

# BAWe

Bundes-  
aufsichtsamt  
für den  
Wertpapier-  
handel

## Annual Report 1999

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### **Bundesaufsichtsamt für den Wertpapierhandel**

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In implementing the Securities Trading Act (Wertpapierhandelsgesetz; short: WpHG) and establishing the Federal Securities Supervisory Authority (Bundesaufsichtsamt für den Wertpapierhandel; short: BAWe) more than five years ago, the legislator has established the legal and organisational basis for enhancing the proper functioning and the attractiveness of the German financial markets through new regulatory standards. The reform of the supervisory system was intended to provide a reliable framework for securities trading, and at the same time to make a positive contribution to improving the German equity culture.

The positive effects of the new supervisory system have become clearly evident, not least thanks to the BAWe's close co-operation with investment services enterprises, exchanges and listed companies. The continuous increase in the number of ad-hoc announcements from listed companies has played a par-

ticular role in improving market transparency. The prompt publication of price-relevant information about companies enables the market participants to take more knowledgeable investment decisions, and in addition represents a particularly effective tool in preventing insider transactions. In-house monitoring systems assist the BAWe in combating insider trading, with the aim of boosting investor confidence in the integrity of the German financial markets.

Private investors continued to show a growing interest in purchasing shares in 1999. The reasons behind this development included the favourable performance of the stock markets, the comprehensive range of services offered by online banks, and the large amount of initial public offerings, especially of growth stocks in the Neuer Markt. This has created new areas of emphasis for securities supervision in Germany. Of particular interest were issues like the provision, in accordance with the WpHG, of information relating to the allotment criteria which are adopted when an initial public offering is oversubscribed, and the arrangements to be made by online banks with respect to their personnel and technical equipment in order to guarantee a sufficient degree of availability for customers. Moreover, the BAWe felt compelled to improve the protection of German investors by prohibiting the unsolicited making of telephone calls (cold calling).

The introduction of the euro and the liberalisation of investment services have provided a unique basis for the integration of Europe's capital markets. It is the aim of the European securities supervisory authorities comprising the Forum of European Securities Commissions (FESCO) to actively promote the creation of a homogeneous European capital market through close co-operation and the adoption of common regulatory standards. Participation in the comprehensive tasks of FESCO has been an area of major emphasis for the BAWe within the scope of international co-operation.

The efforts made in regard of a convergence of the European capital markets are reflected in the existing and announced cross-border alliances between European exchanges. The securities supervisory authorities concerned will be responsible for establishing, in close co-operation, the regulatory basis for the realisation of such alliances between exchanges.

Georg Wittich  
President  
Bundesaufsichtsamt  
für den Wertpapierhandel

# INVESTOR PROTECTION – RULES OF CONDUCT

Investor protection is an indispensable prerequisite for investors' confidence in the financial markets. The rules of conduct for investment services enterprises set out in the Securities Trading Act (Wertpapierhandelsgesetz; short: WpHG) play a central role in providing this protection. They shall ensure the fair treatment of investors and enable them to independently take their own investment decisions. Investment services enterprises are thus required to provide comprehensive information about the features, costs, and risks of an investment. Moreover, they must comply with extensive organisational duties in order to avoid conflicts of interest, and be able to provide qualified professional service. Monitoring investment services companies' compliance with the rules of conduct is one of the core responsibilities of the BAWe.

## Supervision of Investment Services Companies

The BAWe monitors compliance of investment services companies with the rules of conduct and the reporting requirements for transactions in securities and derivatives. The term investment services com-

panies comprises all credit institutions, financial services institutions and branches of firms whose registered office is outside Germany, and which provide investment services alone or in connection with non-core investment services on a commercial basis or to an extent that requires their provision on a commercial basis. Credit institutions are enterprises which conduct banking business. Financial services institutions are enterprises which provide financial services. Banking business which is also an investment service includes financial commission business and underwriting business. The list of financial services which constitute an investment service but cannot be classified as banking business include investment brokerage, contract brokerage, portfolio management, and own-account trading.

Regular annual examinations of the investment services companies shall help to monitor compliance with the rules of conduct. Also examined in this context is the companies' compliance with the obligation to report to the BAWe all on- and off-floor transactions in securities and derivatives. The enterprises as a rule appoint their own auditors, which enables them to carry out the examination in the framework of their year-end audit. In order to ensure efficient supervision, the BAWe has been granted certain powers concerning the selection of the auditor

### Investment services enterprises include

- ◆ Credit institutions
- ◆ Financial services institutions and
- ◆ Branches of a company domiciled abroad which provide investment services alone or in connection with non-core investment services on a commercial basis or to an extent that requires their provision on a commercial basis.

and the execution of the audit. For example, the BAWe may demand the appointment of a different auditor if this appears necessary with respect to achieving the aim of the examination. In addition, the BAWe may determine the contents and areas of emphasis of an examination, which have to be observed by the auditor. The BAWe may even participate in an examination if it wishes to assess the situation and discover any irregularities on the spot. In the period under review, the BAWe in 94 cases participated in examinations of financial services institutions, in order to receive an overview of the nature and scope of activity of these companies, which have been regulated only since the beginning of 1998. In individual cases the BAWe may request for an examination to be carried out by the supervisory authority itself or by a person it has appointed. Furthermore, the BAWe may always seek information and demand the submission of documents and carry out its own examination at any time during the year without any particular reason.

The auditor must prepare a separate report on his examination of the rules of conduct and reporting requirements and submit it immediately to the BAWe. Moreover, he is obliged to immediately notify the BAWe of serious offences against the provisions of the WpHG. This notification is essential for the BAWe to fulfil its regulatory tasks, enabling it to react without delay to any irregularities observed. If it identifies persistent breaches of the provisions of the WpHG the BAWe informs the BAKred about the results of the examination. The BAKred will take its own regulatory action against the respective com-

#### **Investment services:**

- ◆ Financial commission business: the purchase and sale of securities, money-market instruments or derivatives in one's own name or for the account of a third party;
- ◆ Own-account trading: the purchase and sale of securities, money-market instruments or derivatives by way of own trading on behalf of a third party;
- ◆ Contract brokerage: the purchase and sale of securities, money-market instruments or derivatives in the name and for the account of a third party;
- ◆ Investment brokerage: the arrangement of or information on transactions on the purchase and sale of securities, money-market instruments or derivatives;
- ◆ Underwriting business: the underwriting of securities, money-market instruments or derivatives or the granting of similar guarantees;
- ◆ Portfolio management: the management of individual assets invested in securities, money-market instruments or derivatives on behalf of third parties with scope for decision.

panies. In several cases this has resulted in the revocation of a license, with one of the reasons stated being an infringement of the WpHG.

In its Ordinance on the Examination of Investment Services Enterprises of 06 January 1999 the BAWe passed detailed provisions concerning the nature and scope and the timing of the regular annual examinations carried out with investment services companies. The BAWe requires the auditor to comply with uniform minimum requirements as regards the contents of the examination report and to fill in a questionnaire stating the results of the examin-

ation. By setting up minimum content requirements the BAWe makes sure to receive homogeneous audit documents. The questionnaire permits the BAWe to identify problematic cases at a single glance and to analyse the examination reports according to priority. This makes it possible to take the necessary measures to remedy defects without delay.

#### **Examination of Financial Services Institutions**

At the end of 1999 approximately 1,500 financial services institutions were subject to supervision by the

#### **Non-core investment services:**

- ◆ Safekeeping and management of securities on behalf of third parties, provided the German Safe Custody Act (Depotgesetz) is not applicable;
- ◆ Granting of credits or loans to others for the purpose of carrying out investment services by the enterprise that grants or has granted the credit or loan;
- ◆ Giving of advice with respect to investments in securities, money-market instruments or derivatives;
- ◆ Foreign exchange transactions or forward exchange transactions that are related to investment services.

BAWe. Added to this came some 700 companies which acted as agents exclusively for account and on behalf of investment services enterprises. These companies are indirectly subject to supervision by the BAWe because their activities are considered to be belonging to the respective investment services enterprises. Due to the introduction at the start of 1998 of the obligation to obtain a license for the provision of financial services, and the resultant legal requirements, many companies have either suspended their activities or are now providing services that do not require a license.

In 1999 the emphasis of activities was placed on analysing the initial examinations carried out with financial services institutions. Particular attention was paid to the obligation to provide proper information about the relevant costs and fees, and on pricing agreements with other companies (kick-back agree-

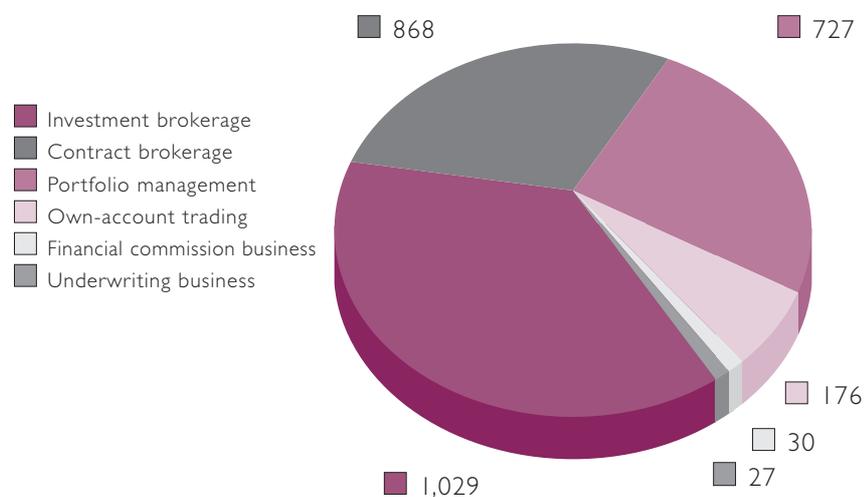
ments or agreements about commissions charged by brokers for keeping securities on behalf of a customer). The obligation to inform customers of the respective costs and fees forms an essential part of compulsory customer information. Furthermore, due to possible conflicts of interest customers must be informed about kick-back agreements and agreements with third parties on commissions charged for the keeping of securities on behalf of a customer. In addition to this general area of interest, in 45 cases the BAWe set up individual examination criteria tailored to the specific nature and scope of activity of the respective entities under examination. This made it possible to adjust the scope of the examinations on a case-by-case basis and detect possible weak points of each individual company.

An analysis of the examination reports revealed that compliance with the rules of conduct of financial ser-

vices institutions was insufficient in some areas. Many complaints concerned shortcomings in seeking information about customers' financial circumstances, investment experience and investment goals, and the required provision of adequate information about the planned investment. In many cases the financial services institutions did not possess the appropriate means for ensuring compliance with the rules of conduct and handling the flow of sensitive information within the company, while avoiding conflicts of interest as far as possible. Other complaints concerned the record-taking requirements, in particular the obligation to keep a record of the customers' orders and the corresponding instructions, as well as the name of the accounts manager receiving the order. In addition, in a large number of cases no record was kept of orders submitted to other investment services companies in the context of portfolio management, and of orders for own account. An analysis of the examination reports caused the BAWe to take regulatory action in 135 cases. Where an examination or analysis of examination reports revealed shortcomings in compliance with the rules of conduct or reporting requirements the company was required to remedy these shortcomings. If this was impossible or if a financial services institution did not follow the request the BAWe informed the BAKred, which in turn decides as to whether it should take action as well.

The regular annual examination of financial services companies by an auditor appointed by the company turned out to be particularly problematic. Especially smaller financial services institutions often failed to meet their obligations to appoint a

**Financial Services Institutions Including Securities Trading Banks: a Breakdown by Types of Business (As at 09 February 2000, Including Multiple Indications)**



### **Functional Approach to Supervision**

Investment services companies need to be licensed pursuant to the Banking Act (Gesetz über das Kreditwesen; short: KWG). The competent authority for granting the license is the Federal Banking Supervisory Authority (Bundesaufsichtsamt für das Kreditwesen; short: BAKred). Once they have been admitted, the enterprises are also subject to supervision by the BAWe. Regulation by the two authorities is based on a functional approach. The BAKred is responsible for licensing and solvency control. The supervisory tasks of the BAKred include checking the trustworthiness and professional qualification of the managers, and supervising on an ongoing basis the economic situation of the firms. The BAWe is responsible for market surveillance of the licensed companies. Whilst solvency control aims at ensuring the functioning of the financial system as a whole, market surveillance has the objective of immediate customer protection.

suitable auditor and carry out the examination in time. In several cases the BAWe therefore made use of its right to carry out the annual examination itself or appoint an auditor. In the year under review four such examinations were carried out.

Another regulatory instrument is the right to request an extraordinary examination without any particular reason. In the year under review the BAWe made use of this right if there were obvious indications of financial services institutions violating the rules of conduct. In 1999 the BAWe in 17 cases demanded for an extraordinary examination to be carried out, with one of the reasons being complaints from customers or hints from third parties.

### **Investor Complaints – Financial Services Institutions**

Customer complaints often provide important indications with regard to violations of the rules of conduct. They are helpful in detecting such violations or weak points in a company's organisational structure. In

1999 the BAWe received 144 written complaints about financial services institutions. Some of them concerned transparency or the amount of fees charged, or were related to shortcomings in the compulsory provision of customer information and the execution of orders. Very often customers complained about cold calling, i.e. the contacting of potential customers by means of unsolicited telephone calls. The BAWe regards this form of advertising as an irregularity in the sense of the Securities Trading Act. In cases of non-compliance with the rules of conduct or of organisational shortcomings, the BAWe made use of its right to carry out exceptional examinations or determine particular areas of interest in the examinations.

When dealing with complaints the BAWe acts exclusively in the public interest. As a result, it is not allowed to provide assistance to complainants suing for damages in a civil suit. The BAWe may neither act as an arbitrator nor give legal advice to the complainant. Where permissible, it will notify the complainant of the results of his or her request. However, the

duty to observe secrecy prohibits the BAWe from providing information about any measures taken on grounds of a complaint – for example an exceptional examination.

### **Guidelines for Financial Services Institutions**

In November 1999 the BAWe passed a new guideline on the details concerning the organisational duties of investment services enterprises. It replaced the guideline of 02 December 1998, which was identical in content but applied only to credit institutions, and extended its scope of application to financial services institutions regulated since the beginning of 1998. An analysis of the initial examination reports on financial services institutions revealed that smaller companies, including many financial services companies, need to establish only basic organisational structures (basic compliance). However, even these companies must make arrangements for the provision of securities services with care, expert knowledge and diligence in the interests of their customers. The particular requirements have to take account of the size, the type of business activities, and the structure of the respective investment services enterprise.

The guideline on the details concerning the organisational duties of investment services enterprises sets up important minimum standards ensuring compliance with the legal provisions. Beyond this, they leave sufficient scope for investment services companies to establish an organisational structure that provides for the proper execution of all business activities while avoiding conflicts of interest. As a rule, smaller

**Financial services institutions include**

enterprises which provide financial services and which are not credit institutions. The list of financial services which constitute an investment service but cannot be classified as banking business include

- ◆ Investment brokerage
- ◆ Contract brokerage
- ◆ Portfolio management and
- ◆ Own-account trading

companies do not usually possess compliance-relevant information (e.g. inside information). There is thus no need for them to introduce particular measures such as watch lists, restricted lists or Chinese walls. Neither is it necessary for such enterprises to establish a compliance office that monitors compliance with the organisational duties. Instead, this task may be carried out by a suitable staff member or carried out by the management itself. Where business is carried on by a sole proprietor, it may be appropriate and necessary to separate certain activities in order to comply with the legal requirements.

The general and particular rules of conduct which have been specified for credit institutions in the guidelines concerning the rules of conduct of 26 May 1997 are currently under review. In the light of the results of initial examinations carried out with financial services institutions, and the obvious difficulties in applying the act, the legal provisions are to be specified in particular with regard to the newly supervised enterprises and securities services. This measure aims at creating, according to the principle of "same business – same regulations", homogeneous standards for the provision of investment services by credit institutions and financial services institutions. An amended guideline relating to the commission

business, own-account trading and agency business of credit institutions has been published in July 2000 following final consultations with the associations of the companies concerned.

**Examination of Credit Institutions**

Private sector credit institutions are obliged to have their compliance with the rules of conduct pursuant to the Securities Trading Act examined by suitable auditors or accountancy firms. Savings banks are examined by auditors from the Savings Bank Associations, co-operative banks by auditors from the unions of co-operative banks.

The BAWe receives an examination report for each private-sector credit institution. The audit reports for savings banks and co-operative banks are requested from the competent auditors according to specific criteria. Whenever the analysis of previous reports, customer complaints, or indications from auditors, associations or other supervisory authorities have revealed indications of shortcomings the BAWe will demand submission of the relevant reports. In addition, the BAWe requests to be shown a certain number of audit reports even without having acquired knowledge of any particular shortcomings.

In the year under review the BAWe analysed 582 reports on credit institutions for the financial year 1998. In 394 cases further action was taken owing to shortcomings detected in the analysis. Of particular concern were questions regarding compliance with the rules of conduct and the corresponding guidelines concerning the rules of conduct.

The BAWe determined four general areas of interest for audits relating to the financial year 1998, which had to be examined with regard to each credit institution:

- ◆ How were customers informed about the conversion from DM to euro?
- ◆ How did the credit institution avoid delays in the execution of transactions when the volume of incoming orders was high?
- ◆ Has the enterprise geared its fixed-price business to market prices?
- ◆ Were customers always informed about the allotment procedures for new issues?

An analysis of the examination reports revealed that the credit institutions had thoroughly informed their customers even about the impact on securities transactions of the conversion from DM to euro.

In the year under review, the large number of incoming orders constituted a problem in particular for online banks. Usually the credit institutions attempted to handle the high order intake by creating additional capacities, in terms of both technical equipment and personnel.

