Mads Andenas · Gudula Deipenbrock
Editors

Regulating and Supervising European Financial Markets

More Risks than Achievements

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Contents

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More Risks than Achievements?

Mads Andenas and Gudula Deipenbrock

1 Setting the Scene

Regulating and supervising financial markets efficiently and effectively has never been more complex than in the era after the 2007/2008 crisis. This is true in particular for the approach taken by the European Union and its Member States. The European Commission proposed more than forty legislative and other measures as part of the financial reforms since the 2007/2008 crisis. Critics increasingly doubt whether market players, regulators and supervisors have sustainably learned their lessons from recent crisis scenarios. For instance, some elements of the Capital Markets Union prominently featuring currently on the European legislator's agenda seek to revive the securitisation market without fully recognising the financial stability risks it poses. The main thrust of any regulatory effort is tackling dysfunctions of financial markets. Firstly, it aims at addressing flaws revealed in former crises. Secondly, it shall prevent or at least mitigate the development of new dysfunctions and risks. The latter preventive objective has become particularly important in the context with systemic risks. Global financial markets appear to be a permanently fertile ground for new crises. Dysfunctions and risks appear on a global scale. International cooperation of states, supranational entities and

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institutions in the realm of financial markets is more than ever in need. This, however, is not specific to financial markets regulation and supervision. Other crucial global risks in need of a joint international regulatory response include the current refugee influx in the European Union and climate change. Such developments in recent decades show that the principle of territoriality has so far lost its predominant role as a starting point for regulatory and supervisory measures. Supranational and international cooperation efforts whether in financial markets regulation and supervision or in the realm of combatting climate change or solving the question of refugees have gained remarkable momentum. They follow the insight that the dichotomy of internal and external affairs is no longer an uncontested tenet. The interconnection of climate change and the question of refugees in a not strictly legal sense is obvious. The progressing climate change—if not mitigated sustainably—is considered to become an important cause for population displacements leading to further migration waves. The interconnection of climate change and financial markets is meanwhile also acknowledged. The G20 Financial Stability Board announced at the Paris Climate Summit in December 2015 to set up a task force on climate-related financial disclosures. From the legal perspective this requires however rethinking and reshaping traditional legal concepts in all realms of law. This is particularly true for the realm of public law such as constitutional and administrative law but also for private law. This trajectory of further Europeanization and globalisation of traditionally national realms of law might however not be taken for granted. Strong opposite political movements particularly in some Member States of the European Union challenge such developments. Such movements include considering an exit from the European Union. Other different forms of strong opposition to further supranationalization or globalisation are evidenced by nationalist and also separatist tendencies gaining strength. The political landscape and the often unpredictable shifts and turns in political disputes at European level require undivided attention when discussing the idea of further centralisation of regulatory and supervisory powers at European level and thereby any continuous erosion of the principle of territoriality.

The European Union and the United States of America (US) might currently still be considered the most important players in the realm of regulation and supervision of financial markets. The main impetus for regulatory reforms worldwide came from the G20 Summits in Pittsburgh in 2009 and Seoul in 2010 (see on this Kern Alexander in Part I of this book). The regulatory and supervisory landscape for financial markets players in the European Union has radically changed since then. The processes of designing and implementing the reforms at European level since the 2007/2008 crisis have been critically conveyed by a vibrant academic literature. Such analyses were conducted against the backdrop of earlier stages of a work in progress. Many issues remained to be seen. Studies made during the peak(s) of the 2007/2008 crisis and in the immediately following years were produced without knowing the final shape of the regulatory reforms. Despite their high analytical and scientific value earlier assessments remained preliminary due to the lack of reliable experience with the operation of the introduced reform framework. In contrast to

such earlier analyses the editors and authors of this book enjoy the benefit of hindsight in various instances. An advanced although not final profile—if there will ever be one—of the various measures in the realm of regulating and supervising financial markets—in particular the originally introduced European System of Financial Supervision—has unfolded meanwhile. Focus of this book is on whether and to what extent the design, the organisational and operational structure, tasks, powers and instruments of the authorities forming the European System of Financial Supervision and the European Central Bank have allowed the authorities to respond to the challenges posed by financial globalisation and the rapidly deepening integration and interconnection of European financial markets. This is no textbook introducing the fundamentals of the European regulatory and supervisory regime. It rather compiles in-depth analyses of legal and economic issues of interest to an academic audience and to legislators, regulators, supervisors, courts and individual players in the regulated financial markets. The range of themes addressed is wide. A balanced account of the multiple issues worth exploring is hard to give. The chapters aim at exemplifying some of the major risks and achievements of the European approach to this sector of the internal market. Starting point for the contributions in this volume is the status of operation of the European regulatory and supervisory architecture. The emphasis is mainly on the institutional perspective, complemented by some practically important related substantive issues. A recurrent theme linking the majority of contributions is the notion and 'fencing' of risks, which occur in multiple shapes and different constellations at various levels. Identifying and preventing systemic risks affecting the whole European financial system as well as other risks linked in particular to individual financial markets actors are core concerns. Several years of operation of the sophisticated system of European macro-prudential and micro-prudential supervision allow some more advanced sound assessments on whether it has started to deliver on its ambitious goals and tasks. As to the European Central Bank, micro-prudential supervisory powers regarding credit institutions were conferred on it later and became operative in late 2014. The short term it has been in operation only allows assessments of the legislative approach and design of the European Single Supervisory Mechanism.

