

BAWe

Bundes-
aufsichtsamt
für den
Wertpapier-
handel

Annual Report 1998

Abridged English Version

ANNUAL REPORT 1998

Preliminary Remarks

The Federal Securities Supervisory Office (Bundesaufsichtsamt für den Wertpapierhandel, BAWe) is an independent superior federal authority within the ambit of the Federal Ministry of Finance. The BAWe is located in Frankfurt am Main and has its legal basis in the Securities Trading Act (Wertpapierhandelsgesetz) and the Prospectus Act (Verkaufsprospektgesetz).

In the year under review a major focus was placed on the improvement of investor protection. Consequently, on 1 January 1998, the BAWe's range of responsibilities was extended to cover a large number of firms operating in the capital market which had hitherto not been supervised or had been supervised only in accordance with the provisions of the Commercial Code. These firms, defined as financial services providers, include primarily investment brokers and portfolio managers. The extension of the BAWe's supervisory powers results from an amendment of the Securities Trading Act made to further implement the European Investment Services Directive. Through this amendment a deficiency in the German regulatory regime was eliminated which had caused investors considerable financial losses in recent years.

Further improvements with regard to investor protection were introduced through the Third Financial Market Promotion Act which came into effect on 1 April 1998. The core elements of the Act were further amendments to the Exchange Act and the Securities Trading Act, the

Prospectus Act, the Investment Companies Act, and the Equity Investment Companies Act. Due to the changes in the Prospectus Act and the Securities Trading Act the supervisory and investigative powers of the BAWe were extended.

Another important aspect of the BAWe's efforts in 1998 was the further development of international co-operation with foreign securities supervisory authorities. In the context of cross-border alliances of European stock exchanges as well as pan-European IPOs the international element of securities supervision is gaining relevance. Along with this development the BAWe signed several agreements on the mutual exchange of information. In early 1999, a multilateral Memorandum of Understanding on the exchange of information and the surveillance of securities activities was signed by the members of the Forum of European Securities Commissions (FESCO). Also, the BAWe actively participated in the work of the International Organization of Securities Commissions (IOSCO).

Investor Protection – Rules of Conduct

In coherence with the BAWe's objective to improve investor protection, the rules of conduct set forth in the Securities Trading Act are of major importance. These regulations not only aim at the fair treatment of investors by investment services providers and credit institutions but also play a major role to sustain the integrity of the securities markets.

On 12 December 1998, the BAWe issued guidelines on the „Organisational requirements of investment

services enterprises“ („Compliance Guidelines“). Their aim is to guarantee the fair treatment of customers by credit institutions. The guidelines set out in detail the credit institutions' compliance duties.

According to the guidelines, credit institutions must effect their investment services with care, diligence and expert knowledge in the interest of their customers. They have to ensure that when unavoidable conflicts of interests occur the interests of the customers are guaranteed. The guidelines oblige the credit institutions to have in place adequate means and methods to continuously monitor the orderly provision of investment services. The organisation and internal procedures must be in line with the size, business activities and structure of the respective credit institute. The measures taken in this respect are to be documented and incorporated in the internal regulations.

Credit institutions that regularly have access to sensitive information are required to take additional measures. The BAWe considers the creation of areas of confidentiality („Chinese walls“) as well as watch lists and restricted lists to be suitable measures. The flow of information across Chinese walls is to be reduced to the absolute minimum. Furthermore, an independent compliance entity must be set up which is directly responsible to the executive management.

Investor Protection – Deposit of Prospectuses

Comprehensive information on the prospects and risks of investments are a substantial element of investor protection. To provide this informa-

tion the Act on the Prospectus for Securities Offered for Sale (Prospectus Act) requires persons offering securities that are not admitted to trading on a domestic stock exchange to publish a prospectus prior to the first public offer. To ensure compliance with the Prospectus Act a copy of the prospectus is to be deposited with the BAWe. Due to an amendment by the Third Financial Market Promotion Act the BAWe, as of 1 April 1998, no longer only acts as a depository but is also responsible for examining the prospectuses as to their completeness.