Pursuant to Section 33 WpHG and no. 2.2. of the guidelines concerning the organisational duties of investment enterprises, credit institutions are obliged to maintain and use efficiently the resources and procedures required for the proper conduct of investment services. However, in accordance with the principle of proportionality it is not necessary to make provisions for any conceivable case, but only for cases that are reasonably likely to occur. Where credit institutions did not make adequate provisions the BAWe required that the shortcomings be remedied. Compliance with this obligation is checked by the BAWe within the framework of its further examination activities.

The examinations revealed that credit institutions did not in all cases gear their fixed-price transactions to market prices. Fixed-price transactions are contracts between the credit institution and a customer where a fixed price is agreed, and commissions, third-party charges and other expenses are not stated separately. The agreed price shall take its bearing from the price, e.g. the market price, of a reference security. In some cases internal control of the orientation at market prices, which shall prevent customers from being put at a disadvantage, was insufficient. Enterprises violating the principle of orientation at market prices were requested by the BAWe to comment on the matter and remedy the deficiencies.

An analysis of the provision of information about the allotment procedure for new issues came up with diverse results. Transparency concerning the allocation scheme was ensured through different measures. As a rule, customers were informed

about the allocation, scaling down or non-allocation of shares only after the public offering had taken place, often by means of a statement of account. In some cases customers were told that information regarding the respective allotment criteria was available, or they were notified of the non-execution of their orders due to over-subscription. Further ways of informing customers included notifications displayed on the counter, or the reference to and submission of the prospectus if it comprised details on the allotment procedure - likewise, customers were informed that a prospectus was available. Some credit institutions pointed out that long-standing customer relationships would be taken into particular consideration. In several cases customers were not notified at all about the allocation procedure and the steps taken in the case of over-subscription. In these cases the BAWe requested the enterprises concerned to comment on their non-compliance with the transparency requirements and – where necessary – to improve transparency.

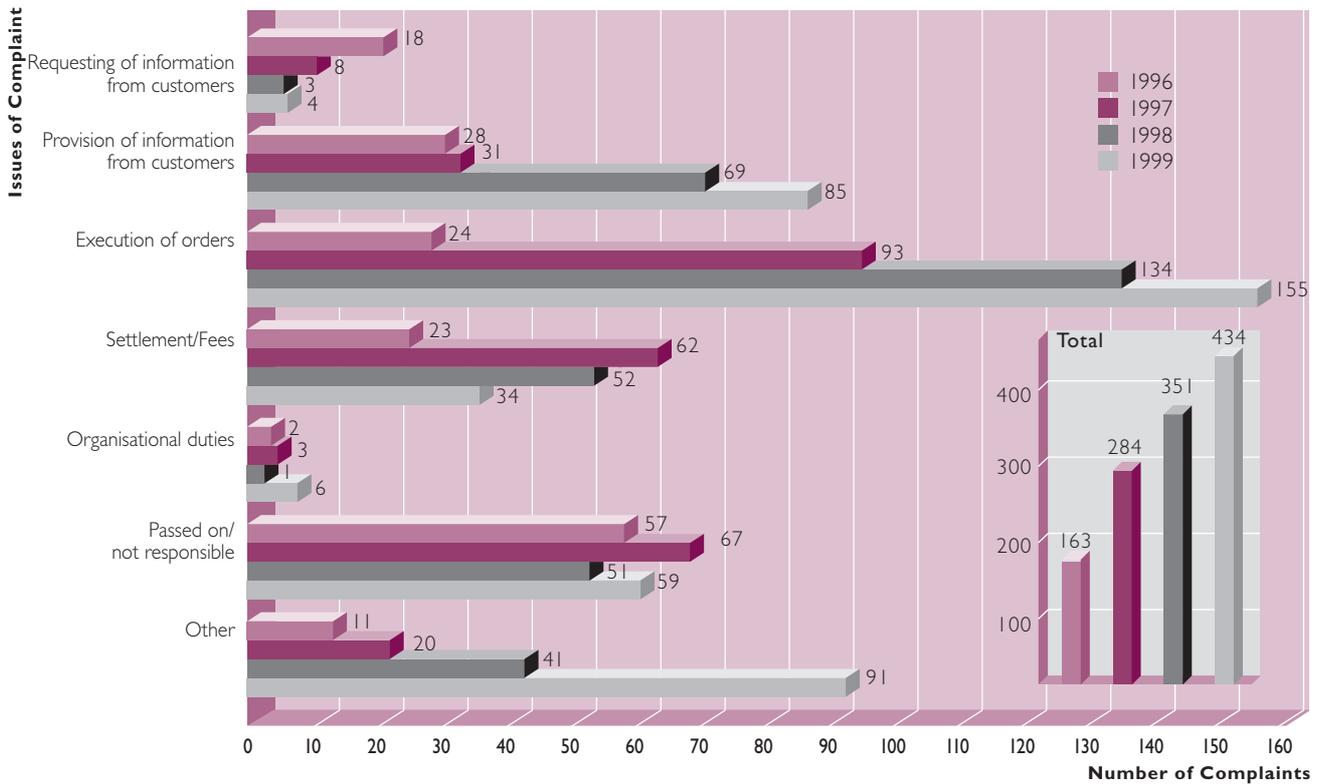
### **Investor Complaints – Credit Institutions**

In the year under review the BAWe received 434 complaints from customers. As in the years before, most investors complained about shortcomings in the execution of orders. Typical examples included delays in the transferral of orders, the incorrect execution of orders, or the failure to observe limits. Some complaints referred to trading in securities not yet issued (so-called "when issued trading"), where delivery claims are offered OTC before the shares' initial listing on the stock exchange. While the buyer

of delivery claims expects prices to rise after the IPO, the seller bets on a lower price level. Expectations of investors who bought delivery claims hoping to see price increases, have been fulfilled only in parts. Many investors were not aware of the specific risks of pre-market trading such as the comparatively low liquidity - when measured against trading on the stock market - which provides the basis for price fixing.

Some complaints concerned structured bonds, i.e. debentures where the issuer's obligation to pay depends on certain conditions. If these conditions are fulfilled, e.g. the price of a reference security drops below a given threshold, the bond may become payable. Due to the nature of these instruments investors may lose the entirety of their investment. Many investors purchased such bonds mainly because the interest rates were higher than in other segments of the bond market, but they were not aware of the risks. In most cases the securities had not been recommended by credit institutions but were ordered by the investors themselves, who failed to consult the terms of the bonds in order to acquaint themselves with the risks involved. Reverse convertibles are another example of structured bonds. They are debentures carrying a repayment option. Depending on whether the price of the bond exceeds or drops below a certain level, on the date of maturity the investor is paid, in addition to the current interest, either the nominal value of the bond, or shares. Since the price of some shares was substantially lower than the level determined in the bond terms many investors were surprised to receive not the nominal value of the bond, but instead

**Complaints About Credit Institutions 1996 – 1999**



shares whose market price was below the nominal value.

The BAWe checks each complaint for soundness. If a complaint is not obviously unfounded the BAWe requests the credit institution concerned to comment on the matter. Where permissible, it will notify the complainant of the results of his or her request. However, the duty to observe secrecy prohibits the BAWe from providing information about any measures taken on grounds of a complaint – for example an exceptional examination.

**Initial Public Offerings**

As in 1998, the allotment procedures used for initial public offerings were again a controversial issue. As a result of the large number of new issues in the Neuer Markt and the resultant high demand from invest-

ors, the problem was dealt with by the Bundestag, the Börsensachverständigenkommission (Exchange Expert Commission) and the banking associations. The guideline on the details concerning Sections 31 and 32 WpHG relating to the commission, fixed price and agency business of credit institutions, under No. 4.4. Allotment of Securities reads as follows:

If an investment services enterprise offers private investors to purchase securities by way of subscription it must provide the customers with information concerning the criteria of allotment to customers, especially with regard to over-subscription.

The business management or the agency appointed by it shall decide on the particulars concerning the allotment to members of staff or third parties on behalf of whom the

respective member of staff acts. The investment services enterprise must take preliminary action to avoid that its members of staff are given preferential treatment over the customers of the investment services enterprise.

From a supervisory point of view the decisive feature of an allotment procedure is transparency. The customer must be informed about the criteria underlying the allocation process. If the credit institution favours a particular group of customers this has to be announced and explained. However, there is no imperative provision which would require the consideration and equal treatment of all subscribers. The principle of equal treatment is not immediately applicable to the relationship between an investment services enterprise and its customers, which is based on private law. The underwriting of securities for

placement on a stock exchange is not only an investment service (underwriting business, Section 2 paragraph 3 no. 5 WpHG) but also a legal transaction under civil law which involves personal risks. There is no obligation to contract in such transactions. The freedom of contract permits the parties involved to decide with whom they would like to enter into business. A credit institution's customer is therefore not automatically entitled to consideration in the allotment process, nor is a credit institution obliged to allocate the securities according to a particular procedure (e.g. drawing by lots). The decision which procedure to use is incumbent upon the management of the company concerned.

Quite often, however, the issuer has a substantial amount of influence on the type and nature of a placement. When a security is issued the terms of placement are determined in a contract between the issuer and the investment services enterprises (credit institutions) comprising the syndicate.

In the framework of its regular annual audits the BAWe may determine the contents of the examinations and define areas of particular interest, which have to be observed by the auditor. The letter to the auditors for the calendar year 1998 included the following question of particular interest (excerpt):

Which measures are taken to ensure that customers are informed about the allotment procedure in an initial public offering, in particular in the case of over-subscription, and that members of staff are not given preferential treatment over customers?

An analysis of the focal points of the examination revealed that investment services enterprises are proceeding differently (see chapter "Examination of Credit Institutions"). It has become obvious that investors find it easier to accept non-consideration in an allotment procedure if the procedure itself has been transparent. Their acceptance, in turn, plays an important role in shaping Germany's equity culture. By ensuring that the transparency criteria are complied with in the allotment procedure, investment services enterprises will help to improve the German equity culture. The BAWe trusts in the self-regulatory mechanisms of the companies concerned. Only if this does not lead to the necessary result will the BAWe consider to take regulatory measures.

### **Prohibition of Cold Calling**

The BAWe made another important contribution to investor protection by passing on 12 August 1999 the general order concerning the prohibition of cold calling. Cold calling is defined as the unsolicited making of telephone calls to new customers with the aim of acquiring orders. Investment services enterprises are now generally prohibited from using such means of advertising. The BAWe considers cold calling to be an irregular type of advertising, and in the light of numerous investor complaints and the corresponding audit results for some financial services institutions felt compelled to adopt the above-mentioned measure. The general prohibition of cold calling for investment services enterprises shall help to protect customers' privacy and freedom of decision. In many cases the aggressive use of cold calling made it

impossible for customers to think about their investment decisions carefully.

The general order prohibits investment services enterprises from making telephone calls to private customers with whom no business relations have been established with respect to investment and non-core investment services. Exemptions are to be made only if the customer has consented thereto prior to such a call. Although unsolicited telephone calls are prohibited by the Unfair Competition Act (Gesetz gegen den unlauteren Wettbewerb) the provisions of this act do not allow the BAWe to take action. The general order, however, provides a basis for the BAWe to proceed against such advertising measures of investment services enterprises. Violations against the general order may be punished with fines of up to DM 200,000. First experience shows that cold calling as a means of customer acquisition and preparing the ground for new business has been losing much of its importance with investment services enterprises. Since evidence is often difficult to furnish the BAWe is always interested in receiving information from investors regarding prohibited business practices.

### **Day Trading**

Of particular interest in the year under review were the developments in day trading. Day trading permits retail investors to buy and sell the same securities and derivatives within the same day – in some cases even more than once. The customers are provided with real-time prices and an electronic order routing system, which enables them to place orders electronically them-

selves. The orders are passed on without delay for execution to the stock exchange.

In practice, there are two different types of day trading. Firstly, day trading can be carried out via an online bank admitted to stock exchange trading from a computer in the customer's home. Secondly, a customer may lease an IT workstation with Internet access from a day trading centre. Here, he can either use a computer workstation situated in the day trading centre itself, or have such a workstation installed at home. Usually the day trading centre will establish the contact to a securities services enterprise which enables the customer to electronically place his order, and provides for the almost immediate transmission of the order to the stock exchange. In spite of advertising slogans such as "trading in real-time" the customer is not granted "direct" access to the stock exchange. Rather, he is offered an electronic system for transmitting his order to the investment services enterprise, which in turn passes it on to the stock exchange.

Day trading centres providing investment brokerage services require a license from the BAKred and are subject to supervision by the BAWe. With the aim of implementing adequate regulatory measures, the BAWe had informative discussions with various day trading centres. Its focus of interest was placed on the respective types of advertising, customer information, and the ability to take action in the case of a customer incurring excessive losses. Responsible for this were the frequently sensationalistic and alluring advertisements for day trading which contrast sharply with the high loss

exposure. Where day trading is made available to private investors the BAWe attaches high importance to the provision of information about the specific risks involved in such transactions. Day trading is not to be forbidden to private customers but they have to be aware of the risks they are taking.

### **Guiding Principles for Staff Transactions**

Even before the WpHG came into force the Bundesaufsichtsamt für das Kreditwesen published the "Statement of the Federal Banking Supervisory Office on the requirements for the regulations to be taken by credit institutions concerning employees' transactions of 30 December 1993". Since the provisions concern not only the area of activity of the BAKred but also of the BAWe, the two supervisory authorities agreed to jointly amend the guiding principles for staff transactions after thoroughly assessing the situation. On the one hand, the new guiding principles aim at defining the respective responsibilities and including the newly regulated financial services institutions. On the other hand, with respect to the protection of institutions and customers, the provisions shall be limited to the necessary minimum

(in order to avoid the creation of "transparent employees"). Employees shall disclose information relating to their accounts, securities accounts, and powers of attorney granted to them only upon particular request from their employer or when a legitimate interest is proved. Particular obligations such as the ongoing disclosure of securities transactions, or particular holding periods or trading prohibitions, shall be imposed only on those employees who in the framework of their professional duties and on a regular basis come into possession of information that would be likely to affect the market. The guiding principles shall establish minimum standards which permit the companies to set up further provisions and leave room for flexible action tailored to the requirements of each individual situation. This supports the idea that supervision starts with the respective institution. January 2000 saw a hearing of the associations of the industries concerned. An amended version of the guiding principles has been published in July 2000.

### **Administrative Fines**

Since the beginning of 1998, financial services institutions have been subject to yearly examinations of their compliance with the rules of

#### **Day Trading**

is a type of securities trading where securities or derivatives are bought and sold within the same day – in some cases even more than once. The customers are provided with real-time prices and an electronic order routing system, enabling them to place orders electronically themselves. The orders are submitted without delay for execution to the stock exchange. In practice, there are two different types of day trading. Firstly, day trading can be carried out via an online bank from a computer in the customer's home. Secondly, special day trading centres enable the customer to carry out his transactions from workstations with Internet access that have been installed exclusively for this purpose.

conduct and reporting requirements pursuant to the WpHG. They are obliged to appoint an auditor before the end of the financial year. In 36 cases the BAWe instituted proceedings to impose administrative fines on financial services institutions which failed to or were late in appointing an auditor. Fines were imposed on seven companies, three of which were not yet final and conclusive at the end of the year under review. Five cases were suspended because it became obvious in the course of the investigations that despite original notifications to the contrary the companies concerned had not carried out any business that should have been regulated. One case was suspended on grounds of insignificance. 26 proceedings were still pending at the end of the year.

### **Outlook**

The year 2000 shall see the creation of guidelines on portfolio management specifying the general and particular rules of conducts, which will be tailored to the specific requirements of this investment service. Also planned is the passing of a guideline specifying the duties relating to the rules of conduct for operators of day trading centres.

Past experience has revealed difficulties in monitoring investment services companies' compliance with the rules of conduct. This would be likely to improve if the BAWe was authorised to impose sanctions against particular infringements of the rules of conduct. Therefore, in the context of establishing the Fourth Financial Markets Promotion Act it should be taken into consideration to extend the provisions on fines set out in the WpHG.

# INVESTOR PROTECTION - PROSPECTUSES

The Act on the Prospectus for Securities Offered for Sale (Prospectus Act) and the Ordinance on the Prospectus for Securities Offered for Sale (Prospectus Ordinance) shall protect investors in Germany to whom securities are offered publicly for the first time. The Prospectus Act relates to securities that are not admitted to trading on a German stock exchange (official trading or regulated market). Prospectuses shall provide comprehensive information about securities and their issuers in order to enable the investor to make his or her own assessment of the offer. Issuers of securities that are not admitted to trading in Germany, and which will be offered to the public for the first time, are therefore obliged to publish a prospectus at least one working day before the public offer is made. The prospectus may be published only when the BAWe has explicitly permitted its publication or if ten working days have elapsed since its submission to the BAWe.

The BAWe permits the publication of a prospectus if it contains the information required under the Prospectus Act and the Prospectus Ordinance. It will not, however, check the correctness of the information in the prospectus. For this reason the mere deposit and publication of a prospectus does not guarantee the seriousness of an offer or the issuer's creditworthiness. This is often misunderstood by investors.

The BAWe prohibits the publication of a prospectus if it does not com-

ply with the legal requirements. Furthermore, public offers of securities will be prohibited if the issuer has failed to publish a prospectus in advance. Research carried out on the Internet or the examination of articles in the press often enable the BAWe to identify such offers. In addition, the BAWe usually investigates into information received from the public, consumer associations, and police departments. In this context, too, it makes use of its right to request the submission of documents, thereby inhibiting activities on the grey capital market. Breaches of the obligation to publish and deposit prospectuses are sanctioned with fines. Penalties on violations against the provisions of the Prospectus Act can amount to as much as DM 1 million.

