CURRENT DEVELOPMENTS

EUROPEAN UNION LAW

Edited by Joseph McMahon

I. RESETTING THE LOCATION OF REGULATORY AND SUPERVISORY CONTROL OVER EU FINANCIAL MARKETS: LESSONS FROM FIVE YEARS ON

A. The Single Rulebook

Some five years on from the Autumn 2008 collapse of Lehmans, the regulatory dust from the Global Financial Crisis has settled. Significant regulatory policy debates are still underway internationally, notably with respect to the treatment of shadow banking.[1] But the main contours of the crisis-era regulatory landscape are now clear. Internationally, most major economies, including the EU, have implemented the G20 reform agenda, set out initially in the 2008 Washington Declaration,[2] and covering, *inter alia*: bank capital, liquidity and leverage; hedge funds; rating agencies; and the over-the-counter (OTC) derivatives markets. That major regulatory change would have followed the financial crisis is not, of course, a surprise.[3] Observation of responses to major financial crises over the years from the 1929 Crash to the 'dotcom bubble' era and beyond[4] makes clear that what Professor Coffee has vividly described as the 'regulatory sine curve'[5] leads to a regulatory boom after financial market bust.

In the EU, G20-based regulatory reform has additionally been accompanied by a relocation of regulatory control over financial markets.[6] Over the first major reform era, the 1998–2005 Financial Services Action Plan (FSAP) period, liberalization-driven regulatory reform in support of cross-border activity had seen the location of financial market regulation shift to the EU from the Member States. The crisis-era, driven by the financial stability agenda and the need to address the pathologies of liberalization as well as the G20 agenda, has witnessed the almost complete ascendancy of the EU. This has been driven by a host of factors, including political commitment to a 'single rulebook' and the removal of regulatory divergence; the G20 agenda and the EU's related concern to shape the international rulebook; institutional reform (notably the

[1] Recent key developments include Financial Stability Board (FSB), *Strengthening Oversight and Regulation of Shadow Banking* (2013) and Commission Green Paper, *Shadow Banking* (COM (2012) 102).

[2] G20, Declaration, Washington G20 Meeting, 14–15 November 2009.

[3] eg R Romano, *Regulating in the Dark* (2012) Yale Law & Economics Research Paper No 442, available at <http://ssrn.com/abstract=1974148>.

[4] F Allen and D Gale, *Understanding Financial Crises* (OUP 2007) 190–215.

[5] J Coffee, 'The Political Economy of Dodd-Frank: Why Financial Reform Tends to be Frustrated and Systemic Risk Perpetuated' (2012) 97 CornellLRev 101.

[6] This short review focuses for the most part on securities markets and not on the banking reforms. For further analysis of the crisis-era rulebook see N Moloney, 'The Legacy Effects of the Financial Crisis on Regulatory Design in the EU' in E Ferran et al, *The Regulatory Aftermath of the Global Financial Crisis* (CUP 2012) 111.

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establishment of the European Supervisory Authorities (ESAs) as part of the new European System of Financial Supervision (ESFS) in 2011 and which are conferred with a range of quasi-rule-making powers); extensive reliance on administrative rule-making by the Commission, including the new process for adopting 'Binding Technical Standards' (BTSs) which are proposed by the ESAs (the European Securities and Markets Authority (ESMA) in the securities markets sphere) but adopted by the Commission;[7] strong institutional backing from the Commission and Parliament for an extension of the perimeter of EU regulation; and considerable political and institutional support for the curbing of speculation and of financial market intensity and innovation, driven in part by the toxic transformation of the financial crisis into a sovereign debt crisis as the costs of bank failures threatened sovereigns' borrowing capacity, and related concerns as to the role of speculators in the sovereign debt markets. The extent to which rule-making power has moved to the EU is well illustrated by the Commission seizing the initiative when the global interest-rate fixing scandal broke over summer 2012 and producing a related proposal for reform.[8]

