cepStudy

European Supervisory Authorities

Room for improvement at Level 2 and Level 3

Study on Behalf of the fpmi Munich Financial Centre Initiative

This study has been prepared by the Centre for European Policy (cep) on behalf of the Finanzplatz München Initiative (fpmi). The opinions expressed herein are those of the authors and do not necessarily reflect the view of fpmi.

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List of Abbreviations

TFEU	Treaty on the Functioning of the European Union
BaFin	Federal German Financial Supervisory Authority
BRRD	Banking Resolution an Recovery Directive
CEBS	Committee of European Banking Supervisors
CEIOPS	Committee of European Insurance and Occupational Pensions Supervisors
CESR	Committee of European Securities Regulators
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
EBA	European Banking Authority
ECON	Economic and Monetary Affairs
EIOPA	European Insurance and Occupational Pensions Authority
EMIR	European Market Infrastructure Regulation
EP	European Parliament
ESAs	European Supervisory Authorities
ESFS	European System of Financial Supervision
ESMA	European Securities and Markets Authority
ECJ	European Court of Justice
EUV	Treaty on the European Union
FSC	Financial Services Committee
IDD	Insurance Distribution Directive
ITS	Implementing Technical Standard
MEP	Member of the European Parliament
MiFID	Markets in Financial Instruments Directive
MiFIR	Markets in Financial Instruments Regulation
MREL	Minimum Requirement for Eligible Liabilities
PRIIPs	Packaged retail and insurance-based investment products
RTS	Regulatory Technical Standard
VwGO	Rules of the Administrative Court

EXECUTIVE SUMMARY

Context

- This study examines the regulatory role of the European Supervisory Authorities (ESAs). Level 2 measures developed by the ESAs include draft binding regulatory technical standards (RTS) which are adopted by the Commission as delegated acts. Level 3 measures issued by the ESAs are non-binding guidelines.
- In view of the large backlog of measures, binding RTS are about to take on even greater significance. ESA guidelines are not only increasing in number, they are also seeing widespread compliance in the EU Member States and have therefore become almost binding in nature.
- The ESAs and the EU Commission should observe four essential principles when carrying out their regulatory work: adherence to the mandate, subsidiarity, proportionality and consistence.
- The following procedures exist to assess compliance with these principles:
  - ex ante "political scrutiny" of the ESAs and the Commission by the Council and the European Parliament and
  - ex post "judicial scrutiny" by way of claims by e.g. banks, insurance companies or investment firms.

Current Situation

Ex-Ante Political Scrutiny

- Political scrutiny of Level 2 measures currently takes place primarily in the European Parliament. The Parliament's methods in this respect are mainly informal and characterised by the dedication of individual MEPs. The Council – despite some effort – has not yet managed to set up similarly effective working methods.

- Political scrutiny of ESA guidelines (Level 3) is not foreseen at EU level. The European Parliament has, however, repeatedly expressed its unease at the scale and number of guidelines. In Germany, the Bundestag wants BaFin to refrain from implementing guidelines which do not correspond to preferred political objectives.

Ex-Post Judicial Scrutiny

- The action for annulment and interim measures constitute two instruments for the judicial scrutiny of RTS and ITS. Their practical importance is, however, limited for the purposes of allowing the ECJ to ensure that Level 2 measures adhere to the mandate and comply with the principles of subsidiarity and proportionality.

- Financial market players cannot currently take judicial action against ESA guidelines at EU level. Following a comply decision by the competent national authority, they may, however, have recourse to national courts if and insofar as legal action is possible. In certain circumstances, the respective national court can or must then submit a legal question to the ECJ in the preliminary ruling procedure. In Germany, however, it seems that recourse to the courts is seldom possible.

Necessary Modifications

Recommendation 1

Political conflicts must be settled at Level 1. The European Parliament and the Council of Ministers should therefore resist the temptation to seek the solution to intractable political differences by way of Level 2 clarifications. It is advantageous for both the EU legislator and the ESAs to have mandates which are very clear as regards scope, content, purpose and objective. Hearings with the ESAs at an early stage in Parliament and the Council promote a uniform understanding of the mandate, prevent the mandate from being exceeded and contribute to consistent regulation.

Recommendation 2

The Council's work structures are inadequate for providing sufficient political scrutiny of the Level 2 activities of the ESAs and the Commission. The Council should reflect on its strengths and develop structures which allow it to use these strengths for the scrutiny of RTS and draft RTS. The recommendations of the Financial Services Committee (FSC) should be implemented as soon as possible. Effective structures in the Council are essential for overseeing adherence to the mandate, proportionality and regulatory consistence.

Recommendation 3

Sufficient "breathing space" between the entry into force of Level 2 measures and the application of the Level 1 Directive or Regulation is desirable. It allows the Council and Parliament to adequately check the Commission's delegated acts and gives companies enough time to comply with the more detailed provisions. Ideally, this "breathing space" will be adopted ex ante - i.e. in the Level 1 measures - and the effective date of the Level 1 provisions will be dependent on entry into force of the delegated acts. Although an ex post postponement of the effective date of the Level 1 measure is a possible alternative, it requires the Commission to submit a corresponding legislative proposal.

Recommendation 4

In view of the huge volume of Level 2 measures, the Council and the European Parliament should examine the possibility of collaborating on political scrutiny at Level 2. In particular, in the case of selected issues on which there is broad agreement between the two institutions, joint working groups could ensure efficient scrutiny of the ESAs and the Commission and ward off disproportionate regulatory conditions or prevent the ESAs and the Commission from exceeding their mandates. At the same time, the Council and the Parliament could deploy their scant resources more effectively.

Recommendation 5

The Commission should inform the Council and European Parliament, at an early stage, of modifications which it intends to make (or has made) to draft RTS from the ESAs. Such targeted information increases the likelihood of proportionate and consistent regulatory conditions at Level 2.

Recommendation 6

The hurdles faced by the European Parliament and the Council when raising objections to the Commission's delegated acts (and therefore to RTS) are currently exceptionally high. A treaty amendment should make it clear that, in the Council, a qualified majority of 55% of the Member States is sufficient to revoke an empowerment or to file an objection against a delegated act.

Recommendation 7

The bundling of several RTS by the Commission into a single delegated act should not reduce the ability of the European Parliament and the Council to exercise political scrutiny over the Level 2 activities of the ESAs and the Commission. They should therefore be in a position to reject individual RTS which have been bundled into a delegated act. This will not necessarily have a negative impact on the consistency of Level 2 legislation.

Recommendation 8

In order to maintain the ability of the European Parliament and the Council to carry out effective scrutiny of the Level 2 measures of the ESAs and the Commission, the very informal procedure which currently exists should be subject to a moderate level of formalisation. A joint register for the ESAs, Commission, Council of Ministers and Parliament would safeguard knowledge that is also necessary for future political scrutiny. In addition, greater transparency would increase the acceptance of the results of negotiations.

Recommendation 9

The ESAs should only be able to pursue plans to develop guidelines where the Council and the Parliament raise no objections (barrier to exercising the mandate). This increases the likelihood that guidelines will be compatible with the Principle of Subsidiarity.

Recommendation 10

At national level, political scrutiny - by Parliament or the responsible ministry - of whether EU guidelines should in fact be complied with, is perfectly legitimate. This scrutiny should provide national supervisors with the necessary room for manoeuvre but at the same time prevent guidelines from offending against the national political will. This scrutiny can also be helpful for overseeing the proportionality and consistency of legislation. In Germany, the increased transparency, demanded by the Bundestag, regarding BaFin's Level 3-collaboration with the ESAs, requires a continuous flow of information between the Parliament’s Finance Committee, Federal Finance Ministry and BaFin.

SECTION 1 THE EUROPEAN SUPERVISORY AUTHORITIES (ESAs)

1 Introduction and Main Players

1.1 The ESAs, EU Commission, Council of Ministers, European Parliament

The European Supervisory Authorities (ESAs) are EU agencies which form part of the European System of Financial Supervision (ESFS)[1]. There are three ESAs, the European Banking Authority (EBA) in London, the European Securities and Markets Authority (ESMA) in Paris and the European Insurance and Occupational Pensions Authority (EIOPA) in Frankfurt. They have been in operation since 2011.

The ESAs replaced the former European financial supervisory committees (CEBS, CESR, CEIOPS) which were set up as part of the Lamfalussy Procedure, a four-phase legislative procedure in the area of financial supervision. These committees had no power to make decisions of a mandatory nature. Their task was simply to advise the Commission on the procedure for issuing Level 2 technical standards and to provide the Commission with recommendations in this regard. In addition, they could develop non-binding guidelines and recommendations for the harmonisation of national administrative requirements for the implementation of Level 2 measures taken by the Commission.[2]

The ESAs were established on the recommendation of the Larosière Group[3]. They are independent, autonomous Union authorities with their own legal identity. They develop regulatory and implementing technical standards which are adopted by the Commission either as delegated acts under Art. 290 TFEU or as implementing acts under Art. 291 TFEU.[4] In the event of a crisis, persistent breaches of EU law by national authorities and differences of opinion between national authorities, they can adopt decisions, which are aimed directly at, and are legally binding upon, financial institutions/financial market players and national supervisory authorities.[5] This evolution from simple committees to ESAs was affirmed by the ECJ in its Judgement on short selling restrictions.[6,7] The task of the ESAs is to promote the enduring stability and effectiveness of the

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1 The ESAs were established by way of the ESA Regulations, i.e. Regulation (EU) No. 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC; Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC; Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC.

2 Final Report of the Committee of Wise Men on the Regulation of European Securities Markets, available at http://ec.europa.eu/finance/securities/docs/lamfalussy/wisemen/final-report-wise-men_en.pdf, last accessed on 3.8.2016.

3 Report of the High-Level Group on Financial Supervision in the EU commissioned by the EU Commission, February 2009, available at: http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf, last accessed on 3.8.2016.

4 Art. 10 and 15 ESA Regulations.

5 Cf. Art. 8 (2) (e) and (f) in conjunction with Art.17 (4); Art. 18 (3) and (4); Art. 19 (3) and (4). ESA Regulations.

6 ECJ, Case No. C-270/12 of 22 January 2014, ECLI:EU:C:2014:18, United Kingdom / Parliament and Council. Prior to this Judgement, the compatibility of the ESAs with Union law had been controversial. The ECJ affirmed that ESMA's

financial system in the EU.[8] With this aim, they contribute by regulatory means (more detail on this in: Section 2.1) to the creation of a "single-rule-book"[9] and carry out supervisory tasks (more detail on this in: Section 2.2) as well as tasks relating to consumer protection policy (more detail on this in: Section 2.3).

Under Art. 17 TEU, the **Commission** is the guardian of the Treaties. It oversees the application of the EU Treaties and of measures adopted pursuant to them, and thus the application of primary and secondary law in the EU.[10] As a rule, the Commission has an exclusive right of initiative and is therefore the only Union institution that can submit legislative proposals.[11] The Commission adopts the draft technical standards developed by the ESAs in the form of delegated acts under Art. 290 TFEU and in the form of implementing acts under Art. 291 TFEU. Only the Commission can adopt delegated acts:[12] Sub-delegation to other institutions is prohibited.[13]

The European Parliament (EP), in conjunction with the Council, is the EU's legislative organ. It consists of 751 representatives of the Union citizens, elected every five years.[14] In the usual "ordinary legislative procedure", Council and Parliament have equal rights.[15] To be adopted, a Commission proposal generally requires a simple majority of the votes cast in the EP.[16]

The Council of the European Union (Council of Ministers), in conjunction with the EP, is the legislative organ of the EU. It takes part in the legislative procedure by approving and passing legislative proposals from the Commission. It is made up of representatives of the Member States at Ministerial level.[17] Council Resolutions generally require a qualified majority of at least 55% of the Member States representing more than 65% of the EU population.[18]

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powers are sufficiently "circumscribed by various conditions and criteria which limit ESMA's discretion" so that the principles established in the Meroni Case, under which powers with a wide margin for discretion can only be conferred upon bodies established by Treaty, have been met (para. 45 of the Judgement).

7 On this Judgement see: Baran/Van Roosebeke, Review of the European Supervisory Authorities, 12 recommendations, cepInput 04 | 2014, http://www.cep.eu/fileadmin/user_upload/cep.eu/Studien/cepInput_ESA/cepInput_ESA.pdf, p 5.

8 Art. 1 (5) ESA Regulations.

9 Cf. Art.8 (1) (aa) ESA Regulations.

10 Art. 17 (1) TEU, Art. 258 TFEU.

11 Art. 17 (2) TEU, Art. 294 (2) TFEU. The Commission has no right of initiative in cases under Art. 294 (15) TFEU. On the initiative of a group of Member States, the recommendation of the European Central Bank or at the request of the European Court of Justice, the Council and Parliament can formulate draft legislation without the prior involvement of the Commission and adopt it by way of the ordinary legislative procedure.

12 Gellermann, in: Streinz, EUV/AEUV, 2nd Edn., Verlag C.H. Beck, München 2012, Art. 290 TFEU, para. 5; Nettesheim, in: Grabitz/Hilf/Nettesheim, Das Recht der Europäischen Union, 58th Update, Verlag C.H. Beck. München 2016, Art. 290 TFEU, para. 30; Ruffert, in: Calliess/Ruffert, AEUV/EUV, 5th Edn., Verlag C.H. Beck ,München 2016, Art. 290 TFEU, para. 4.