Critics worldwide have considered the current European supervisory structure of financial markets as a major development, or even a quantum leap, in European supervisory history. One might even share this view despite any criticism as to its various components. From the institutional perspective, the reshuffle of regulatory and supervisory powers of national and European authorities and institutions within the European and national constitutional limits added further complexity to the system. The increasing volume of legislative and non-legislative measures at European level adds to the opaqueness of the legal framework. This in turn might cause negative ramifications for its smooth operation. It is the operation and way of implementation of the European regulatory and supervisory regime, which will decide on its effectiveness and efficiency in the long run. Evaluations conducted at the level of regulating and supervising authorities and relevant European institutions including consultations involving stakeholders are necessary but not sufficient prerequisites to critically explore whether the European legislator chose and

continuously follows the right path. A broader scholarly perspective is in need to dissect the tension between the 'law in books' and the 'law in action'. Academia has a crucial role to play in this context. Scholarly research is committed to objective, un-biased methodology free of conflict of interests. Such methodology allows categorising the meticulous details of the legal framework in order to put it in a systematic context. It is committed to a wider scientifically driven long-term view. Its approach aims at avoiding biases. Such biases might in the case of assessments made by relevant authorities be due to their pressure for delivery on their missions and the narrowness of the intra-institutional perspective. In the case of the European institutions, particularly the European Commission, such biases might be caused by their pressure for political compromise, performance and self-assertion. In the case of (other) financial markets players such as banks, investment funds and credit rating agencies biases are caused by their individual economic interests to thrive in the markets. Financial markets appear to be particularly prone to conflict of interests as shown in recent crises as well as sectoral and corporate scandals due to the predominant role of money in the sector and the prospect of high yields (the greed factor).

The chapters of this book written by academics and researchers reflect the commitment to the principle of scientific objectivity in the realm of financial markets law. Such scientific objectivity is also in need to neutralise the specific language developed by financial markets. New technical terms have been and are invented continuously to describe specific financial markets phenomena such as products, scenarios and interventions. The inaccessibility of terms is increased by the use of equally opaque abbreviations. Technical neologisms are oddly supplemented by highly emotional delineations of events and developments in financial markets. The two extremes of over-confidence on the one hand and an exaggerated feeling of doom on the other hand alternate depending on the concrete situation. Objective legal language emancipating from such subjective perception plays a crucial role in gaining a realistic view on what interests are at stake. Apart from this common ground of scientific objectivity the individual approaches taken in the chapters of this book are refreshingly diverse. Firstly, the book covers chapters written from the perspective of law as well as the perspective of economics. Secondly, the book provides chapters written by senior and experienced scholars, legal counsel and young researchers. All the contributors take a fresh look at aspects of the regulatory and supervisory regime while developing at the same time some new ideas and critical views. The chapters written from the perspective of long-standing research experience in this field provide an integral way of viewing the European supervisory architecture for financial markets by putting its essential legal as well as economic components into a broader context. By that, the developing lines, structures, old and new pitfalls and achievements of financial markets regulation and supervision become visible. The approach taken in these chapters facilitates understanding the subject matter even by an audience not yet familiar with it. Thirdly, the diversity of chapters written from the legal perspective reflects the diversity of jurisdictions, legal traditions and scholarly or other professional environments from where the authors come. It is the authors'

commitment to a European autonomous interpretation of the European legal acts, which makes this diversity of legal backgrounds an important element in finding a substantially European approach. This latter diversity is likely to foster also comparative approaches in the realm of financial markets regulation and supervision. Here, such comparative approaches are required to analyse and understand—amongst others—the operational aspects of the institutional framework. This applies in particular to assessing the cooperation between national competent authorities and European authorities and institutions in regulating and supervising financial markets.

2 Structure of the Book

This book is structured as follows. It comprises 16 chapters arranged in two parts. The 16 chapters explore multiple different institutional and substantive aspects of the European supervisory architecture for financial markets. Those chapters addressing the European System of Financial Supervision as originally introduced and related issues are arranged in Part I of this book. Those chapters addressing the European Central Bank and banking supervision and related issues are arranged in Part II of this book. Focus of this book lies on the realm of capital markets and the banking sector. The editors chose these sectors of financial markets in order to limit appropriately the scope of this book to a manageable size. In so far as some chapters deal more generally with the European Supervisory Authorities covering the European Insurance and Occupational Pensions Authority, they also address the regulation and supervision of the insurance sector.

3 Some Substantive Highlights of this Book

Part I covers selected aspects of the European System of Financial Supervision—as originally introduced—with a focus on institutional issues from a European and comparative law as well as economic perspective. The first chapter by Gudula Deipenbrock explores the European Securities and Markets Authority and its regulatory mission. Focussing on the regulatory and not the supervisory role of the European Securities and Markets Authority allows valuable insights into the complexity and opaqueness of the rule-making process and the rules resulting from it. In this chapter, Deipenbrock identifies serious obstacles to the efficiency and effectiveness of the European Securities and Markets Authority in its role as regulator. Deipenbrock concludes with a plea requiring the European Union legislator and the European Securities and Markets Authority within its remit to steer a middle course regarding European capital markets regulation. By that, this chapter aims also to address the players directly, particularly the European Commission and the European Securities and Markets Authority. In considering and correcting the

various dysfunctions highlighted in this chapter both entities might mitigate the rather negative dynamics observed in the regulatory process without initiating any further reforms.