Some five years on, the EU regulatory landscape, previously shaped by liberalization, has changed almost out of all recognition. Two distinct phases to the construction of the new rulebook can be identified. The first wave of reforms was closely related to the G20 agenda and concerned with financial stability and ensuring a secure regulatory perimeter and the effective regulation of previously unregulated sectors; it was also concerned with the distinct risks to the EU market arising from cross-border risk transmission and, as the sovereign debt crisis took hold, the destructive feedback loop between the fiscal implications of banking failure and the resilience of sovereigns. These reforms focused on strengthening EU banking regulation (most notably through the massive 2013 Capital Requirement Directive reforms which have implemented the Basel III reforms to bank capital, liquidity, and leverage regulation[9] and introduced additional, primarily governance-related reforms, and through the ongoing bank recovery and resolution reforms[10]); and on reinforcing EU securities market regulation which, hitherto, had not engaged closely with stability, being traditionally more associated with disclosure-related regulation and the efficiency and transparency of markets and with pan-EU market access. The latter reforms are exemplified by two perimeter-changing measures which have captured market actors not previously subject to EU regulation. The Alternative Investment Fund Managers Directive 2011[11] has extended the asset management regime, which was previously liberalization-driven and focused on the retail-market-oriented 'UCITS' collective investment scheme and its management,

[7] The European Markets Infrastructure Regulation 2012, eg, (Regulation (EU) No 648/2012 OJ (2012) L201/1 (EMIR)) is amplified by nine sets of BTSs.

[8] Commission Proposals COM (2011) 651 and COM (2011) 654 (both bringing benchmark manipulation within the EU's market abuse regime); a wider regulatory reform is also in train.

[9] The final banking rulebook takes the form of the 2013 Capital Requirements Directive (which covers governance, sanctions, capital buffers, supervision, and a reduction in reliance on rating agencies) and the Capital Requirements Regulation (which covers capital, liquidity, leverage and counterparty credit risk) (respectively, Directive 2013/36 OJ (2013) L176/338 and Regulation (EU) No 575/2013 OJ (2013) L176/1).

[10] There are two elements to the reform; the harmonized rulebook governing bank recovery and resolution (COM (2012) 280) (a negotiating position was reached by the ECOFIN in June 2013); and the establishment of a Single Resolution Mechanism as part of Banking Union) (COM (2013) 520).

[11] Directive 2011/61 OJ (2011) L174/1 (the AIFMD).

to include almost all non-UCITS fund managers, including private equity, property, and commodity fund managers, although it has become most associated with hedge fund regulation. The 2012 EMIR (European Market Infrastructure Regulation) has brought radical change to the over-the-counter (OTC) derivatives markets, requiring in-scope derivatives to be cleared through Central Clearing Counterparties (CCPs) and, in effect, imposing major infrastructure reform on a previously lightly-regulated segment of the financial markets. The securities market stability agenda also includes the EU's new rating agency regime, composed of Credit Rating Agency (CRA) Regulations I (2009),[12] II (2011)[13] and III (2013)[14] and the 2013 CRA Directive[15] (which together have led to a new regulatory regime for rating agencies, their supervision through ESMA, and a series of reforms to the rating of sovereign debt), and the 2012 Short Selling Regulation, which imposes new restrictions on short selling in a range of financial instruments, including sovereign debt.[16] This phase can also be associated with the major institutional reforms which have reshaped EU financial system governance: first, the initial 2011 establishment of the ESFS, composed of national competent authorities, the ESAs (conferred with a range of quasi-regulatory and supervisory tasks[17]) and the European Systemic Risk Board, charged with macro-prudential system oversight;[18] and second, the 2013 agreement on the Single Supervisory Mechanism element of the Euro Area Banking Union,[19] which provides for the supervision of Euro Area banks through the European Central Bank.[20]

A second wave of reform has followed and has led to the reform programme extending beyond financial stability and embracing reforms which can be more closely associated with market efficiency (and in particular the effectiveness of markets in