13 Gellermann, in: Streinz, EUV/AEUV, 2nd Edn., Verlag C.H. Beck, München 2012, Art. 290 TFEU, para. 5; Nettesheim, in: Grabitz/Hilf/Nettesheim, Das Recht der Europäischen Union, 58th Update, Verlag C.H. Beck. München 2016, Art. 290 TFEU, para. 30.

14 Art. 14 (1) and (2) TEU.

15 Art. 289 (1) TFEU, Art. 294 TFEU.

16 Art. 231 (1), Art. 289 (1), Art. 294 TFEU.

17 Art. 16 (1) and (2) TEU.

18 Art. 16 (4), sub-para. 1 EUV.

2 Main Areas of Activity of the ESAs

2.1 Involvement of the ESAs in regulatory proposals

2.1.1 Level 2 Measures: Regulatory technical standards and implementing technical standards

Where power has been delegated by the EU legislator, the Commission can adopt legally binding regulatory technical standards (RTS) by way of delegated acts under Art. 290 TFEU and implementing technical standards (ITS) by way of implementing acts under Art. 291 TEU.[19]

RTS serve to ensure the "consistent harmonisation" of the areas of the financial market which fall within the scope of the legislative acts referred to in Art. 1 (2) of the ESA Regulations.[20] They must be "technical", cannot contain any "strategic decisions or policy choices" and are limited in content by the legislative act on which they are based.[21] ITS serve to determine "the conditions of application" of the legislative acts referred to in Art. 1 (2) of the ESA Regulations.[22] They must also be "technical" and cannot contain any "strategic decisions or policy choices".[23]

The ESAs develop draft RTS and ITS. Before the ESAs can submit these to the Commission, the Board of Supervisors of the respective ESA must approve them by way of a qualified majority which requires at least 55% of its voting members (made up of at least 15 members) covering at least 65% of the EU population.[24] Preparing for the decisions on RTS and ITS by the Board of Supervisors is undertaken by what are known as Standing Committees.[25] These Committees bring together national experts who are supported by representatives of the ESAs.[26] They are usually chaired by a Member of the Board of Supervisors.[27] Technical advice is generally obtained from Consultative Working Groups made up of practitioners, consumers and other end-users.[28] Before the ESAs submit draft RTS and ITS to the Commission, they usually have to hold "open public consultations", analyse the potential related costs and benefits and obtain the opinion of the respective stakeholder group.[29] Under the ESA Regulations, the Commission must decide within three months whether to endorse the draft RTS or ITS.[30] It can endorse the drafts "in part only, or with amendments, where the Union's interests so require".[31] The grounds given for this rule are that the ESAs are "in close contact with and knowing best the daily functioning of financial markets".[32]

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19 Art. 10 et seq. and Art. 15 ESA Regulations.
20 Art. 10 (1), sub-para. 1 in conjunction with Art. 1 (2) ESA Regulations.
21 Art. 10 (1), sub-para. 2 ESA Regulations.
22 Art. 15 (1), sub-para. 1 ESA Regulations.
23 Art. 15 (1), sub-para. 1 ESA Regulations.
24 Art. 44 (1), sub-para. 2 ESA Regulations in conjunction with Art. 16 (4) TEU.
25 https://www.esma.europa.eu/about-esma/working-methods, last accessed on 21.7.2016.
26 Ibid.
27 Ibid.
28 Ibid.
29 Art. 10 (1), sub-para. 3 and Art. 15 (1) sub-para. 2 ESA Regulations.
30 Art. 10 (1), sub-para. 5 and Art. 15 (1) sub-para. 4 ESA Regulations. In practice, however, there have been long delays.
31 Art. 10 (1), sub-para. 5 and Art. 15 (1) sub-para. 4 ESA Regulations.
32 Recital 23 of the ESA Regulations.

Changes must be coordinated between the Commission and the respective ESA, but it is the Commission that has the final decision.[33]

RTS are adopted by the Commission as delegated acts under Art. 290 TFEU and ITS as implementing acts under Art. 291 TFEU, in the form of binding Regulations or Decisions respectively.[34]

The EP or the Council have two ways of preventing the entry into force of delegated acts (and thus of RTS).[35]

- Firstly, they can revoke the general delegation of power contained in the basic legislative act at any time.[36] A revocation is passed by the EP by way of a majority of its members (absolute majority) and by the Council by way of a qualified majority. [37], [38] A resolution by one of the two institutions is sufficient for effective revocation. The validity of delegated acts (and thus RTS) which have already come into effect, will not be affected by a revocation.[39]
- Secondly, the EP and the Council can raise objections to a specific delegated act (and thereby to one or more of the RTS contained therein[40]).[41] In this regard, the same voting majorities are required as for revocation.[42] The time limit for this is three months and may be extended by a further three months.[43] Where the Commission adopts an RTS by way of a delegated act without amendment, in the version submitted by the ESA, the time limit is one month and can be extended twice, by one month.[44]

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33 Art. 10 (1), sub-para. 6, 7 and 8 and Art. 15 (1) sub-para. 5, 6 and 7 ESA Regulations.

34 Art. 10 (1), sub-para. 1, and (4) and Art. 15 (1) sub-para. 1, and (4) ESA Regulations.

35 In the case of implementing acts (and thus ITS), on the other hand, the EP and Council have no possibility to issue a revocation or raise an objection. With regard to the scrutiny mechanisms of the Member States via Committees, see Regulation (EU) No 182/2011 of the European Parliament and of the Council of 16 February 2011 laying down the rules and general principles concerning mechanisms for control by Member States of the Commission's exercise of implementing powers. Under Art. 11 of this Regulation, the EP and the Council may indicate to the Commission that, in their view, a draft implementing act exceeds the implementing powers. The Commission must look into such an assertion and inform the EP and the Council of its findings.

36 Art. 12 (1) ESA Regulations.

37 Art. 290 (2), sub-para. 2 TFEU in conjunction with Art. 16 (4) TEU.

38 The Council assumes that the qualified majority under Art. 290 (2) TFEU is determined according to Art. 238 TFEU. This would mean that a majority in the Council of 72% of the Member States representing at least 65% of the EU population would be required in order to revoke a delegation of power to adopt delegated acts or to pass an objection to a delegated act.

39 Art. 12 (3) ESA Regulations.

40 In practice, they are often bundled together: several RTS are bundled together and passed by way of a single delegated act. Thus the question arises as to whether the EP or the Council can only object to the delegated act (which may contain a large number of RTS) or can also object to individual RTS within a delegated act. Cf. Section 3, para. 2.1.2.2

41 Art. 13 (1), sub-para. 1 ESA Regulations.

42 Art. 290 (2), sub-para. 2 TFEU in conjunction with Art. 16 (4) TEU.

43 Art. 13 (1), sub-para. 1 ESA Regulations.

44 Art. 13 (1), sub-para. 2 ESA Regulations.

Figure 1: Stages in the Development of an RTS

2.1.2 Empirical Results: Relevance of Level 2 Measures

2.1.2.1 Adopted RTS and ITS

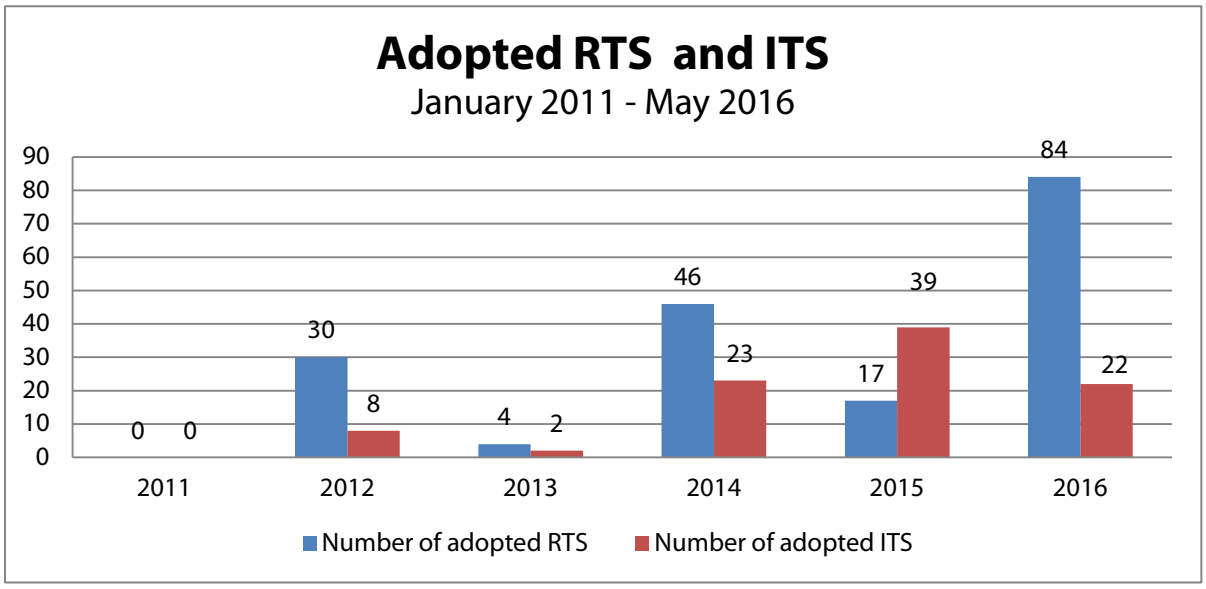

Figure 2: Adopted RTS and ITS
Source: Commission, http://ec.europa.eu/finance/general-policy/docs/level-2-measures/level2-measures_en.pdf

As Figure 2 shows, the Commission adopted a total of 181 RTS in the form of delegated acts between the start of 2011 and mid-September 2016.[45] In this regard, no clear upward or downward trend for RTS and ITS can be observed. However, a large number of RTS and ITS were adopted in 2014, 2015 and 2016. The overall low figures in the initial years is due to the fact that important legislative acts (e.g. CRD IV/CRR, MiFiD II/MiFIR), involving a large number of Level 2 measures, were only concluded at Level 1 in those years. It is also interesting that during 2016 (up until mid-September) 84 RTS in the form of delegated acts were adopted thus the previous year's levels were already exceeded by the middle of September.

The number of ITS, issued in the form of implementing acts is, at 94, lower than the number of adopted RTS (see Figure 2). It reached its highest level so far in 2014 and 2015 with 23 and 39 ITS adopted by the Commission respectively. This is primarily due to consolidation standards developed by EIOPA for the insurance industry in the Solvency II Directive.

[45] The number of RTS reflects the delegations of power in the respective primary legislative acts. Several RTS are often bundled together into one delegated act. The number of delegated acts, based on delegations of power to adopt RTS, is 63. The same applies to ITS. Several ITS are sometimes bundled together into one implementing act.

2.1.2.2 Outstanding Level 2 Measures

The 181 RTS and 94 ITS adopted by the Commission between 2011 and mid-September 2016, do not provide the complete picture of Level 2 legislation. Numerous RTS, in the form of delegated acts, and ITS, in the form of implementing acts, are still due for adoption because a Level 1 mandate already exists. In the case of RTS, this figure (105) is only slightly below the number of RTS already adopted (181) (see Figure 3). And in the case of ITS too, the Commission still has a lot of work to do in the coming months and years as 49 ITS are still outstanding.

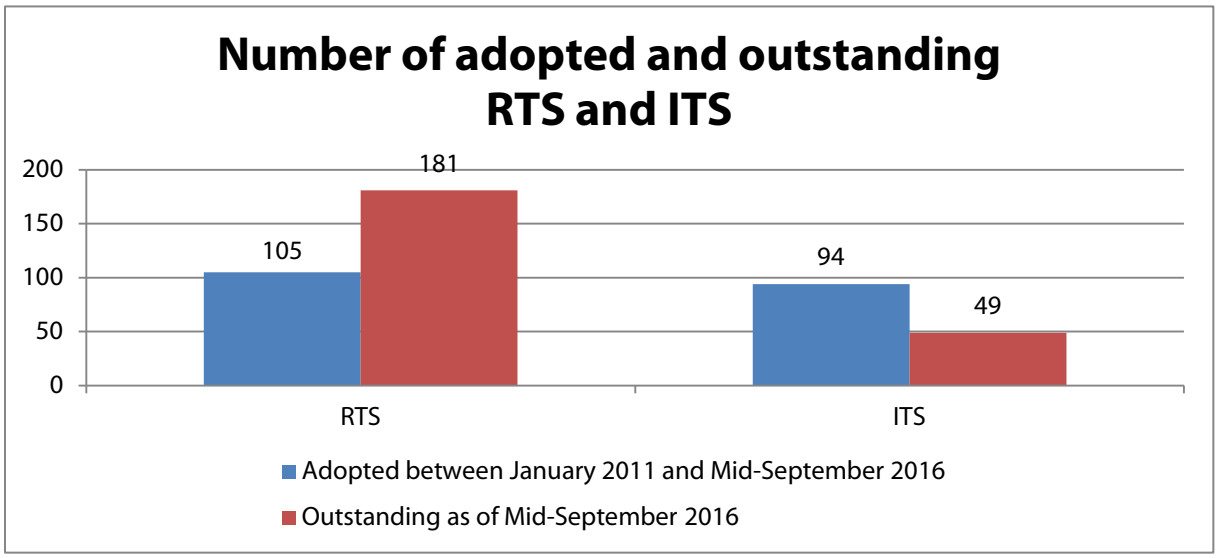

Figure 3: Adopted v. Outstanding RTS and ITS
Source: Commission, http://ec.europa.eu/finance/general-policy/docs/level-2-measures/level2-measures_en.pdf

Before the Commission adopts an RTS or an ITS, in the form of a delegated act or an implementing act as appropriate, these are prepared by the respective ESA and submitted in a draft version. The number of RTS/ITS adopted by the Commission in a year is not identical to the number of draft RTS/ITS because the Commission is allowed a certain amount of time for adopting the delegated acts. Figure 4 shows the number of standards drafted between 2011 and 2015. The large number of draft RTS and ITS in 2015 leads one to expect that the number of adopted RTS and ITS will again rise sharply in 2016.