As of the fourth quarter of 1998, the BAWe strongly concentrated on initial placements of shares via the Internet addressed to German private investors. In conducting these investigations the BAWe traced seven offers which were not in accordance with the deposition and publication requirements. While the BAWe encourages the use of new media, investor protection will remain the most important regulatory concern. To the extent that securities are

offered directly to private investors through advertising on the Internet, the BAWe will consider this as a public offer. The party making the offer is thus obliged to publish a prospectus after having deposited it with the BAWe. It is irrelevant whether a print medium or an electronic medium such as the Internet is used for advertising purposes. The BAWe will foster its efforts in scrutinising the Internet and therefore co-operate with foreign securities supervisory authorities.

Market Integrity – Prohibition of Insider Trading

Equal access to price-sensitive information is an essential precondition for investors' confidence in the integrity of the securities and derivatives markets. Hence, the prohibition of insider trading which does harm to this confidence is of utmost importance.

To enforce the prohibition of insider trading the BAWe, in 1998, investigated a total of 67 cases in which unlawful insider trading was suspec-

Insider investigations of the BAWe

	Number of investigations		Investigations concluded in the period under review			Open investigations at the end of the period under review
	Newly taken up in the period under review	Open at the start of the period under review	Total	Result of the investigations		
				Discontinued	Passed on to a Public Prosecutor's Office	
1995	24	0	23	16	7	1
1996	59	1	44	27	17	16
1997	55	16	62	40	22	9
1998	58	9	37	21	16	30
Total 1995-1998	196	◇	166	104	62	◇

◇: figures are not applicable

ted. The facts of 16 investigations were reported to the competent public prosecutor's office; there were convictions in four cases. In 13 other cases the public prosecutor discontinued the investigative proceedings after the defendants had paid civil penalties – of up to DM 150,000 – to charitable organisations and the public treasury.

Since 1 January 1996, all transactions in securities and derivatives must be reported electronically to the BAWe. Reports must be made by credit institutions, brokers and, as of 1 February 1998, by investment services institutions with the permission to conduct proprietary trading. Also firms domiciled abroad and admitted to trading on a German stock exchange are subject to the reporting requirements in respect of the transactions they carry out on German exchanges. In the year under review, some 215 million reports were submitted to the BAWe. Compared to 1997, this

represents an increase of about 74 per cent and corresponds to an average of about 855,000 reports per trading day (1997: 492,000).

The rapid growth of reports is caused, inter alia, by the increased number of foreign participants of the stock exchanges. Since September 1998 the derivatives exchanges Eurex Deutschland and Eurex Zurich – the successors of the Deutsche Terminbörse (DTB) and Swiss Options and Financial Futures Exchange (SOFFEX) – have operated the common derivatives trading platform Eurex. Consequently, the former participants of SOFFEX are now obliged to report to the BAWe, as well as former SOFFEX products now being subject to German reporting requirements.