The BAWe may accept prospectuses from foreign issuers which have been approved by the supervisory authority of another member state of the European Union or the European Economic Area. It will not check the completeness of these prospectuses, which makes it easier for issuers domiciled abroad to access the German capital market. Furthermore, the BAWe decides whether a prospectus may be written "in a language which is not uncommonly used in the field of cross-border securities trading". The complete or partial translation of the prospectus into English is usually acceptable.

## Deposit of Prospectuses

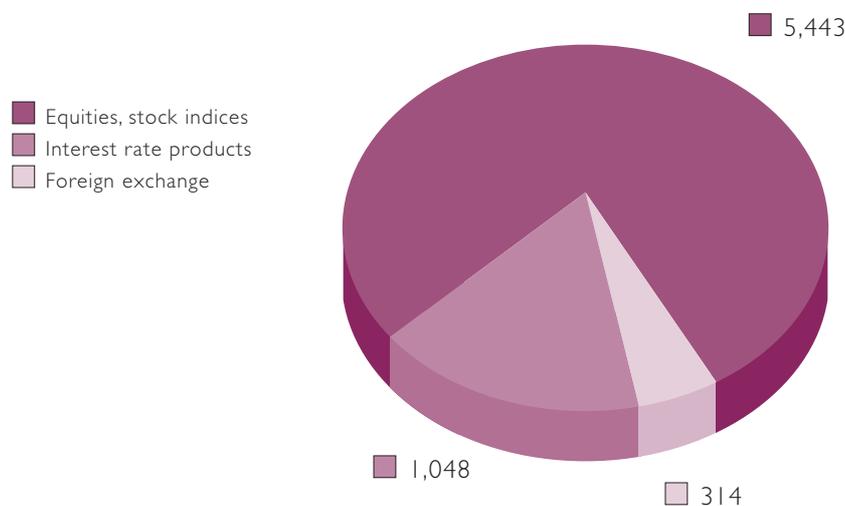
In 1999, prospectuses for 7,358 security issues were deposited with the BAWe. 6,805 of these securities were issued in the warrant market. In 30 cases the BAWe prohibited the publication of a prospectus

because legally required information was lacking. In another 33 cases the public offer was prohibited because no prospectus had been published.

### Announcement Relating to the Prospectus Act

On 21 September 1999 the BAWe published a revised version of its Announcement relating to the Prospectus Act, which serves as a means of reference and source of information for persons in charge with the production and deposit of prospectuses. The main reason behind the revision besides the emergence of new questions of interpretation was the amendment of the Prospectus Act as at 01 April 1998.

### Deposit Requirement for Warrant Issues (Full year 1999, total: 6,805)



Experience gained in almost one year of interpreting the new provisions has been taken into consideration in the announcement.

In the announcement, the BAWe draws a distinct line between public offers and advertising and points out that with a public offer it must

actually be possible for interested parties to subscribe to the security. In addition, the announcement includes a definition of bonds issued on a continuous basis within the meaning of Section 3 No. 2 Prospectus Act. Bonds within the meaning of this provision are only those securities whose terms and conditions provide for redemption of the nominal amount of capital and whose issuer promises payment of interest (either variable or fixed-rate).

With regard to the period set out in Section 9 paragraph 1 Prospectus Act it is pointed out that the prospectus must be published at least one working day before the public offer is made. Moreover, the BAWe

provides a definition of changes which "are of material significance for the assessment of the issuer or the securities" as set out in Section 11 Prospectus Act.

The announcement also deals with the mutual acceptance of prospectuses within Europe (Section 15

paragraph 3 Prospectus Act). If an offer is made in several Member States of the European Union the prospectuses of issuers domiciled abroad may be published in English.

### Public Offers on the Internet

In the period under review the BAWe identified a growing number of offers which the respective issuers had made accessible on the Internet without publishing the required prospectus. Upon dealing with these cases, the BAWe was frequently told by the parties concerned that the offer in question had not been considered a domestic public offer, because the server was situated abroad (usually in the USA). The new Announcement relating to the Prospectus Act has made it clear that a public offer is deemed to be made in Germany if domestic investors are actually able to subscribe to the securities. As regards Internet offerings, it is of no relevance from where the data has been loaded or where the server is placed from which the data can be downloaded. The decisive fact is that the offer is addressed to German investors. This can be inferred for example from the use of the German language or the mentioning of German contact persons, provided such pages are not obviously addressed exclusively to other German-speaking countries. The latter could be made clear by means of a disclaimer stating that investors in Germany are excluded from subscription.

In order to meet the legal requirements it is not sufficient to publish a prospectus only on the Internet. A publication made solely on the Internet would fail to meet the

objectives of the obligation to publish a prospectus. The density of Internet connections is still comparatively low in Germany. As a result, investors do not have equal opportunities in accessing the information. However, issuers of a security are allowed to release the prospectus on the Internet in addition to publishing it in the legally required way.

The year 1999 saw a pronounced increase in the number of Internet offerings. The BAWe identified 22 offerings where no prospectus was published and deposited. Appropriate regulatory measures were taken.

## **Cross-Border Securities Offers**

The deposit procedure has been simplified for securities which are simultaneously offered in Germany and in another Member State of the European Union. In order to avoid the creation of different prospectuses for the various legal systems and to facilitate foreign companies' access to the German capital market, a prospectus admitted in another Member State may also be admitted in Germany. In such cases the BAWe does not check the prospectus for completeness, it only monitors compliance with the publication procedure. A notable example of such simplified procedures was Vodafone AirTouch Plc.'s takeover bid to the Mannesmann AG shareholders.

From the second quarter of 1999 onwards the number of prospectuses submitted to the BAWe for mutual acceptance has increased considerably. They concerned in particular simultaneous offers in Germany and in Luxembourg,

Belgium, the Netherlands, France and the United Kingdom. Co-operation with foreign authorities certifying the admission of prospectuses has generally been positive. The BAWe is not authorised to write out similar certificates for a prospectus that has been checked for completeness, permitting the issuer to apply for admission thereof in another Member State of the European Union or the European Economic Area. Certificates for prospectuses relating to securities that are officially listed have to be prepared by the admission boards of stock exchanges.

With the aim of developing a common European basis for the mutual acceptance of securities offers, in 1999 the Forum of European Securities Commissions (FESCO) established an experts group on "European Public Offers". This group discusses different methods of dealing with cross-border securities offerings and develops criteria for mutual recognition. The European Union in its Financial Services Action Plan advocates likewise a revision of the existing legislation, in particular of the Admission and Listing Particulars Directives, with the aim of eliminating legal obstacles in cross-border capital raising within Europe.

## **Fees**

The BAWe charges a fee for the deposit of prospectuses. The legal basis is laid down in Section 16 paragraph 2 of the Prospectus Act in conjunction with the Ordinance on the Fees Levied for the Deposit of Prospectuses (Verkaufsprospektgebührenverordnung - VerkProsp-GebV) which came into effect on 01 April 1999.

Before the ordinance was amended the fees that were levied were determined by the total issuing price of the securities, whereas now the BAWe charges a uniform fee of DM 400 for each complete prospectus and DM 300 for each incomplete prospectus, plus DM 100 for each supplement pursuant to Sections 10 and 11 of the Prospectus Act. This has led to a pronounced reduction in fees in comparison with the amounts charged under the previous fee charging system.

The Ordinance on the Fees Levied for the Deposit of Prospectuses lays down the steps to be taken when a prospectus is deposited. It stipulates that the obligation to pay the fee arises as soon as a document has been deposited with the BAWe. If the prospectus is withdrawn from publication before the BAWe has checked its completeness the deposit fee will be reduced.

The Administrative Court of Frankfurt in 1997 dismissed the complaint of a credit institution concerning the fees on prospectuses for bearer warrants. The Higher Administrative Court of Hesse confirmed the Administrative Court's decision through final judgement in August 1999, supporting the view of the BAWe that bearer warrants are not to be classified as bonds, which pursuant to an exception laid down in the Prospectus Act do not require a prospectus.

In addition, with reference to the former legislative framework it was made clear that the fees are charged for each prospectus. The provisions of Section 16 paragraph 2 sentence 1 Prospectus Act refer to the deposit of a prospectus. A separate prospectus must be pub-

lished for each security specified by a securities identification code (Wertpapierkennnummer; WKN). Prospectuses in the sense of the Prospectus Act do not necessarily have to consist of a set of physically linked documents. Where in an incomplete prospectus for bearer warrants the details regarding the respective warrants are specified in supplements, the incomplete prospectus plus the supplements are considered to establish a prospectus for which a fee must be paid.

considering to enable investors to access a list of the prospectuses deposited with it on its home page.

### **Administrative Fines**

In the period under review the BAWe instituted 74 new proceedings on grounds of the failure to or a delay in publishing a prospectus. All in all, 126 proceedings were pending, of which 15 cases were concluded after fines were imposed amounting up to DM 80,000. In 21 cases suspicion was invalidated. Another 20 cases were discontinued on grounds of insignificance. By the end of 1999, 70 cases were still pending.

### **Outlook**

For the year 2000, the BAWe expects another increase in the issuing volume and thus in the number of prospectuses to be examined. This trend will receive particular momentum from the existing tendency towards submitting public offers via the Internet, which is likely to be accompanied by a growing number of offences against the provisions of the Prospectus Act. The BAWe does not only regard the Internet as an additional area to be supervised, it is also attempting to use it as a means for precautionary investor protection. For example, the BAWe is

# MARKET INTEGRITY – PROHIBITION OF INSIDER TRADING

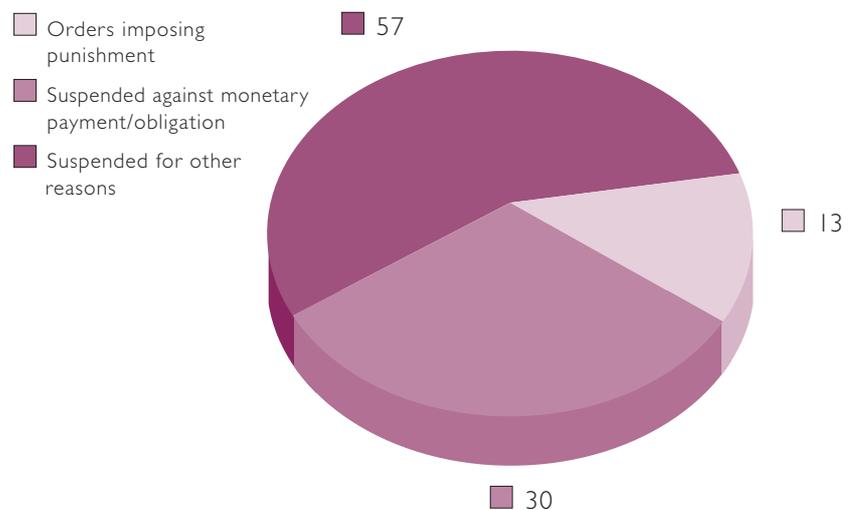
The BAWe is responsible for monitoring on an ongoing basis all on- and off-exchange transactions in insider securities in order to counteract any violations of the provisions on insider surveillance set out in the WpHG. The WpHG grants the BAWe rights to request information and carry out investigations. Where the BAWe establishes facts giving reason to suspect a criminal insider offence it must inform the competent public prosecutor's office.

The area of application of the insider provisions of the WpHG is analogous to the definition of insider securities set out in Section 12 WpHG. The central feature of insider securities is their admission to trading on a domestic stock

exchange or a stock exchange of another Member State of the European Union or the European Economic Area. A security is deemed to be admitted to trading on an organised market or in the third market segment (Freiverkehr) as soon as the relevant application thereto has been submitted or publicly announced. Securities or derivatives traded on other markets are not subject to the insider provisions. The WpHG - as well as the European Insider Dealing Directive which is the basis for Sections 12 et seq. of the WpHG - shall help to ensure investor confidence in the organised capital markets.

Persons having knowledge of inside information (insiders) are prohibited from taking advantage of their knowledge of such information in order to deal in insider securities either on or off an exchange. Inside information is any piece of information that is not publicly known and which relates to one or several issuers of insider securities, or to insider securities, and which, if it

## Notifications from the Public Prosecutors' Offices Relating to Suspension of Insider Proceedings 1995 - 1999



were made public, would be likely to have a significant effect on the price of the insider security.

While the prohibition to purchase or sell securities concerns also secondary insiders, the prohibition to pass on information and give recommendations is applicable only to primary insiders as defined in Section 13 paragraph 1 WpHG. The latter group includes any person who by virtue of membership of the management or supervisory body of the issuer, or as a personally liable partner in the issuer or in an enterprise associated with the issuer, possesses knowledge of inside information. Primary insiders in addition include persons having knowledge of inside information by virtue of their holdings in the capital of an issuer or of an undertaking associated with the issuer, or by virtue of their profession or employment in accordance with the regulations.

## Insider Investigations

In 1999 the BAWe investigated 39 new cases of suspected violations against the insider provisions. Some of the investigations were initiated by the stock exchanges' Trading Surveillance Units (Handelsüberwachungsstellen). The BAWe reported 13 cases to the competent public prosecutor's office. In 27 cases the suspicions proved to be unfounded, 45 investigations – some of them from previous years – were still pending at the end of the period under review. The year 1999 did not witness any convictions on grounds of prohibited insider dealing. In ten cases the public prosecutor's office refrained for the time being from bringing a charge pursuant to Section 153a Code of Criminal Procedure (Strafprozessordnung;

short: StPO). Some of the defendants were punished by high fines. The circumstances were as follows:

◆ In July 1998, a dealer with a bank (market maker) sold 50 contracts of a DAX call option on Eurex, at a price of 167 points. After this transaction he immediately purchased 100 contracts of the same option from another dealer of his bank who sold them on behalf of a customer at a price of 165 points. He was suspected of capitalising on his knowledge of the colleague's forthcoming customer order when selling the 50 contracts (front running), thereby committing an insider crime with his colleague. In the proceedings against the two dealers the public prosecutor's office in Frankfurt refrained from bringing a charge against payment of a fine of DM 1,000 each, pursuant to Section 153a StPO.

◆ In April 1998, an official broker of the Frankfurt stock exchange with price determination responsibility for the company concerned sold 400 shares on Xetra at a price of DM 824.50. Beforehand, he had closed the order book and identified a surplus on the buying side at a price of DM 820. Following several changes of the estimated price the broker fixed a price of DM 820 on the floor and purchased 400 shares for own account. He was suspected of making use of his preferential knowledge of the order situation on the floor when he bought the 400 shares (front running), thereby breaching the prohibition on insider dealing.

In May and September 1998 the same official broker after consult-

ing the order book for floor trading sold shares on Xetra of companies for which he fixed the price. Again in these cases he

### Frontrunning

Front running is the purchase or sale of insider securities while capitalising on knowledge of an impending order by a third person which, if it were made public, would be likely to have a substantial impact on the price of the insider securities concerned.

bought shares for own account at a lower price in floor trading afterwards, and again he allegedly exploited his knowledge of the order situation on the floor when carrying out the transactions via Xetra.

The broker generated a profit of DM 6,920 with the above transactions. The public prosecutor's office in Frankfurt am Main refrained from bringing a charge and imposed a fine of DM 10,000, pursuant to Section 153a StPO.

◆ On February 17, 1997, Pfeleiderer Vermögensverwaltung GmbH & Co. KG notified the public by means of an ad hoc announcement pursuant to Section 15 WpHG of its intention to call in for repayment as at 31 May the profit participation certificates issued in 1989. In addition, the company submitted a voluntary offer valid until May 30, 1997 to buy back at a price of DM 140 the profit participation rights issued at a price of DM 105. After the announcement was made the price of the profit participation certificates dropped

from DM 196 to DM 140, i.e. to the level of the redemption price. The calling in of the profit sharing certificates and the voluntary purchase offer were deemed to be inside information.

Four family members of a primary insider of the company sold their entire holdings of the profit participation certificates before the announcement was published. The primary insider was suspected of having passed the inside information on to his family who in turn made use of their knowledge and sold the certificates. The public prosecutor's office in Nuremberg-Fürth in the proceedings against the five persons refrained from bringing a charge against payment of fines ranging from DM 1,500 to DM 9,000, pursuant to Section 153a StPO.

A tax official and his son – the former had frequently been an auditor of the company - sold all profit participation certificates of the company before the notification was released. The tax official allegedly obtained the inside information in his capacity as an auditor, i.e. primary insider, and used it to sell his profit participation rights and inform his son accordingly. The latter was suspected of capitalising on his knowledge of the inside information to sell his own profit participation rights. The public prosecutor's office against payment of DM 9,000 and DM 3,000 respectively refrained from bringing a charge pursuant to Section 153a StPO.