[12] Regulation (EU) No 1060/2009 OJ (2009) L302/1.
[13] Regulation (EU) No 513/2011 OJ (2011) L145/30.
[14] Regulation (EU) No 462/2013 OJ (2013) L146/1.
[15] Directive 2013/14 OJ (2013) L145/1.
[16] Regulation (EU) No 236/2012 OJ (2012) L86/1.
[17] On the ESAs see eg M Everson, *A Technology of Expertise: EU Financial Services Agencies* (2012) LEQS Working Paper No 49/2012, available at <http://ssrn.com/abstract=2085233>; E Ferran 'Understanding the Shape of the New Institutional Architecture of EU Financial Market Supervision' in G Ferrarini, K Hopt and E Wymeersch (eds), *Rethinking Financial Regulation and Supervision in Times of Crisis* (OUP 2012); P Schammo, 'EU Day-to-Day Supervision or Intervention-based Supervision: Which Way Forward for the European System of Financial Supervision?' (2012) 32 OJLS 771; N Moloney, 'The European Securities and Markets Authority: A Tale of Two Competences. Part (1) Rule-Making' (2011) 12 European Business Organization Law Review 521; and N Moloney 'The European Securities and Markets Authority: A Tale of Two Competences: Part (2) Rules in Action (2011) 12 European Business Organization Law Review 177.
[18] See eg K Alexander and E Ferran, 'Can Soft Law Bodies be Effective? The Special Case of the European Systemic Risk Board' (2010) European Law Review 751.
[19] Banking Union is composed of a number of elements, including a harmonized banking rulebook (contained in the 2013 CRD reforms), harmonized national deposit protection schemes (the related proposal is currently stalled), a Single Resolution Mechanism and a Single Supervisory Mechanism based on ECB supervision of Euro Area banks: Commission, *A Roadmap towards a Banking Union* (2012) (COM (2012) 510).
[20] See further E Ferran and V Babis, *The European Single Supervisory Mechanism* (2013) University of Cambridge Faculty of Law Research Paper No 10/2013, available at <http://ssrn.com/abstract=2224538>.

supporting long-term savings and growth[21]), transparency and integrity, and with consumer protection. The cornerstone of investment firm and trading market regulation, for example, the 2004 Markets in Financial Instruments Directive (MiFID I)[22] is being overhauled by the MiFID II and Markets in Financial Instruments Regulation (MiFIR) reforms[23] which have the effect of capturing a much wider range of firms, markets, and trading practices within the regulatory net. The asset management regime, for example, has been further expanded by discrete regimes for venture capital funds, social entrepreneurship funds, and long-term investment funds, designed to enhance the ability of markets to raise capital.[24] The consumer protection regime is undergoing major reforms which include the adoption of a new, cross-sector measure designed to address the distribution of packaged investment products and their disclosure regulation, and to close gaps in the current regime (the Packaged Retail Investment Products (PRIPs) reform[25]). Long-standing elements of EU securities market regulation, including the capital-raising regime,[26] the market abuse regime[27] and the UCITS investment fund regime[28] have all been reformed.

The recast regulatory regime still has a youthful feel and remains somewhat unstable. Most of the 'second wave' measures have yet to be formally adopted[29] and the momentum implications of Banking Union for securities markets and for Member States not part of the Euro Area are not clear. But much, including an extensive administrative rulebook, is now in place; the review process is already underway, underlining the state of permanent revolution which EU financial market regulation has been in since October 2008. The 2012 Short Selling Regulation, for example, is under review,[30] and the 2013–14 ESA review is underway. It is therefore possible to make some preliminary if necessarily tentative observations as to the cumulative impact of the reform programme, particularly with respect to the new and wider perimeter of the crisis-era rulebook.

[21] Commission, Green Paper. 'Long-Term Financing of the European Economy' (2013) (COM (2013) 150/2).

[22] Directive 2004/39 OJ (2004) L145/1.

[23] COM (2011) 656 (MiFID II) and COM (2011) 652 (MiFIR). The European Parliament and Council reached negotiating positions in October 2012 and June 2013 respectively.

[24] Respectively, Regulation (EU) No 345/2013 OJ (2013) L115/1; Regulation (EU) No 346/2013 OJ (2013) L115/18; and COM (2013) 462.

[25] COM (2012) 352.

[26] The cornerstone Prospectus Directive has been reformed (Directive 2010/73 OJ (2010) L327/1) as has the Transparency Directive, which governs ongoing disclosure (COM (2011) 683; the Council and Parliament reached political agreement in May 2013), and the related accounting regime (Directive 2013/34/EU OJ (2013) L182/19). These reforms are broadly designed to streamline the relevant regulatory regimes and bring greater efficiencies to the capital-raising process.

[27] COM (2011) 651 (Market Abuse Regulation) and COM (2011) 654 (Market Abuse Directive – on criminal sanctions). Political agreement was reached between the Council and Parliament in June 2013.