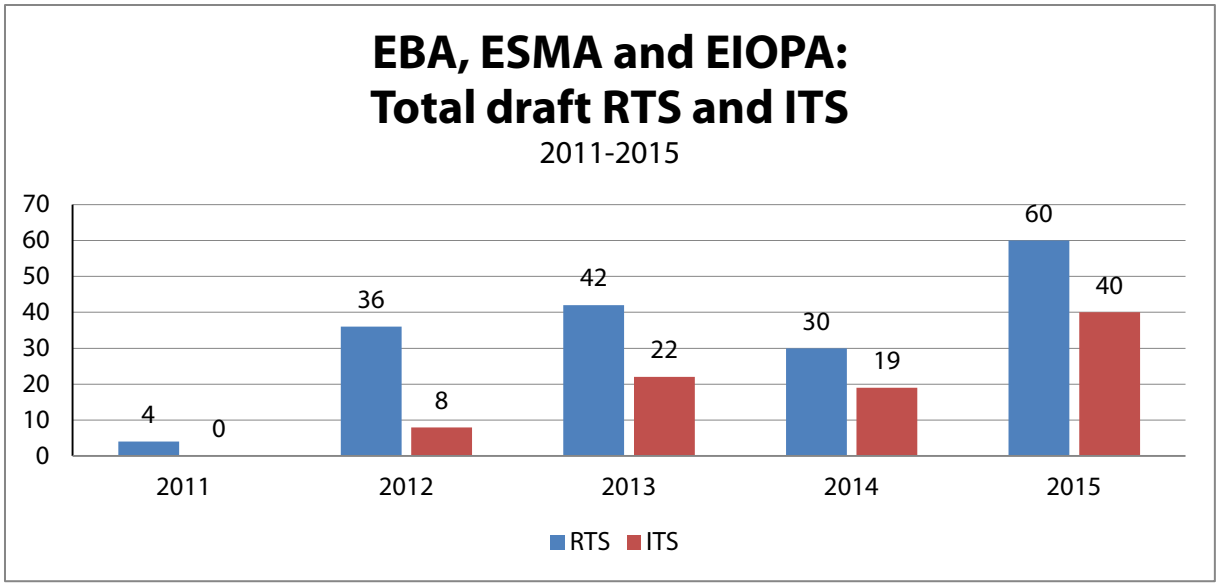

Figure 4: Draft RTS and ITS submitted by the ESAs
Source: Annual Reports of the ESAs, own calculations

2.1.3 Level 3 Measures: Guidelines and Recommendations

The ESAs can issue guidelines and recommendations addressed to the competent authorities and financial institutions/financial market players.[46] Guidelines and recommendations aim to create "consistent, efficient and effective supervisory practices" and ensure "common, uniform and consistent application of Union law".[47] They cover areas in which the ESAs are not permitted to adopt RTS and ITS.[48] Guidelines, like RTS and ITS, are decided by the Board of Supervisors of the respective ESA by way of a qualified majority.[49]

The preparations for decisions of the Board of Supervisors on guidelines proceed in the same way as for RTS and ITS (cf. Section 2.1.1, page 6). Notably, consultations must generally be held, a cost-benefit analysis carried out and the opinion of the respective stakeholder groups obtained.[50]

The competent national authorities and financial institutions/financial market players have to "make every effort" to comply with the guidelines and recommendations.[51] Where the competent authority does not comply or does not intend to comply with a guideline or recommendation, it must notify the respective ESA, stating its reasons, within 2 months of the issuance of the guideline or recommendation ("comply or explain").[52] The respective ESA must publish the fact that a competent authority does not comply or does not intend to comply with the guideline or

46 Art. 16 (1) ESA Regulations.
47 Art. 16 (1) ESA Regulations.
48 Recital 26 of the ESA Regulations.
49 Art. 44 (1), sub-para. 2 ESA Regulations in conjunction with Art. 16 (4) TEU.
50 Art. 16 (2) ESA Regulations.
51 Art. 16 (3), sub-para. 1 ESA Regulations.
52 Art. 16 (3), sub-para. 2 ESA Regulations.

recommendation; it may publish the reasons for non-compliance.[53] In their annual reports, the ESAs must indicate which guidelines and recommendations they have adopted and which competent national authorities have not complied with them.[54] By contrast with the authorities, financial institutions/financial market players only have to report, in a clear and detailed way, whether they comply with a guideline or recommendation if such report is required by the said guideline or recommendation.[55]

Guidelines and recommendations are not binding. In the case of recommendations, their non-binding nature arises directly from Art. 288 TFEU. Guidelines, on the other hand, are not mentioned in Art. 288 TFEU. Since this provision contains a conclusive list of binding EU measures, guidelines cannot be binding.[56] Furthermore, the lack of binding force is supported by the fact that the EU legislator has linked the ESAs' power to adopt guidelines to the comply-or-explain mechanism.[57]

In the vast majority of cases, the competent national authorities comply with guidelines (cf. Figure 6). One reason for this, apart from the comply-or-explain mechanism, could be the duty of the ESAs to publish the failure of a competent national authority to comply with a guideline or recommendation, and to include it in their annual report, which gives rise to "public exposure"[58]. Thus guidelines assume "de facto binding force".[59]

This is helped by the fact that guidelines and recommendations exert influence on judicial decisions, and thus indirectly affect legal practice.[60] Financial institutions/financial market players and supervisory authorities will in turn generally base their conduct on the case law.[61]

2.1.4 Empirical Results: Relevance of Level 3 Measures

2.1.4.1 Adopted guidelines

Although it varies, the number of guidelines passed by EBA, ESMA and EIOPA is rising year on year (see Figure 5). In total, 108 guidelines were adopted by ESAs up to the end of 2015. Half of those can be attributed to 2015 alone. [62]

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53 Art. 16 (3), sub-para. 3 ESA Regulations.

54 Art. 16 (4) ESA Regulations.

55 Art. 16 (3), sub-para. 4 ESA Regulations.

56 Michel, Institutionelles Gleichgewicht und EU-Agenturen, Duncker & Humblot GmbH, Berlin 2015, p. 239.

57 Manger-Nestler, in: Grieser/Heemann, Europäisches Bankaufsichtsrecht, Frankfurt School Verlag GmbH, Frankfurt am Main 2016, p. 98; Lehmann/Manger-Nestler, Das neue Europäische Finanzaufsichtssystem, ZBB 1/11, p. 2 (13).

58 Manger-Nestler, in: Grieser/Heemann, Europäisches Bankaufsichtsrecht, Frankfurt School Verlag GmbH, Frankfurt am Main 2016, p. 98.

59 Michel, Institutionelles Gleichgewicht und EU-Agenturen, Duncker & Humblot GmbH, Berlin 2015,p. 240.

60 Cf. Frank, Die Rechtswirkungen der Leitlinien und Empfehlungen der Europäischen Wertpapier- und Marktaufsichtsbehörde, Nomos-Verlagsgesellschaft, Baden-Baden 2012, p. 171.

61 Ibid.

62 Individual sub-guidelines are often collected together into guidelines by the ESAs. Figure 5 shows the number of collected guidelines.

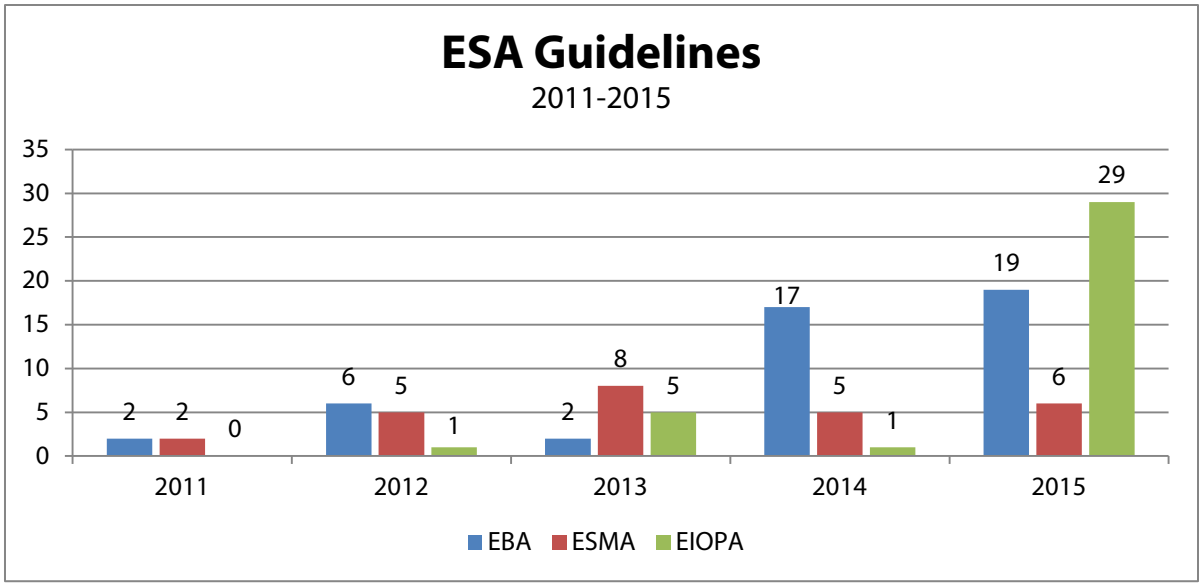

Figure 5: ESA Guidelines
Source: Annual reports of the ESAs, ESMA: Esma final guidelines, 11.12.2015

2.1.4.2 Compliance with the Guidelines:

As explained in Section 2.1.3, the competent national authorities have, in principle, two possibilities with regard to the guidelines. They can declare that they will comply with them or they can declare that they do not intend to comply with them. In the latter case, they must explain their conduct. Compliance tables, published by all three ESAs, indicate that the vast majority of the guidelines submitted by the ESAs are complied with (see Figure 6).[63,64]

[63] The compliance tables show numerous differences between EBA, ESMA and EIOPA. EIOPA usually breaks up the guidelines into sub-guidelines which the competent national authorities can accept or reject separately. EBA subsumes this under "partial comply" whilst ESMA makes no such categorisation. Both ESMA and EIOPA have the category "not applicable"). This includes cases where the guideline refers to financial institutions which do not exist in a Member State. EBA does not have this category. It is, however, the only ESA which has the category "no response".

[64] For the purposes of this evaluation, the "not applicable" responses in the case of ESMA and EIOPA were left out of the calculation. In the case of EBA, "partial comply" and "no response" were classed as non-compliance.

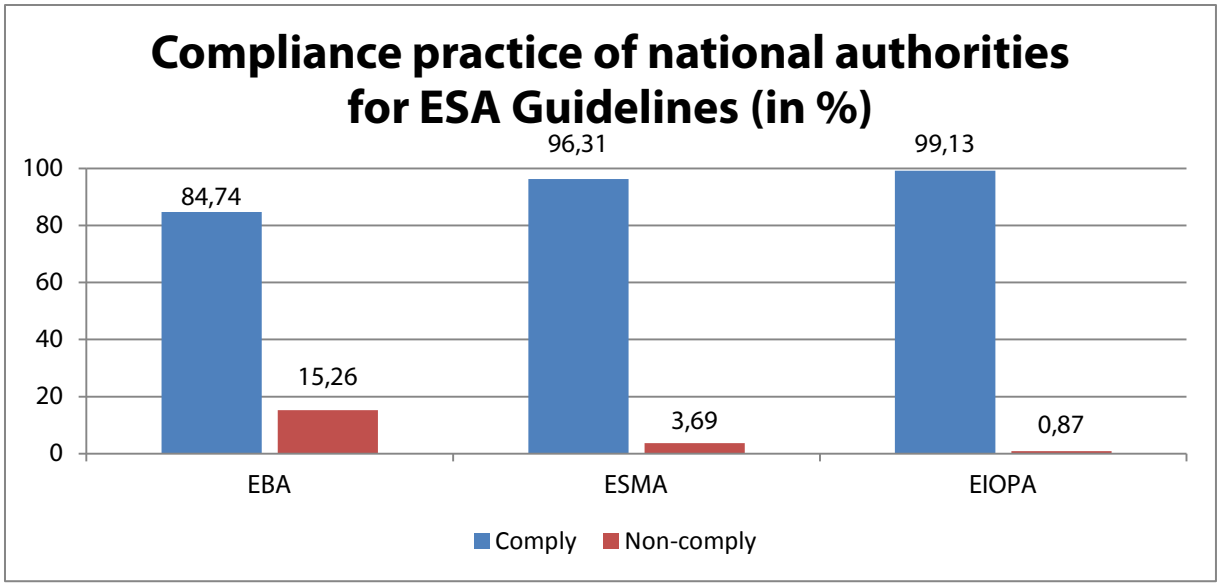

Figure 6: Compliance practice of national authorities for ESA Guidelines
Source: Compliance tables for Guidelines, ESAs website, own calculations (Data as at: 1 July 2016)

Compliance rates are very high for all three ESAs. Whilst EBA guidelines are complied with in around 85% of cases, the figure for ESMA is about 96%. In the case of EIOPA, the compliance rate is over 99%.