The second chapter by Trude Myklebust focuses on another important component of the originally introduced European System of Financial Supervision, the European Systemic Risk Board. Myklebust explores the essential institutional features of the European Systemic Risk Board and draws some conclusions as to its potential to perform its tasks successfully. The chapter ends on a more general note recommending clarifying the scope and reach of concepts such as systemic risk, macro-prudential supervision and financial stability in particular in order to allow an appropriate use of the macro-prudential powers at European level. The third chapter in this Part I by Iris Chiu takes a fresh look at the European financial regulatory architecture focussing on inter-agency relations, agency independence and accountability. Chiu argues that although a multiple-agency approach at European level may appear complex and anachronistic it has the potential to make the coordination and accountability of the various agencies work. Chiu concludes that the observations made might also be helpful for the effective functioning of the Single Supervisory Mechanism and the Single Resolution Mechanism and the effectiveness and legitimacy of European Union agencies in a wider context. The fourth chapter by Georgina Tsagas explores the European Supervisory Authorities with a focus on their regulatory powers. The constitutional, political and functional considerations and observations complement happily the ideas put forward in the preceding chapters. Tsagas suggests in particular clarifying the role and objectives of the European Supervisory Authorities in order to potentially allow a better balance between the European Commission and the European Supervisory Authorities in context with the regulatory process and help also ensuring an effective accountability mechanism in cases of conflicts.

The fifth chapter by Federico Della Negra aims at bridging the traditional methodological distinction between specific realms of law, here between European (public) law and domestic contract law. Della Negra makes an outstanding contribution in this field, and he explores the intersections between the (exercise of) powers of the European Securities and Markets Authority and national contract law. Della Negra argues in particular that such powers might strengthen the uniform interpretation and enforcement of contract law across jurisdictions. The sixth chapter by Giuseppe Bianco makes another outstanding contribution by building another bridge, the one of cooperation between the European Union and the United States of America in the realm of regulating and supervising financial markets. The chapter analyses strengths and weaknesses of the supervisory cooperation between the European Securities and Markets Authority and the US Securities and Exchange Commission. Bianco concludes that the European Securities and Markets Authority might well be considered as fostering its international activities. The seventh chapter by María Jesús Muñoz-Torres and Juana María Rivera-Lirio supplements the preceding analyses by some novel ideas on a sustainability impact assessment as regards the European Supervisory Authorities from the economic perspective. The

chapter suggests an expert system based methodology in order to measure the impact assessment of the European Supervisory Authorities with a view to sustainability. The methodology put forward uses inference rules to express human expert knowledge and experience. This enables Muñoz-Torres and Rivera-Lirio to propose one single sustainability index, which aggregates economic, governance, social and environmental performance indicators to an overall score. This innovative economic approach fits well in with the broader context of exploring the interconnection of financial markets and climate change risks as pointed out above.

The following two explorations of the eighth and ninth chapter are completing Part I of this book. They take a broader perspective on the developing lines of international financial regulation and financial supervision. The eighth chapter by Kern Alexander analyses the reforms in international financial regulation along macro-prudential lines. It focuses on the Financial Stability Board in addressing macro-prudential financial risks. The chapter explores how prudential financial regulation has evolved from an almost exclusively micro-prudential regulation of individual firms to a broader macro-prudential approach that attempts to identify and monitor systemic risks across the financial system and broader economy. Alexander discusses in particular how such change of regulatory focus caused institutional changes of international financial regulation under the oversight of the Financial Stability Board and the G20. Alexander also highlights other issues related to the debate on macro-prudential regulation such as environmental and social risks. In considering also these latter risks this chapter complements the discussion of the preceding chapter by Muñoz-Torres and Rivera-Lirio. The ninth chapter by Régis Bismuth discusses the federalisation of financial supervision in the United States of America and the European Union from the historical-comparative perspective. Here again, a broader international approach is taken to financial supervision by exploring in particular how political and legal differences between the systems of the European Union and the United States of America have shaped their institutional designs and structures of supervision. Bismuth concludes that such a comparative study highlights significant differences as to the interplay between federal and state supervisors.

Part II addresses selected aspects of the European Central Bank and banking supervision from the institutional perspective covering the legal and economic view. It comprises seven chapters, the tenth to the sixteenth chapter. The tenth chapter by Kern Alexander addresses the European Central Bank and banking supervision asking the question whether the Single Supervisory Mechanism provides an effective regulatory framework. It explores the institutional and legal context of the Banking Union. Alexander raises the critical question whether the strong form of independence of the European Central Bank is appropriate also for its new role as bank supervisor. He raises furthermore the question whether the narrowly defined supervisory powers of the European Central Bank as to individual banking institutions is adequate to address macro-prudential financial risks. This chapter is of great interest to the European legislator and the Member States of the European Union. It makes clear that the current shape of the Banking Union

requires further adjustments to allow the European Central Bank to become an effective bank supervisor. The role of the European Banking Authority after the establishment of the Single Supervisory Mechanism is analysed in the following eleventh chapter by Christos V. Gortsos. This chapter explores in particular the amendments made to the tasks and powers and the governance of the European Banking Authority and its redefined relationship to the European Central Bank. Gortsos concludes in particular that the complexity of the institutional constellation here raises legitimate concerns. The following chapter by Raffaele D'Ambrosio—the twelfth chapter in Part II—provides an analysis of the Single Supervisory Mechanism, highlighting some core concerns in this context. D'Ambrosio argues in particular that it is unjustified that the European Central Bank enjoys no limitation of liability in its role as supervisory authority. He suggests that within the Single Supervisory Mechanism the European Central Bank and the National Competent Authorities enjoy equal supervisory powers and that they should be subject to the same liability regime. To remedy this shortcoming D'Ambrosio suggests intriguing alternative solutions. In his view one could either infer a limitation of the liability of the European Central Bank from the Member States' laws providing legal protection for supervisors. Alternatively, D'Ambrosio suggests inferring a limitation of the European Central Bank's liability from the case law of the Court of Justice of the European Union and the 'sufficiently serious violation' criterion therein.

