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Présente :

ON-LINE TRADING: THE EUROPEAN LEGAL FRAMEWORK

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Financial services and products, already widely dematerialised in the developed economies, easily lend themselves to being offered on the Internet. The " network of networks ", by its world-wide, decentralised nature, allows for an almost infinite multiplication of the distribution channels particularly in the field of stock-market trading on the Internet ("on-line securities trading"). This sector, a fully committed member of e-commerce, is experiencing a dazzling expansion. Thus, in the United States, the forerunners in this matter, 8.5 million accounts were inventoried in March 1999, with 80 "on-line" brokers, totalling 523 billion dollars-worth of assets. It is often a question of "discount brokers", who, for low commissions, simply execute orders without providing the investor with any advice. Europe has already been caught up in the phenomenon.

However, such a development raises a number of legal problems. We are going to look at a few of these.

1. Determining the applicable law

Within the European Union, determining the law applicable to contractual obligations between a financial services provider and a consumer residing in another member State is governed by the Treaty of Rome. Pursuant to Article 5.2 of the Treaty, the choice by the parties of the law applicable may not result in depriving the consumer of the protection provided by the mandatory terms of the law of the country in which he normally resides from the moment when one of the following two hypotheses is encountered: (i) the conclusion of the contract has been preceded in the consumer's country by a specially prepared proposal or by some advertising and the consumer in that country has completed the actions necessary for the conclusion of the contract; (ii) the consumer's co-contractor or his representative has received the order in that country.

In the matter of on-line financial services, if the consumer concludes the contract on the Internet, for example by completing an ad hoc form on the provider's web-site, he must be considered as having completed in his country "the actions necessary for the conclusion of the contract".

With regard to the question of knowing whether the conclusion of the on-line contract has been preceded in the consumer's country by a specially prepared proposal or by electronic advertising, it may be considered that:

1. the fact for the consumer of surfing the Internet, of reaching the provider's site and deciding to enter into a contract there escapes the application of Article 5.2 of the Treaty of Rome, as

in such a case there has been no active canvassing on the part of the provider.

2. unsolicited offers by e-mail originating from financial service providers are covered by that provision. The applicable law will therefore necessarily be that of the consumer in such a case.

However, some situations are more difficult to define. For example, a financial services provider could, with the help of a marketing company specialising in the subject, arrange for a banner leading directly to his interactive business site to appear on the screen of a search engine, associated with the marketing company, each time a net-surfer inputs a key word, suggestive of the services offered by the provider, in the engine's dialogue window. Such a technique, being used more and more frequently, could come under active canvassing, since the net-surfer did not initially request the service offered, so that the applicable law would have to be that of the consumer.

2. Distribution of powers among the financial regulation authorities

With the appearance of e-commerce, the financial products and services have been directly marketable from any point on the globe, even from far-distant, complaisant countries where the statutory constraints encountered in industrialised countries may prove to be fewer, or even non-existent.

In such conditions, which will be the competent regulating authority when the same financial product is offered on the Internet, from a site which can be consulted throughout the world? How to avoid "universal" power of all the regulatory authorities in relation to one and the same financial operation?

It is especially to try to bring some elements of an answer to these questions that the International Organisation of Securities Commissions (IOSCO), grouping together the regulatory authorities from the main industrialised countries, adopted in September 1998 a set of recommendations on offering financial services via the Internet. These recommendations have already been adopted to a large extent, particularly in France, Belgium, the Netherlands, Italy and Canada.

In substance, according to the IOSCO recommendations, a regulatory authority will be able to declare itself competent to apply its rules when:

- a body of evidence indicates that a given national market is being targeted or canvassed by the supplier. Such pointers may be many and preferably a combination (use of a language other than English, advertisement in the local printed press of the site details, warnings on the welcome page stating that the marketing of the product is or is not authorised within some jurisdictions, obligation to register oneself by a password and

giving one's nationality and residential address before accessing the interactive business site, etc....).

- the activities conducted from abroad by the transmitter or provider of the financial services have a significant impact on the investors or the markets located within the regulator's jurisdiction. Such would be the case when a "virtual stock market" site generates substantial demand on the part of investors in a given State.

- in all cases, the regulatory authorities are competent in cases of fraud damaging or likely to damage the investors, whom their mission is to protect.

Inversely, some factors may lead to a regulator considering itself not competent:

- the provider states clearly to whom his offer is directed,

- the web-site contains a list of the jurisdictions within which it has or has not been authorised to make offers of financial services via the Internet,

- the provider takes reasonable precautions to avoid offering its services to residents in the regulator's State.