The Federal Financial Supervisory Authority (BaFin), as the competent authority in Germany, has not failed to comply with a single EBA guideline so far whereas it has rejected 17.6% of the ESMA guidelines. The underlying data available from ESMA only covers 17 guidelines however; of these BaFin has failed to adopt 3. In the case of ESMA, BaFin is well above the EU average. Regarding compliance with EIOPA, BaFin is in line with the EU average. Here, however, the general rejection rate is very low (see Figure 7).

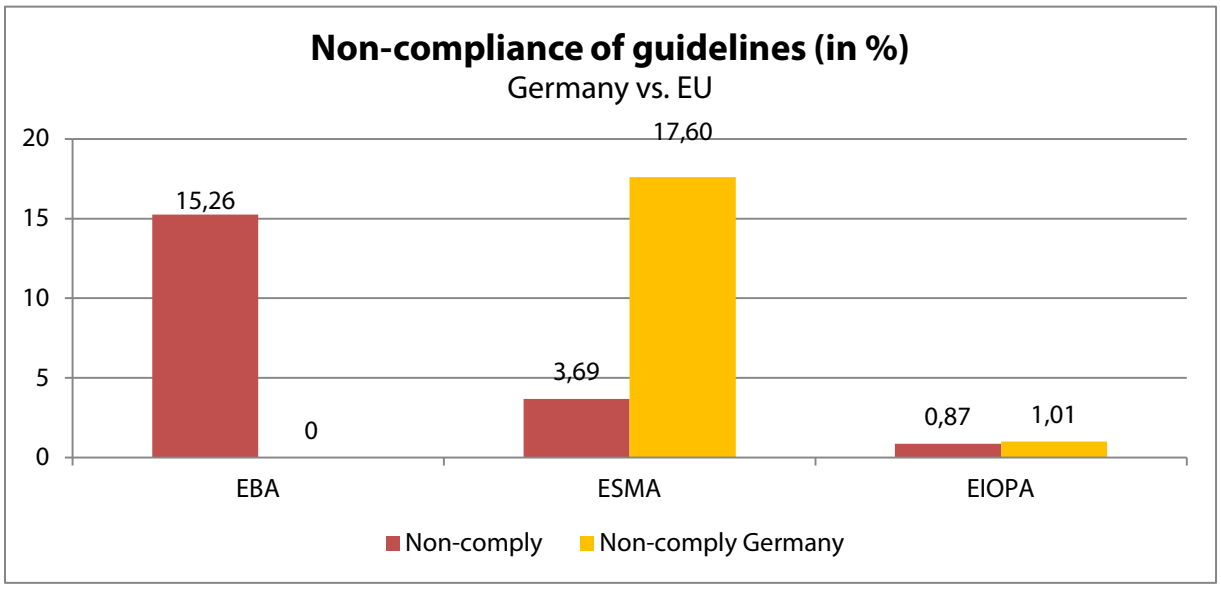

Figure 7: Germany's compliance practice for ESA Guidelines compared with EU
Source: Compliance tables for Guidelines, ESAs website, own calculations (Data as at: 1 July 2016)

2.2 Supervision

2.2.1 Breach of Union Law

The ESAs can, on request or on their own initiative, investigate any alleged breach or non-application of a provision of one of the legislative acts referred to in Art. 1 (2) ESA Regulations by a competent national authority.[65] By no later than two months after the start of the investigation, the ESAs can address a recommendation to the competent national authority concerned setting out the action necessary to comply with Union law.[66] Where the competent national authority fails to comply with the ESA's recommendation within one month, the Commission may issue a formal opinion requiring the respective competent national authority to take the action necessary.[67] The time limit for the Commission in this regard is three months after adoption of the recommendation by the ESA and may be extended by one month.[68]

Where the respective competent national authority does not comply with this formal opinion within the specified period of time, the ESAs may, subject to the provisos that the relevant requirements of the acts referred to in Article 1(2) are directly applicable and that it is necessary to remedy such non-compliance in a timely manner, adopt a binding decision, addressed directly to the affected financial institutions/financial market players, requiring that the necessary action be taken.[69]

2.2.2 Action in emergency situations

Where the Council of Ministers formally determines the existence of an emergency situation, the ESAs can, in certain exceptional circumstances, require the competent authorities to take the necessary action in accordance with the legislation referred to in Article 1(2) ESA Regulations.[70]

Where a competent authority fails to comply with such a decision within the specified period, the requirements of the legislative acts referred to in Article 1(2) ESA Regulations are directly applicable. Where the competent authority fails to apply these requirements or applies them unlawfully and urgent action becomes necessary, the ESAs can address a decision directly to a financial institution/financial market player requiring the necessary action to be taken.[71]

2.2.3 Settlement of disagreements in cross-border situations

In the case of cross-border disagreements between competent national authorities in cases specified in the acts referred to in Article 1(2) ESA Regulations, ESAs can assist in reaching an agreement.[72] In this regard, ESAs can set a time limit for conciliation between the competent

65 Art. 17 (2), sub-para. 1 ESA Regulations.
66 Art. 17 (3), sub-para. 1 ESA Regulations.
67 Art. 17 (4), sub-para. 1 ESA Regulations.
68 Art. 17 (4), sub-para. 2 ESA Regulations.
69 Art. 17 (6) ESA Regulations.
70 (Art. 18 (2) and (3) ESA Regulations)
71 Art. 18 (4) ESA Regulations.
72 Art. 19 (1) ESA Regulations.

national authorities.[73] If the competent national authorities fail to reach an agreement within this time limit, ESAs can take a decision with binding effect requiring the respective competent national authorities to take or refrain from taking specific action to ensure compliance with Union law.[74]

Where a competent authority fails to comply with such a decision and where the requirements of the legislation referred to in Art. 1 (2) are directly applicable, the ESAs can adopt a decision addressed directly at a financial institution/financial market player, requiring the necessary action to be taken.[75]

Instead of this binding settlement of disagreements, ESAs can also carry out "non-binding" mediation whose result is without obligation and cannot therefore be enforced by the ESAs.[76]

2.2.4 Empirical Results: Relevance of ESA Supervision

Since coming into existence, the ESAs have only discovered one breach of EU law: In 2014, EBA found that the Bulgarian National Bank and the Bulgarian Deposit Insurance Fund had breached EU law[77] by unlawfully refusing investors access to protected investments which they held with two Bulgarian banks (Corporate Commercial Bank AD [KTB] and Commercial Bank Victoria EAD [VCB].[78]

The ESAs have however investigated a large number of potential breaches of EU law in recent years. Here are just a few examples. Thus, EBA alone carried out nine investigations in 2015, the majority of which were, however, dropped due to inadmissibility; in a small number of cases the investigations are ongoing.[79] EIOPA registered six cases in 2014. Five were abandoned due to inadmissibility, while one case had not yet been decided at the end of 2014.[80] ESMA investigated a total of 30 cases in 2012. Twelve of them resulted at the time to increased correspondence between ESMA and the competent national authorities but none of the investigations resulted in an official examination of a breach of EU law.[81] ESMA did however send, inter alia, several Opinions to the competent national authorities as a precursor to finding a breach.[82,83] Overall, there is some indication that scrutiny of ESA compliance with EU law tends to take place at an informal level. Formal, binding decisions by ESAs are in any case rare; until now only one such decision has been passed. It is unclear whether the competent national authorities are yielding to the ESAs' interpretation of the law or whether the ESAs are shying away from binding decisions.

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73 Art. 19 (2) ESA Regulations.

74 Art. 19 (3) ESA Regulations.

75 Art. 19 (4) ESA Regulations.

76 Art. 31 (1), sub-para. 2 (c) ESA Regulations.

77 Art. 1 (3) (i) and Art. 10 Deposit Guarantee Directive 94/19/EC

78 EBA (2014) Recommendation to the Bulgarian National Bank and Bulgarian Deposit Insurance Fund on action necessary to comply with Directive 94/19/EC

79 EBA (2015) Annual Report

80 EIOPA (2014) Annual Report

81 European Parliament (2013): Review of the New European System of Financial Supervision (ESFS), Directorate General for Internal Policies, Policy Department A: Economic and Scientific Policy, October 2013, p.101

82 Ibid, p. 123

83 EU Commission (2014): Report from the European Commission to the European Parliament and Council on the operation of the European Supervisory Authorities (ESAs) and the European System of Financial Supervision (ESFS), Commission Staff Working Document, SWD(2014) 261, 8.8.2014

The ESAs can intervene in emergency situations provided the Council of Ministers determines the existence of an emergency situation. Since they came into existence no such situation has arisen; the ESAs have not yet been able to use their power in this regard.

No use has yet been made of the instrument for the binding settlement of disagreements by either EBA, ESMA or EIOPA, although in some cases they have been commissioned by the national authorities to carry out an assessment. Thus in 2014, EBA was commissioned to investigate two cases but these were settled amicably prior to the submission of an arbitration decision.[84]

Here too, greater use seems to be being made of informal processes. "Non-binding" mediation has already been used by EBA in several cases, such as in 2012, when it was formally requested to find a solution to the imposition of "ring fencing measures" at national borders.[85,86] In 2014, EBA was also active in two cases involving non-binding mediation.[87]

2.3 Consumer Protection

2.3.1 ESAs' Mandate

The ESAs have the express task of helping to "enhance customer protection" and foster depositor and investor protection.[88] Firstly, ESAs can pass RTS, ITS and Guidelines on consumer protection subject to the aforementioned requirements (cf. 2.1.1 and 2.1.3). Secondly, ESAs can promote "transparency, simplicity and fairness in the market for consumer financial products or services" by, inter alia, developing training standards for the industry and contributing to the development of common disclosure rules.[89] The ESAs' clearest power is their authority to issue warnings in the event that a financial activity poses a "serious threat" to consumer protection.[90]

Although, in its report on the activities of ESAs, the Commission considers the ESAs' power pursuant to Art. 9 (5) ESA Regulations under the heading "Consumer protection role",[91] the power allows the ESAs to temporarily prohibit or restrict financial activities that threaten the orderly functioning and integrity of financial markets or the stability of the EU financial system in the cases and under the conditions laid down in the legislative acts referred to in Article 1(2) or, in the case of an emergency situation, in accordance with Article 18.[92] Thus the ESAs would ultimately have to justify such a prohibition based on protection of the financial markets or financial stability and could only cite consumer protection indirectly.

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84 EBA (2014) Annual Report, p. 56

85 European Parliament (2013): Review of the New European System of Financial Supervision (ESFS), Directorate General for internal policies, Policy Department A: Economic and Scientific Policy, October 2013, p. 67

86 EU Commission (2014): Report from the European Commission to the European Parliament and Council on the operation of the European Supervisory Authorities (ESAs) and the European System of Financial Supervision (ESFS), Commission Staff Working Document, SWD(2014) 261, 8.8.2014. p. 13

87 EBA (2014) Annual Report, p. 56

88 Art. 1 (5) (f) and Art. 8 (1) (h) ESA Regulations.

89 Art. 9 (1) ESA Regulations.

90 Art. 9 (3) ESA Regulations.

91 Report COM(2014) 509 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) of 8.8.2014, p. 8.

92 Art. 9 (5) ESA Regulations.

2.3.2 Empirical Results: Relevance of the ESAs' consumer protection role

Since coming into existence, ESAs have only issued six warnings in order to ward off a threat to consumer protection. ESMA has shown itself to be the most active with 4 warnings [in 2011 about trading in foreign exchange (forex)[93], in 2012 about online investments[94], in 2014 about the risks of investing in complex products[95] and in 2016 about "contracts for difference, binary options and other speculative products"[96]]. In addition, ESMA issued a warning together with EBA (in 2013 about over-complex contracts for difference[97]). EBA has so far only issued one independent warning (in 2013 about the risks of buying, holding and trading in virtual currency such as Bitcoins[98]). EIOPA has not issued any warnings.

ESA Warnings							
	2011	2012	2013	2014	2015	2016	Total
EBA	0	0	1	0	0	0	1
ESMA	1	1	0	1	0	1	4
EIOPA	0	0	0	0	0	0	0
Joint Warnings	0	0	1	0	0	0	1

Table 1: ESA Warnings
Source: ESA websites

3 Conclusion: Relevance of the regulatory role

So far, the preparatory regulatory work of the ESAs at Level 2 (RTS and ITS) and Level 3 (guidelines) has proven to be particularly relevant. In view of the large backlog of measures, legally binding RTS passed by the Commission are about to take on even greater relevance. ESA guidelines are steadily increasing in number. Despite some divergences, they are widely adhered to.

93 ESMA (2011): Investor Warning: Trading in foreign exchange (forex), ESMA/2011/412, 05.12.2011

94 ESMA (2012): Investor Warning: ESMA warns retail investors about the pitfalls of online investing ESMA/2012/557, 10.09.2012

95 ESMA (2012): Investor Warning: ESMA warns retail investors about the pitfalls of online investing ESMA/2012/557, 10.09.2012

95 ESMA (2014): Investor Warning: Risks of investing in complex products, ESMA/2014/154, 07.02.2014

96 ESMA (2016): Investor Warning: Warning about CFDs, binary options and other speculative products, ESMA/2016/1166, 25.07.2016

97 ESMA and EBA (2013), Investor Warning: Contracts for difference, 28.02.2013

98 EBA (2013): Warning to consumers on virtual currencies, EBA/WRG/2013/01, 12.12.2013

SECTION 2 FOUR PRINCIPLES FOR THE REGULATORY WORK OF ESAs

In view of the overwhelming relevance of the regulatory work performed by ESAs, the following section provides four binding principles for appropriate action by ESAs in this area.