The thirteenth chapter in Part II is written by Maren Heidemann and Dania Thomas. It takes the case of the sovereign debt crisis as a starting point for an analysis of the judicial review in the eurozone and the resulting potential of the court system to act as a regulator, subject to the way in which the authors have defined their understanding of regulation. The authors combine in their chapter the legal perspective and the economic view on the subject and the status of justiciability of the financial institutions and in particular the European Central Bank. They argue that the actual use of the court system in financial regulation may impact negatively on the rule of law in the European Union and its Member States, and consequently compromise not only the effectiveness and efficiency of the supervisory and regulatory system in this area of law, but also its democratic acceptance. This could play further into the hands of the strong anti-European political movements.

The last three chapters of Part II, the fourteenth, fifteenth and sixteenth chapter, further investigate systemic risk(s) and related issues. The fourteenth chapter, by Jan Dalhuisen, takes a legal approach to the subject matter. Dalhuisen argues that systemic risk or more generally the stability of the financial system has superseded other regulatory concerns and become the major regulatory issue. His in-depth analysis provides insights into what it takes to adequately manage systemic risk and how regulators and supervisors best approach the matter. His main conclusion is that the present legal framework of the European Union concerning systemic risk and its regulatory supervision is neither robust nor transparent. Dalhuisen concludes in particular that after 2008 policy considerations prevailed over the protection of financial intermediaries, depositors and investors. The fifteenth chapter by Andreas

Horsch explores the regulation of systemic risk from an economic point of view. It analyses the regulation of Systemically Important Financial Institutions in the European Union. Horsch concludes in particular that the current European approach appears to be not well thought-out and prone to trigger unwanted market processes in future. The ideas presented in this chapter should become compulsory reading for the European legislator in order to better assess the risks linked to its regulation of Systemically Important Financial Institutions. The latter assessment is also true for the last chapter in Part II and the last one of this book, the sixteenth chapter which is by Jacob Kleinow. This chapter discusses from the economic perspective the concept of loss-absorbing capacity of banks. Kleinow introduces the concept of loss-absorbing capacity as an approach to orderly bank resolution in the European Union. This economic analysis by Kleinow as well as the complementary preceding one by Horsch allow a better understanding of the economic implications of regulating Systemically Important Financial Institutions. Both chapters concluding Part II and this book demonstrate convincingly the high value of innovative economic research for better laws in financial markets.

4 Outlook

This book provides insights into the structure and operation of the European regulatory and supervisory architecture for financial markets from various angles covering various different facets. Has it gone far enough to provide a sufficient system to reduce or mitigate systemic and other risks and handle financial crises? Or has it gone too far? No definite answer might be provided against the backdrop of the critical legal and economic analyses of this book. The picture is rather mixed. Achievements as well as still unresolved issues and even new challenges and risks have been identified. Apart from the unpredictability of future relevant political developments, it is in particular the complexity and increasingly accelerating change of financial markets and the still opaque interconnection of their components, which complicate any assessment as to whether the current European regulatory and supervisory design has proved itself to be efficient and effective against the backdrop of its operation. A multitude of diverse issues has been meticulously explored in this book. As the topics of the various chapters mainly address still—more or less advanced—work in progress the critical analyses and assessments provided in the chapters might well partly be considered also as (advanced) work in progress. They are contributions to the current and never more needed scholarly debate and will—it is hoped—enrich further reform discussions at the European and global level.

Part I
The European System of Financial Supervision as Originally Introduced from the Institutional Perspective: Selected Aspects from the European, Comparative Law and Economic View

The European Securities and Markets Authority and Its Regulatory Mission: A Plea for Steering a Middle Course

Gudula Deipenbrock

Abstract The European Securities and Markets Authority (ESMA) has played a pivotal role in shaping the operation of the European supervisory structure since its establishment in January 2011. The overall objective of the European Supervisory Authorities (ESAs) is to safeguard the stability and orderly functioning of the European financial system. ESMA shall achieve this objective in the realm of European capital markets (securities trading). Against the backdrop of ESMA's operation so far, this chapter will revisit from a scholarly perspective the organisational and operational design, tasks, powers and governance of ESMA. Focus is on ESMA's regulatory role, not its supervisory mission. ESMA's regulatory tasks are likely to keep it on top of the watch-list of the European Commission (Commission). In context with the Commission's work on establishing a Capital Markets Union (CMU) the Commission has emphasized particularly the importance of well-regulated capital markets. Main areas for action in this context are linked to ESMA's remit. Have ESMA's design and powers allowed it to contribute adequately to the development of a high-quality single rulebook as an essential element of an enhanced regulatory harmonisation and coherence? Has ESMA's institutional profile fostered or hindered it to become an efficient and effective 'rule-maker'? What features of ESMA's current design have proved themselves to be appropriate? Which of ESMA's institutional characteristics remain areas of improvement with a view to ESMA's regulatory mission?