[28] COM (2012) 350 (the 'UCITS V' reforms, which focus in particular on the UCITS depositary). A wide-ranging UCITS VI reform agenda has also been presented: Commission, 'UCITS. Product Rules, Liquidity Management, Depositary, Money Market Funds and Long-term investments' (2012).

[29] Leading the European Parliament to criticize the lack of progress on key proposals, including those relating to deposit protection schemes: European Parliament, *Resolution on European Parliament Priorities for the Commission's Work Plan 2014*, 26 June 2013 (B7-0325/2013).

[30] ESMA has published its review: ESMA/2013/614.

The perimeter of EU financial market regulation has been cast around a vastly greater set of market participants and actors. In the securities market sphere, for example, a wide array of asset managers (under the AIFMD), proprietary traders and dealers (under MiFID II/MiFIR), previously unregulated OTC markets (under MiFID II/MIFIR and EMIR), and rating agencies (CRA I-III), to identify only a few examples, are now within the EU rulebook. Similarly, EU securities market regulation, which traditionally has been concerned, more or less, with the equity trading markets and with the major public trading markets will address a much wider range of asset classes and a host of trading venues. Under the MiFID II/MiFIR reforms most forms of organized trading in bonds and derivatives will come within the EU rulebook, while the combined effect of MiFID II/MiFIR, the Short Selling Regulation, and EMIR is to impose an entirely new and detailed rulebook on derivatives trading in the EU which, for the most part, had largely been a function of market discipline prior to the crisis. Entities which do not participate in the financial markets professionally but which engage in incidental financial activities are being pulled into the regulatory net; EMIR, for example, has led to the imposition of complex and potentially costly rules on non-financial entities which use derivatives as hedging tools for their commercial business. Market-shaping regulation has always been a feature of EU financial market regulation, most notably in relation to the MiFID I order execution reforms which reallocated the benefits of trading across different trading venues, but it has become pronounced. EMIR and MiFID II/MiFIR, for example, re-engineer the organization of the OTC derivative markets by interposing CCP clearing and by requiring that these derivatives trade on regulated trading venues rather than bilaterally. MiFID II/MiFIR is also designed in part to pull more trading on to regulated venues and away from the lightly regulated OTC markets.

Leaving aside the well-worn debate on the relative merits and demerits of harmonization versus competition, and on the risks associated with harmonization on this scale, regulation of this ambition, range, depth and intensity places great pressure on the EU rule-making process. From the very many challenges which arise, two can be highlighted. First, careful calibration of regulation is required given the differential impact which rules of this range and intensity can have on market actors, based on their size, complexity, and business model. The AIFMD, for example, has required careful calibration through administrative rules and ESMA guidance given the wide range of fund managers which come within its scope. Second, unintended consequences, which can include a reduction in market efficiency where regulatory costs prejudice risk management and thereby liquidity, can be significant: the Short Selling Regulation's prohibition of certain short sales in relation to sovereign debt, for example, was untested and imposed with very little empirical evidence; the proposed new MiFID II/MiFIR regime for regulating bond and derivative trading venues similarly has a thin empirical base; and there is considerable uncertainty as to the cumulative impact of the reform programme generally on the availability of the high-quality collateral (or assets) now required to secure a range of different transactions.[31]

The vulnerability of the institutionally fragmented and highly politicized EU law-making processes to producing sub-optimum financial system rules has been

[31] The cumulative impact of the G20 reform programme on the stock of global high-quality collateral has become a recurring theme in the international policy debate. The Commission has also raised concerns: Commission, *Financial Stability and Integration Report* (2012) (SWD (2013) 156) 26.