1 Principle 1: Adherence to the mandate

1.1 Adherence to the mandate

Under the principle of the legality of administration, recognised by the ECJ as a general principle of law,[99] the administration is not permitted to act without a legal basis (no acting without law) and is bound in its work by the requirements of the legislator (supremacy of the law). In a Level 1 legislative act, the EU legislator delegates power to the ESAs to draft delegated and implementing acts (and thereby RTS and ITS) and authorises the Commission to adopt them. In the hierarchy of legislation, legislative acts take precedence over Level 2 delegated acts and implementing acts (and thereby over RTS and ITS) and over Level 3 guidelines. Higher ranking law "overrides" subordinate law. Thus a Level 2 or Level 3 measure which conflicts with a Level 1 legislative act is void.

The political will of the legislator and the intended purpose of the legislative proposal must be taken into account when interpreting the Level 1 proposal and thus play a particular role in determining the limits of the mandate.

The following two scenarios are relevant:

- The mandate granted in Level 1 legislation is exceeded, i.e. in their regulatory work, the ESAs and/or Commission exceed the limits of their mandate;
- Conflicts with other Level 1 legislation, i.e. the regulatory work of the ESAs and/or Commission conflicts with other Level 1 legislation.

1.2 Relevance to Level 2 Regulation

Adherence to the mandate is of particular relevance to ESA Level 2 measures because these result in RTS or ITS and thus in legally binding standards. This is no doubt also the reason why the draft RTS and ITS ("drafts") prepared by the ESAs are increasingly being commented on by financial market players.

The power conferred, by the EU legislator in a Level 1 legislative act, upon the ESA (to draft delegated and implementing acts and thereby also RTS and ITS) and upon the Commission (to issue them), is relevant in cases where the mandate is exceeded. Where the ESAs and/or the Commission act outside the mandate (Scenario 1) or where the RTS/ITS conflicts with other Level 1 provisions (Scenario 2), the delegated and implementing acts are void.

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[99] Streinz/Michl, in: Streinz, EUV/AEUV, 2nd Edition, C.H. Beck Verlag, München 2012, Art. 6 TEU, para. 31.

Criticism not related to breaches of the mandate or to other conflicts with Level 1 requirements, but to other aspects of the RTS or ITS, is legitimate but poses no problem for the issue of adherence to the mandate.

Box 1: MREL as an example of exceeding the mandate (?)

One recent example involving a dispute about the limits of the mandate is an RTS developed by EBA under the Bank Resolution Directive (BRRD).[100] The Directive provides that banks must maintain sufficient own funds and liabilities eligible for a bail-in in the event of a bank failure ("minimum requirements for own funds and eligible liabilities, MREL"). The actual amount of the requirement is established for every bank by the competent resolution authority. EBA was commissioned to draft an RTS, defining in more concrete terms the Level 1 criteria[101] which the resolution authorities must take into account when establishing the requirements.[102] In its final draft, EBA stipulated that, in the case of systemically relevant banks, authorities should require own funds and eligible liabilities of at least 8%.[103] This 8% rate is referred to in the BRRD Directive as the minimum amount above which the bank resolution fund may also be used for a bank recapitalisation.[104]

In the Commission's view, EBA thereby exceeded the legislator's mandate. It considers that by specifying the 8%, EBA implicitly established a harmonised MREL requirement. It sees this as incompatible with the Level 1 provision which provides that the MREL rate must be laid down by the bank resolution authorities specifically for each bank.[105] The Commission therefore modified the draft.[106]

EBA, however, believed that its approach did not establish a harmonised minimum level and set out its reasoning in an Opinion to the Commission.[107]

Adherence to the mandate by the ESAs (and the Commission) in Level 2 legislation is important for two reasons.

- Firstly, it must be left up to the democratically mandated legislator (in this case: EP and Council) to decide for itself on the desired scope of its regulatory decisions. Level 2 activities on the part of the ESAs (and the Commission) must not run counter to the decisions of this legislator.

100 Art. 45 (2), Bank Resolution Directive (BRRD), 2014/59/EU

101 See Art. 45 (6) BRRD

102 Art. 45 (2) BRRD

103 EBA (2015): EBA Final Draft Regulatory Technical Standard on criteria for determining the minimum requirement for own funds and eligible liabilities under Directive 2014/59/EU, EBA/RTS/2015/05, 03.07.2015

104 Art. 44 (5) BRRD

105 European Parliament (2016): Scrutiny of delegated acts and implementing measures, Contribution of a representative of the EU Commission, Meeting of the Committee for Economic and Monetary Affairs, 30 June 2016.

106 Commission (2016), Delegated Regulation supplementing Directive 2014/59/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the criteria relating to the methodology for setting the minimum requirement for own funds and eligible liabilities, C(2016)2976

107 EBA (2016): Opinion of the European Banking Authority on the Commission's Intention to Amend the Draft Regulatory Technical Standards Specifying Criteria Relating to the Methodology for Setting Minimum Requirement for Own Funds and Eligible Liabilities According to Article 45(2) of Directive 2014/59/EU, EBA/Op/2016/02, 16.02.2016

- Secondly, although correction by the EP and the Council is possible – at least in the case of delegated acts (and therefore RTS) –[108], the hurdles to this are significant. In the Council, a qualified majority (of 55% of the Member States making up 65% of the EU population) is required; in the EP an absolute majority[109].

1.3 Relevance to Level 3 Regulation

In Level 3 legislation (guidelines and recommendations) too, ESAs must respect the principle of adherence to the mandate. Here, though, the mandate is seldom exceeded because the ESAs' mandate to issue guidelines and recommendations under Art. 16 (1) of the ESA Regulation is very broadly defined. The practice of the EU legislator of including, in Level 1 provisions, specific authorisations for issuing guidelines does not in any way affect this general authorisation because Art. 16 ESA Regulation contains an independent authorisation and thereby sets itself apart from Art. 10 to 15 of the Regulation which only contain the "procedural framework" for RTS and ITS.[110]

The mandate of the ESAs to issue guidelines[111], can be interpreted in three different ways:[112]

- Firstly, the narrow interpretation indicates that the ESAs can only issue guidelines and recommendations where the specific legislative act invokes Art. 16 ESA Regulation. This interpretation is not, however, compatible with the wording of the statute: Art. 16 (1) ESA Regulation clearly does not require any additional reference to itself.
- Secondly, the broad interpretation states that the ESAs can issue guidelines and recommendations where they (a) establish consistent, efficient and effective supervisory practices within the European System of Financial Supervision (ESFS) **or** (b) ensure the common, uniform and consistent application of Union laws.[113] This interpretation is also unconvincing because the wording of Art. 16 ESA Regulation contains the word "**and**".
- Thirdly, there is the interpretation which states that the ESAs can issue guidelines and recommendations where these serve to create consistent supervisory practices in areas regulated by EU law; this means that there must be a general point of reference in EU law for ESA guidelines and recommendations.

The third interpretation is convincing and is consistent with the principle of legal certainty: it respects the wording of Article 16 (1) ESA Regulation and corresponds to Recital 26 of the ESA Regulation which states that the ESAs can issue guidelines and recommendations "on the

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[108] Cf. (Art. 290 (2) (b) TFEU).

[109] In the case of implementing acts (and thus ITS), the possibilities for correction are more narrowly defined; see Footnote 35.

[110] Cf. van Rijsbergen, On the enforceability of EU Agencies' Soft Law at the National Level: The Case of the European Securities and Markets Authority, http://www.utrechtlawreview.org, Volume 10, Issue 5 (December) 2014, URN:NBN:NL:UI:10-1-115854, S. 122 (last accessed on 29 July 2016).

[111] Article 16 (1) ESA Regulation.

[112] Baran/Van Roosebeke, Review of the European Supervisory Authorities, 12 recommendations, cepInput 04 | 2014, http://www.cep.eu/fileadmin/user_upload/cep.eu/Studien/cepInput_ESA/cepInput_ESA.pdf, p 8.

[113] Cf. van Rijsbergen, On the enforceability of EU Agencies' Soft Law at the National Level: The Case of the European Securities and Markets Authority, http://www.utrechtlawreview.org, Volume 10, Issue 5 (December) 2014, URN:NBN:NL:UI:10-1-115854, S. 122 (last accessed on 29 July 2016).

application of Union law".[114] Thus the ESAs can only introduce guidelines on consistent supervisory practices in relation to an area which is regulated by EU law.[115]

Such a link to EU law is generally likely to be present in the case of ESA guidelines and recommendations, thus the limits of the Level 3 mandate are unlikely to be exceeded.

Guidelines which contradict the substantive Level 1 rule are void. In the case of abstract policy conflicts, there is a grey area when it comes to the question of whether ESA guidelines exceed the mandate. The fact that, in 95% of cases, Guidelines are accepted by the national authorities and thus become legally binding by indirect means, exacerbates the problem.

1.4 Conclusion

The ESAs must remain within their mandate when carrying out their regulatory work. Their mandate arises from a basic legislative act (for RTS and ITS as well as many guidelines) and/or directly from the ESA Regulation (for other guidelines). The ESA's are acting in breach of their Level 2 mandate if they exceed the limits of their mandate or if their regulatory work is incompatible with other Level 1 provisions. In the case of non-binding Level 3 measures, the mandate is less likely to be exceeded; the ESA mandate at this level is too broad for that. Guidelines which contradict the substantive Level 1 rule are void.

2 Principle 2: Subsidiarity

2.1 EU Overregulation

Any EU action which does not fall within the EU's exclusive area of competence must respect the Principle of Subsidiarity.[116] This states that the EU will only act as long and insofar as the envisaged objectives cannot be adequately achieved by the Member States but can be better achieved at Union level. Thus decisions in the Union will be reached as close to the citizen as possible[117] whilst, at the same time, effectively avoiding over-regulation at EU level.[118]

Since the Lisbon Treaty, national parliaments and their chambers have had the right to challenge ex ante a breach of subsidiarity by the EU. For this they must indicate, within eight weeks from the date of transmission of a draft legislative act, why the draft, in their view, does not comply with the Principle of Subsidiarity [Art. 6, para. 1, sentence 1 Subsidiarity Protocol (SubsProt)]. The EU institution that submits the draft must take account of these "reasoned opinions" (Art. 7 (1), sub-para. 1 SubsProt).

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[114] Baran/Van Roosebeke, Review of the European Supervisory Authorities, 12 recommendations, cepInput 04 | 2014, p. 8.

[115] Ibid.

[116] The Principle of Subsidiarity is laid down in Art. 5 (3) TEU and in the protocol on the application of the principles of subsidiarity and proportionality.

[117] Protocol on the application of the principles of subsidiarity and proportionality.

[118] Cf. cepInput 04|2015, Reviving the Principle of Subsidiarity, p. 5 et seq., online at: http://www.cep.eu/fileadmin/user_upload/cep.eu/Studien/cepInput_Subsidiaritaet/cepInput_Reviving_the_Principle_of_Subsidiarity.pdf

In this regard, each Member State has two votes. In the case of a bicameral Parliamentary system, each chamber has one vote. In Member States with a single chamber, it has both votes (Art. 7 (1), sub-para. 2 SubsProt).

Where the number of reasoned opinions represents at least one third[119] of all the votes allocated to the national Parliaments, the Commission must review the draft; it is under no obligation, however, either to withdraw the draft or to amend it (so-called **yellow card**, Art. 7 (2) SubsProt).

Where the number of reasoned opinions achieves a simple majority of all the votes allocated to the national Parliaments (so-called **orange card**) and the Commission maintains its proposal, the European Parliament and the Council will examine whether it breaches the Principle of Subsidiarity. If, the Council, by a majority of 55 %, or the European Parliament, by a majority of the votes cast, agree with the subsidiarity complaint, the Commission's proposal will not be given further consideration (in that case: **red card**).

Since the Lisbon Treaty came into force a yellow card has been raised on only two occasions.[120] In both cases, the EU Commission maintained its proposal following a successful subsidiarity check. The Monti-II proposal was subsequently withdrawn however, due to a lack of political support. No orange or red cards have yet been raised.

The establishment of a "green card" is also discussed from time to time. This procedure aims to encourage national parliaments to provide the EU Commission with constructive and non-binding recommendations on EU policy or legislative proposals.[121] Unlike the subsidiarity complaints procedure ("yellow card"), its aim is not to stop a Commission proposal but to provide national parliaments with an instrument for constructive participation.

As regards the meaningfulness and concrete design of a "**green card**" procedure, however, opinions differ, including those of the national parliaments.[122] Some parliamentary chambers point out that national parliaments can submit legislative proposals to the EU Commission without a "green card").[123] The majority of national parliaments have not yet adopted an official position on the green card. They are awaiting further clarification of the concept or do not believe that there is anywhere near enough support for a "green card".[124]

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119 Where the draft legislative act relates to the area of freedom, security and justice (Art. 67 et seq. TFEU), a quarter of all these votes are sufficient (Art. 7 (2), sub-para. 1, sentence 2 SubsProt).

120 This concerned the proposals for Regulations on the exercise of the right to take collective action within the context of the freedom of establishment and the freedom to provide services [COM (2012) 130; "Monti II"] and the establishment of the European Public Prosecutor's Office [COM (2013) 534].

121 Luxembourg Presidency of the Council of the European Union, Information Note in relation to the COSAC Working Group on „green card", last accessed on 9.12.2015

122 For an overview see 24 th Bi-Annual COSAC Report on Developments in European Union: Procedures and Practices Relevant to Parliamentary Scrutiny of 4 November 2015; last accessed on 9.12.2015

123 Thus the Dutch Tweede Kamer, 24 th Bi-Annual COSAC Report on Developments in European Union: Procedures and Practices Relevant to Parliamentary Scrutiny, p. 11

124 The Parliaments/parliamentary chambers in Germany, United Kingdom, Netherlands, Belgium, Poland and Croatia are taking a "wait and see" approach. Finland, Italy and Romania are opposed.