Keywords ESMA • ESFS • European Securities and Markets Authority • European Supervisory Authorities • ESA • ESAs • European System of Financial Supervision • Financial markets regulation • Capital markets regulation • Financial crisis • Agencification • European agencies • Micro-prudential level • Macro-prudential level • ESMA Regulation • Meroni doctrine • Meroni rulings • Court of Justice of the European Union • Centralization • RTSs • ITSs • Lamfalussy process • Lamfalussy II process • Level 1 of legislation • Level 2 of legislation • Article 290 TFEU • Article 291 TFEU • Credit rating agencies • Accountability • De Larosière Report • Independence • German Federal Constitutional Court • Board

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of Supervisors • Regulatory task • Management Board • CRA III • Commission Delegated Regulation • Efficiency • Effectiveness • Over-complex • Opaqueness • Volumization • Dysfunctional • Dynamics • Financial stability • Harmonisation • Single rulebook • Institutional structure • Complexity • Complexification • Reform mode • European capital markets law • Rule-making

> 'The true strength of our democracies – understood as expressions of the political will of the people – must not be allowed to collapse under the pressure of multinational interests which are not universal, which weaken them and turn them into uniform systems of economic power at the service of unseen empires.'[1]

1 Introduction

The European System of Financial Supervision (ESFS) has been in operation mainly since 2011. It has widely been considered a key building block of the reforms the European Union (Union) enacted in response to the 2007/2008 financial crisis. Since its establishment, the ESFS—the European Systemic Risk Board (ESRB), the three European Supervisory Authorities (ESAs) working within the network of competent or supervisory authorities and the Joint Committee of the ESAs—has been challenged by on-going crises of various kinds. The European Commission (Commission) delivered its first report on the operation of the ESAs and the ESFS in August 2014 (Commission 2014 Report).[2] Beforehand, the European Parliament (EP) adopted a resolution with recommendations to the Commission on the ESFS review.[3] In addition to the ESFS, the European Banking Union has been conceived to ensure a more efficient and effective supervision of banks and an easier way of resolving them, if necessary. Mandatory for all Member States of the European Union (Member States) in the euro area and open to all other Member States are the Single Supervisory Mechanism and the Single Resolution Mechanism. The European Central Bank under the Single Supervisory Mechanism—operational since November 2014—has become the banking supervisor for all banks in the euro area, directly supervising the largest banking groups.

The ESFS addresses both the macro-prudential level and the micro-prudential level. At macro-prudential level focus lies on the avoidance of systemic risks to the entire European financial system. It is the responsibility of the ESRB to contribute

[1] The Holy See, Visit of His Holiness Pope Francis to the European Parliament and to the Council of Europe, Address of Pope Francis to the European Parliament, Strasbourg, on 25 November 2014.

[2] Report from the Commission to the European Parliament and the Council on the operation of the European Supervisory Authorities (ESAs) and the European System of Financial Supervision (ESFS), COM (2014) 509 final of 8 August 2014.

[3] European Parliament Resolution of 11 March 2014 with recommendations to the Commission on the European System of Financial Supervision (ESFS) Review, 2013/2166 (INL).

to ensuring the general stability of the European financial system. At micro-prudential level focus lies on the supervision of individual actors in the European financial markets in particular. This task has been assigned to the ESAs—the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA)—working within the network of competent or supervisory authorities and the Joint Committee of the ESAs. The ESAs started their operations in January 2011. This chapter focuses on selected institutional aspects of the regulation of European capital markets as one important sector of European financial markets. Reference is made to the widely accepted distinction between regulation of capital markets[4] and supervision of capital markets. Regulatory and supervisory actions might at times significantly overlap. Capital markets regulation shall describe any type of legislation not only by parliamentary legislators but also rule-making by public authorities or privately organised committees.[5] Capital markets supervision refers mainly to the application and enforcement of the relevant rules.[6] National capital markets laws in the Member States are increasingly influenced by European legal acts.[7] The use of European regulations[8] instead of European directives and the tendency towards maximum instead of minimum harmonisation[9] in general have been fostering this development. Hence, ESMA's regulatory role is of growing importance to the development and design of the European and the relevant national capital markets regulation. The aspiration of the Commission to complete the single financial market by fostering the Capital Markets Union (CMU)[10] is likely to add further dynamics to the regulatory agenda in practice. Such dynamics require critical monitoring and assessment from the scholarly perspective. This chapter explores selected current aspects of ESMA's regulatory role and performance from the institutional view. Focus lies on whether the organisational and operational design, tasks, powers and governance of ESMA allow it to fulfil its regulatory mission, effectively and efficiently. The chapter thereby aims to contribute also to the scholarly debate on the challenges posed by the continuing process of '*agencification*'[11] at Union level. The present author undertakes this

[4] The term capital markets law or capital markets regulation and securities regulation shall mean the same. Despite being used for ESMA's name, the latter term is generally more often employed in English and US-American law. See e.g. Moloney (2014).

[5] For more information on this with further references, see Walla (2013a), p. 27.

[6] For more information on this with further references, see Walla (2013a), p. 27.

[7] In Germany more than 80 % of the national capital markets law is based on European Union law. For more information on this with further references, see e.g. Buck-Heeb (2014), p. 10.

[8] See e.g. the European regulations on credit rating agencies. For more information on the regulatory and supervisory regime for credit rating agencies with further references, see e.g. Deipenbrock (2014a) and Deipenbrock (2014b).