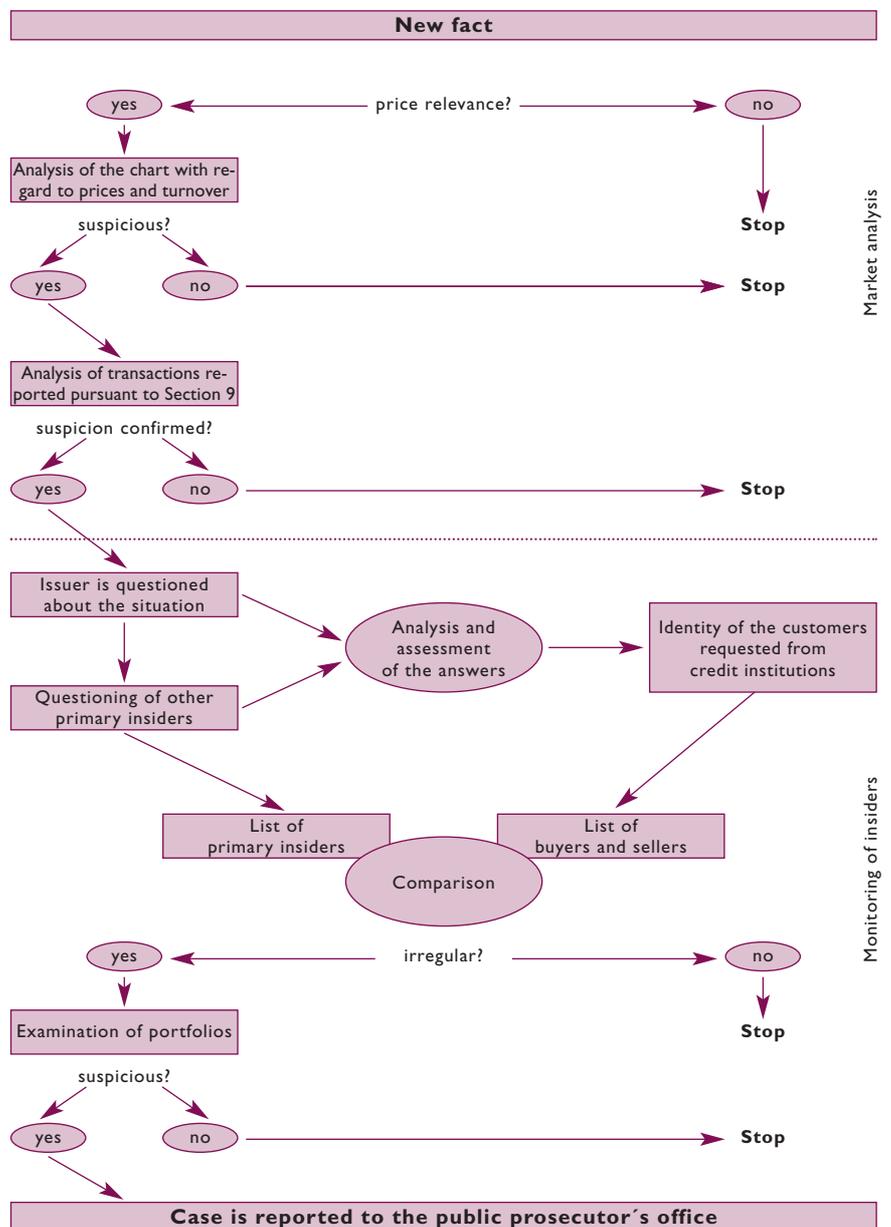
In 1999, a German court opened main proceedings for the first time

on account of an insider offence. The defendant was suspected of acquiring in his capacity as leading administrative official of Cologne knowledge of the forthcoming takeover bid to be submitted by Moeller Holding GmbH & Co. KG to the shareholders of Felten & Guillaume AG. He allegedly made use of this information to purchase shares of Felten & Guillaume AG

for his own account before the offer was submitted to the public. The defendant was sentenced to pay a fine of DM 37,500 (150 daily units of DM 250). The sentence is not yet final.

Below you will find a chart displaying a typical insider investigation of the BAWe. The examinations are carried out on a regular basis in

**Typical Insider Investigation of the BAWe**



connection with ad hoc announcements from listed companies, which concern information that is likely to have substantial impact on the price of the security. To start with, a team of analysts examines with regard to unusual trading volumes and price developments all transactions in the respective security that have been reported to the BAWe during a certain period before and after the announcement. In the further course of the investigation, the details furnished by the issuer about the group of persons with knowledge of the inside information are compared with the transaction data reported by the credit institutions. If the analysis and an examination of securities accounts reveal further indications of violations against the law, the BAWe will report the respective case to the competent public prosecutor's office.

## Reporting Requirements for Transactions in Securities and Derivatives

The reporting requirements for transactions in securities and derivatives pursuant to Section 9 WpHG were established in Germany on 01 January 1996. Credit institutions, financial services institutions authorised to conduct trading for own account, and domestic companies admitted to stock exchange trading are obliged to re-port to the BAWe all transactions in securities and derivatives. The reporting requirements concern all securities and derivatives which are admitted to trading on a stock exchange in a member state of the European Union or of the European Economic Area, or which are traded on the third market segment (Freiverkehr) of a German stock exchange. The reporting

requirements apply also to undertakings domiciled abroad - such as banks or brokers - which are authorised to trade on a German stock exchange, with respect to their transactions on a stock exchange. The provision's objective is to discover violations against the prohibition of insider trading.

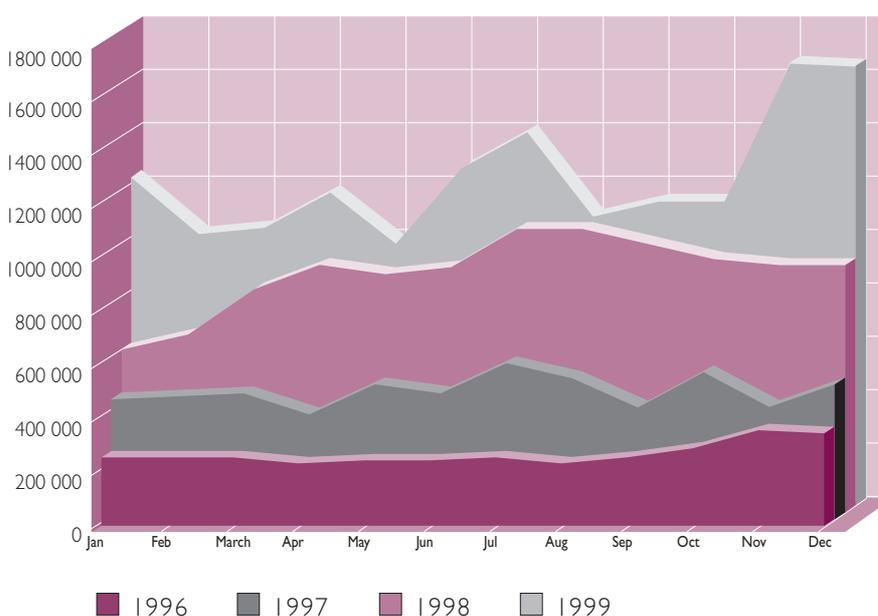
In September 1999 the Helsinki Futures Exchange joined the common trading platform of Eurex Deutschland and Eurex Zürich, founded in 1998. Due to their admission to a German exchange the members of the former Helsinki Futures Exchange are now subject to the reporting requirements in Germany. Likewise, the derivatives traded on the Helsinki Futures Exchange were made subject to the reporting requirements in Germany after they were admitted to trading on Eurex Deutschland.

The number of reported transactions in 1999 amounted to 318 million. In the year before, only 215

million transactions had been reported to the BAWe. This represents an increase by about 103 million, i.e. 47.9 per cent. In 1999, the BAWe was notified of an average 1.2 million transactions per day, compared with 855,000 transactions in 1998. The highest activity was recorded on 14 December 1999 when the BAWe was notified of more than 2.1 million transactions.

The pronounced increase in the number of reported transactions was mainly attributable to the reduction on all German stock exchanges of the minimum transaction volume, the extension of trading hours, the disproportionate increase in the number of listed companies on the Neuer Markt, and of foreign members on Eurex and Xetra. Having amounted to 216 (= 5.5 per cent) in 1998, the number of foreign enterprises obliged to report nearly doubled in the course of 1999 to reach 320 (= 8.6 per cent) by the end of the year. The number of domestic entities

Monthly Average of Daily Reporting Volumes 1996 – 1999



**Reporting Parties**

Country	Reporting Parties 31.12.1999	Proportion in % <sup>1</sup>	Reporting Parties 31.12.1998	Proportion in % <sup>1</sup>
Germany	3,402	91.40	3,682	94.46
United Kingdom	83	2.23	77	1.97
Switzerland	50	1.34	47	1.20
USA	34	0.91	18	0.46
France	32	0.86	28	0.72
Austria	26	0.70	8	0.20
Netherlands	23	0.62	14	0.36
Spain	19	0.51	7	0.18
Finland	16	0.43	5	0.13
Italy	10	0.27	3	0.08
Belgium	5	0.13	3	0.08
Ireland	5	0.13	1	0.02
Luxembourg	5	0.13	2	0.05
Sweden	5	0.13	2	0.05
Denmark	4	0.11	-	-
Gibraltar	1	0.03	-	-
Norway	1	0.03	1	0.05
Portugal	1	0.03	-	-
total	3,722	100.00	3,898	100

<sup>1</sup> Figures have been rounded off

obliged to report declined over the same period by 280, i.e. 7.6 per cent, from 3,682 to 3,402.

At 91.4 per cent, in the year under review the overwhelming majority of the notifying parties came from Germany. The trend was to the downside, however (in the previous year the figure was 94.5 per cent). Further reporting parties came from 16 European countries and the USA. The BAWe continues to expect an

above-average increase in the number of parties obliged to report and in the reporting volume. Furthermore, in the year 2000 trading hours have been extended to 8:00 p.m. in a first step towards electronic 24-hour trading, and several public holidays have ceased to be trading holidays. Moreover, Deutsche Börse AG is seeking the authorisation to introduce the electronic trading system Xetra to the USA. In addition to leading to a

further increase in reporting volumes, the growing number of stock exchange alliances will become a new challenge for the BAWe in regard of its reporting activities.

### Securities Watch Application (SWAP)

In the year under review, the BAWe used technological means in combating insider dealing to an increasing extent. Of growing

importance was the automated analysis system "Securities Watch Application (SWAP)". Developed in-house, the system will automatically filter out any irregular trading from the data on transactions in securities and derivatives that have been reported pursuant to Section 9 WpHG.

SWAP makes it possible to generate independent indicators which take account of the securities' specific volatility and liquidity. These indicators display the statistical likelihood to find certain aspects (e.g. price, net yield) on a particular day, when compared with a certain reference period. The BAWe receives a sorted list of several indicators, tailored to the respective analysis requirements. The first version of the system has been tested successfully and is already being used. Within the scope of further developing its automated analysis systems the BAWe is making use of international contacts to other supervisory authorities (e.g. the London Stock Exchange or the British Financial Services Authority).

## **Fines and Administrative Procedures**

In 1999, the BAWe instituted two proceedings to impose administrative fines due to infringements of the requirement to furnish information on insider transactions (Section 16 paragraph 4 WpHG). The parties concerned had either failed to notify the BAWe at all or furnished incorrect information. One of the enterprises required to furnish information was punished with a fine of DM 5,000. Neither of the two proceedings has been concluded so far.

Objections were made against three requests to furnish information, which were settled - or withdrawn - after the parties were heard and the required information was submitted. The BAWe opened eight new proceedings due to violations of the obligation to furnish information on transactions in securities and derivatives pursuant to Section 9 WpHG. 14 proceedings were pending at the start of the period under review. 16 proceedings were suspended on grounds of insignificance.

## **Scalping - an Insider Crime**

The regional court of Frankfurt am Main in its decision of 09 November 1999 determined that the purchase of securities upon knowledge of the impending release of a valuation or recommendation thereto, and with the aim of benefiting from the resultant price gain (referred to as scalping), is prosecutable as an insider offence. The regional court thus shares the legal opinions of the both BAWe and the public prosecutor's office on this issue.

In addition, the court's criminal division pointed out that even mental processes such as the intention to release a recommendation can represent inside information. The publication of a recommendation as such shall remain permissible, however. According to the court, a business journalist shall be permitted to recommend a share for buying. He is not allowed, however, to inform third parties in advance about the kind of shares he is going to recommend. Neither is he allowed to purchase these shares himself once he has decided to make a public recommendation, provided this recommendation is likely to affect the share price.

In the case in question the criminal division refused to open the trial. Arguably according to the court it would have been impossible to furnish conclusive evidence that at the time of buying the shares, the journalist concerned had already decided to recommend them in his next TV show. Circumstantial evidence made it clear that there could have been other reasons for him to buy the shares beside his intention to release a recommendation. In addition, the share price performance between the purchasing day and the recommendation day would have been a perfect reason for recommending the shares. The public prosecutor's office filed an immediate appeal, which has been rejected by the higher regional court of Frankfurt am Main.

## **Obligation to Keep a Record**

Securities services enterprises and companies domiciled in Germany that are admitted to trading on a domestic stock exchange are required to establish and record, before executing orders relating to insider securities, the identity of the principals and the persons benefiting or incurring a liability from these transactions (Section 16 paragraph 2 sentence 5 WpHG). Within the context of insider investigations the BAWe identified a number of violations against this provision. For example, no record was kept of the natural persons behind portfolios of legal persons. Upon request, the BAWe did not receive information relating to the principal of the transaction at issue, nor on any authorised persons acting on behalf of the principal. Only the portfolio owners were disclosed. The BAWe instituted

proceedings to impose administrative fines. In future, higher emphasis will be placed on monitoring compliance with the relevant provisions in order to ensure the effective prosecution of insider cases. If necessary, the BAWe will make use of its right to impose fines.

## **Co-Operation**

On 16 March 1999, the fourth forum on insider law and ad hoc disclosure was held on the premises of the regional Bundesbank branch in Hesse-Thuringia. It was jointly hosted by Deutsches Aktieninstitut e.V. and the BAWe and attended by some 100 public prosecutors, police officers, and other members of the legal profession and criminal prosecution. The lecturer side comprised representatives of the Frankfurt stock exchange's Trade Surveillance Unit and of the Frankfurt-based State Commissioner's Office (Staatskommissariat), a division of the Exchange Supervisory Authority. The aim of the forum, which takes place every year, is to provide a platform for the exchange of experience and efficient co-operation between the prosecuting authorities and the BAWe. In addition, meetings were held with representatives of the State and Federal Offices of Criminal Investigation.

# MARKET TRANSPARENCY - AD HOC DISCLOSURE

Transparency is a fundamental requirement for the functioning of the financial markets. Ad hoc disclosure contributes to giving the market participants early access to relevant information, which provides the basis for them to make competent investment decisions. In addition, ad hoc disclosure shall help to prevent violations against the insider trading prohibition. Once a price relevant fact is known to the public it can no longer be used for prohibited insider transactions.

## Prerequisites for Ad hoc Announcements

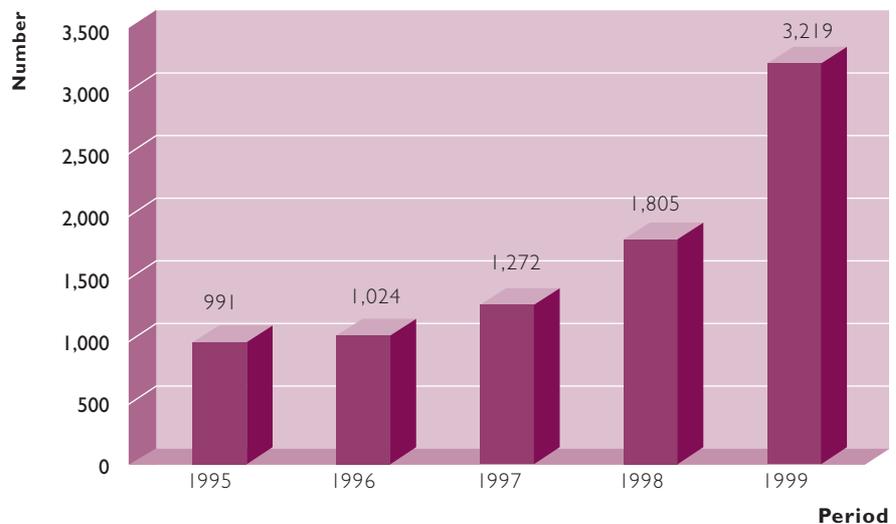
Issuers of securities admitted to official trading or to the regulated market of a German stock exchange must publish an ad hoc announcement if the following prerequisites are fulfilled:

- ◆ The fact must be new and unknown to the public;
- ◆ The information must occur within the issuer's sphere of activity;
- ◆ The fact must be likely to affect the assets or financial situation or the general trading position of the issuer;
- ◆ The fact must be likely to exert significant influence on the stock exchange price because of the above-mentioned effects or, in the case of listed bonds, to impair the issuer's ability to meet his liabilities.

