of banks' information flows seriously.

In April 2006, the FSA hit Deutsche Bank with a £6.3 million fine for allegedly giving instructions for proprietary trading at a sensitive time during a book build in shares of Scania, a Swedish company, that prevented investors from fully understanding the nature of supply and demand for the Scania shares, and for allegedly making incomplete or inaccurate announcements about the Scania transaction. Deutsche also allegedly conducted a stabilization of Cytos shares on the Swiss SWX exchange through a trader in Zurich. The FSA also fined Deutsche's former

head of European trading £350,000 individually in connection with the Scania transaction.

In December 2005, the FSA fined a finance director of Cambrian Mining £25,000 for allegedly buying Cambrian shares on two occasions when he had non-public information. Had he sold the shares after the information was announced, which he did not, he would have had an imputed profits totalling £6,400 – meaning that the fine was three times the amount of a hypothetical profit, a particularly aggressive approach even by SEC standards.

Corporate disclosures

In June 2006, investigators from the AMF, the French securities regulator, raided the offices of EADS in Paris as part of an investigation of the timing of disclosures concerning delays in production of the new Airbus super jumbo airliner. French police raided the EADS offices in December 2006, meaning that EADS experienced this tactic on securities regulatory matters twice in one year.

In August 2005, the FSA won jury verdicts convicting two individuals for "recklessly" making a misleading, false or deceptive statement concerning turnover and profit at their company. This was the FSA's first criminal action, and the FSA's enforcement director commented that it demonstrates the FSA's "willingness and capability" to prosecute criminal charges for securities violations. Recklessness will not support criminal securities fraud charges in the US (prosecutors must prove intent) and the SEC may not itself prosecute criminal charges, a power reserved to the US Justice Department.

Internal controls/books and records

In August 2006, the FSA fined clearing firm The Kyte Group £250,000 for alleged systems and controls failures resulting in inadequate client money protection and poor accounting systems. The FSA noted Kyte's cooperation and remedial action to improve systems and controls. The same month, the FSA fined Merrill Lynch International £150,000 for alleged transaction reporting failures that showed its status as agent rather than principal. In March 2006, the FSA fined Capita Financial Administrators £300,000 for poor antifraud controls over client identities and accounts that allegedly contributed to actual and attempted frauds against the firm's customers.

Retail sales cases

In August 2006, the FSA obtained a High Court order for liquidation of Securetrade & Title Company after it allegedly assisted overseas boiler room activities. In September 2006, the FSA fined Braemar Financial Planning £182,000 in a matter challenging the suitability of advice to certain pension investors. The FSA said that, but for Braemar's cooperation, "the fine imposed would have been substantially higher," and noted that Braemar qualified for a 30% discount for settling early.

"Europeans might consider approaches more often used in SEC matters"

Questionable payments cases

In November 2006, more than 200 German police raided offices and homes of Siemens employees in an investigation of alleged commercial bribery. Officials in Italy and Switzerland are conducting parallel investigations. Noting that the SEC and the US Justice Department could begin their own investigations, Siemens appointed a US law firm to conduct an independent investigation of the company's financial controls.

Powerful new enforcement bodies

The increasingly vigorous securities enforcement now being experienced across Europe has followed the recent creation of new European securities regulators. These new European regulators, cast in the US model, are already well beyond where the SEC was in its evolution until fairly recently. The SEC did not get authority to impose substantial penalties and to bar officers and directors until 1990, and it really only began taking these powers to their limits after the Enron collapse in late 2001. The new European regulators will have an easy time catching up with the SEC's current programme in the present environment, and European regulators have some powers that already exceed the SEC's.

United Kingdom

The Financial Services and Markets Act 2000 (the FSMA) authorized the newly established FSA to act as an independent regulatory body financed by the financial services industry, but accountable to HM Treasury and ultimately parliament. The FSA has extensive investigative powers to identify potential violations, and can also carry out investigations for foreign regulators. If it considers enforcement proceedings warranted, it will make a recommendation to the Regulatory Decisions Committee (RDC), a body consisting of financial services professionals, which then decides whether to accept the recommendation and commence proceedings. A firm or individual can have the RDC's determination reviewed *de novo* by the Financial Services and Markets Tribunal, a separate body run by the Department of Constitutional Affairs. The FSA has a discount programme to encourage early settlements.