At the same time, a number of parliamentary chambers are concerned that the "green card" should not be confused with the right to initiate legislative proposals which is the prerogative of the EU Commission. Some parliaments point out that there is a need to examine what impact a "green card" would have on the position of the European Parliament.[125] There is currently no sign of widespread support for the "green card" in the European Parliament.[126]

2.2 Relevance to Level 2 Regulation

Level 2 regulation by the ESAs requires a corresponding mandate in a basic Level 1 act. At this point, the question of whether, in the context of the Principle of Subsidiarity, the EU should act at all, has already been answered in the affirmative. As the ESAs' Level 2 role is confined to the definition of Level 1 legislation, the question as to whether RTS and ITS drafted by the ESAs are compatible with the Principle of Subsidiarity, no longer arises.

Strict compliance with the Principle of Subsidiarity at Level 1 by the legislator is therefore crucial. The ESAs cannot be held to blame where European over-regulation at Level 1, which is not compatible with the Principle of Subsidiarity, results in ESA activity at Level 2.

2.3 Relevance to Level 3 Regulation

The picture for Level 3 measures is different. An express mandate in a basic Level 1 act is not a mandatory requirement for Level 3 measures by the ESAs. The ESAs can also adopt guidelines without such a Level 1 mandate (and the associated decision on subsidiarity by the legislator).[127] Consequently, subsidiarity is particularly relevant as a barrier to the exercise of powers at Level 3 because the ESAs have a broadly defined power to adopt non-binding guidelines and recommendations.[128]

The relevance of subsidiarity monitoring at Level 3 is magnified by the widespread incorporation of non-binding guidelines into national law.[129] This increases the risk of over-regulation which in this case, admittedly, cannot be attributed to the EU alone. Officially, such regulation takes place at national level: without the guideline being adopted into national law - for which the competent national authority takes responsibility - there would be no over-regulation. The potential advantages of Level 3 regulation are undisputed: particularly where there is a lack of clarity in Level 1 or Level 2 measures, guidelines provide a genuine added European value.

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[125] See e.g. Belgium and Germany in: Luxembourg Presidency of the Council of the European Union, Information Note in relation to the COSAC Working Group on „green card", last accessed on 9.12.2015.

[126] The green card is, however, mentioned in the Draft Report by the British MEP Sajjad Karim on the Annual Report 2014 on the application of subsidiarity and proportionality; Cf. PE587.620 of 5.8.2016; available at: http://www.europarl.europa.eu/sides/getDoc.do?type=COMPARL&reference=PE-587.620&format=PDF&language=EN&secondRef=01.

[127] Cf. page 2.

[128] Art. 16 ESA Regulations.

[129] Cf. Figure 6.

2.4 Conclusion

As regards Level 2 regulation, it is the EP and the Council rather than the ESAs that bear the responsibility for non-compliance with subsidiarity. They should only act at Level 1 where European action has more value. The wide-ranging power of the ESAs to adopt non-binding guidelines increases the relevance of compliance with subsidiarity in Level 3 measures. The respective competent national authority, however, plays a major role in avoiding over-regulation. Only when it adopts the guideline into national law does it become quasi-binding.

3 Principle 3: Proportionality

3.1 One-size-fits-all Regulation

Like the principle of subsidiarity, the principle of proportionality also limits the role of EU institutions by regulating the exercise of power. The content and form of EU measures must not exceed what is necessary to achieve the objectives of the EU Treaties.[130] This also applies to the ESAs and their regulatory work. Disproportionate legislative provisions issued by the ESAs can give rise to a range of problems. Particularly relevant is the danger of non-risk-based regulation, i.e. regulation whose scope and level of intervention does not correspond to the level of risk. Examples of unreasonable regulation are generalised over-regulation or one-size-fits-all regulation which does not differentiate between the actual risks and may therefore place a disproportionate burden on low-risk financial players.

3.2 Relevance to Level 2 Regulation

Following adoption by the Commission, the RTS and ITS from the ESAs are legally binding. They often involve costs for the affected financial market players which can vary greatly depending on the design of the regulatory measure. Although the ESAs are not responsible for the basic decision on whether EU legislation is necessary in the first place (cf. 2.2) or whether the Level 1 measure is proportional, the ESAs nevertheless retain significant latitude when it comes to adhering to the mandate in drafting RTS and ITS. The specific extent and design of reporting obligations, position limits etc. in Level 2 measures may very well result in over-regulation.

Box 2: Disproportionate transparency requirements for non-equity securities

ESMA was commissioned to draft an RTS defining the transparency requirements in the MiFIR Regulation[131] on trading in non-equity securities.[132] The Commission criticised ESMA's draft RTS. The Commission wanted to delay the introduction of the transparency requirements and suggested a gradual, non-automatic approach. As a result, it will take four years for the

[130] The Principle of Proportionality is laid down in Art. 5 (3) TEU and in the protocol on the application of the principles of subsidiarity and proportionality.

[131] Regulation (EU) No. 600/2014.

[132] Art. 9 and 11 MiFIR.

requirements to achieve ESMA's required standard.[133] ESMA issued an opinion basically welcoming the Commission's changes but still insisting on automatic introduction.[134] Ultimately, the Commission opted for its "more cautious approach".[135]

3.3 Relevance to Level 3 Regulation

Widespread adoption of non-binding guidelines into national law by the competent national authorities[136] increases the relevance of the proportionality of ESA guidelines. Officially, such regulation takes place at national level: Without the guideline being adopted into national law - for which the competent national authority takes responsibility - over-regulation or one-size-fits-all regulations would not arise. The reference to the EU legislator's formulation of the ESA mandate relevant when examining the proportionality of Level 2 measures, only has limited validity because some ESA guidelines have been adopted without a specific Level 1 mandate, i.e. by recourse to Art. 16 ESA Regulations.

Box 3: EBA guidelines on remuneration policy

EU own funds rules (CRD IV)[137] require that, when establishing staff remuneration policies, banks comply with "principles in a manner and to the extent that is appropriate to their size, internal organisation and the nature, scope and complexity of their activities".[138] Some EBA members considered it necessary, in accordance with the principle of proportionality, to stipulate in a guideline[139] that small and non-complex institutions could partially or fully waive the remuneration requirements. They found this to be justified "from a policy perspective".[140] Both the EBA legal department[141] and the Commission took the clear view that a complete waiver was not possible from "a legal view". Proportionality rules would not justify the complete waiver.[142] Ultimately, EBA decided against including a waiver for small banks in its guideline.[143]

133 EU Commission (2016): Letter from Olivier Guersent (EU Commission) to Steven Maijoor (ESMA): FISMA C3/TL/alf(2016)2368644, 20.4.2016.

134 ESMA (2016): Opinion of Steven Maijoor (ESMA): ECON MiFID II/MiFIR Scrutiny Session – 21 June 2016, ESMA/2016/940, 21.6.2016.

135 EU Commission (2016): Letter from Olivier Guersent (EU Commission) to Steven Maijoor (ESMA): FISMA C3/TL/alf(2016)2368644, 20.4.2016

136 Cf. Figure 6.

137 Directive 2013/36/EU.

138 Art. 92 (2), Directive 2013/36/EU (CRD IV).

139 EBA (2015): Guidelines on sound remuneration policies under Articles 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013, EBA/GL/2015/22, 21.12.2015.

140 EBA (2015): Letter from Mr Andrea Enria (EBA) to Ms Paraskevi Michou (EU Commission): Interpretation of the proportionality principle as set out in article 92(2) of the Capital requirements Directive - Remuneration policies, 08.02.2017.

141 Ibid.

142 EU Commission (2015): Letter from Ms Paraskevi Michou (EU Commission) to Mr Andrea Enria (EBA): Interpretation of Article 92(2) of the Capital Requirements Directive - remuneration policies, 23.02.2015.

143 EBA (2015): Guidelines on sound remuneration policies under Articles 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013, EBA/GL/2015/22, 21.12.2015.

3.4 Conclusion

Legally binding RTS and ITS sometimes involve significant costs for the affected financial market players. The ESAs should therefore use the scope of their mandate for proportional Level 2 regulation in order to prevent over-regulation and inefficient one-size-fits-all regulation. In view of the frequent adoption of Level 3 measures by national authorities, proportionality is almost as important for Level 3 measures as for Level 2.

4 Principle 4: Consistency

4.1 Inconsistent regulation

The regulatory work of the ESAs should be consistent across all sectors. Ideally, similar ESA provisions apply to similar risks, whether regarding banks, insurance companies or investment firms. Divergent rules increase the regulatory costs for suppliers operating across sectors and ultimately result in higher costs for the end-customer. In addition, where services in differing financial sectors are in competition with one another as a result of their substitutability, there is a risk of distortions of competition and/or a varying level of consumer protection.

4.2 Relevance to Level 2 Regulation

Two factors impede consistent Level 2 regulation in the EU.

- Firstly, a large part of Level 1 regulation is sector specific and there are certainly compelling arguments for this. Thus, liquidity risks are substantially more relevant to banks than to insurance companies. In the case of diverse micro-prudential risks, sector specific Level 1 regulation makes sense. Other regulatory aspects are, however, of a more horizontal nature; they apply equally to all financial sectors and could be regulated across sectors. This applies for example to large areas of consumer protection.

  Nevertheless, consistent cross-sectoral regulation of these aspects is limited in the EU. With few exceptions (notably the PRIIPS Regulation[144]) consumer protection requirements for the respective sector-specific activity is contained in Level 1 provisions. This would not be a problem if these Directives and Regulations took a consistent approach. The consistent use of standard terms supplemented (where appropriate) by identical or (alternatively) system-identical material requirements, would reduce the costs of compliance for cross-sectoral suppliers increasing comparability and thereby also competition.

  This situation makes it tremendously difficult to achieve consistent cross-sectoral Level 2 regulation. The ESAs' RTS mandates are often contained in different, sector-specific Level 1 texts. The inconsistency in Level 1 measures very often therefore extends to Level 2.

[144] The PRIIP Regulation (EU) No. 1286/2014 contains rules on key information documents for packaged retail and insurance-based investment products and is therefore relevant inter alia to both banks and insurance companies.

- Secondly, the European System of Financial Supervision has been structured in silos. Each of the three main financial sectors (banks, insurance companies, investment firms) has its own independent supervisory authority. In view of the largely vertical regulatory structure of Level 1 legislation, the willingness of the three ESAs to coordinate and cooperate is an absolute must for achieving consistent regulatory conditions. Until now, only 3 of the 63 RTS have been drafted collectively by more than one ESA.

4.3 Relevance to Level 3 Regulation

The arguments applicable to Level 2 regulation apply equally to ESA guidelines. The relevance of regulatory consistency at Level 3 arises from the widespread adoption of non-binding guidelines into national law by the competent national authorities[145]. Officially, such regulation takes place at national level.

4.4 Conclusion

The regulatory work of the ESAs should be consistent across all sectors. Risks which are similar for banks, insurance companies or investment firms should be reflected in similar, if possible identical, regulations. This would reduce the costs of regulatory compliance for cross-sectoral suppliers, improve the comparability of the products and increase competition. This is being hindered, however, by a preponderance of vertical, sector-specific Level 1 regulatory conditions in the EU and by the silo-structure of the ESAs. The resulting risk of inconsistency may extend to Levels 2 and 3.

5 Summary: Relevance of the four principles to the regulatory level of the ESAs

Thus we discern four principles for the regulatory work of the ESAs. These have different levels of relevance for Level 2 and Level 3 measures drafted by the ESAs. Whilst the principle of adherence to the mandate is primarily relevant to Level 2, and the question of subsidiarity only arises at Level 3, the proportionality and consistency of regulatory conditions must be guaranteed at both Level 2 and Level 3. The following chart summarises the relevance of the principles.

	Adherence to the mandate	**Subsidiarity**	**Proportionality**	**Consistency**
Level 2	X		X	X
Level 3		X	X	X

Figure 8: Relevance of the four principles to each regulatory level of the ESAs

[145] Cf. page 8.

SECTION 3 MECHANISMS FOR SCRUTINISING APPLICATION OF THE PRINCIPLES

1 Introduction

Two mechanisms are appropriate for scrutinising whether the regulatory work of the ESAs complies with the four aforementioned principles.

Political scrutiny is essentially carried out at EU level by the European Parliament and the Council of Ministers. As the commissioning principals, they must oversee correct performance of the order by the respective agent (ESA and Commission) and take corrective action where required. For Level 3 measures, political scrutiny at national level is also possible.

Judicial scrutiny refers to the use of all possible legal remedies against RTS or guidelines drafted by the ESAs. Judicial scrutiny is generally carried out by players who are affected financially by the regulatory activities of the ESAs.

The following section will examine the extent to which existing political and judicial scrutiny mechanisms at European and national level ensure compliance with the four principles for the regulatory work of the ESAs at Level 2 and Level 3. In cases where the existing scrutiny is insufficient, whether due to faulty mechanisms or failure to apply the correct mechanisms, the necessary modifications will be supplied.