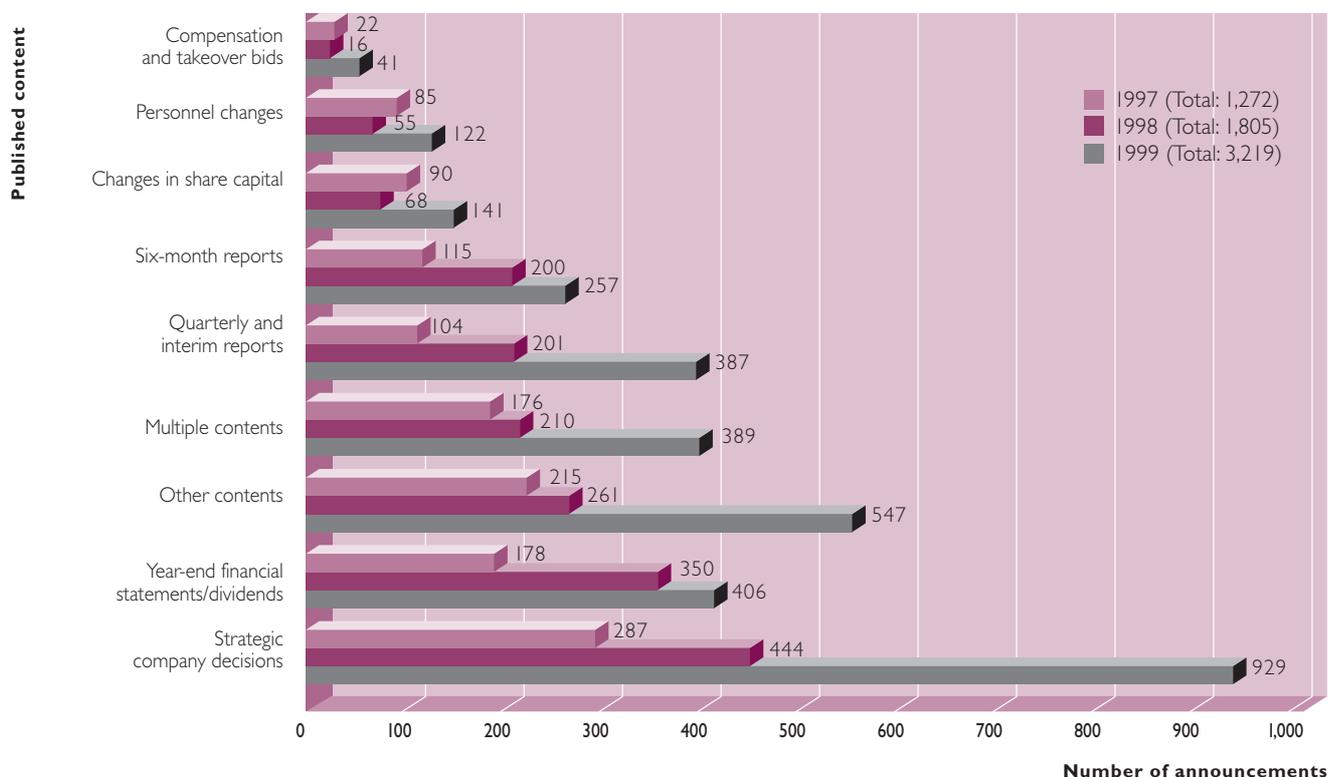
## Number and Contents of Ad hoc Announcements

In 1999 the BAWe received 3,219 ad hoc announcements from German issuers (1998: 1,805). Approximately 780 domestic stock corporations were admitted to official trading or trading on the regulated market on 31 December 1999,

**Number of Ad hoc Announcements from Domestic Issuers  
1995 - 1999**



**Contents of Ad hoc Announcements Published by Domestic Issuers in 1997 - 1999**



618 of which released one or more ad hoc notifications. It has to be taken into consideration that all Neuer Markt issuers were admitted to trading on the regulated market. As in the previous year, the majority of ad hoc announcements provided information pertaining to financial statements or six-month results, especially profit/loss and sales figures that were to be published in the annual and six-month reports as well as other interim reports, e.g. quarterly reports. Released were in particular deviations of these figures from the respective comparable period, from forecasts of the company or from market expectations. As in 1998, another emphasis was placed on strategic company decisions such as structural changes, the purchase or sale of participations, or mergers.

**Misuse of Ad hoc Announcements**

The number of ad hoc announcements showed another pronounced increase from the previous year's level. To a certain extent this increase was attributable to companies admitted to the Neuer Markt for the first time in the year under review. The Neuer Markt companies turned out to be particularly ready to disclose information. However, the growing number of ad hoc notifications was not always accompanied by the respective improvement in transparency. Instead, there was a rising amount of unnecessary announcements that did not fulfil all legal requirements, making it increasingly difficult for the public to discern from the multitude of announcements those facts which

would actually be likely to have a considerable impact on the market price.

A certain number of issuers quite obviously misused the attention attached to any information published in accordance with the legal publication requirements and entitled "ad hoc announcement pursuant to Section 15 WpHG" for other purposes besides ad hoc disclosure. They could be sure that even the most irrelevant information or advertising would immediately reach investors, traders and analysts through electronic media. The public is forced to at least take note of the information in order to avoid missing out on important information. However, dates of press or analyst conferences, lengthy quotations of directors, or the

description of general business profiles do not fulfil the requirements of Section 15 WpHG. The same is true for facts or assumptions concerning the area of activity of competitors established in the framework of business relations.

The BAWe considers such announcements to be undesirable developments pursuant to the WpHG (Section 4 paragraph 1 sentence 2 WpHG). Several successive steps are taken against such irregularities. The first step involves giving the issuer the opportunity to comment on the accusation. Only if it is not possible to reach a suitable solution will the BAWe in a second step give binding orders and, if necessary, apply coercive measures to enforce them. So far, the latter has not been necessary. In most cases – although sometimes only when threatened with a prohibitive order - the companies concerned promised to refrain from publishing further unnecessary ad hoc notifications.

Moreover, in the period under review even issuers who are traded

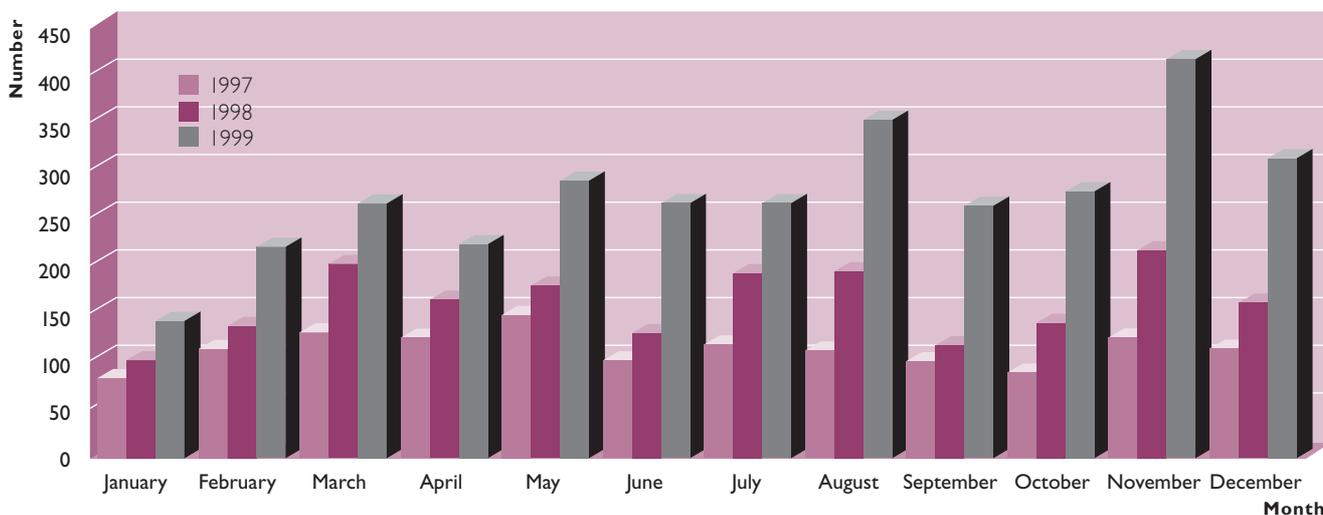
on the third market segment (Freiverkehr) and who are not subject to the provisions of Section 15 WpHG published ad hoc announcements. Some regional exchanges concluded corresponding agreements under civil law with Freiverkehr issuers, obviously with the aim of improving the attractiveness of the third market segment for potential investors. It is necessary, however, to draw a distinct line between duties established under public law and terms agreed under civil law. Any improvement of transparency through regulations under civil law will generally be welcome. A limit is however arrived at when this means of improving the disclosure behaviour begins to impair the legally required transparency.

One conceivable way of improving transparency in the third market segment would be the institutionalisation of another notification channel beside the legally required ad hoc disclosure. With regard to the scope and speed of disseminating the information, the relevant terms and conditions might be

based on the provisions of Section 15 WpHG. However, it must remain possible to distinguish legal requirements from voluntary provisions. For example, an announcement relating to the third market segment might read as follows: "XY AG: Important company information, listing on the free market of Dusseldorf and Hamburg".

However, market transparency suffers not only from unnecessary ad hoc announcements. Notifications whose contents do comply with the requirements are frequently too long, as some issuers do not confine themselves to publishing only the price-relevant information and a short explanation thereof. Many publications comprise lengthy quarterly and six-month reports, forcing the public to search the text for decisive information. Ad hoc announcements on quarterly reports should include only core information on the company's performance over the last quarter, which can usually be summarised in ten to twenty typed lines. Comprehensive explanations and back-

### Ad hoc Notifications from Domestic Issuers: a Monthly Breakdown



ground information should be provided within the framework of regular disclosure.

### Exemptions from the Publication Requirement

The BAWe may temporarily exempt an issuer from the publication requirement if publication of the information is likely to damage the legitimate interests of the issuer (Section 15 paragraph 1 sentence 2 WpHG). This is a discretionary decision, since the BAWe must consider in each individual case whether the company's interest in being granted confidential treatment of the information must be rated higher than the capital market's interest in receiving such information.

In the period under review the BAWe received eight applications for exemption from the publication requirement. Six applications were accepted, another two were withdrawn by the applicants. All temporary exemptions were made in view of restructuring measures carried out by the companies.

### Administrative Fines

In 1999 the BAWe instituted four new proceedings to impose administrative fines due to breaches of

the legal provisions governing ad hoc disclosure. Together with the pending procedures from previous years this added up to a total of 35 cases. Two of them were determined by final judgement. Eleven proceedings were suspended, and seven of the companies concerned were able to provide rebutting evidence. Four proceedings were suspended on grounds of insignificance.

### Share Buybacks and Ad hoc Disclosure

The Act on Corporate Control and Transparency (Gesetz zur Kontrolle und Transparenz im Unternehmensbereich; KonTraG) which came into force on 01 May 1998 permits stock corporations to buy back own shares on a larger scale. Issuers are now allowed to purchase up to 10 per cent of the share capital, provided they have been granted an authorisation from the annual general meeting lasting for up to 18 months which establishes the highest and the lowest price as well as the proportion of share capital (Section 71 paragraph 1 sentence 1 number 8 Stock Corporation Act). Listed companies deciding to purchase own shares may be required to publish a notification pursuant to Section 15 WpHG.

The mere decision of the annual general meeting to authorise the board of managers to buy back up to 10 per cent of the share capital does not require the publication of an ad hoc announcement. Although the share price might rise following the decision, for example because investors expect the permission to buy back own shares to entail positive future effects in the sense of a better shareholder value policy, it is not possible to know at the time the general meeting makes its decision whether and when the buyback of shares will actually take place. Moreover, neither the volume nor the date of the share buyback have been fixed at this early stage, and the price range for purchasing the shares is still an open question.

The managing board's eventual decision to make use of its authorisation to buy back own shares, however, is likely to be of particular relevance for the price. This decision has to be disclosed to the public by means of an ad hoc notification comprising the main features of the decision and a reference to the authorisation from the general meeting. Where the supervisory board must give its approval of the share buyback the publication requirement will not be established until both boards have presented their decisions. In July 1999 the BAWe sent a letter to the managing boards of listed companies setting out in detail the legal provisions relating to the planned buyback of own shares. You may consult this letter on the home page of the BAWe under (www.bawe.de).

### Ad hoc Disclosure of Profit Warnings

Profit warnings must be disclosed to the public in an ad hoc announce-

#### Access to Electronically Published Ad hoc Announcements:

Ad hoc announcements are accessible via the following addresses:

**Internet:** www.bawe.de/links.htm#a1  
www.dgap.de  
www.vwd.de/adhoc

**T-Online:** \*vwd#

**Fax polling:** Computel (0190-576647)

**Video text:** n-tv (S. 360), ARD/ZDF (S. 448)

ment only if they are based on information within the meaning of Section 15 WpHG. If this condition, i.e. the existence of such information, is not fulfilled the issuer concerned is not obliged to publish an ad hoc announcement.

The decisive feature in this context is the definition of "information". Only the existence of such information establishes an obligation to publish an ad hoc notification, provided the other conditions set out in Section 15 WpHG are fulfilled. In this case the respective information must be disclosed without delay. "Information" in the sense of Section 15 is something that has happened and can be proved.

If for example an issuer's management comes to the view that due to a general deterioration of the business climate – e.g. within the sector – the company's result might not be as good as in the previous year, or that the previous year's result is unlikely to be exceeded, this will not be regarded as information in the sense of Section 15 WpHG. Instead, it would be deemed an undifferentiated assessment of the earnings situation, not information, which does not establish an obligation to publish an ad hoc announcement. The issuer is nevertheless free to publish a profit warning, for example in a press release. The situation is different, however, if due to the deteriorating environment the management of a company prepares an interim statement and realises that the current year's result, at the time of preparing the statement, is significantly lower than in the previous year. In this case the preparation of the statement has established a fact that may quite well require the publication of an ad hoc announcement,

provided the other conditions are fulfilled as well, in particular the likelihood of the information to have substantial influence on the price.

### Other Issues

The second issue of the leaflet "Insider Trading Prohibitions and Ad hoc Disclosure Pursuant to the German Securities Trading Act (Wertpapierhandelsgesetz)", published in 1998 in co-operation with Deutsche Börse AG and with contributions from many business associations, was still strongly in demand in the year under review. It furnishes explanations and recommendations regarding the treatment of facts which are likely to affect the share price, in view of the insider provisions of the WpHG. A particular focus has been placed on the provisions on ad hoc disclosure. A copy of the guidelines can be received free of charge from Deutsche Börse AG or from the BAWe. It is also available on the home page of the BAWe.

The market participants' interest in the issue of ad hoc disclosure was also reflected in the substantial number of participants in the annual forum on ad hoc disclosure. The forum is jointly hosted by Deutsche Börse AG, Deutsche Gesellschaft für Ad hoc-Publizität mbH (DGAP) and the BAWe. The issues treated in the year under review were headlined "Do analysts need ad hoc disclosure?", "Ad hoc disclosure without price relevance?", "Share buybacks and ad hoc disclosure", and "Exchanges and ad hoc disclosure".

In 1999, DGAP created an Internet database comprising all ad hoc announcements which are published

by means of electronic media. All ad hoc announcements released so far can be accessed via DGAP's Internet archives ([www.dgap.de](http://www.dgap.de)).

# MARKET TRANSPARENCY -

## HOLDINGS OF VOTING RIGHTS

### Notifications and Disclosures, Exemptions

The disclosure of certain changes in the holdings of voting rights in listed companies plays an important role in improving transparency in the securities markets.

The legal notification and disclosure requirements help to prevent the misuse of inside information and permit investment decisions to be taken on more broadly based information. The provisions require the notifying party to inform the company and the BAWe of changes in the percentage of voting rights. The companies concerned must make the notification known to the public.

The notification and disclosure requirements concern voting rights in enterprises which are domiciled in Germany and whose shares must be admitted to official trading on an exchange in a Member State of the European Union or the European Economic Area. Holders of voting rights in foreign enterprises whose shares are admitted to trading on a German exchange are not subject to such notification requirements, but nevertheless the companies concerned are obliged, when becoming aware of such changes, to disclose the information.

At the end of 1999, 640 domestic and foreign companies were admitted to official trading on German exchanges.

In 1999, the BAWe received 1,059 notifications regarding changes in the percentage of voting rights. Many of these notifications did not comply with the legal requirements. Shortcomings could be observed in particular with regard to the failure to disclose the relevant thresholds, and in respect of the day on which this threshold had been reached, exceeded or fallen short of. The obligation to disclose this date was established in April 1998. Often the notifying parties did not observe the requirement to count voting rights additionally. In some cases shareholders submitted voluntary notifications about changes in their holdings of voting rights without having reached the relevant thresholds. The companies concerned usually published the notifications.

The BAWe welcomes such voluntary announcements and publications as a contribution towards higher transparency in the financial markets.

Companies furnishing investment services which are admitted to trading on an exchange of a Member State of the European Union or the European Economic Area may request exemption of their trading portfolio from the notification requirements. The trading portfolio will remain unconsidered in a calculation of the percentages of voting rights.

Shares that are exempt from the notification requirements will not bear voting rights in a general meeting if in the case of their non-exemption they would be subject to the notification requirement. In 1999, 121 enterprises made use of this possibility.

## Administrative Fines

In 1999, the BAWe opened 132 new proceedings due to infringements of the notification requirements. 26 proceedings were pending from the previous year. Particularly unusual was the rising number of breaches of the obligation to notify the BAWe of the first-time admission of shares to official trading (Section 21 paragraph 1a WpHG). Of the new proceedings, 55 concerned this provision, whereas 47 cases were related to the failure to or delay in notifying of changes in holdings of voting rights pursuant to Section 21 paragraph 1 WpHG. Another 30 procedures were instituted because the listed enterprises concerned failed to or were late in publishing the notifications they had received (Section 25 WpHG). In 16 cases fines were imposed of up to DM 15,000. Proceedings were suspended on grounds of insignificance in 36 cases, and for lack of evidence in 19 cases.

Statements made during the proceedings revealed that some of the institutions accompanying public offerings did not provide sufficient information about the notification requirements pursuant to Sections 21 ff. WpHG, even though the issuers are expecting them to do so. Adequate information on the part of the credit institutions might prevent a large number of notifications from being issued late.

## No Notification Requirement for Proxy Voting

The growing number of companies issuing registered shares has raised the question whether the registration of credit institutions in the share register on behalf of their

customers establishes a notification requirement. The BAWe believes that this is not the case. The WpHG sets out that the notification requirement applies only to those persons who are entitled to the voting rights connected with their shares (Section 21 WpHG). It is the membership rights embodied in the shares which are purchased or sold, not the voting rights. The Stock Corporation Act prohibits the separation of voting rights from the membership rights. This does not conflict with Section 67 paragraph 2 Stock Corporation Act which lays down that with regard to registered shares, the only persons to be treated as shareholders shall be those registered as such in the share register. In order to be registered in the share register the party in question must have been authorised accordingly by the owner of the shares. The buyer of shares bearing voting rights, be it registered shares or bearer shares, is free to decide whether to exercise these voting rights or not. With regard to bearer shares, the BAWe does not place under the obligation to report persons who are merely authorised to exercise voting rights on their own behalf or in the name of third parties. Neither do the provisions of Section 22 paragraph 1 number 7 WpHG establish a notification requirement because the Stock Corporation Act prohibits credit institutions from exercising proxy voting rights at their own discretion.

