

Procedure file

Basic information		
INI - Own-initiative procedure	2003/2082(INI)	Procedure completed
The future of hedge funds and derivatives		
Subject 2.50.03 Securities and financial markets, stock exchange, CIUTS, investments		

Key players			
European Parliament	Committee responsible	Rapporteur	Appointed
	ECON Economic and Monetary Affairs	PPE-DE PURVIS John	20/05/2003

Key events			
05/06/2003	Committee referral announced in Parliament		
02/12/2003	Vote in committee		Summary
02/12/2003	Committee report tabled for plenary	A5-0476/2003	
15/01/2004	Decision by Parliament	T5-0031/2004	Summary
15/01/2004	End of procedure in Parliament		

Technical information	
Procedure reference	2003/2082(INI)
Procedure type	INI - Own-initiative procedure
Procedure subtype	Initiative
Legal basis	Rules of Procedure EP 54
Stage reached in procedure	Procedure completed
Committee dossier	ECON/5/19608

Documentation gateway					
Committee report tabled for plenary, single reading		A5-0476/2003	02/12/2003	EP	
Text adopted by Parliament, single reading		T5-0031/2004 OJ C 092 16.04.2004, p. 0340-0407 E	15/01/2004	EP	Summary

The future of hedge funds and derivatives

The committee adopted the own-initiative report by John PURVIS (EPP-ED, UK) on the future of hedge funds and derivatives. It began by pointing out that the term "hedge funds" covers a wide range of financial products, which might more appropriately be called "sophisticated alternative investment vehicles" (SAIVs). As many of these funds operate offshore and are not subject to EU regulation, the committee urged the Commission to introduce EU legislation in order to make lending by EU financial institutions to such offshore funds more transparent. MEPs stressed, however, that any EU-wide regulatory regime for SAIVs should be sufficiently "light-handed" so as not to negate their role as an alternative investment medium of choice or impede the freedom of investment managers to employ innovative techniques and instruments, take strong positions (including by the use of shorting, leverage and derivatives) and be remunerated relative to their importance, provided that their investment and operating methods are disclosed in appropriate terms to those who invest with them directly or indirectly. The committee therefore called for an appropriate regime to be developed for SAIVs which would help attract them to locate in the EU and provide the benefits of a common European passport by means of mutual recognition. It stressed that such a regime should concentrate especially on the distribution and sales methods employed, so as to avoid investment in them by persons for whom they are inappropriate. The report added that it was essential to provide individuals investing in SAIVs with a clear and simple risk description and warning to be acknowledged by them as representing their understanding of the risks involved. The committee stressed that derivatives were a completely different area and could not therefore be regulated in the same way as hedge funds. While useful, such financial instruments were also high risk and could increase volatility and threaten financial stability. The Commission should therefore pay particular attention to derivatives when drafting new or amended directives concerned with financial services and also at the implementing stage of the Lamfalussy process. Along with national and relevant international institutions, the Commission should also instigate a means of measuring and monitoring global exposure in derivatives and, in particular, the accumulated credit risk of credit derivatives. Lastly, the report called on the Commission to ensure that European derivatives exchanges should have fair and equal access to foreign market places and said that recent protectionist moves by US competitors were unacceptable. ?

The future of hedge funds and derivatives

The European Parliament adopted a resolution based on the own initiative report drafted by John PURVIS (EPP-ED, UK) on hedge funds and derivatives. (Please see the summary of 02/12/03.) Parliament felt that it was timely to develop a light handed and appropriate EU-wide regulatory regime for SAIVs which will help to attract them to locate in the EU and provide the benefits of a common European passport by means of mutual recognition. Furthermore, the regulator must verify that the promoters, directors and managers of a SAIV are fit and proper persons to be entrusted with responsibility for the savings and investment funds of third parties and are adequately expert and well-informed in the investment techniques and instruments employed in that undertaking. The risks inherent in any SAIV must be clearly advertised and communicated to investors, the advertised style of investment and level of risk must not be exceeded and risk should be properly monitored and controlled. The SAIVs regime should concentrate most particularly on the distribution and sales methods employed, so as to avoid investment in them by persons for whom they are inappropriate. It is essential to provide individuals investing in SAIVs with a clear and simple risk description and warning to be acknowledged by them as representing their understanding of the risks involved. Parliament stated that it expected the Commission to take action against Member States which, by differential taxation, additional regulatory requirements or other means, discriminate against SAIVs domiciled in other Member States. With regard to derivatives, Parliament asked the Commission to draw together the various relevant items of EU legislation in order to facilitate comprehensive legislative treatment (inter alia) of derivatives. The latter should also instigate a means of measuring and monitoring global exposure in derivatives and the accumulated credit risk (including settlement risk) of credit derivatives. Only those with appropriate capital cover may deal in derivatives, in order that, in periods of crisis, losses do not have to be borne by taxpayers. Parliament did recognise that significant regulation and regulatory structures already exist to cover derivatives. Reporting requirements must have adequate product coverage and relevant regulators should have the resources and expertise to assess this data effectively. Parliament went on to urge accountancy and investment management associations to require a high level of understanding of derivatives, their mechanisms and risks, as part of their qualification criteria. In addition, derivatives exposure (including timing gaps), which gives a fair and consistent indication of a company's true condition, should be a required disclosure in the accounts of European companies. Derivative valuations should take into account, by way of contingency reserve, the additional risks which could pertain in difficult market conditions and relative to the credit standing of counter parties. ?