When working out these recommendations, the IOSCO was directly influenced by an interpretative communication dated March 1998 issuing from the American regulatory authority, the Securities and Exchange Commission (SEC). With regard to the notion of "reasonable precautions", the SEC stipulates there that the fact of allocating a password to new customers against the prior on-line communication of a foreign postal address and telephone number is considered as a reasonable procedure. Moreover, the American regulator deems that the "offshore" provider cannot be held responsible for any eventual false declarations which might be made in this respect by American residents, unless there is evidence for the belief that the customer would in reality be of American nationality (for example, payment for orders by cheques drawn on an American bank) and that the provider does not proceed with wider investigations to ensure that such is not the case (for example, obtaining a copy of the passport by fax). The SEC doctrine has also inspired the Australian financial regulator.

3. The legal validity of electronic documents

Within the framework of remote financial relationships, numerous electronic documents may have been exchanged (order or confirmatory e-mails, etc.). What is their legal validity?

In the majority of European countries, the validity of electronic documents is nil or uncertain. It is in order to raise these uncertainties that a European Directive has just been adopted on electronic signatures and the providers of certification services.

The Directive provides that an electronic signature cannot be legally dismissed for the sole reason of its electronic form. Moreover, some electronic signatures, called "advanced", will automatically be classed as hand-written signatures when they are based on certificates issued by certification service providers who satisfy a series of reliability and safety conditions. In the present state of the technology, these definitions in fact refer back to the digital or numerical signature, based on asymmetrical encryption, which enables communications to be rendered secure by encoding the messages sent.

4. The draft European Directive on distance selling of financial services

There already exists a Directive on consumer protection within the framework of distance contracts (including e-commerce), but the financial services were expressly excluded from it. It is to fill this gap that, on 14th October 1998, the European Commission presented a draft Directive establishing a statutory framework for the remote marketing of financial services, i.e. by telephone, mail, or electronic means (the Internet, for example). The draft was recently amended, on 26th July 1999, following amendments from the European Parliament. Its final adoption is not expected for several months.

The draft Directive includes to a great extent the terms of the Directive on remote contracts. It introduces, in particular, for the benefit of the consumer, a right of withdrawal of 14 to 30 days, which may be exercised by using the supplier's e-mail address.

5. The obligations to know and to inform the customer

Article 11 of the European Directive of 10th May 1993 on investment services imposes on financial intermediaries the requirement to inform themselves of the financial situation of their customers, their experience in matters of investments and their objectives with regard to the services requested. Moreover, they must communicate the relevant information in a suitable manner within the framework of their negotiations with their customers.

The application of these rules of conduct raises a particular problem in the case of on-line trading, to the extent that this is characterised by an absence of any "direct" or "vocal" contact between the intermediary and the customer, who may directly place an order without having been informed or placed on his guard by the intermediary as to the possible risk of the operation (the "execution only" system).

Some regulatory authorities have already given their opinions on this delicate question. Thus, in Belgium, the Banking and Financial Commission, in its circular dated 9th March 1999, has expressed itself favourable towards the introduction of minimum obligations, such as the prior definition of the profile and the know-how of the customer in investment matters, by applying if necessary limits to the operations authorised, the following-up of the operations to check to what extent the customer shows proof of good sense and a considered investment strategy (notably by establishing a posteriori control mechanisms enabling the establishment to detect possible abnormal transactions),or the distribution, either on its web-site or via hypertext links, of generic information on investments and on the general evolution of the markets.

At international level, the IOSCO has recommended that financial intermediaries should continue, even within the framework of on-line trading, to obtain sufficient, verifiable information about their customers, by means of on-line questionnaires or otherwise, and that they should arrange to provide suitable advice.

We do not think that the traditional personalised advice is required within the framework of on-line trading. In effect, the technology comes to the "rescue" of consumers by offering them, depending on the case, "educational" pages on the financial terms used, detailed reports about the stocks, software for portfolio analysis and management, stock-evaluation software, sometimes very detailed as well as simplified mechanisms to help with reaching a decision through a questionnaire enabling the risk-profile of the investment-surfer to be defined. In addition, in the near future, artificial intelligence programs will also be offered in order to assist customers, in a personalised manner, to reach informed decisions on their investments.

However, if an e-broker makes recommendations to purchase stock, outside any contractual obligation to give advice, for example by means of banners displayed on his web-site or by e-mails, he will have to be particularly attentive in providing a service suited to the customers concerned, on penalty of engaging his liability. In the United States, this is the reservation which has been long expressed by the SEC and the National Association of Securities Dealers (NASD).