## Internet Database

In August 1997 the BAWe created a database providing an overview of major shareholdings in companies domiciled in Germany, whose shares are admitted to trading on an ex-

change in a Member State of the European Union or of the European Economic Area. Access to the database is granted on the Internet under [www.bawe.de](http://www.bawe.de). Several search options enable the investor to access information on current ownership structures. The data is updated on the 1st and 15th day of each month on the basis of the notifications submitted to the BAWe.

## Outlook

The Fourth Financial Market Promotion Act should make another contribution towards improving transparency. This is why the BAWe wishes for the regulated market to be included in the existing provisions relating to the notification and disclosure of major holdings of voting rights in listed companies. Since the Neuer Markt issuers are admitted to the regulated market, this measure would place the companies and their shareholders under the notification and disclosure requirements pursuant to Sections 21 et seq. WpHG. The notification and disclosure requirements play an important role in achieving the highest possible degree of transparency in the capital markets.

# CO-OPERATION IN GERMANY

## **Bundesaufsichtsamt für das Kreditwesen**

Under the functional approach (see page 9) the Federal Banking Supervisory Office (Bundesaufsichtsamt für das Kreditwesen; BAKred) is responsible for the licensing and the solvency control of investment services enterprises. It monitors the managers' trustworthiness and professional qualification, and the companies' financial situation. The protection of the institutions is the main regulatory objective of the BAKred. The BAWe is responsible for supervising customer transactions in securities and derivatives. In the context of market supervision it monitors compliance with the rules of conduct which are designed to ensure the proper execution of transactions in the interest of the customers. The main regulatory objective of the BAWe is to achieve investor protection.

Close co-operation of the supervisory authorities is essential for efficient supervision. This includes the regular exchange of data between the BAKred and the BAWe. For example, the BAWe's address administration system was restructured with data received from the BAKred. In addition, the authorities co-operate on a regular basis with regard to the issue of outsourcing activities to third companies.

Regular meetings between the BAKred and the BAWe held at management and at working level shall help to exploit synergies. In

1999, several meetings were held with the Federal Insurance Supervisory Office (Bundesaufsichtsamt für das Versicherungswesen) where representatives of the three authorities discussed the issues of derivatives, capital investments, supervision of stakeholders, and international co-operation.

The authorities also co-operate in terms of interpreting important legal concepts of the KWG and the WpHG. A uniform definition and interpretation shall be provided of concepts included in both acts. For example, last year the two authorities jointly examined whether operators of day trading centres can be considered to offer investment services, which would call for their supervision. Furthermore, the authorities co-ordinate their respective ordinances, guidelines, announcements and statements.

## **Wertpapierrat**

The securities council (Wertpapiererrat) held its annual meeting in September 1999. Apart from representatives of the 16 federal states, it can also be attended by representatives of the Federal Ministries of Finance, Justice, Economics and Technology, and of the Deutsche Bundesbank and the BAKred. The securities council advises the BAWe in basic issues relating to its regulatory tasks.

In its meeting, the securities council discussed among other subjects the issue of cold calling, which was prohibited by the BAWe in a general order released in August 1999. Another subject on the agenda was the Y2K problem. In the critical phase from 31 December 1999 to 02 January 2000 the BAWe operated an

"emergency centre" and remained in close contact with the individual federal states. Finally, the securities council dealt with new ordinances, amendments of guidelines and a revision of announcements relating to the Prospectus Act.

### **Länderarbeitskreis Börsenwesen**

Co-operation between the Exchange Supervisory Authorities in the various federal states has been given an institutional framework in the Working Committee of the Federal States on Securities and Exchange-related Issues (Arbeitskreis der Länder für Börsen- und Wertpapierfragen; short: Länderarbeitskreis Börsenwesen). The forum's meetings are regularly attended by a representative of the BAWe since some of the issues on the agenda concern the BAWe's area of responsibility. During its meetings in March and September 1999, the working committee discussed among other issues the proposed drafts for an amendment of the legal provisions relating to exchange brokers (Maklerrecht) and the prohibition of market manipulation. Other areas of emphasis included the supervision of alternative trading systems and the erection of trading screens of foreign exchanges in Germany. An extraordinary meeting with regard to the latter issue was held in April when the participants discussed details of the treatment of such applications.

### **Börsensachverständigen- kommission**

In 1999, the major issue occupying the Exchange Expert Commission (Börsensachverständigenkommis-

sion), which the BAWe attends as a guest, was the takeover code. One year after the amendments to the takeover code entered into force, in February 1999 the Commission presented a paper suggesting the creation of a legal framework for corporate takeovers. Also on the agenda were the other major aspects of the Fourth Financial Market Promotion Act, in particular the provisions relating to futures transactions, and the possible creation of a European stock exchange alliance. Working parties were founded that will deal with the issues of futures transactions and market manipulation.

The initial public offerings of shares on the Neuer Markt tended to be oversubscribed several times over in 1999. Private investors who did not receive shares often felt discriminated against when compared with institutional investors. This was a reason for the Exchange Expert Commission to establish a working party "Allocation in Case of New Issues (Zuteilung bei Aktienemissionen)" whose task is to set up principles for allocation procedures that can be complied with on a voluntary basis by the enterprises involved. In the meantime, the Exchange Expert Commission has passed these principles.

### **Finanzplatz e.V.**

In the year under review the association representing the interests of the German financial community, Finanzplatz e.V., worked out the paper "Grey Market and Dubious Business Practices" (Grauer Kapitalmarkt und unseriöse Geschäftspraktiken), and presented it at a press conference in February 1999. The BAWe was involved in its preparation. The paper shall provide an

overview of the various aspects of the grey capital market and give recommendations to investors. In addition, it provides the basis for an objective discussion of the grey capital market problem. Not least owing to the exceptionally positive reaction from the media and private investors, Finanzplatz e.V. will continue to deal with the issue of the grey capital market. In the scope of the "Finanzplatz Dialogues", a series of events hosted by Finanzplatz e.V., the president of the BAWe on 22 November 1999 in New York talked about the "Regulatory Considerations for Germany and the New Europe". A particular focus of his speech lay on the role of the national supervisory authorities in view of the ongoing process of integration in the European financial markets. To an ever greater extent the European supervisory authorities are challenged with the task of harmonising the legal provisions, thereby eliminating existing obstacles to cross-border securities transactions. The organisation dealing with this task is FESCO. The series of events "Finanzplatz Dialogues" address top representatives of the world's major financial centres and shall contribute to promoting the image of Germany as a financial centre. Finanzplatz e.V. comprises representatives of the industrial and banking sectors, investors, issuers, and the media.

# LEGISLATIVE PROJECTS

National borders are losing their importance to the extent that technological development facilitates the cross-border exchange of financial services.

## Fourth Financial Market Promotion Act

The Fourth Financial Market Promotion Act will take account of the growing importance of the Internet and the ongoing globalisation of securities trading. Its emphasis will presumably be on a reform of the Exchange Act, as well as on amendments to the provisions of the WpHG. There are plans to revise the provisions on market manipulation and on the capability to trade in futures and options. In addition, other laws, including the Prospectus Act, will have to be amended as well. A revision of the provisions on market manipulation will be necessary for investor protection reasons. As a result of the process of internationalisation in the investment business, and in the light of the planned co-operation among exchanges, manipulation will no longer only concern individual exchanges but take place across various exchanges or even across borders. This development has to be countered with updated legal provisions.

Over 40 amendments to the WpHG and the Prospectus Act have been proposed, which have arisen due to the BAWe's practical experience. Below we shall outline some of the proposed changes which are of particular importance to the BAWe:

- ◆ Establishing the legal basis for the treatment of certain cases of prohibited insider transactions as administrative offences, which shall exist in addition to the existing possibility of treating such cases as criminal offences.
- ◆ Establishing the legal basis for the imposition of fines in order to facilitate the enforcement of Part 5 of the WpHG, in particular compliance with the information requirements and the special rules of conduct pursuant to Section 32 WpHG, as well as the obligations relating to the outsourcing of services laid down in Section 33 paragraph 2 WpHG.
- ◆ Adjusting the reporting requirements for transactions in securities and derivatives to the changing market structures in the European Union and the European Economic Area, which are due, for example, to mergers among exchanges.
- ◆ Extending the notification and publication requirements in the case of changes of significant holdings of voting rights to companies whose shares are admitted to the regulated market.

## Takeover Rules

Another central issue in designing the legal framework for Germany as a financial centre has been the creation of a binding set of rules governing company takeovers. The Federal Government has declared that the relevant legislation will be passed in 2000. The BAWe is likely to be assigned the responsibility for monitoring compliance with the new provisions.

# INTERNATIONAL CO-OPERATION

The WpHG grants the BAWe comprehensive powers for co-operating with the competent foreign securities and exchange supervisory authorities. National supervisory systems are forced today to supervise internationally oriented and tightly knit securities markets and the players thereon with means that are restricted by national borders. International co-operation is therefore becoming increasingly important. The BAWe is authorised to pass on information to foreign authorities that is necessary for monitoring their respective exchanges and other securities markets. If necessary, it may likewise request similar information from foreign authorities.

## Insider Investigations

Within the scope of insider investigation the BAWe is authorised to request from market participants information about securities transactions or the respective principal's identity, when such information has

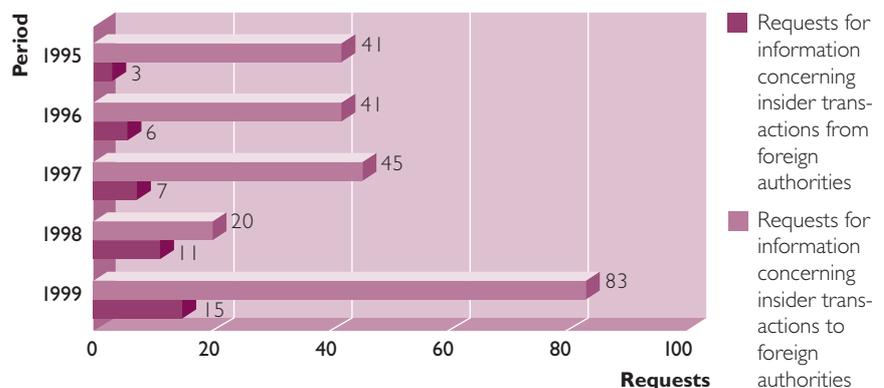
been asked for by foreign supervisory authorities. The confidential information may be passed on to the requesting foreign authorities. On the other hand, with respect to its own investigations carried on abroad the BAWe depends on the support granted by foreign authorities.

In the period under review the BAWe made use of its right to exchange information by submitting 83 requests to foreign authorities. The requests were related to 70 insider proceedings. In return, the BAWe was able to assist foreign supervisory authorities in 15 cases.

## Co-operation within Europe

Securities services enterprises domiciled in a Member State of the European Union or the European Economic Area are allowed to offer their services or establish a branch in all countries of the EEA without requiring an admission from the respective host country. They only need an admission in their home country. Securities services enterprises from other European states wishing to use the opportunities granted by the European Passport must inform the supervisory author-

## Requests for Information Concerning Insider Transactions from and to Foreign Authorities



ity of their home country, which in turn informs the BAWe and the Bundesaufsichtsamt für das Kreditwesen (BAKred). In the period under review 164 securities services enterprises benefited from the opportunities granted by the European Passport.

Of the 164 notifications, 154 concerned companies intending to offer cross-border investment services. Ten enterprises established a branch in Germany. The notifications were submitted by 14 different states, with more than half of the number coming from the United Kingdom. For the first time, securities services enterprises from Portugal and Greece took up business in Germany.

Within the scope of international co-operation in monitoring com-

## Projects for European Directives

A draft directive governing the takeover of companies has been presented in November 1997. The purpose of this directive is to protect minority shareholders when a company is taken over. According to the draft the offeror in a takeover shall be obliged to submit an offer to all shareholders, who shall be granted an adequate period for considering the offer. Takeover bids may provide that shares are offered for exchange, provided these shares are traded on a regulated market. The managing board shall be permitted to adopt defensive measures against a takeover only after the necessary approval has been granted by the general meeting.

The directive governing the distance marketing of financial services equally

European Commission. Rather than being granted a period for considering an offer, the customer shall be permitted to rescind the contract within a 30-day period. This does not apply to transactions in securities. The directive will probably be passed in the second half of 2000.

## EU Action Plan

In May 1999 the European Commission presented the Council of Economic and Finance Ministers (ECOFIN) with an action plan whose purpose is to improve the internal financial services market. At their summit in Cologne in June 1999 the heads of state and government expressed their consent with this objective. A particular target to be achieved is the creation of modern regulatory provisions that meet the demands of increasing globalisation, for example by revising the EU capital adequacy requirements in the area of banking supervision. High priority is given to the passing of a directive on takeover bids and a directive governing investment funds. The Admission Directive and the Listing Particulars Directive shall be amended in order to eliminate obstacles to the cross-border raising of capital in the internal market. In order to strengthen the common legal framework governing the securities and derivatives markets, the EU is planning to revise and, if necessary, change the Investment Services Directive and create a directive on combating market manipulation. Of particular importance for private customers is the adoption of directives concerning the distance marketing of financial services and on e-commerce, which are likely to facilitate and/or permit the access to the internal financial market. Both

### European Passport

Securities services enterprises are entitled to receive the European Passport for taking up business in another Member State of the European Union or the European Economic Area due to an admission from their home countries. The European Passport permits them to establish branches in other Member States of the European Union or the European Economic Area and to offer their services in these countries without having to undergo a separate application procedure in the host country. Apart from a few exceptions which concern in particular the rules of conduct, the companies are supervised by their respective home countries. Furthermore, the European Passport grants them immediate cross-border access to the electronic trading systems of the European exchanges.

pliance with the rules of conduct, the BAWe responded to 81 requests from foreign supervisory authorities. In 33 cases the BAWe contacted foreign regulators and asked them to provide information due to requests for assistance from German authorities ahead of criminal investigations.

aims at ensuring investor protection. The directive will concern financial services contracts which are concluded exclusively through remote means of communication. Following an initial reading of the draft, in May 1999 the European Parliament suggested fundamental changes that have been largely accepted by the

## Notifications Relating to the European Passport

Country	Notifications relating to the cross-border provision of services				Notifications relating to the establishment of a branch			
	1996	1997	1998	1999	1996	1997	1998	1999
Austria	–	–	4	13	–	–	–	1
Belgium	–	–	6	6	–	–	–	–
Denmark	5	3	–	1	–	–	–	–
Finland	–	–	1	13	–	–	–	1
France	1	29	5	7	–	–	1	–
Greece	–	–	–	1	–	–	–	–
Ireland	33	3	6	2	2	–	1	1
Italy	–	1	1	3	–	–	–	–
Luxembourg	–	–	1	2	–	–	–	1
Netherlands	20	5	2	12	1	–	–	–
Norway	–	8	5	–	–	–	–	–
Portugal	–	–	–	1	–	–	–	–
Spain	–	2	1	10	–	–	–	–
Sweden	13	2	–	1	–	–	1	–
United Kingdom	618	54	57	82	2	1	6	6
Total	690	107	89	154	5	1	9	10

proposals occupy a prominent position in the action plan.

### FESCO

In December 1997 the securities supervisory authorities of the 15 Member States of the European Union as well as Iceland and Norway founded the Forum of European Securities Commissions (FESCO). The president of the BAWe has been chairing FESCO since May 1998.

In January 1999 the 17 members of FESCO signed a multilateral memorandum of understanding (MoU) in order to facilitate and accelerate the exchange of information among the securities supervisory author-

ities. The aim of the MoU is to improve the transparency and integrity of the European securities markets and to enhance investor protection. The BAKred, Banca Italia and the Belgian pension fund joined the MoU in 1999. A group of high-ranking representatives of the supervisory authorities (FESCOPOL) is responsible for implementing the agreement.

FESCO's experts group "Standards on Fitness and Propriety" concluded its task in 1999. The members of the group passed minimum standards for the admission of investment services enterprises, guaranteeing the application throughout Europe of uniform standards for monitoring the fitness and propriety

of the management of securities services enterprises.

In December 1999 another FESCO experts group passed a paper on "Standards for Regulated Markets". The group was charged with establishing uniform standards for the areas of organisation, governance, market access, settlement and admission to trading, which shall specify the few existing provisions of the Investment Services Directive regarding this issue, and level out differences in the existing national provisions.

Also in December 1999, an experts group passed its "Market Conduct Standards for Participants in an Offering", which shall serve as a

basis for a common European level of investor protection. Participants in a securities issue have to make sure that sensitive information will not be misused to the detriment of investors.

Another experts group is charged with harmonising the rules of conduct for securities services enterprises. The purpose of this group is to streamline the rules of conduct derived from the Investment Services Directive, whose terms are rather general. In March 2000 the group presented as an interim result a definition of the professional investor.

With the aim of developing a common European basis for the mutual recognition of securities offers, at the end of 1998 the Forum of European Securities Commissions (FESCO) set up the experts group "European Public Offers". The group discusses different methods of cross-border securities offerings and develops criteria for the mutual recognition of such offerings. In its Financial Services Action Plan the European Union likewise advocates a revision of the legislation in force, in particular the Admission Directive and the Listing Particulars Directive, in order to eliminate legal obstacles to capital raising at a European level.

FESCO established three new experts groups in 1999:

- ◆ The group "Primary Market Practices" deals with stabilisation measures, trading in securities not yet issued and the allotment of securities, with the aim of working out recommendations for a common European practice.

- ◆ The group "Alternative Trading Systems (ATS)" classifies the different types of trading platforms which permit securities trading off the exchanges, and analyses their respective advantages and risks for investors. The cross-border activities of ATS require a European solution to the problems presenting themselves to the supervisory authorities.