[9] See e.g. Veil (2013b), p. 71; see also e.g. Buck-Heeb (2014), p. 10.

[10] For more information on the extent to which the CMU has already been completed, see e.g. Veil (2014).

[11] For more information on this and its constitutional implications, see Lenaerts (2014).

institutional analysis in particular against the backdrop of the following two developing lines in European capital markets regulation which deserve further attention: Firstly, the problem of increasing volume, (over-) complexity and inaccessibility of capital markets regulation, and secondly—partly linked to the first developing line—an inappropriate over-emphasis on the importance of capital markets services compared to that of real goods. The amount of capital markets rules has continuously increased. The regulatory regime provides further growth potential. The processes of making and amending of European capital markets rules have accelerated, also. European capital markets regulation is likely to remain in a permanent reform mode. These developments and the intricacies of the rule-making procedures, the flaws of legislative drafting and translation as well as methodological inaccuracies and the partly lack of systematics and consistent terminology[12] have led and are likely to further lead to over-complex rules. Such volumization and over-complexity have—amongst multiple other causes—also the effect that the importance of capital markets services is over-emphasized in relation to other areas of the internal market. Undoubtedly, the functioning of European capital markets is essential for economic growth. However, the present author pleads for bearing in mind that capital markets are not offering real goods but only special services. Such services shall serve to satisfy human needs and are not an end in themselves.[13] The principle of the serving function of capital markets services should essentially inform any capital markets regulation. It appears to be a *conditio sine qua non* for achieving sustainability or sustainable development as a high level objective of European Union primary law. It is provided prominently in Article 11 of the Treaty on the Functioning of the European Union (TFEU) and also in Article 3 of the Treaty on European Union (TEU) and its Preamble.[14] Against the backdrop of these more fundamental observations, the present chapter analyses selected institutional aspects of ESMA with a view to its regulatory role. It begins with critically introducing ESMA's mission and the legislative objectives as provided particularly in the Regulation establishing ESMA (ESMA Regulation).[15] The chapter proceeds with a concise depiction of ESMA's regulatory tasks, powers and institutional design including selected aspects of ESMA's operational and organisational structure. ESMA's 'position' shall be highlighted in relation to the core political European institutions and the Commission in particular including ESMA's part in the European legislative procedure. Focus lies on ESMA's independence and accountability. The chapter then assesses ESMA's regulatory performance in its

[12] For more information on e.g. the Financial Terminology Study of the Commission, see http://ec.europa.eu/finance/general-policy/terminology/index_en.htm, accessed 31 July 2015.

[13] See also e.g. Siekmann (2010a), p. 107.

[14] For more information on the Union's objective of sustainable development in context with corporate sustainability, see e.g. Deipenbrock (2011b) and Deipenbrock (2012). See also Deipenbrock (2013b).

[15] Regulation (EU) No 1095/2010 establishing a European Supervisory Authority (European Securities and Markets Authority), OJ L 331/84 (2010), as amended by Directive (EU) No 2011/61, OJ L 174/1 (2011) and Directive (EU) No 2014/51, OJ L 153/1 (2014).

first years of operation. To what extent has ESMA contributed or is likely to further contribute to the counterproductive developments in European capital markets regulation such as volumization, over-complexity and the over-emphasis of its importance compared to other sectors of the internal market? The chapter then concludes.

2 ESMA: Legislative Objectives and Mission

Any legislative objectives and mission of ESMA are to be considered against the backdrop of the overall objective of the Union to establish an internal market. European capital markets law developed tightly connected to the Union's aspiration to complete the internal market.[16] Accordingly, the legal basis of the regulations establishing the various components of the ESFS including the ESMA Regulation is Article 114 TFEU.[17] This article is the first one of Chapter 3 on 'Approximation of Laws'. It expressly refers to the achievement of the objectives set out in Article 26 of the TFEU: the establishment and functioning of the internal market. This broader European Union primary law context should be the starting point for any interpretation of ESMA's objectives and mission. Article 1 (5) of the ESMA Regulation provides ESMA's objectives. It begins with an 'umbrella goal': ESMA shall protect the public interest by contributing to the short, medium and long-term stability and effectiveness of the financial system, for the Union economy, its citizens and businesses. This is followed by more specified legislative objectives of ESMA. As the present chapter explores the regulatory role of ESMA, it might focus only on those legislative objectives relevant to ESMA's regulatory tasks and powers and their achievement. As to the internal market in general, ESMA shall contribute in particular to a sound, effective and consistent level of regulation and supervision. With a view to the financial markets, ESMA shall contribute to ensuring their integrity, transparency, efficiency and orderly functioning, and shall also contribute to the strengthening of international supervisory coordination, preventing regulatory arbitrage and promoting equal conditions of competition. ESMA is required to contribute also to ensuring an appropriate regulation and supervision of the taking of investment and other risks and to enhancing 'customer' protection. The express objective of 'customer' protection in context with the tasks related to consumer protection in Article 9 of the ESMA Regulation[18] mirror again

[16] For more information on the various phases of legislative activities at Union level in the realm of European capital markets law with further references, see Veil (2013a), pp. 2 et seq.

[17] For more information on this with further references, see Gruber (2011), pp. 4 et seq.