The FSA can bring civil cases in the UK courts and seek remedies similar to those ordered by the US courts in cases brought by the SEC – injunctions against future violations and restitution orders providing for disgorgement of illegal gains or compensation of victims for their losses. However, unlike the SEC, the FSA can also bring criminal cases. Criminal penalties can include a fine and imprisonment up to seven years. The FSA can also ask the court in civil proceedings for an asset freeze; for a winding-up order that will put a firm out of business, even if the firm is not technically insolvent; and for disposition of an individual's assets through a bankruptcy order. In April 2005, the FSA appointed Margaret Cole, formerly a London partner of a US law firm, as its new director of enforcement.

France

In 2003, the Financial Security Act established the Autorité des Marchés Financiers, an independent public body whose members must comprise specified numbers from particular backgrounds (judicial, legal, financial, accounting and labour) to ensure a full range of relevant competencies. The AMF staff investigates a matter and can, with court approval, enter premises and seize documents, a power that the SEC lacks. The staff sends its report to the AMF Board, which independently decides whether to start a sanction proceeding. If it does so, it serves the staff's investigation report on the defendant and provides access to the underlying evidence. A member of the Enforcement Committee hears witnesses and prepares an independent report, which then goes to the defendant for a written response. The case then goes to the full Enforcement Committee (or a division of the Committee) for arguments and decision. Throughout, the defendant has the right to assistance from counsel.

AMF sanctions include a fine that can run (both for individuals and entities) as high as €1.5 million or 10 times the amount of unlawful profits earned. If a matter involves regulated persons or entities, the AMF (like the SEC) may reprimand them or temporarily or permanently bar them from engaging in business. If an offence might be criminal, the AMF refers the matter to the Paris public prosecutor and, unlike the SEC, the AMF may itself act as the complaining party in criminal cases.

Germany

In 2002, Germany combined securities, banking and insurance supervision into a new supervisory and regulatory body, the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin), with authority to enforce rules pertaining to insider trading, money laundering, company disclosures, investment services firms, price and market manipulation, directors' dealings and dissemination of false information. BaFin can itself prosecute some cases as administrative matters, and sanctions for violations include fines of up to €1.5 million. More serious offences must be referred to the Public Prosecutor's Office for criminal prosecution. Conviction of a criminal offence can result in imprisonment for up to five years or a fine.

EU enforcement directives

Europe is undergoing convergence in securities regulation. EU Directive 2003/6/EC (the Market Abuse Directive) required that, by October 12 2004, EU member states have legislation prohibiting, among other things, insider trading, market manipulation, an issuer's selective disclosure of information likely to have a price impact, an issuer's unjustified delay in publicly disclosing information, and management's failure to publicly disclose personal transactions in the issuer's shares. Although leaving some discretion to member states, the EU Directive specifies the elements of each of these offences. Also, EU Directive 2004/109/EC required that, by January 20 2007, member states have legislation ensuring transparency of information about issuers, including detailed disclosure requirements relating to issuers' financial condition and large shareholdings.

The Market Abuse Directive requires that each EU member state have a regulatory body with all necessary supervisory and investigatory powers, including the right to: (i) obtain copies of documents; (ii) demand information, and summon and hear witnesses; (iii) conduct on-site inspections; (iv) obtain phone and data traffic records; (v) require cessation of violating conduct; (vi) suspend trading; (vii) request asset freezes and sequestration; and (viii) request temporary professional suspensions. This EU directive on a securities regulator's powers mirrors benchmarks established in 1998 by the International Organization of Securities Commissions (Iosco) in its "Objectives and Principles of Securities Regulation". Iosco includes securities regulators in 108 jurisdictions that regulate over 90% of the world's securities markets, so its positions reflect sentiment well beyond Europe.

To ensure effective cross-border enforcement, the Market Abuse Directive requires regulators to "cooperate with each other whenever necessary"; "exchange information and cooperate in investigation activities"; and "on request, immediately supply any information required". Information so obtained can be used in administrative and judicial proceedings. If a regulator in one member state learns that conduct violating the directive is occurring in another state, it must promptly notify the regulator in that state. A regulator in one state may request another state to conduct an investigation, and may ask that its own personnel accompany the other regulator in conducting that investigation.