### FESCO

The Forum of European Securities Commissions was founded on 08 December 1997 by 17 European securities supervisory authorities. The organisation's task is to improve investor protection and increase the transparency and integrity of the markets. The members exchange information and experiences, develop common regulatory standards in experts groups, and assist each other in monitoring the markets.

- ◆ The group "Market Abuse" deals with the issue of market manipulation which up to now has been dealt with completely differently in the various member states. The further development of a common European market for financial services requires the creation of uniform rules which establish the basis for efficient co-operation of the individual national supervisory authorities. The European Union is planning to pass a directive that will take account of the results worked out by FESCO.

FESCO established its own web site ([www.eurofefesco.org](http://www.eurofefesco.org)) at the end of 1999, making its publications – for example the common standards,

consultative papers and press releases – available to a broader public. A separate part that is accessible only to FESCO members facilitates and accelerates co-operation within the organisation.

### Outlook - FESCO

FESCO plays an important role within the EU Action Plan. In particular, it is expected to give recommendations with regard to new legislative measures of the European Union in the area of securities. When issues relating to securities supervision are on the agenda the chairman of FESCO participates in the meetings of the European Commission's "Financial Services Policy Group". In addition, FESCO has been granted observer status with the five forum groups of the European Union set up to implement the Action Plan. In these groups FESCO advocates that investor protection as well as the transparency and integrity of the securities markets be improved. In 2000, FESCO will deal with questions concerning the publication of ad hoc notifications, given the fact that the legal situations in the major financial centres of Frankfurt and in London are very different. It is especially important to find a solution to these and other matters in the light of the announced merger between Deutsche Börse AG and the London Stock Exchange. On 06 December 1999, FESCO conducted a workshop on the regulatory implications of co-operation or mergers between stock exchanges.

The Internet has developed into a major distribution channel for services and products. The growing number of households which are connected to the Internet has

equally led to changes in the area of financial services. The securities supervisory authorities in Europe consider this to be a positive development, but they are aware of the risks involved.

Private investors are able today to access current stock prices through their computers and carry out real-time securities transactions via quick and safe connections. News groups and chat forums provide investors with a large variety of information and enable them to exchange their respective investment strategies. However, the apparent anonymity of the Internet, in particular of the news groups and chat forums, opens up new opportunities for manipulation. For example, in 1999 Germany saw the first case of a misleading ad hoc notification being distributed

### **Memoranda of Understanding**

Memoranda of Understanding are bilateral letters of intent concerning the exchange of confidential information between supervisory authorities, which enable or facilitate cross-border co-operation by means of international assistance. The supervisory authorities undertake to provide assistance in the case of requests relating to investigations into insider cases, market manipulation or other offences, within the scope of their respective national laws. The information received may be used only for the purpose specified in each individual case, and confidentiality must be guaranteed. The standardisation of requests and transmission procedures makes it easier for the supervisory authorities to comply with their legal tasks.

through the Internet with the aim of manipulating the share price. Adequate protection of investors must be guaranteed to the extent in which the Internet facilitates the dissemination of information across national borders, thereby permitting issuers and investors to conclude cross-border securities transactions. In the next few years the European securities supervisory authorities will be required to work out means to ensure efficient investor protection in a changing environment. The efforts taken by the European Union to set up a new directive take account of the fact that attempts at manipulation will not be stopped by national borders. This makes it even more necessary to co-ordinate the European-wide prosecution of market manipulation and establish a functioning way of exchanging information.

### **Bilateral Co-operation**

Whereas co-operation with the supervisory authorities of the Member States of the European Union and the European Economic Area has to a large extent been regulated through EU directives, co-operation with the supervisory authorities of countries outside this region is usually based on bilateral agreements. The exchange of information with these countries depends on the extent to which national laws permit the request for and the collection and exchange of information, and on the obligations concerning the information requested which the competent supervisory authority has to comply with.

In practice, the supervisory authorities frequently sign written agreements on exchanges of information which are called Memoranda of

Understanding (MoU). In many cases MoUs serve the immediate needs of the German financial market. MoUs can be a prerequisite for the establishment of trading screens, for allowing German banks to take up business abroad, or for admitting the shares of foreign enterprises to trading on a German exchange. At the end of May 1999 the BAWe signed Memoranda of Understanding with the supervisory authorities of Poland and Brazil. The agreements have enabled the BAWe to intensify international co-operation with the respective authorities in the area of securities supervision, and to eliminate market barriers which in this form no longer exist in the European Union. In addition to a multilateral MoU with all countries of the European Union as well as of Norway and Iceland, similar agreements were signed before with the supervisory authorities of Hungary and the Czech Republic, with the SEC and the CFTC of the USA, and with the supervisory authorities of China, Taiwan, Hong Kong, Australia and Argentina. An exchange of letters takes place with Switzerland. In May 2000, the BAWe signed further MoUs with the supervisory authorities of Singapore and Turkey. An agreement with Japan's supervisory authority is currently being prepared.

### **IOSCO**

The International Organization of Securities Commissions (IOSCO) is responsible for enhancing multilateral co-operation between the various national securities supervisory authorities at a global level. As a member, the BAWe takes an active part in the efforts taken by IOSCO and represents the interests of Germany in its committees.

In May 1999 the members of IOSCO convened for their 24th Annual Conference in Lisbon. The main purpose of the Annual Conference lies with the presentation and discussion of the reports and recommendations on international standards which have been elaborated by IOSCO's working groups. At the Annual Conference, the Presidents' Committee decided to relocate the organisation's General Secretariat, which has been in Montreal since 1986, to Madrid. The General Secretary will take up his work in Madrid in the year 2000. Among other aspects, the relocation to Madrid should be seen as a sign of the growing importance of the European Member states in IOSCO.

It is of great importance to the BAWe to take an active part in all of IOSCO's committees in order to attend to Germany's interests. The BAWe is therefore represented through its president in the Executive Committee (central organisation) and the Technical Committee (committee comprising the supervisory authorities of the 15 most important capital market states). In addition, the BAWe is represented in each of the Technical Committee's five working groups and takes part in the drawing up of IOSCO's reports and resolutions.

Following the creation in 1998 of its report "Objectives and Principles of Securities Regulation" which provides comprehensive information relating to the requirements to be met by an efficient system of securities supervision, in the year under review the organisation dealt with the question of implementing at Member State level the three main targets and the 30 principles set out in the report. To this end it has been

## IOSCO

IOSCO (International Organization of Securities Commissions) was founded in 1983, developing out of a pan-American organisation established in 1974. Today it comprises 163 members from over 90 countries, including many supervisory authorities from the emerging markets. The organisation is first of all a forum for exchanging experiences. It takes efforts to develop globally accepted standards in major areas in order to guarantee the functioning and safety of the international financial system. The recommendations issued by IOSCO are not legally binding, but as a matter of fact the individual countries would hardly be able to ignore them. A major objective of IOSCO is to improve co-operation between the supervisory authorities and to provide mutual assistance in the prosecution of breaches of law.

necessary first of all to establish to what extent the principles have already been implemented by the Member States. In the year under review, a working group set up by IOSCO created detailed questionnaires which, once they have been completed and returned by the Member States, will in 2000 provide a basis for establishing the degree of implementation of the principles in the respective Member States. The necessary measures for implementing the principles will be carried out in co-operation with international financial organisations, in particular the World Bank and the International Monetary Fund, as well as with the regional development banks which have sent delegates to IOSCO working groups.

In 1998, within the scope of a comprehensive project whose objective was to facilitate multinational share issues and stock exchange admissions, IOSCO formulated standards on the maximum requirements to the contents of a selling or listing prospectus which a Member State may demand for cross-border listings. In the period under review IOSCO dealt mainly with the accounting standards underlying the preparation of an internationally compatible prospectus. An IOSCO working group examined whether the International Accounting Standards (IAS), developed by the International Accounting Standards Committee (IASC) upon consultation of IOSCO, are adequate to the special requirements of financial markets and investors. In May 2000, IOSCO recommended its members to permit the preparation of annual financial statements according to the 30 "IASC 2000 Standards" when securities are issued across borders. A company intending to be listed in a foreign country should be obliged to meet only a few of the national accounting principles when preparing its financial statements.

In a reaction to the near collapse of the US-American hedge fund Long-Term Capital Management in 1998, IOSCO established a task force that took up operations at the start of the year under review. Its task was to examine the activities of hedge funds and other highly leveraged institutions under supervisory aspects, with the aim of developing measures that will help to avoid systemic risks and ensure market stability. The BAWe took part in the task force. In its report published in November on "Hedge Funds and Other Highly Leveraged Institutions (HLIs)", the task force recom-

mended enterprises maintaining business relations to HLLs to establish efficient risk management processes. The report includes suggestions as to the design of such structures and processes, and how monitored companies might be convinced to implement them. Furthermore, the report advocates that HLLs be required to furnish more extensive information to the public, and that hedge funds be given incentives to improve transparency on a voluntary basis. An interdisciplinary working group is currently elaborating specific proposals for more extensive disclosure requirements for market intermediaries, which include HLLs. This working group comprises representatives of IOSCO, the Bank for International Settlement (BIS) and the International Association of Insurance Supervisors (IAIS).

### **Joint Forum: IOSCO – Basle Committee - IAIS**

With the aim of preparing themselves for the computer problems expected for the transition from 1999 to 2000, IOSCO, the Basle Committee on Banking Supervision (Basle Committee), the Committee on Payment and Settlement Systems (CPSS), and the IAIS set up the Joint Year 2000 Council in April 1998. Whereas initial efforts were dedicated to increasing the market participants' awareness of the problem, from autumn 1999 onwards the Council established a comprehensive information and notification system. The system, located with the BIS, made a significant contribution during the transition from 1999 to 2000 in facilitating the flow of information relating to the functioning of foreign financial markets. IOSCO likewise dedicated much of its efforts to the technical preparation

of market participants and its members for the year 2000 problem. The organisation set up emergency contacts in all Member States, who were even available at the turn of the year. IOSCO had reminded its Member States of preparing for Y2K in time in a declaration released as early as in June 1997. Thanks to the thorough preparation on the part of all participants from the financial sector, the transition to the year 2000 was made without any problems at all. The BAWe was responsible for the co-ordination of and reporting on the German securities markets. The remaining areas of the German financial markets were covered by the Deutsche Bundesbank, the Federal Banking Supervisory Office, and the Federal Insurance Supervisory Office.

IOSCO and the Basle Committee continued to co-operate closely in the area of risk management. Since 1995, the IOSCO Technical Committee and the Basle Committee have been publishing annual statements pertaining to the disclosure practice of internationally active credit institutions in respect of their trading and derivatives activities. The report for 1999 reveals an improvement in the companies' disclosure behaviour, in particular with regard to market risks. The analysis was carried out on the basis of guidelines set up by IOSCO and the Basle Committee. These guidelines establish minimum requirements for the collection of information about the banks' exposure to trading and derivatives that have to be met by the supervisory authorities. In addition, they define standards for informing the public that have to be observed by financial intermediaries. An amendment published in October 1999 to the Disclosure Guidance for Trading and

Derivatives Activities of Banks and Securities Firms includes categories of information which are of particular importance for the market participants. Supervision of internationally operating financial conglomerates continues to be an issue of close co-operation between IOSCO, the Basle Committee and IAIS. Financial conglomerates are active in several areas of the financial market, for example in the securities, banking and insurance businesses. Even on a domestic scale the supervision of such conglomerates is complex and demanding. At an international level it requires even greater efforts. At the start of the year under review the Joint Forum passed five papers concerning an improvement of the supervision of financial conglomerates, and recommended them for implementation at a national level. Another two papers were passed in October 1999, which defined principles to be observed by the supervisory authorities with regard to the monitoring of risk concentration and financial transactions, and liabilities within a corporate group. The tasks of the supervisory authorities therefore include ensuring that the companies take adequate measures for risk management, carrying out regular examinations, and co-operating with other supervisory authorities.

In December 1999 the Joint Forum was given an updated mandate to deal with issues of common interest to the participating supervisory authorities. Moreover, the mandate requires the elaboration of measures to facilitate supervision and improve the sharing of information in the context of supervising financial conglomerates. For details, please consult the web sites of the organisations involved ([www.iosco.org](http://www.iosco.org); [www.bis.org](http://www.bis.org)).

Apart from co-operating with the Basle Committee, in 1999, IOSCO also worked closely together with the Financial Stability Forum. The purpose of this group is to maintain the stability of the financial system and to reduce systemic risks, which shall be achieved by means of improving the exchange of information and through more intensive international co-operation in supervision. In addition, IOSCO maintains relations to the Committee on Payment and Settlement of the BIS. In July 1999, their co-operation led to the publication of a report on "Securities Lending Transactions: Market Development and Implications".

### Outlook - IOSCO

The international committees will continue to be responsible for adjusting the terms of financial supervision to the changing market environment, and for improving the regulatory standards even further. Weak points in the regulatory systems of some countries may easily have negative effects even on the financial markets and the economies of countries with sound supervision. It is therefore necessary to make every possible attempt at an international level – for example in the working group responsible for the implementation of IOSCO's core principles of securities regulation - to identify and close any gaps in supervision.

Improving co-operation at an international level will continue to be a major objective of the BAWe and of securities regulators throughout the world. The development of international supervisory structures has to keep pace with the rapid internationalisation of the markets and the creation of supranational

### Joint Forum

The Joint Forum (formerly: Joint Forum on Financial Conglomerates) came into existence at the beginning of 1996 and comprises the International Organization of Securities Commissions (IOSCO), the Basle Committee on Banking Supervision (Basle Committee), and the International Association of Insurance Supervisors (IAIS); it is a successor to the Tripartite Group. One of its aims is to work out standards for the supervision of financial conglomerates with international activities, thereby helping to ensure the stability and integrity of the financial systems. Financial conglomerates are defined as companies which are active in at least two areas of the financial markets – i.e. securities, banking or insurance. The Joint Forum helps to improve the exchange of information between the supervisory authorities concerned and to elaborate principles for more effective supervision of financial conglomerates. The Joint Forum currently comprises 13 countries, including Germany. The European Commission has been granted observer status.

exchange structures. In an environment where markets are becoming increasingly international it is necessary to avoid deficits and gaps in the supervision and prosecution of irregular behaviour – e.g. fraudulent investment broking or market manipulation. Particularly helpful in this context are the ten basic principles for the improvement of international co-operation in the context of criminal offences and breaches of law in the financial sector, which have been agreed upon by the G7 states - under German presidency - in the year under review. The G7 states advocate better co-operation between supervisory authorities and prosecutors at an international level. An IOSCO working group has worked out a report on the different types of market manipulation and the methods for discovering and combating such practices. The report was presented at the annual conference of IOSCO in May 2000. The efforts made with regard to international co-operation in the supervision of investment activities on the Internet are of particular importance in this context. The

usage of electronic means of communication in the financial sector is still growing rapidly. Therefore, in 2000 IOSCO will continue to deal with the regulatory challenges of the Internet – an issue it had started to address in 1998 with the creation of its Internet Task Force and the publication of its report "Securities Activity on the Internet". The Internet Task Force is chaired by the president of the BAWe.

# BAWe - INTERNAL AFFAIRS

higher service, 47 employees of the higher intermediate service, 29 employees of the intermediate service, one employee of the lower service, and two drivers.

## Personnel

In 1999 the BAWe was allocated twelve additional positions, adding to a total of 144 positions. However, in the context of the general reduction in the number of employees with the Federal Administration, staff was reduced by 7 as at 31 December 1999. The remaining 137 positions were respectively occupied by 86 civil servants, 36 white collar workers and two blue collar workers. Also employed with the BAWe were ten apprentices and one civil servant who had been delegated by the Federal Audit Office (Bundesrechnungshof) for a six-month period. Two civil servants were delegated to the EU Commission and to the Federal Ministry of Finance for a period of two years and six months respectively. The selection procedure for the twelve new positions assigned to the BAWe for the budget year 1999 was concluded by the end of the year.

Seven employees were granted extended leave (maternity leave, absence for family reasons). One person was hired on a temporary basis, and nine persons were working part-time. The share of female employees with the BAWe amounted to 37.9 per cent at the end of the year, the proportion of disabled persons came to 6.45 per cent. The average age was 34 years. Apprentices and the persons on leave or delegated to other authorities not included, the BAWe's staff was comprised of 45 employees of the

## Vocational and Further Vocational Training

In 1999 another two young persons were offered an apprenticeship to qualify as specialists for office communication. The BAWe is making this contribution to the vocational training of school leavers within the scope of its membership of the "Frankfurter Ausbildungsring", an association comprising 14 companies and local and state authorities in the Rhein-Main area which offer training opportunities to young people. Furthermore, the BAWe offered several legal trainees the opportunity to obtain an insight into the responsibilities and tasks of the BAWe.

The employees of the BAWe benefited from various job-related training opportunities. Seminars were held by the Federal Academy for Public Administration (Bundesakademie für öffentliche Verwaltung), the Federal Academy for Finances (Bundesfinanzakademie), and the Federal Office of Languages (Bundessprachenamt), as well as various private providers.

In-house seminars were held in areas such as information technology and stock exchange and securities matters. In addition, the BAWe offered its staff English language lessons. Some employees were able to visit foreign securities supervisory authorities to become acquainted with their work at first hand. Six persons successfully passed an exam as exchange traders.

## Organisation

On 15 August 1999 the BAWe adjusted its organisational structure to the changing environment, taking account of the new requirements of the markets, the growing sphere of its responsibilities, and the obligation to act economically. The division for insider supervision was subdivided into two independent divisions – insider supervision (II 1) and market analysis (II 4) – and additional staff was assigned to these divisions. Furthermore, it was necessary to reorganise the division for rules of conduct for credit institutions. Since then, division III 2 has been responsible for supervising compliance with the rules of conduct of savings and co-operative banks, whereas division III 3 is responsible for the supervision of compliance with the rules of conduct of foreign and private sector banks.