[18] See e.g. also Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the European Central Bank—Regulating Financial Services for Sustainable Growth, COM (2010) 301 final of 2 June 2010, p. 6, where the Commission refers to consumer protection in one of the headlines but to both consumers and investors in the text.

the internal market perspective of the Union legislator on financial markets regulation. Investor protection is not listed expressly as an objective. But it is listed as one of the manifold tasks of ESMA in Article 8 of the ESMA Regulation.[19] Whether this corresponds to the approach taken in the various capital markets laws of the Member States requires further comparative analysis. In German capital markets law, investor protection is a predominant objective.[20] However, ESMA's legislative objectives might dogmatically not clearly be distinguished from its concrete tasks. The Union legislator has drafted the relevant goals at a high level of abstractness employing vague taxonomies open to interpretation. These goals address the meta-level as well as the substantive contents of capital markets regulation. In addition to the legislative objectives as laid down in the TFEU and the ESMA Regulation, the Commission's interpretation of the ESAs' mission and ESMA's own view are relevant, also. In the Commission's view the overall objective of the ESAs is to sustainably reinforce the stability and effectiveness of the financial system throughout the Union.[21] The Commission stresses the part that the ESAs shall play in the development of a single rulebook applicable in all Member States by preparing uniform standards and ensuring supervisory convergence and coordination thereby contributing also to the functioning of the Single Market.[22] ESMA views itself as required to enhance investor protection and promote stable and well-functioning financial markets in the Union.[23] ESMA's (potential of) achievement of these goals will be considered below.

3 ESMA: Regulatory Tasks, Powers and Institutional Design

ESMA's institutional design and also that of the other ESAs have been informed by the recommendations of the High-Level Group on Financial Supervision in the EU[24] (de Larosière Report). The three ESAs have been shaped using the same pattern of organizational structure. Vesting legal status on the ESAs—see Article 5 of the ESMA Regulation regarding ESMA—has been one core policy decision in this context. It marked the shift from the preceding design of a 'network' of national

[19] See Sect. 3.1.

[20] For more information on this, see e.g. Buck-Heeb (2014), p. 4. See e.g. Mülbert (2013), p. 162.

[21] Report from the Commission to the European Parliament and the Council on the operation of the European Supervisory Authorities (ESAs) and the European System of Financial Supervision (ESFS), COM (2014) 509 final of 8 August 2014, p. 3.

[22] Report from the Commission to the European Parliament and the Council on the operation of the European Supervisory Authorities (ESAs) and the European System of Financial Supervision (ESFS), COM (2014) 509 final of 8 August 2014, p. 3.

[23] See ESMA's 2015 Work Programme, ESMA/2014/1200 rev of 18 February 2015, p. 1.

[24] Report of the High-Level Group on Financial Supervision in the EU of 25 February 2009.

supervisory authorities to integration as a form of centralization.[25] As stated in Recital 9 of the ESMA Regulation, the ESFS should be an integrated network of national and Union supervisory authorities, leaving day-to-day supervision to the national level. Another core policy decision has been to maintain the distinction between the regulation and supervision of the three sectors—capital markets, banks and insurances—as opposed to an all-finance supervisory approach. ESMA's regulatory tasks and powers are hence sectoral, limited to European capital markets. The horizontal interconnection of the three sectors is safeguarded by the Joint Committee of the ESAs.[26] In addition, the Boards of Supervisors of the ESAs comprise—amongst others—also of one representative of each of the other two ESAs as non-voting members. Before exploring ESMA's regulatory mission more specifically, it is required to stress that ESMA's supervisory mission, tasks and powers are equally important.[27] Both areas might overlap and inform each other. Both areas deserve separate in-depth analyses that allow exploring in more detail the interplay between ESMA's institutional design and the relevant mission. Rich literature exists also on ESMA's supervisory tasks and powers. One of the outstanding realms of supervision pivotal for assessing its supervisory performance is ESMA's role as single supervisor of credit rating agencies in the Union.[28] From the institutional perspective the Union's single supervisory authority approach to the credit rating sector has been highly conducive to an effective and efficient supervision of the European credit rating sector.[29] ESMA has remarkably contributed to the progress made in the realm of rating-directed supervision.[30] Any further exploration of ESMA's pivotal supervisory mission from the institutional perspective lies beyond the scope of this chapter.

3.1 Regulatory Tasks and Powers of ESMA

The chapter now turns to ESMA's main regulatory tasks and powers. The analysis starts from the perspective of the 'law in books'. ESMA's relevant tasks and powers are provided in general in Articles 8 et seq. of the ESMA Regulation. They address both supervision and regulation. Several European capital markets rules adopted

[25] For more information on this with further references, see Granner (2011), pp. 34 et seq. For more information on the developing lines of European capital markets law, see e.g. Wilhelmi (2014), in particular pp. 700 et seq.

[26] For more on this with further references, see Granner (2011), p. 35.

[27] For more information on ESMA's supervisory mission, see e.g. Moloney (2011b).

[28] For more information on the developments and multiple aspects of the regulation and supervision of credit rating agencies in the Union, see e.g. Deipenbrock (2009); Deipenbrock (2011a); Deipenbrock (2013a) and Deipenbrock (2014a).

[29] For more information on the preceding institutional design with further references, see Andenas and Deipenbrock (2011), pp. 10 et seq.