2 Status Quo: Existing scrutiny mechanisms and their application

2.1 Political Scrutiny at Level 2

2.1.1 Theory

2.1.1.1 The Principal-Agent Theory as a basis for conflict between legislator, ESAs and Commission

During the financial crisis, the European legislators decided to set up the European Supervisory Authorities (ESAs). This action was based on the legislator's desire to handover the task of determining the complex details of regulating the European financial markets to the ESAs and the Commission. The legislator thereby opted to transfer some of its own powers and responsibilities to the ESAs and the Commission in the hope of being able to increase legislative efficiency and reduce information costs by using the specialist knowledge of the authorities and the Commission.

The relationship between EU legislator, on the one hand, and the ESAs and Commission, on the other, is therefore equivalent to that of Principal (as the Client) and Agent (as Contractor). Such relationships have already been analysed in more detail in what is called the Principal-Agent Theory, definitively established by Jensen and Meckling [146].

The basis of the theory is the existence of a contractual relationship in which one or more clients,

[146] Jensen, Michael C., and William H. Meckling. "Theory of the firm: Managerial behavior, agency costs and ownership structure." Journal of financial economics 3.4 (1976): 305-360.

the "Principals", commission others to take on specific tasks. These are the contractors or "Agents". This type of relationship involves several problems, however:

- As a rule, both actors are benefit optimisers who are keen to pursue their own interests. This is a potential conflict situation because the interests of Principal and Agent may diverge. Agents therefore do not always act in the best interests of the Principal.
- There are often knowledge gaps between Principals and Agents. Usually the Principals lack full knowledge about how the Agents carry out the tasks assigned to them and obtaining information involves costs for the Principal.
- The individual assessment of risks also plays a role. Depending on the propensity for risk taking, the actions of the different parties may vary.

In order to combat these problems and thus lower the cost of delegating work, the Principal will usually therefore make efforts to monitor the Agent's work and minimise any divergence from his own interests. He must therefore bear monitoring costs which would not be incurred if he had full information about the agent's activities and about the subject area on which the agent's work is based. He must continually check whether his agents are exercising the powers and responsibilities assigned to them in accordance with the prescribed limits. The principal can also try to motivate the agents by way of specific incentives to comply with certain conduct so that the Agent's interests can be brought into line with his own.[147,148,149]

De facto, however, this gives rise to a dilemma On the one hand, the outsourcing is connected to the aforementioned benefits. At the same time, monitoring of the agent by the principal gives rise to costs.

This dilemma also exists as regards the relationship between the European Parliament and the Council, on the one hand, and the ESAs and the Commission, on the other. In this relationship, the European Parliament and the Council act as the two "principals" and the ESAs and the Council are their "agents". Thus the ESAs develop technical standards, adopt guidelines and submit recommendations, on behalf of the European Parliament and the Council who are the legislators. The Commission can modify the standards. This procurement method, however, gives rise to the aforesaid problems, namely:

- The interests of the three ESAs and the Commission, as agents, and those of the European Parliament and the Council, as principals, may diverge. As all six actors are, in principle, anxious to assert their individual preferences, conflicts about, for example, the interpretation of the mandate for developing an RTS, are likely.
- During the development of technical standards, guidelines and recommendations,

147 Jensen, Michael C., and William H. Meckling. "Theory of the firm: Managerial behavior, agency costs and ownership structure." Journal of financial economics 3.4 (1976): 305-360.

148 Ordelheide, Dieter; Rudolph, Bernd; Elke, Büsselmann (1991): Betriebswirtschaftslehre und ökonomische Theorie, p. 150 et seq.

149 Eisenhardt, Kathleen M. "Agency Theory: An Assessment and Review." The Academy of Management Review 14.1 (1989): 57-74.

informational asymmetries arise. The ESAs build up professional and technical expertise in order to carry out their legislative task as a result of which their knowledge starts to outstrip that of their principals. At the same time, there is a growing danger that the European Parliament and the Council will not, at least not without accepting higher costs, be able to assess whether the ESAs are carrying out their assigned tasks properly and as defined.

To avoid or at least reduce this problem, therefore, the legislator has implemented some institutional procedures. The right of the European Parliament and the Council to challenge RTS adopted by the Commission, is one of these. This is an attempt to take away the incentive of the ESAs and the Commission to pursue their own interests rather than those of the principal.

The relationship between the ESAs and the Commission cannot be regarded as a principal-agent relationship. It is the EU legislator and not the Commission that commissions the ESAs to develop draft RTS. Nevertheless, the Commission does "monitor" the ESAs to a certain extent: It can examine the ESAs' draft RTS to ensure that they comply with EU law[150]. This is in the Commission's own interest because the RTS will ultimately be adopted as delegated acts of the Commission. The Commission also carries out an examination of the content of the draft RTS and can implement changes "where the Union's interests so require".[151]

2.1.1.2 Politico-economic explanations for the low rejection level of RTS and of failures by the Commission and the ESAs to adhere to the mandate

Until now, in the area of financial market regulation, the European Parliament has only once spoken out against a delegated act with which the Commission intended to adopt an RTS[152]. The Council has never done so. By contrast, the Council and the EP have made efforts in a few cases to influence the content of RTS prior to their adoption. These efforts were aimed, on the one hand, at influencing the ESAs, that draft the RTS, and on the other, at the Commission as the body adopting the RTS. What is the explanation for this pattern of behaviour?

2.1.1.2.1 Lack of incentive for members of the Council and the EP to exercise scrutiny

In order to reject an adopted RTS, a qualified majority is required in the Council, and an absolute majority in the EP. A significant amount of effort on the part of the members of the institutions is therefore necessary in order to achieve these majorities against an RTS. Negotiations and votes in the committees are necessary, lobbying must be carried out and, where appropriate, subject-specific expertise must be established. RTS are generally also highly technical and therefore a prodigious amount of time is required to understand them. Due to the limited time allotted, Council members and MEPs therefore find themselves confronted by opportunity costs. Is it worth taking action to block an RTS or would it be individually "more profitable" to work on other

[150] In an "early legal review", offices of the Commission check the legality of the ESAs' draft RTS and ITS at an early stage.

[151] Cf. 2.1.1 page 6.

[152] European Parliament resolution of 14 September 2016 on the Commission delegated regulation of 30 June 2016 supplementing Regulation (EU) No 1286/2014 of the European Parliament and of the Council on key information documents for packaged retail and insurance-based investment products (PRIIPs) by laying down regulatory technical standards with regard to the presentation, content, review and revision of key information documents and the conditions for fulfilling the requirement to provide such documents, P8_TA(2016) 0347.

proposals, that are competing with the RTS for attention? Two further aspects are also relevant in this decision-making process. Firstly, the question of whether the action is "in the interests" of the voter, which is generally unlikely in view of the technical nature of the issues relating to RTS. Secondly, there is a risk of free-riding whereby everyone shies away from making their own efforts in the hope or expectation that someone else will take them on. This individually rational strategy for the avoidance of "costs" can however mean that no-one campaigns for the rejection of an RTS even though, as a group, they would certainly welcome such a decision. The non-rejection of the RTS would not therefore fail because of a lack of "common will" of the Members of the European Parliament to do so, but because of a lack of "developing" this common will. Where the incentive to make individual effort is so lacking, collective action is accordingly less pronounced. This may in turn allow the ESAs and the Commission to extend their scope for action and/or mandate.[153,154]

2.1.1.2.2 Cost reduction by negotiation prior to adoption of RTS

Rather than undertaking the major effort necessary to obtain the majorities for a veto against an RTS, negotiations prior to the adoption of an RTS can be an effective way to bring about amendments. They are less costly for the actors involved than obtaining majorities and are therefore a preferred method. Ad hoc intervention by individual MPs or Council members in combination with the credible threat of a veto can thus bring about a turn around on the part of the ESAs or the Commission ex ante, during the development of the RTS, and persuade them instead to accommodate the wishes of the EP or Council. By contrast with joint action, this method also allows the players a chance "to generate direct successes which they can claim for themselves".[155,156]

2.1.2 Practice

2.1.2.1 European Parliament

Although the ESA Regulations provide that the European Parliament can raise objections to RTS adopted by the EU Commission (see page 6), the Parliament has only rejected a single RTS (in the form of a delegated act).[157]

This does not, however, mean that the European Parliament is passive. The Parliament has, in fact, substantially extended its rights of scrutiny contained in the ESA Regulations and is in a position not only to reject "as a whole" RTS adopted by the Commission as delegated acts but can also enforce substantive changes to individual parts of the RTS at an earlier stage.

This was brought about by the firm stand taken by the European Parliament in 2013. Following the EMIR Regulation (EU) No. 648/2012, ESMA had submitted six draft RTS to the Commission. The

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153 Ibid, p. 25.

154 Kaeding, Michael, and Kevin M. Stack. "Legislative Scrutiny? The Political Economy and Practice of Legislative Vetoes in the European Union." JCMS: Journal of Common Market Studies 53.6 (2015): 1268-1284.

155 Moe and Wilson (1994), p. 10.

156 Kaeding and Stack (2015).

157 On September 14th 2016, the European Parliament objected to the EU Commission's delegated regulation regarding the PRIIPs-Regulation, P8_TA(2016)0347.

Commission had adopted five of these as delegated acts without amendment and rejected one RTS.

Under the aegis of Rapporteur Werner Langen MEP, strong opposition to the Commission's delegated acts arose in the European Parliament's ECON Committee. The Committee criticised the Commission's conduct to the effect that

(1) the Commission was six weeks late informing the Committee of the rejection of the draft RTS[158] and

(2) the Commission did not react to the written comments of some MEPs on ESMA's draft RTS until after the delegated acts had been adopted.[159]

In a proposed draft resolution from the ECON Committee, the European Parliament openly threatened the Commission with rejection of the delegated acts.[160] The Commission obviously took this to be a credible threat. In an opinion, the Commission promised to work together with the European Parliament on the future planning of RTS. In addition, the Commission agreed to meetings between Commission staff and MEPs when preparing RTS.[161] The draft resolution was then withdrawn.

As a result of this precedent, a large number of informal procedures have arisen bringing a new level of quality to the scrutiny of RTS by the ECON Committee of the European Parliament. The Parliament has further developed its right to reject a delegated act per se and is now in a position to exert influence on the concrete design of RTS at an early stage.

There is no regulated procedure for this extended exertion of influence. In practice, three activities appear to be relevant.

- Written interventions by MEPs addressed to the ESAs or to the EU Commission[162];
- Monthly "scrutiny slots" in the ECON Committee during which the MEPs can ask representatives of the ESAs and the Commission about the design of RTS;
- Other personal meetings between Commission, ESAs and MEPs.

Although the ECON Secretariat is responsible for handling the practical side of these elements, the level of scrutiny depends on the initiative of individual MEPs. The "negotiating team" has proven to be relevant in this regard, that is to say the group of MEPs responsible for looking after the

158 ECON-Committee, Motion for a Resolution, PE504.099v02-00 of 4.2.2013, para. D.

159 ECON-Committee, Motion for a Resolution, PE504.099v02-00 of 4.2.2013, para. L.

160 ECON-Committee, Motion for a Resolution, PE504.099v02-00 of 4.2.2013, para.

161 Declaration of the EU Commission, 15.12.2014, available at: https://polcms.secure.europarl.europa.eu/cmsdata/upload/7fd7b35c-1bfc-49ad-8c09-18afe6677766/att_20130208ATT60780-940662385801784106.pdf, last accessed on 29.07.2016.

162 Cf. Letter from ECON Chairman (Roberto Gualtieri) and the MiFID Rapporteur (Markus Ferber) of 27.11.2015 to the EU Commission on the MiFID/MiFIR RTS 2, 20 and 21. In the letter, the ECON Committee expresses its dissatisfaction about the fact that ESMA only partly complied with the Committee's request of 23 July 2015 to amend the draft RTS. It suggests to the Commission a detailed list of changes to "prevent Parliament from raising objections to the RTS".

underlying Level 1 legislation. The aforementioned activities are therefore often limited to the Rapporteur and Shadow Rapporteur. The coordinators of the political groups are informed and can take part. The other MEPs are not usually involved. They can, however, take part in the scrutiny slots. These take the form of a hearing and took place ten times in 2015 and so far six times in 2016 (as of: end of July). The Committee MEPs who are not directly involved are then informed when the final delegated acts adopted by the Commission are available. Due to the lack of a definite procedure or document register, the influence exercised by specific MEPs is not readily identifiable or easy to understand. Although a rejection of these delegated acts is then still possible, the informal procedure aims to avoid this. Until now, Parliament has not rejected a single RTS.

Two phases of the European Parliament's fledgling extended scrutiny procedure appear to be particularly relevant.

- Phase 1: After the opening of the public consultation phase held by the ESAs on an RTS. Here the ESAs are the main point of contact for the ECON MEPs.
- Phase 2: After submission of the draft RTS to the Commission by the ESAs. Here the Commission is the main point of contact for the ECON MEPs.

In the absence of a public document register for the extended scrutiny procedure, a conclusive assessment about the relative relevance of the two phases is difficult. Nevertheless, changes to the RTS document in Phase 1 are much easier than in Phase 2 because the Commission must agree changes to the RTS with the ESAs. In the (albeit controversial) area of MiFID/MiFIR RTS, the Commission has only rejected 3 of 42 RTS from ESMA[163]. From this we may conclude that Phase 1 represents the decisive phase for exercising influence but it is probably still too early for any definitive judgement. In the case of MiFID und MiFIR in particular, some MEPs have taken part in the public consultations held by ESMA on RTS and have also sought direct contact with ESMA. Whether the concentration of a large number of MiFID/MiFIR-RTS in a short space of time was responsible and whether this development will continue in the extended scrutiny procedure, remains to be seen.