"What begins as a local investigation could soon morph into parallel investigations, with the possibility of harsher sanctions"

The Committee of European Securities Regulators is preparing its second set of guidance on regulators' "common understandings" after two years of experience under the Market Abuse Directive. CESR held hearings in Paris in October 2006, and time for public comment on its draft guidance closes on February 2 2007. Although acknowledging that "there are still some delays" in enacting the Directive into member states' laws, CESR is pushing forward for "convergent implementation and application" of the Directive, and has established a permanent operational group of member states' enforcement representatives to enhance cross-border cooperation and "make information flow across borders between CESR members as rapidly as it would internally".

Cross-border cooperation will be vital for European regulation of investment firms, especially large financial conglomerates that passport their services through direct cross-border dealings or through branches in multiple EU member states. The Markets in Financial Instruments Directive (Mifid, to be implemented by April 30 2006), which aligns national rules on investment services and exchange operations to permit passporting, provides that regulators "shall cooperate with each other whenever necessary" and "shall exchange information ... in any investigation or supervisory activities". Mifid also provides for cooperation with regulators outside Europe. Given the general increase in the provision of passported financial services, it is likely that regulators will increasingly engage in pan-EU enforcement actions.

Most European securities regulators (and the SEC and other regulators outside Europe) have by now signed Iosco's "Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information," adopted in 2002, that commits signatories to provide "the fullest assistance permissible" to foreign regulators – even where the conduct in question would not violate local law. This MOU provides for assistance in obtaining: (i) information and documents; (ii) records to reconstruct securities and derivatives transactions; (iii) identities of beneficial owners and participants in transactions; (iv) identities of persons who beneficially own or control entities organized in the regulator's jurisdiction; and (v) statements and testimony, if necessary under compulsion. Iosco's multilateral MOU builds on an existing network of bilateral MOUs, over 30 of which include the SEC, as well as CESR's own multilateral MOU adopted in 1999. The SEC recently reported that its requests to foreign regulators climbed to 561 in fiscal 2006, up from 438 the year before, and foreign regulators asked the SEC's assistance on 353 occasions, up from 315.

The "new generation of cooperation"

On March 14 2006, the FSA and the SEC entered into an MOU that the director of the SEC's Office of International Affairs, Ethiopis Tafara, called "a new generation of cooperation between securities regulators". Where previous MOUs dealt largely with case-specific information requests and technical assistance, this new MOU is focused more broadly on market oversight and the supervision of financial services firms, and is intended to respond to "the growing globalization of the world's financial markets and the increase in cross-border operations and activities of financial services firms, including large complex financial conglomerates". But "while information is not to be gathered under the auspices of this MOU for enforcement purposes," the regulators recognize that "subsequently [they] may want to use the information for law enforcement ... including in conducting investigations or bringing administrative, civil or criminal proceedings," and this is possible after first seeking consent from the other regulator.

Among other things, this new FSA-SEC MOU provides for: (i) advising of "any material event that could adversely impact" the other regulator's markets or stability of a firm in its jurisdiction, including "changes in the operating environment, operations, management, or systems and controls"; (ii) upon request, sharing information about a firm's "capital structure, liquidity and funding profiles, and internal control procedures"; (iii) also sharing "interim and annual financial statements; information drawn from regulatory reports and filings; early warning notices that a firm is required to submit ...; and information drawn from examination reports"; (iv) routinely exchanging inspection reports of investment advisers, investment fund managers, fund administrators, fund trustees, investment companies and investment funds that are regulated by both the SEC and FSA (dually regulated); and (v) permitting and assisting each regulator to conduct on-site inspections in the other regulator's country of entities that are headquartered in the requesting regulator's country or that are dually regulated.

Cross-border clout

Both the EU and the SEC have thrown their full weight behind cross-border cooperation and enforcement. Increasingly, securities enforcement investigations and cases will be multijurisdictional efforts that will require companies and individuals to respond to two or more national regulators. As regulators proceed down this road, the challenge will be to balance national interests and preference for familiar enforcement approaches with a frank appreciation for the demands of global trading and markets.

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