The growing responsibilities of the BAWe were to be taken into account in the area of central administration as well. Organisation, budget, cost allocation and controlling are now unified in an independent division (I 1). New areas of responsibility include cost-performance accounting, internal revision and the auditing of contract awards. The analysis of internal organisational structures and personnel requirements, which was started in 1997, the introduction of cost-performance accounting, and the creation of a modern controlling system are now carried out by this division. The other organisational unit within central administration is division I 2, whose duties include the areas of personnel, vocational and further vocational training, and internal administration.

## Information Technology

In view of the constantly increasing amount of incoming notifications pursuant to Section 9 WpHG – towards the end of 1999 the threshold of two million data records per day was exceeded for the first time – the BAWe upgraded the hard- and software of its database servers. The system architecture of a parallel computer and database environment has proved successful and has been maintained. The demands on the hard- and software solutions used by the BAWe are unique within the Federal Administration and are tailored to the requirements of the market environment. The majority of the necessary data migration and reconfiguration activities were carried out in-house.

The first version of SWAP (Securities Watch Application) has provided the BAWe with an effective means of detecting irregularities in the market and cases of insider trading. By means of statistical processes the system analyses the data submitted to the BAWe and generates indicators which provide direct indications of irregularities in transactions in the individual securities and of the notifying parties. The simultaneous examination of various indicators enables the BAWe to search the entirety of transactions for specific aspects and events. Further modules permitting an even more precise analysis as well as the identification of regulatory aspects are either in preparation or are already being tested.

The data of all tradable securities and derivatives are accessible via the Intranet from each work station of the BAWe. Furthermore, the

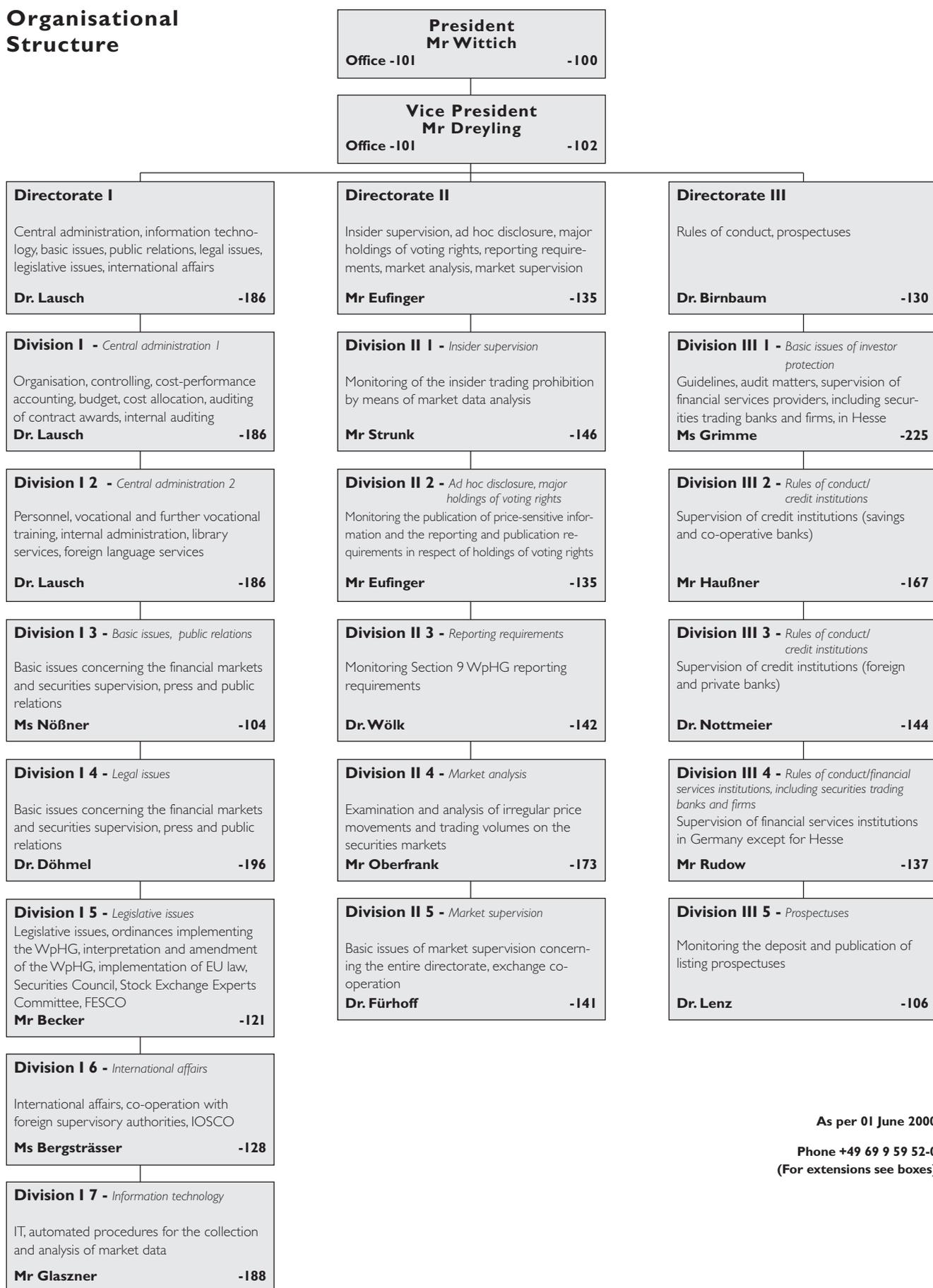
employees are able to retrieve real-time security prices as well as company and financial market news from a renowned information provider.

The BAWe has increased the respective capacities in order to take account of the growing importance of the Internet. Internet training programmes for users focus primarily on research techniques. With regard to the BAWe's regulatory tasks, this is of particular importance when it comes to monitoring the deposit and publication requirements relating to prospectuses. Access to Usenet and chat forums enables the competent divisions to monitor online activities, in particular with a view to detecting indications of market abuse. Moreover, the employees are able to send and receive electronic mail via the Internet from all work stations. These additional facilities have been integrated in the BAWe's IT concepts in terms of organisational structures and safety concerns.

## Budget

The BAWe is a superior federal authority within the ambit of the Federal Ministry of Finance and carried in the Federal budget under chapter 0806. All cash transactions are settled through the Federal Cash Office (Bundeskasse) in Frankfurt am Main and the Federal Tax Agency in Bonn. BAWe expenditures in 1999 amounted to approximately DM 17.5 million. Of this figure, DM 9.4 million was spent on personnel and DM 8.1 million on material costs and investments, the latter including an amount of DM 4 million which was spent on information technology.

## Organisational Structure



As per 01 June 2000

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(For extensions see boxes)

As a result of the amendment of the WpHG as at 01 January 1998, the BAWe's area of responsibility has been extended to include financial services enterprises, which were thus added to the list of the parties obliged to reimburse the costs of the BAWe. The cost allocation scheme was adjusted to take account of the additional group.

Ninety per cent of the costs of the BAWe shall be reimbursed to the Federal Republic of Germany by the parties obliged to reimburse the costs set out in Section 11 paragraph 1 sentence 1 WpHG. Apart from credit institutions, official brokers and other enterprises admitted to stock exchange trading, for the first time the newly regulated financial services enterprises were obliged to reimburse part of the costs as well in 1999. 68 per cent of the costs are to be reimbursed by the credit institutions, four per cent by official brokers and other companies admitted to stock exchange trading, and nine per cent by the issuers and financial services institutions. Ten percent of the costs are borne by the Federation. The parties obliged to reimburse costs were notified of the respective amounts.

The obligation to reimburse costs is set out in Section 11 paragraphs 1 and 2 WpHG in conjunction with the "Ordinance on the Allocation of the Costs of the Bundesaufsichtsamt für den Wertpapierhandel" (Umlage-Verordnung-Wertpapierhandel). The minimum amount to be reimbursed is DM 50. The costs must be reimbursed even if the legal requirements do not exist during the whole of the year.

The costs to be reimbursed by credit institutions as well as official

brokers and other companies admitted to stock exchange trading are allocated, pro rata, on the basis of the transactions disclosed pursuant to Section 9 paragraph 1 WpHG. The proportion of costs to be reimbursed by financial services institutions is determined on the basis of the ordinary result or – where proof is provided – of the gross return achieved through securities or own-account transactions. Finally, the costs to be reimbursed by issuers are based on the stock exchange turnover of their securities admitted to official trading or to the third market segment.

### Public Relations

The annual report for the year 1998 was presented to the public at a press conference on 12 August 1999. The focus of reporting was on the prohibition of cold calling announced at the press conference, i.e. the making of unsolicited phone calls to private customers, and on the success achieved in combating insider dealing. Also dealt with were the misuse of ad hoc disclosure and the BAWe's requests to the legislator.

Initial public offerings and the allotment of new shares to private investors were frequently mentioned issues in the press. At the start of 1999, the question of what should be regarded as an adequate degree of transparency in an allotment was intensively discussed. From the end of August 1999 onwards the media focused on the insider investigations into the takeover of Felten & Guillaume Energietechnik AG by Moeller Holding GmbH & Co. KG.

The leaflet "Geldanlage in Aktien, Renten und Derivaten: Wie Sie sich vor unseriösen Geschäftsmethoden

schützen können" ("Investment in shares, bonds, and derivatives - How to protect yourself against dubious business methods", only available in German) was extremely successful. Shortly after its publication a reprint was published in co-operation with Deutsches Aktieninstitut e.V. Approximately 75,000 copies were distributed in 1999, most of them to private investors, credit institutions, banking associations and consumer associations. The persistently high demand led to a third print run of 50,000 copies at the end of 1999. A contributory factor in the success of the leaflet was a television broadcast on 15 March 1999, in the course of which experts from the BAWe and Deutsches Aktieninstitut e.V. answered questions from the audience relating to the grey capital market.

On 23 February 1999 the BAWe held its first seminar for representatives of the press. Attended by some 30 journalists, it was the aim of the seminar on "Insider supervision by the BAWe" to inform journalists about the legal basis for insider prosecution and the nature of the BAWe's activities. The journalists were able to acquaint themselves with the complex background in direct talks with analysts and investigators from the BAWe.



# A SUMMARY OF SECURITIES SUPERVISION IN 1999

## **12 January 1999**

Preparation of the leaflet "Geldanlage in Aktien, Renten und Derivaten – Wie Sie sich vor unseriösen Geschäftsmethoden schützen können" in co-operation with Deutsches Aktieninstitut e.V.

## **15 January 1999**

Entry into force of the Ordinance on the Examination of Investment Services Enterprises pursuant to Section 36 of the Securities Trading Act (Investment Services Examination Ordinance) of 06 January 1999.

## **26 January 1999**

Signing of a multilateral memorandum of understanding on the exchange of information between the BAWe and the securities supervisory authorities comprising FESCO in Paris. In the context of the agreement it was decided to establish FESCOPOL, a permanent committee responsible for the practical aspects of co-operation.

## **27 February 1999**

Entry into force of the Ordinance on the Allocation of the Costs of the Bundesaufsichtsamt für den Wertpapierhandel (Umlage-Verordnung-Wertpapierhandel) of 22 February 1999.

## **12 March 1999**

The BAWe warns investors in a press release of payments to a false exchange supervisor.

## **16 March 1999**

Fourth forum on insider law and ad hoc disclosure held by the BAWe and Deutsches Aktieninstitut e.V. for judges, public prosecutors and criminal police officers.

## **18 - 19 March 1999**

25<sup>th</sup> international conference of representatives of the futures exchanges, market participants and supervisory authorities in Boca Raton, USA.

## **26 April 1999**

FESCO adopts minimum standards for the admission of securities services enterprises in Athens.

## **7 May 1999**

Entry into force of the Ordinance on the Fees Levied for the Deposit of Prospectuses (Verkaufsprospektgebührenverordnung - VerkProspGebV) of 7 May 1999, with retroactive effect as of 01 April 1999.

## **24 - 28 May 1999**

Annual Conference of IOSCO in Lisbon. IOSCO's General Secretariat to be relocated to Madrid.

**26 May 1999**

Memorandum of understanding between the BAWe and the securities supervisory authorities of Poland (KOMISJA PAPIRÓW WARTOŚCOWYCH I GIELD) and Brazil (COMISSÃO DE VALORES MOBILIÁRIOS).

**28 June 1999**

Letter to the managing boards of listed stock companies concerning the purchase of own shares pursuant to Section 71 paragraph 1 sentence 1 number 8 Stock Corporation Act.

**27 July 1999**

The BAWe adopts a general order pursuant to Section 36 b (1) and (2) Securities Trading Act concerning Advertising by means of Cold Calling.

**12 August 1999**

Annual press conference of the BAWe and presentation of the Annual Report 1998 in Frankfurt am Main.

**21 September 1999**

Publication of the announcement of the BAWe relating to the Act on the Prospectus for Securities Offered for Sale and of the Ordinance of the Prospectus for Securities Offered for Sale of 06 September 1999. The announcement replaces the previous announcement relating to the Prospectus Act of 15 April 1996.

**27 September 1999**

Fifth meeting of the Securities Council with the BAWe.

**6 November 1999**

Publication of the guidelines on the details concerning the organisational duties of investment services enterprises pursuant to Section 33 paragraph (1) of the Securities Trading Act of 25 October 1999. They replace the guidelines of 02 December 1998.

**22 - 23 November 1999**

Roadshow of Finanzplatz e.V. in New York in co-operation with the BAWe.

**17 Dezember 1999**

FESCO adopts "Standards for Regulated Markets" and "Market Conduct Standards for Participants in an Offering" in Paris.

**31 Dezember 1999**

Exchange of information during the transition from 1999 to 2000 about the functioning of the stock exchange and securities sectors (Joint Year 2000 Council).

# STATISTICAL APPENDIX

## Number of Insider Investigations

	New investigations	Investigation results in the period under review		Pending investigations at the end of the period under review
		Suspended	Passed on to the public prosecutor's-offices	
1995	24	16	7	1
1996	59	27	17	16
1997	55	40	22	9
1998	58	21	16	30
1999	39	27	13	45*)
<b>Total 1995 – 1999</b>	235	131	75	□

\*) figure corrected

□ figures do not make any sense

## Notifications from the Public Prosecutors' Offices Relating to Suspension of Insider Proceedings

	Total	Suspended proceedings		Court decisions		
			Of which: suspension against pay- ment of a fine	Final order imposing punishment	Final convictions	Final acquittals
1995	4	2	0	2	0	0
1996	7	3	1	4	0	0
1997	18	15	6	3	0	0
1998	25	21	13	4	0	0
1999	46	46	10	0	0	0
<b>Total 1995 – 1999</b>	<b>100</b>	<b>87</b>	<b>30</b>	<b>13</b>	<b>0</b>	<b>0</b>

Source: investigating public prosecutors' offices

**Number of Ad hoc Announcements**

	Total	Issuer's domicile		Means of publication	
		Germany	Abroad	Electronic media	Official stock exchange gazette
1995	1,001 *)	991	10*)	n.a.	n.a.
1996	1,058	1,024	34	1,020	38
1997	1,279	1,272	7	1,229	50
1998	1,856	1,805	51	1,798	58
1999	3,417	3,219	198	3,358	59
H1 1999	1,426	1,368	58	1,388	38
H2 1999	1,991	1,851	140	1,970	21
Q1 1999	635	615	20	616	19
Q2 1999	791	753	38	772	19
Q3 1999	911	857	54	901	10
Q4 1999	1,080	994	86	1,069	11
January	137	133	4	131	6
February	223	215	8	218	5
March	275	267	8	267	8
April	230	220	10	220	10
May	298	279	19	293	5
June	263	254	9	259	4
July	264	257	7	259	5
August	376	348	28	373	3
September	271	252	19	269	2
October	289	274	15	287	2
November	449	416	33	443	6
December	342	304	38	339	3

\*) figure corrected

**Proceedings to Impose Administrative Fines**

Subject matter	Year	Number of proceedings		Proceedings concluded finally in the period under review			Pending proceedings at the end of the period under review	
		Pending proceedings at the start of the period under review	New proceedings at the period under review	Total	Concluded through			
					Fines	Suspension		Transferral to public prosecutor's-office or other authorities
Reporting requirements pursuant to Section 9	1995	0	0	0	0	0	0	
	1996	0	0	0	0	0	0	
	1997	0	13	6	1	5	0	
	1998	7	12	5	2	3	0	
	1999	14	8	16	0	16	0	
Ad hoc announcements	1995	0	11	2	0	2	0	
	1996	9	16	7	0	7	0	
	1997	18	9	3	1	1	1	
	1998	24	13	6	0	5	1	
	1999	31	4	13	2	11	0	
Holdings of voting rights	1995	0	74	16	0	16	0	
	1996	58	179	88	15	73	0	
	1997	149	61	152	17	135	0	
	1998	58	29	61	12	49	0	
	1999	26	132	71	16	55	0	
Prospectuses	1995	0	20	10	0	9	1	
	1996	10	46	26	0	24	2	
	1997	30	74	30	7	23	0	
	1998	74	43	65	7	58	0	
	1999	52	74	56	15	41	0	
Other	1995	0	0	0	0	0	0	
	1996	0	0	0	0	0	0	
	1997	0	0	0	0	0	0	
	1998	0	4	2	0	2	0	
	1999	2	40	9	0	9	0	
Total	1995	0	105	28	0	27	1	
	1996	77	241	121	15	104	2	
	1997	197	157	191	26	164	1	
	1998	163	101	139	21	117	1	
	1999	125	258	165	33	132	0	

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