6. Financial offences associated with the use of the Internet

6.1 Insider-dealing offences

Alongside the transactional functions, numerous credit institutions and intermediaries publish financial information on their sites, sometimes abundantly and in detail, or press releases. Some even organise discussion forums on the development of the financial markets.

The question which arises here is that of an insider-dealing offence. In fact, one of the elements constituting the offence is the existence of privileged information which has not been made public, i.e. which has not been broadcast by any means of mass communication.

Is the Internet a means of mass communication, comparable to the printed press and audio-visual media?

Given the web, and this tens of millions of regular users throughout the world, it is tempting to give an affirmative.
However, the Dutch regulatory authority - Stichting Toezicht Effectenverkeer (STE) - in its circular of 14th June 1999, is of a different opinion. In effect, according to the STE, a publication on the Internet cannot be likened to a "publicly available" communication within the meaning of Dutch law on insider-dealing offences. In its recommendation of May 1999 relating to the distribution of financial information on the Internet, the French regulatory authority, the COB, adopted a more realistic attitude by admitting that any information likely to have a significant effect on the Bourse rates may be given out simultaneously on the Internet and on other broadcasting carriers normally employed.

In any case, irrespective of the jurisdiction within which the provider is based, prudence dictates that financial information likely to substantially influence the rates of any financial instrument should not be broadcast on the web, if it has not already or simultaneously been made public in the "traditional" media.

As to the discussion forums, it certainly cannot be argued that they constitute "means of mass communication". The risk here is therefore greater that divulging sensitive information in that way will be classified as an insider-dealing offence.

6.2 Manipulating the market rates

Manipulation of the rates may take on the form of dissemination of information or rumours.

False or misleading information is likely to circulate on a wide scale over the web, for example with the aim of causing the rates of one or more stocks to vary, whether through the intermediary of a web-site, via the discussion forums, e-newsletters or by sending out a mass of e-mails.
In the discussion forums, it is easy to make believe in the existence of a large number of participants sharing the same opinion, for a single person to hide behind several pseudonyms or aliases. Besides those sending messages can include false information in with correct information without this being easily visible to the recipient. For example, with the creation of hypertext links, a site-owner may link his page to another page issued by a well-known financial intermediary or a financial regulatory authority.

In the United States, the editor of a financial newsletter published on the Internet was sentenced to 12 months imprisonment for having recommended in his "newsletter" the purchase of shares in the company Systems of Excellence, whereas he had previously received 250,000 shares in the company from the hands of its Chief Executive. The editor, having generated speculation among his readers, sold his shares, collecting a substantial gain in passing.

7. Obligation in matters of general policy and organisation

In general heavy obligations weigh on the providers of financial services in matters of general policy, particularly as to decision-making and marketing, as well as in the areas of organising accountancy, administration, contracts and information processing.

For example, In Belgium, pursuant to Article 62 of the law of 6th April 1995, stock-market companies and credit institutions must possess a management structure, an administrative and accountancy organisation, audit controls and safety mechanisms within the information-processing field appropriate to the business they are running, as well as internal audit procedures.

It is essentially on the basis of these provisions that the Belgian Banking and Financial Commission (CBF), in its circular of March 1999 on the provision of financial services via the Internet, listed a series of obligations weighing on the financial providers operating on-line.
Without going into details, among the points raised by the CBF may be mentioned: the obligation to ensure the security of the web-site, if need by having recourse to certification by independent organisations, the need to identify the customer in order to comply with the law of 11th January 1993 on the laundering of capital, the procedures for conserving successive versions of the web-site and the electronic orders placed by customers, the precise determination of the contractual framework with customers (use of a confidential password, operations targeted and authorised ceilings, etc.) as well as with the supplier of the Internet technology (liability in the event of a system failure, setting the ceiling per investor, guarantee of continuity of the service in the event of cancellation of the contract), the establishment of control procedures in the case of organising "chat rooms" or "bulletin boards", monitoring the choice of hypertext links referring to other financial sites and their presentation in order not to lead the customer into error regarding the source of the information, etc.
It should be noted that in France, the Financial Markets Council ("Conseil des Marchés financiers") adopted, on 15th September 1999, a regulation relating to the placing or orders via the Internet, which incorporates some of the points cited above, particularly with regard to the obligation on the part of the provider to possess permanently sufficient capacity in his computerised order receiving system, as well as alternative equipment in the event of a computer systems failure (telephone and/or fax). It is also interesting to note that the regulations impose the requirement on the provider to ensure that the

computerised system implemented for receiving orders is correctly rendered secure, with regard to current security standards for computerised systems.