Market Transparency – Ad hoc Disclosure

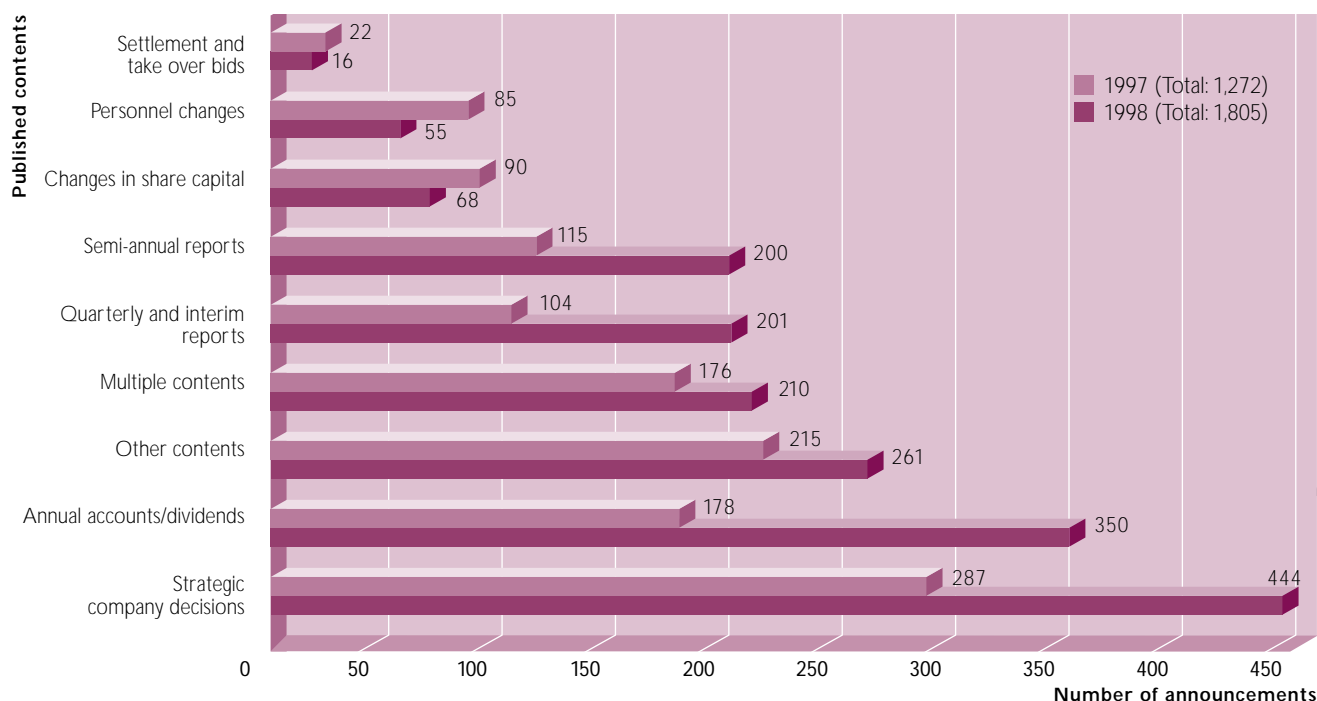
In order to guarantee equal and fair access to information, listed compa-

nies are required under the Securities Trading Act to immediately disclose any new, non-public, potentially price-sensitive information (ad hoc disclosure). In the period under review, a total of 1,856 such ad hoc disclosures were published (1997: 1,279), 1,805 (1,272) of them by German issuers.

Approximately 97 per cent of the ad hoc disclosures were published electronically, the others in journals for statutory stock market announcements. On its Internet website, the BAWe offers a variety of links to providers of ad hoc disclosures. Various television stations also provide ad hoc information via video text. The information advantage of professional investors which had caused inequalities in the past has, to a certain extent, been eliminated.

In June 1998, the second edition of the guidelines „Insider Trading Prohibitions and Ad hoc Disclosure

Contents of ad hoc announcements published by German issuers 1997 – 1998



Pursuant to the German Securities Trading Act" was published. The brochure includes explanations and recommendations for the treatment of potentially price-sensitive information. It can be downloaded from the BAWe website.

Market Transparency – Disclosure of Major Shareholdings

Transparency of the securities market is also achieved by the obligation to publish changes in major holdings of voting rights in officially listed companies. The BAWe maintains on its Internet website a database of voting rights in German listed companies. By the end of 1998, approximately 600 domestic and foreign companies had been officially listed on German stock exchanges. The data, which are also available in English, can be downloaded from the BAWe website, thus easily providing investors with up-to-date information on the major holdings of voting rights. In 1998, 605 notifications concerning changes in voting rights were made.

Co-operation in Germany

With the implementation of the Investment Services Directive and the Capital Adequacy Directive of the European Union, the co-operation between the national supervisors of the German financial market was reinforced.

From 1 January 1998, financial services institutions, such as investment brokers and portfolio managers, require the authorisation of the Federal Banking Supervisory Office (Bundesaufsichtsamt für das Kreditwesen, BAKred); until then, this regulation applied to credit institu-

Distribution of tasks between BAKred and BAWe

Federal Banking Supervisory Office – BAKred	Federal Securities Supervisory Office – BAWe
<ul style="list-style-type: none"> ◆ Licensing of institutions and termination of licenses ◆ Investigation of the reliability and suitability of company management ◆ Control of shareholders ◆ Controlling the financial situation of institutions, including their liquidity and profit situation ◆ Prosecution of unlawful financial services and banking transactions ◆ International co-operation in banking supervision 	<ul style="list-style-type: none"> ◆ Supervising rules of conduct and organisational duties ◆ Depositing prospectuses ◆ Investigating insider trading ◆ Supervising ad hoc disclosure ◆ Supervising publication in case of changes in major holdings of voting rights ◆ International co-operation in securities and stock exchange supervision

tions only. Whereas the BAKred is mainly concerned with fitness and licensing matters as well as with solvency and risk control the BAWe concentrates on market supervision. Irrespective of whether the firms provide investment services alone or in connection with non-core investment services, they will be supervised within the range of the BAWe's market oversight activities, in particular with regard to compliance with the rules of conduct.