extensively documented.[32] It remains to be seen whether the new rulebook will have prejudicial effects, although some indications augur well.[33] But it seems clear that the success of the regime is likely to depend on its ability to correct and calibrate. The extensive review clauses[34] to which all the crisis-era measures are subject (and which were initially used over the FSAP period) provided a means for releasing political tensions during the negotiating process. But they also hold the promise of useful *ex-post* review. ESMA has significantly enhanced the EU's technical capacity in the securities markets sphere at the administrative rule-making level and has demonstrated its ability to corral complex market data, engage with market stakeholders, liaise with international standard-setters, and to adopt complex rules.[35] ESMA has also opened a safety value in that it has shown itself capable of providing temporary mitigations where confusion and the risk of prejudice to market efficiency arise.[36] But correction at the legislative level is likely to remain necessary given the scale of the crisis-era rulebook. Whether or not the law-making process can cope with large-scale refinements and recalibrations remains to be seen. The MiFID I Review, which has led to MiFID II and MiFIR, grappled with the difficulties which MiFID I generated with respect to competition in the trading market sphere, but resolution of these difficulties has proved a politically-charged process and led to old political battles being reopened;[37] on the other hand, the review has led to a significantly more nuanced approach to trading venue regulation.

The extended perimeter also applies to the international market. By contrast with the FSAP-era, the crisis-era reforms have seen the EU export its regulatory model globally. Access to the EU market has increasingly become conditional on compliance with equivalence criteria which are often broadly designed to apply the EU rulebook. The rating agency regime, for example, requires that rating agencies are either established in the EU and registered and supervised by ESMA or that equivalence criteria are met with respect to ratings used in the EU produced by a non-EU rating agency. The AIFMD's highly contested and complex third-country access provisions similarly make market access conditional on equivalence criteria. EMIR makes market access by third country CCPs and the trade repositories which hold OTC derivative market data subject to ESMA registration and compliance with an equivalence assessment. Equivalence

[32] E Ferran, 'Crisis-driven regulatory reform: where in the world is the EU going' in E Ferran et al, *The Regulatory Aftermath of the Global Financial Crisis* (CUP 2012) 1 and L Quaglia, 'The ''Old'' and ''New'' Political Economy of Hedge Fund Regulation in the EU' (2011) 34(3) West European Politics 665.

[33] ESMA has reported that the Short Selling Regulation, despite some febrile speculation as to its potentially prejudicial effects, did not have material adverse effects on market liquidity and price discovery: see (n 30).

[34] Which typically set a date (usually within two to three years of the measure coming into force) within which the measure must be reviewed and identify the particular issues which the review must address; these issues usually include contested measures at the time of the original negotiations as well as proposals for future action.

[35] This was particularly evident from the EMIR BTS process which required ESMA to engage with highly complex regulatory design questions given the regulatory *terra nullius* which the EMIR delegations to BTS preparation represented.

[36] This was particularly the case with ESMA's guidelines on the operation of the Short Selling Regulation's exemption for market makers (ESMA/2013/158).

[37] N Moloney and G Ferrarini, 'Reshaping Order Execution in the EU and the Role of Interest Groups: From MiFID I to MiFID II' (2012) 13 European Business Organization Law Review 557.

assessments are typically linked to regulatory and supervisory assessments and so represent a potentially intensive assessment of third country regimes. Access aside, the extraterritorial impact of EU regulation is strengthening. EMIR's requirements, for example, apply even where both counterparties to the OTC derivative transaction are established outside the EU. The Short Selling Regulation similarly applies to non-EU parties, as long as the financial instrument comes within the scope of the Regulation. Although mitigants apply in each case, in principle the two regimes have significant extraterritorial impact.

The extended international perimeter of the EU rulebook may strengthen the EU's capacity as an international actor and enhance its ability to achieve access by EU actors to third country markets and obtain concessions on the application of third country rules. But it may also create a new location for conflict between the EU and its Member States as to control over the rulebook. Equivalence assessments are increasingly becoming centralized. In the case of the CRA, AIFMD and EMIR regimes, for example, the equivalence assessment is made by the Commission on ESMA's advice. Member States have proved reluctant to lose control over market access in more long-standing areas of market regulation; while the MiFID II/MiFIR regime is likely to lead to greater harmonization of the conditions under which third country firms may establish branches in the EU, the access/equivalence decision is likely to remain with the Member States.