[30] For a concise overview on this, see e.g. Deipenbrock (2014b).

since the establishment of ESMA have extended continuously ESMA's scope of tasks and powers.[31] No strict line might be drawn between tasks and powers on the one hand and the objectives and mission of ESMA on the other hand. Instead, they are rather interconnected and overlap. Starting point of the analysis are some fundamentals on the taxonomy in the realm of secondary European Union law. The Union institutions might adopt regulations, directives or decisions, make recommendations or deliver opinions according to Article 288 of the TFEU. The TFEU designates such instruments as legal acts. A distinction is made between legal acts and legislative acts. Those legal acts that are adopted in a legislative procedure are designated as legislative acts. The ordinary form of such a legislative procedure consists of a joint adoption of a legislative act by the EP and Council following a Commission's proposal. Legislative acts may delegate power to adopt non-legislative acts of general application to the Commission. The Commission might only supplement or amend non-essential parts of the legislative acts without interfering with the essence of the legislative acts. The distinction between legislative and non-legislative acts informs the system of rule-making in European capital markets law and shapes the relevant parts of the Commission and ESMA in it. ESMA has the task to give advice to the Commission regarding its rule-making.[32] ESMA might also develop draft regulatory technical standards (RTSs) and implementing technical standards (ITSs), issue guidelines, recommendations and opinions and take decisions.[33] ESMA's regulatory tasks are tightly linked to the four levels of legislation relevant in European capital markets law, the Lamfalussy process. The Lamfalussy process was first introduced in 2002.[34] The Treaty of Lisbon and the ESMA Regulation caused amendments to the Lamfalussy process, while maintaining in general the four levels of legislation (Lamfalussy II Process[35]).[36] In the Lamfalussy II Process, Level 1 of legislation still covers framework acts enacted by the EP and Council in the ordinary legislative procedure which constitute the foundation of European capital markets law.[37] But in the Lamfalussy II Process Level 2 of legislation has changed. The Treaty of Lisbon introduced Articles 290 and 291 to the TFEU which lay down procedures of delegation and implementation in European Union primary law for the first time.[38] Level 2 of legislation of the Lamfalussy II Process covers delegated acts adopted by the

[31] Parmentier (2014), p. 50.

[32] For more information on this, see Walla (2012), pp. 28 et seq.

[33] For concise information on this with further references, see Walla (2012), pp. 27 et seq.

[34] For more information on this with further references, see Rötting and Lang (2012).

[35] The term 'Lamfalussy II Process' might not be considered as the generally employed term. For more information on this with further references, see Weber-Rey and Horak (2013), p. 721.

[36] In addition, Regulation (EU) No 182/2011, OJ L 55/13 (2011), known as Comitology Regulation, provides important procedural requirements. For more information on this with further references, see Walla (2013a), pp. 28 et seq. and 33.

[37] For more information on this with further references, see Walla (2013a), p. 33.

[38] See Rötting and Lang (2012), p. 8.

Commission after consulting ESMA and also those drafted by ESMA, the RTSs, which complement the Commission's delegated acts and are endorsed by the Commission.[39] Both the Commission's delegated acts and the endorsed RTSs are delegated acts under Article 290 of the TFEU.[40] Apart from that, Level 2 of legislation of the Lamfalussy II Process covers implementing acts of the Commission and ITSs drafted by ESMA and endorsed by the Commission.[41] By that, post-Lisbon and after the establishment of ESMA, Level 2 of legislation of the Lamfalussy II Process has gained much complexity. The 'law in books' provides sophisticated distinctions between legislative and non-legislative acts and complex adoption processes. This over-complex approach is rooted in European Union primary law restrictions as discussed below.[42] In contrast to seemingly sharp dogmatic distinctions, the 'law in action' has shown that neither the distinctions made by Articles 290 and 291 of the TFEU nor the relationship between the Commission's acts and those drafted before by ESMA—the RTSs and ITSs—are always clear.[43] ESMA's powers to develop draft RTSs and ITSs are provided in Articles 10 and 15 of the ESMA Regulation. Both RTSs and ITSs might be developed in the areas specifically set out in the legislative acts referred to in Article 1 (2) of the ESMA Regulation. The Commission might adopt such RTSs and ITSs either as regulations or as decisions. Both RTSs and ITSs thereby become directly applicable. They do not require any transformation by the Member States. ESMA's importance in the rule-making procedure is particularly mirrored in the fact that the Commission is only exceptionally allowed to deny the endorsement of RTSs and ITSs. One might speak of 'quasi rule-making powers'[44] of ESMA.

The different 'nature' of RTSs and ITSs reflecting the dogmatic distinctions made in Articles 290 and 291 of the TFEU corresponds to differences in their contents as provided in the ESMA Regulation. Under Article 10 of the ESMA Regulation, the contents of RTSs shall be limited by the legislative acts on which they are based. RTSs shall be of technical nature. They shall not imply strategic decisions or policy choices. As to their adoption, it is required in particular that the EP and the Council delegate power to the Commission to adopt RTSs by means of delegated acts under Article 290 of the TFEU. Such delegation of rule-making power has to be in line with the fundamental principles of the Union, the rule of law, the principle of checks and balances and the democratic principle in particular. Hence, the power to adopt RTSs is conferred on the Commission under Article 11 of the ESMA Regulation only for a 4-years-period with automatic extensions for periods of an identical duration, unless revoked by the EP or the Council. In its

[39] For more information on this with further references, see Walla (2013a), p. 34.

[40] For more information on this with further references, see Walla (2013a), p. 34.

[41] For more information on this, see Walla (2014), p. 45.

[42] See further below in this Sect. 3.1.

[43] For more information on this, see Walla (2014), pp. 44 et seq. For more information on the CoJ's approach on this, see e.g. Ritleng (2015).

[44] See with a view to the ESAs e.g. Moloney (2011a), pp. 43 et seq.