International Co-operation

Under the Securities Trading Act the BAWe is granted comprehensive powers as regards co-operation with competent foreign supervisory authorities. In 1998, the BAWe made use of the power to exchange information primarily in insider investigations, making a total of 20 enquiries being addressed to such authorities. In return, the BAWe was able to assist foreign supervisory authorities in 11 cases.

Since the implementation of the Investment Services Directive and

the Capital Adequacy Directive on 1 January 1998, German firms have had the opportunity to use the „European passport“. On the other hand, investment services providers in other countries of the European Union have the possibility to provide services to German investors. In 1998, the BAWe received notifications from 98 foreign companies (1997: 108) which intended to provide cross-border investment services or, in nine cases, to set up a branch in Germany.

In December 1997, European regulators founded the Forum of European Securities Commissions (FESCO). FESCO members are the securities supervisory authorities of the fifteen Member States of the European Union as well as those of Iceland and Norway as Contracting States to the Agreement on the European Economic Area. The goal of the new organisation is to improve investor protection, increase market transparency, and ensure market integrity. In the light of the ongoing integration of the European financial markets and the introduction of the Euro,

European passport notifications						
Country	Notification of cross-border services to be introduced			Notification of branch openings		
	1996	1997	1998	1996	1997	1998
Austria	–	–	4	–	–	–
Belgium	–	–	6	–	–	–
Denmark	5	3	–	–	–	–
Finland	–	–	1	–	–	–
France	1	29	5	–	–	1
Great Britain	618	54	57	2	1	6
Ireland	33	3	6	2	–	1
Italy	–	1	1	–	–	–
Luxemburg	–	–	1	–	–	–
Netherlands	20	5	2	1	–	–
Norway	–	8	5	–	–	–
Sweden	13	2	–	–	–	1
Spain	–	2	1	–	–	–
Total	690	107	89	5	1	9

these principles are of particular importance and FESCO provides the appropriate institutional frame for maintaining them. In May 1998, the president of the BAWe, Georg Wittich, was elected chairman of FESCO.

The BAWe actively developed its co-operation on an international level in 1998. To this end, the BAWe signed agreements on the mutual exchange of information with the securities supervisory authorities of Australia, Hong Kong, Hungary, Portugal, China, Argentina and the Czech Republic. With the Swiss securities regulator, the Eidgenössische Bankenkommision, an exchange of letters took place in September 1998, granting close co-operation between the two regulators. In respect of the newly established cross-border trading platform Eurex, the Swiss-German

exchange of letters is of particular importance.

For questions of multilateral co-operation the International Organization of Securities Commissions (IOSCO) represents the most important forum. The BAWe participates in all IOSCO committees where German interests are concerned.

BAWe – Internal Affairs

In order to fulfil its extended supervisory tasks the BAWe was equipped with 40 additional positions. At the end of 1998, the BAWe's personnel reached a total number of 132.

Due to the extension of its tasks and the corresponding increase in staff the BAWe's expenditures rose to approximately DM 17.3 million in 1998 (1997: 13.8m). Personnel costs

amounted to DM 7.7 million (1997: 6.9m), and material costs and investments amounted to DM 9.6 million (1997: 6.9m) of which DM 5.5 million (1997: 3.7m) were spent on information technology. Ninety percent of the BAWe's costs are to be reimbursed to the Federal Republic of Germany by market participants and issuers.