Finally, the extended perimeter may have destabilizing effects on the single/internal financial market which has, from the outset, been the driver for the regulatory programme and remains pivotal, and on which the EU's competence to regulate in this field is dependent. The wider the regulatory perimeter, the greater the risk that EU rules have asymmetric impact across the Member States, given the tendency for financial market segments to concentrate in particular markets. This is particularly the case where EU rules address the wholesale markets, which are largely concentrated in particular Member States, most notably the UK. The construction of the internal market in financial services has long been attended by competing national interests and tensions as to the nature of financial market regulation, which, drawing on the influential Varieties of Capitalism analysis,[38] can be associated with the contrasting Liberal Market Economies, typically associated with market-based financing and a more facilitative regulatory model, and Co-ordinated Market Economies, typically associated with bank-based financing and more intrusive regulation, which obtain in the EU.[39] Prior to the financial crisis, these tensions were, broadly, contained; the regulatory programme was generally facilitative and regulatory costs could be offset by market access benefits. But the crisis-era programme is significantly more regulatory in orientation and has a very wide reach, deep into the wholesale markets in particular, and can more easily be associated with prejudicial regulatory costs and with the differential imposition of regulatory burdens. The uniformity of the rulebook may accordingly come under threat, reviving the costs which the internal market is designed to eliminate. The rule-making process may also come under threat where Member States perceive that internal market rules have a discriminatory impact.

[38] P Hall and D Soskice, *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage* (OUP 2001).

[39] For an application in the context of the financial crisis reform programme see D Mügge, *Financial Regulation in the European Union: A Research Agenda* (2012) Center for European Studies, Harvard University.

The highly contested Financial Transaction Tax (FTT) Proposal provides a useful example. The cacophony of protest which the Commission's 2011 FTT Proposal,[40] widely regarded as an anti-speculation measure, prompted in some markets, and the prospect of a veto from a number of Member States, including the UK, led to its being recast in 2013 as a measure for a smaller group of Member States under the Enhanced Co-operation mechanism.[41] But the spillover effects of the FTT outside the 'FTT-zone' and on the internal market more generally are considerable and have led to the UK challenging the FTT proposal before the European Court of Justice.[42] Internal market tensions can also be identified in the reforms to the regulation of trading markets under MiFID II/MiFIR; the UK successfully negotiated a recital statement that no action taken by a national competent authority or ESMA in the performance of their duties should directly or indirectly discriminate against any Member State or group of Member States as a venue for the provision of investment services and activities in any currency. Similarly, the UK's 2012 challenge to ESMA's powers to impose directly controls on short selling in national markets,[43] while based on the limits imposed on agency powers, can also be associated with a concern to shield the UK from perceived over- and costly supervision, and with the likely differential impact of such powers on the UK market, given the scale of its wholesale market. But it is the construction of a new, centralized governance model for the Euro Area financial system under Banking Union which may ultimately pose the greatest threat to the internal market; the likelihood of the 'Euro Area 17' acting as a block when it comes to rule-making for the 'internal market 28' is real and poses a potentially existential challenge to internal market harmonization. The risks are all the greater as the momentum dynamics which strongly characterize institutional reform in the EU caution against predictions that Banking Union will remain contained within the banking sector, despite its distinct fiscal and political drivers.

B. Supervision and Enforcement: A New Governance Model?

One of the more striking features of the crisis-era reform programme internationally has been the extent to which it has engaged with the achievement of outcomes.[44] This can be observed in the host of institutional design innovations to the structure of regulators—domestically, regionally, and internationally.[45] It can also traced in the much closer focus on the operational supervisory process through which the outcomes which rules seek are pursued through a range of different strategies: risk- and judgment-based supervision, in particular, has acquired a particular prominence.[46] In the EU, this

[40] COM (2011) 594.

[41] COM (2013) 71. Article 20 TEU and Articles 326–334 TFEU allow Member States to establish 'enhanced cooperation' between themselves within the framework of the EU's non-exclusive competences and to use the EU's institutions and competences to do so, as long as the related Treaty conditions are met.

[42] Case C-209/13.

[43] Case C-270/12.

[44] Exemplified at international level by the FSB's peer review programme which monitors compliance with the G20 reform agenda: FSB, *Framework for Adherence to International Standards* (2010). The FSB monitoring programme is based on a novel 'score card' rating system.

[45] On the UK and US institutional reforms, see eg, respectively, E Ferran, 'The Break-up of the Financial Services Authority' 31 OJLS (2011) 455 and D Skeel, *The New Financial Deal: Understanding the Dodd-Frank Act and Its (Unintended) Consequences* (Wiley 2011).

[46] The new UK regulatory authorities, for example, have adopted a new 'judgment-based' supervisory model, which is based on a more proactive, intrusive and *ex-ante* approach to financial

new concern with the achievement of outcomes can also be observed; but, as with the crisis-era rulebook, it can also be associated with a shift in the location of control.

Banking Union will lead to a transfer of supervisory competence to the Single Supervisory Mechanism in the Euro Area. But, for the present, in the securities markets national competent authorities remain the primary supervisors, and national supervision is a key element of the ESFS (composed of the national authorities, ESMA and the ESRB). The supervisory powers required of national authorities have not previously been subject to detailed harmonization. But the crisis-era reform programme has led to the adoption of sector-specific harmonized powers with respect to, for example, product intervention and prohibition (likely under MiFID II/MiFIR), the imposition of position limits on derivatives trading (likely under MiFID II/MiFIR), the introduction of fund management leverage limits (the AIFMD), and the prohibition of short selling (Short Selling Regulation). Sanctions, previously the preserve of the Member States and typically subject only to the requirement that they be adequate and sufficiently dissuasive, are being subject to harmonization; the type of sanctions which Member States must have available, including pecuniary sanctions, are being prescribed as is the process through which sanctions are imposed;[47] a requirement for criminal sanctions has also made its first appearance, under the market abuse reforms. New whistle-blowing requirements are also being adopted. The new focus on outcomes can also be seen in the emerging, if still tentative, concern to deploy private enforcement mechanisms; previously EU-mandated enforcement requirements have been almost entirely directed towards public supervision, reflecting the very significant sensitivities and complexities associated with any harmonization of private enforcement through national courts. The 2013 CRA Regulation III, however, has introduced a harmonized civil liability regime in respect of rating agency ratings. While it is *sui generis* for a range of reasons,[48] it remains an important departure for EU financial system governance.

These rulebook reforms are intensifying the EU's ability to shape national supervisory and enforcement strategies. But the more radical shift in the location of supervisory power is being driven by the ESAs. In the securities markets sphere, ESMA wields a host of powers under the ESMA Regulation[49] which are designed to drive stronger convergence in the application of supervisory powers and best practices by national authorities, and which include peer review and guideline-setting powers. ESMA's coercive capacity with respect to the promotion of convergence is

market intervention, and which deploys sector-based approaches, forward-looking and business model analysis, greater use of intelligence and data, greater use of thematic reviews, and more responsive and flexible use of resources. See eg FSA, *Journey to the Financial Conduct Authority* (2012) and Bank of England and FSA, *The Prudential Regulation Authority's Approach to Banking Supervision* (2012).

[47] The MiFID II/MiFIR process, for example, is likely to specify an extensive range of sanctions, including warnings, injunctions, prohibitions on the exercise of management functions, and pecuniary sanctions, and to require that the determination of the type and level of administrative sanction take into account the gravity and duration of the breach, the degree of responsibility of the person concerned, the financial strength of the responsible person, the importance of the profits gained or losses avoided, the level of cooperation by the responsible person with the competent authority and previous breaches by the responsible person.

[48] N Moloney, 'Liability of Asset Managers: A Comment' (2012) 7 Capital Markets Law Journal 414.

[49] Regulation (EU) No 1095/2010 OJ (2010) L331/84.

considerable; ESMA guidelines, for example, are subject to a 'comply or explain' mechanism which requires that competent authorities explain their non-compliance (ESMA Regulation, Article 16). ESMA's exclusive and direct supervisory powers over rating agencies (CRA Regulation I-III) and trade repositories (EMIR) can be expected to strengthen its ability to shape national supervisory practices more generally as it builds its own supervisory capacity. As has been extensively examined,[50] ESMA also wields a number of direct supervisory powers which allow it to direct national competent authorities and national market participants in cases of breach of EU law (ESMA Regulation Article 17), emergency situations (Article 18) and where it undertakes binding mediation between competent authorities (Article 19); ESMA can also take direct action with respect to short selling (Short Selling Regulation) and will most likely be conferred with direct product intervention powers (MiFID II/MiFIR). The generally strict conditionality attached to these powers, their constitutional instability given the restrictions on transferring discretionary powers to agencies, and their political sensitivity makes it unlikely that they will be regularly wielded (they have not been used to date). But they have injected a hierarchical dynamic into the relationship between ESMA and its constituent national competent authorities and serve to strengthen further ESMA's capacity to influence local supervisory decision-making.