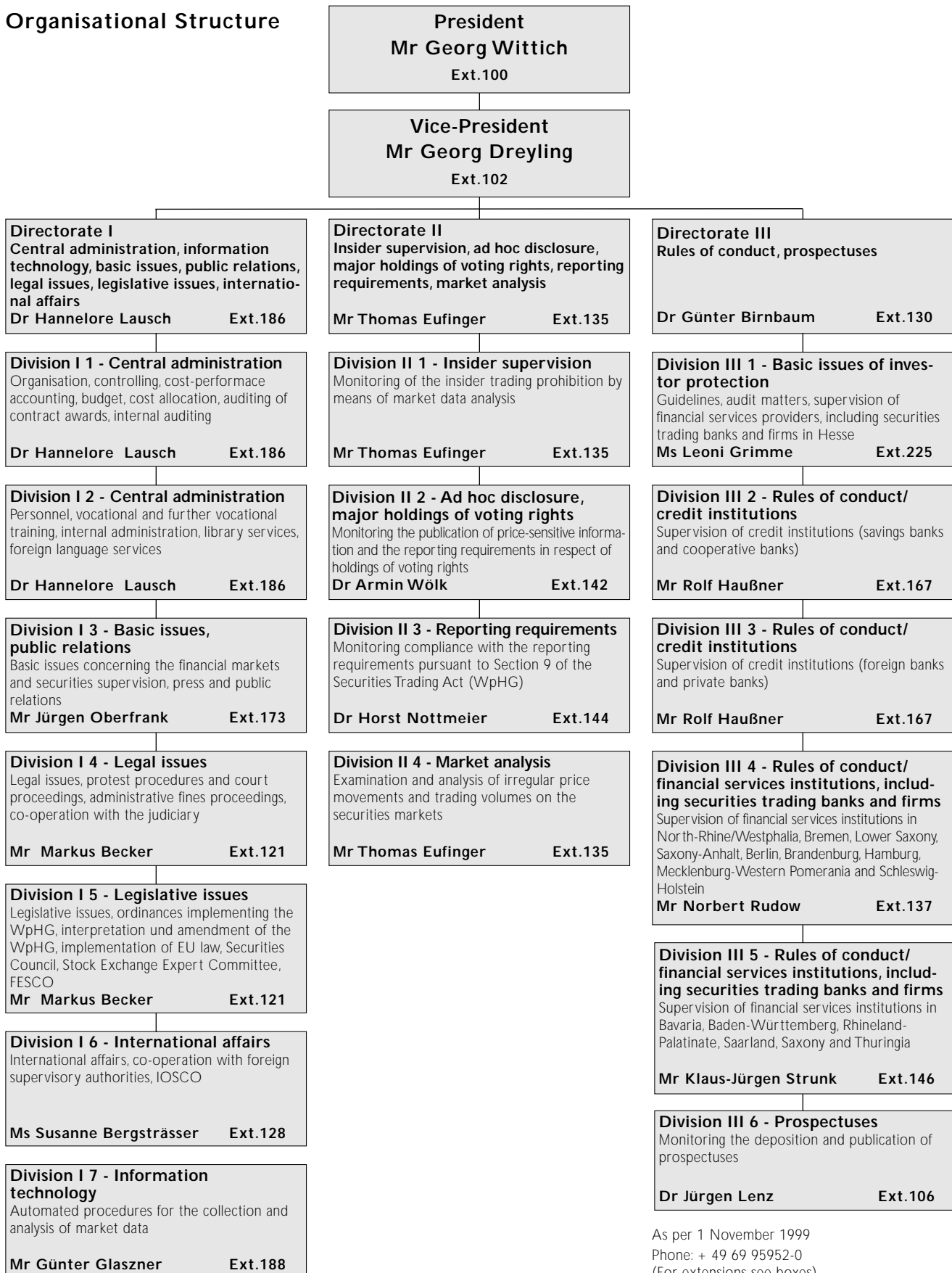
Since the beginning of 1997, the BAWe has maintained its own Internet home page (www.bawe.de) with the goal of directly informing the public of all its activities. Most of the information is also available in English.

Perspectives

With the introduction of the Euro as the single European currency and the implementation of the Investment Services and Capital Adequacy Directives the creation of a genuine European market for financial services has become a priority. By making use of their European passport, investment services enterprises are allowed to offer cross-border services and open branches everywhere in the European Economic Area without being subject to any further admission procedures in the host country.

Moreover, cross-border co-operation and alliances of European stock exchanges as well as pan-European offerings are promoting the integration of the European financial markets. These developments pose a great challenge for the supervisory authorities in Europe. In this context, the BAWe is willing and able to fulfil its duties in line with the principles of securities supervision.

Organisational Structure



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(For extensions see boxes)

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