The supervision of securities markets is likely to be most efficiently located at national level, absent compelling reasons. The fiscal risks and related sovereign debt feedback loop associated with the banking collapse, and which have driven Banking Union, are much less apparent in the securities market field, although certain securities market infrastructures, chief among them CCPs, have the capacity to generate massive systemic risk and fiscal costs.[51] The momentum effects of Banking Union should not be underestimated given the dynamism of institutional evolution in EU financial system governance. But assuming those momentum effects are, for the short term at least, relatively weak, the transfer of direct supervisory powers to ESMA is likely to be slow and incremental. Although ESMA may seem to have rapidly acquired supervisory powers, and the European Parliament has emerged as the standard-bearer for allocating more extensive powers to ESMA, these powers have been limited to emergency powers of varying hue which are subject to strict conditionality and to the supervision of discrete market actors which do not pose fiscal risks and which operate on a pan-EU basis. Further transfers will depend on the extent to which the *Meroni* ruling[52] constraint, which prohibits the delegation of discretionary powers to agencies, can be met, and on the identification of powers which will not lead to the imposition of fiscal responsibility on Member States following an ESMA decision (the political sensitivities associated with the allocation of fiscal responsibility are evident in the ESMA Regulation Article 38 mechanism which allows a Member State to challenge an ESMA decision which it claims generates fiscal risks for the Member State). The upcoming ruling from the European Court on the Treaty validity of ESMA's direct powers to prohibit short selling in any market under the Short Selling Regulation should bring greater certainty to the extent to which supervisory powers can be transferred to

[50] See eg the references at n 17.

[51] Tentative steps are being made towards harmonized resolution processes for systemically significant non-bank institutions, including CCPs: Commission, *Consultation on a Possible Framework Recovery and Resolution Framework for Financial Institutions other than Banks* (2012).

[52] Case C-9/56 and 10/56 [1957/1958] ECR 133.

ESMA.[53] But the fiscal constraint remains real and is well reflected in the location of supervision over CCPs at national level under EMIR, albeit that supervision is coordinated through colleges of supervisors given the potential CCPs have for massive and destabilizing cross-border systemic risk.

The range of channels through which ESMA can influence national supervisory decisions remains, however, significant. It may accordingly be that it is in this more humdrum sphere that changes in the location of supervisory control are most likely to occur over time and where ESMA's influence may be felt most strongly.

The global financial crisis has reordered the location of regulatory and supervisory control over EU financial markets in favour of the EU. The implications of this reordering for financial market efficiency and stability are still unknown. But it is relatively clear that significant new lines of tensions between the EU and its Member States have been exposed, including with respect to the international market, the integrity of the internal market, and the location of direct supervisory powers. As the crisis-era recedes, whether these tensions increase and how they are managed is likely to have a material impact on the post-crisis development of EU financial market regulation.

NIAMH MOLONEY*

II. SURVEYING THE STATE OF EU ENVIRONMENTAL LAW: MUCH BARK WITH LITTLE BITE?

I. INTRODUCTION

In the three years since last surveyed in the Quarterly,[1] EU environmental law has continued to justify its reputation as one of the most fast-moving fields of EU law, with a large number of highly significant legislative and jurisprudential developments. This review selects some of the most important areas of development in the field in recent years: in particular, the EU's new environmental action programme for 2013–20, EU climate and energy law, environmental governance and enforcement, and integration of environmental concerns into other EU policy areas.

II. THE EU'S NEW ENVIRONMENTAL ACTION PROGRAMME (2013–20)

Overarching all of the EU's activity in environmental law and policy is the EU's multi-annual Environmental Action Programme (EAP), setting out the key priorities and vision of the EU's environmental policy activity. Since the first EAP was drawn up by the Commission in 1973, the legal status and policy significance of EAPs has increased dramatically, helped by the formalization of their legal basis within what is now Article 192(3) TFEU. Pursuant to this provision, EAPs are adopted in the form of a

[53] See n 43.

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[1] S Kingston (2010) 59 ICLQ 1129.

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