2.1.2.2 Council of Ministers

Although the Council makes an active decision with respect to all RTS about whether to challenge a delegated act of the Commission, it has not yet done so. The Council always adopts the "intention not to raise objections". The Council's scrutiny activities, however, appear to be significantly behind those of the European Parliament. There are no procedures in the Council comparable to the EP's "scrutiny slots". Although, Council work groups can be set up in Phase 1, on the initiative of the rotating Council Presidency, this has only happened on rare occasions. Even where the Commission hears national representatives in work groups, these meetings do not appear to take the form of negotiations in the way that similar meetings between the Commission and MEPs do.

[163] Statement Steven Maijoor at ECON scrutiny slot of 21.6.2016, available at: https://www.esma.europa.eu/file/18852/download?token=8mvBm6Tz, last accessed on 4.8.2016.

Even the Member States have recognised the potential for improvement. Since the end of 2014, the Council has been looking into the question of how to deal with the abundance of Level 2 measures (RTS and ITS or other delegated acts of the Commission). The Council has therefore entrusted a sub-group of the "Financial Services Committee" (FSC) with the task of developing proposals. The FSC is an internal committee of the Council established in 2003[164], which deals inter alia with issues outside the usual legislative procedure[165].

The FSC submitted recommendations on which processes to improve in the Council. They were confirmed at the beginning of July 2015 by the Economic and Monetary Affairs Committee and Coreper.[166] The FSC recommendation essentially covers six aspects.

Improving transparency during development phase of Level 2 measures The FSC calls on the Commission to improve transparency and dialogue with the ESAs, the EP and the Council when preparing RTS. This applies in particular where the Commission wants to amend an ESA draft RTS. For this purpose, the Commission will set up an early warning system and set out the reasons for the changes which it requires.

In the case of RTS which the Council grades as "high-priority", the ESA will enter into more intensive dialogue with the Council before they submit the draft RTS to the EU Commission (Phase 1). In phase 2, that is after the ESAs have submitted their draft to the EU Commission, the ESAs are obliged to consult Member States. This applies in particular to high-priority RTS and to RTS where the Commission intends to make a change.[167]

Streamlining the Level 2 process The FSC recommends the Council to prioritise Level 2 measures. The most important policy measures should be more effectively accompanied by enhanced arrangements in the Council. For this the FSC proposes greater consultation with experts and more discussions and assessment within the FSC. [168]

Bundling of Level 2 measures The FSC wants the Commission to bundle Level 2 measures together only after active consultations with the Council.[169] This would create confidence and discourage subsequent rejection of the bundled acts. In addition, the FSC highlighted the (albeit controversial)[170] view that, where several Level 2 measures are bundled together into one delegated act, the Council can object to each of them separately.[171]

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[164] The FSC consists of representatives of the Member States and the EU Commission. The ECB and the respective EU regulatory committees have observer status.

[165] Council of the EU (2003): Financial Services Committee, 9160/03 (Press 129), 8.5.2003.

[166] Council of the EU (2015): FSC Report on Level 2 Processes- Endorsement, General Secretariat of the Council to Permanent Representatives Committee (Part 2), 10602/15, 9 July 2015

[167] Council of the EU (2015): FSC Report on Level 2 Processes- Endorsement, General Secretariat of the Council to Delegations, 1759/15, 23 June 2015, p. 7 et seq.

[168] Ibid, p. 13 et seq.

[169] The Commission streamlines the Level 2 process by bundling the various Level 2 measures into one delegated act, for example because they relate to the same subject area.

[170] The Commission, for example, takes the opposite view on this.

[171] Council of the EU (2015): FSC Report on Level 2 Processes- Endorsement, General Secretariat of the Council to Delegations, 1759/15, 23 June 2015, p. 13 et seq.

Improving information flows The FSC sees a need to improve the exchange of information among the Council members about upcoming Level 2 measures. It therefore calls for systems for the exchange of information to be established, such as in the form of dedicated mailing lists to be drawn up by the Council Secretariat. A dedicated communications process should be put in place especially for high-priority Level 2 measures. The exchange of information in this regard should begin in phase 1.[172] The systems for information exchange will help to improve coordination of the rejection of Level 2 measures.[173]

Working parties with the Commission The FSC points out that, owing to the need to gather a qualified majority, the Council has difficulty rejecting Level 2 measures. The short assessment deadlines following submission by the Commission are also a challenge.

The FSC therefore recommends organising working parties with the Commission for the high-priority Level 2 measures. These will improve coordination.

Level 2 limits to the mandate The FSC insists that political issues must be addressed centrally at Level 1 and not deferred to Level 2 in order to avoid political conflicts. Alternatively, players should at least be provided with enough information about the mandate given to them. The ESAs should also be "systematically consulted" during the negotiations between the Commission, Council and EP to establish the Level 2 mandates given to the ESAs at Level 1. [174]

[172] Ibid, p. 18 et seq.
[173] Ibid, p. 20 et seq.
[174] Ibid, p. 23 et seq.

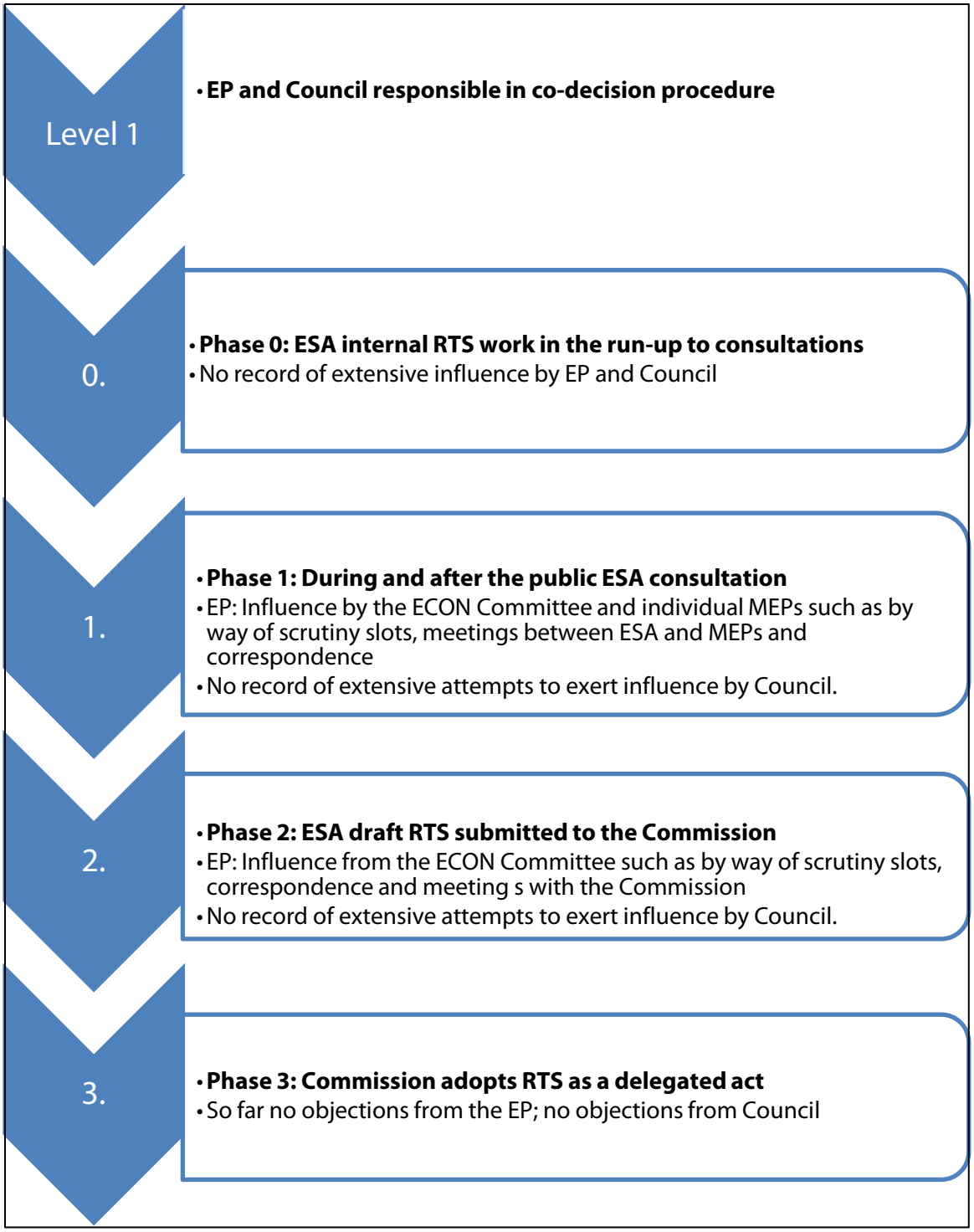

Figure 9: Influence exerted by EP and Council at Level 2

2.1.3 Conclusion

Although neither the Council nor the European Parliament has yet made use of its right to reject RTS (in the form of delegated acts of the Commission), political scrutiny of the regulatory role of the ESAs at Level 2 differs markedly between the EP and the Council. Significant differences exist both between the established procedures and the actual scope of political scrutiny.

The EP's ECON Committee has extended its own bargaining power by way of clever tactical manoeuvring. In the EP, actual political scrutiny of Level 2 activities takes place when the ESAs consult publicly about RTS (Phase 1). The EP also exerts influence after the ESA has submitted a draft RTS to the Commission (Phase 2). The Council – despite some effort – has not yet managed to set up similar working methods. This has a negative effect on its influence.

The main reason for the differences between the Council and the EP is probably that parliamentary scrutiny by the ECON Committee is carried out by the MEPs responsible for the Level 1 basic legislative act, i.e. by the Rapporteur and respective Shadow Rapporteur. This clear assignment of responsibility to a few individuals in combination with the support of the Committee Secretariat makes the coordination of political scrutiny much easier. These two factors do not exist in the Council.

2.2 Judicial Scrutiny at Level 2

Competent authorities and financial institutions/financial market players can challenge RTS and ITS at Level 2 by way of the action for annulment pursuant to Art. 263 TFEU. In addition, there is the possibility of interim measures pursuant to Art. 278 and Art. 279 TFEU.

2.2.1 Proceedings before the ECJ

2.2.1.1 Action for annulment pursuant to Art. 263 TFEU

Competent authorities and financial institutions/financial market players can challenge RTS and ITS adopted in the form of delegated acts by way of an action for annulment in the ECJ pursuant to Art. 263 TFEU. The competent court of first instance is the court whose decisions are subject to a right of appeal to the ECJ on a point of law.[175]

RTS and ITS qualify as a basis for an action under Art. 263 (1), sentence 1 TFEU. All acts of the Commission, provided they are not recommendations or opinions, qualify as a basis for an action insofar as they are legally effective vis à vis third parties. RTS and ITS are enacted in the form of Commission Regulations or Decisions.[176] Draft RTS and ITS, on the other hand, cannot be challenged because they are only preparatory actions within the meaning of the ECJ's case law in the Olivieri case.[177]

[175] Art. 256 (1) TFEU.

[176] Art. 10 (4) and Art. 15 (4) ESA Regulations.

[177] Michel, Institutionelles Gleichgewicht und EU-Agenturen, Duncker & Humblot GmbH, Berlin 2015, p. 275.

Competent national authorities and financial institutions/financial market players are also entitled to bring an action under Art. 263 (4) TFEU. They are so entitled where acts are addressed to them, where an act "directly and individually" concerns them or where a regulatory act, which does not entail implementing measures, is of direct concern to them. The last alternative thus does not require individual concern like that required under the ECJ's so-called Plaumann Formula where the Claimant must be affected by reason of certain attributes which are peculiar to him or by reason of circumstances in which he is differentiated from all other persons, thus making him de facto affected by an action in the same way as the person addressed. [178]

RTS and ITS are regulatory acts within the meaning of Art. 263 (4) para. 3 TFEU. The term "regulatory act" is not defined in the TFEU. According to ECJ case law, however, it includes acts of general application with the exception of legislative acts.[179] Delegated acts under Art. 290 TFEU and implementing acts under Art. 291 TFEU, in particular, constitute such acts.[180] RTS and ITS are enacted as delegated acts and implementing acts.[181]

The criterion of direct concern is intended to exclude persons from being able to bring an action where they are only potentially concerned by an act.[182] A claimant is directly concerned where an act has a detrimental effect on him without any other factors being involved.[183] Thus legislative acts addressed to Member States do not usually have direct effect on an individual unless the Member State is obliged to implement them and has no room for discretion in this regard.[184] Regulations and Decisions do have a direct effect on the parties concerned without any other factors being involved.

"Does not entail implementing measures" is a criterion restricted to cases of formal directness and is thus narrower than the criterion of indirectness.[185] RTS and ITS fulfil this criterion because, since they take the form of Regulations or Decisions, they do not require any further implementing acts.

Grounds for an action are: lack of competence, infringement of an essential procedural requirement, infringement of the Treaties or of any rule of law relating to their application, or misuse of powers.[186]

"Infringement of the Treaties or of any rule of law relating to their application" is a catch-all provision compared to the three other grounds for rejection under Art. 263 TFEU.[187] In practice, it

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[178] ECJ, Case No. C-25/62 of 15 July 1963, ECLI:EU:C:1963:17, Plaumann & Co. / Commission, p. 238.

[179] ECJ, Case No. T-18/10, ECLI:EU:T:2011:419, Inuit Tapiriit Kanatami and Others v Parliament and Council, para. 56; upheld by ECJ Case No. C-583/11 P, ECLI:EU:C:2013:625, para. 60 et seq.

[180] Dörr, in: Grabitz/Hilf/Nettesheim, Das Recht der Europäischen Union, 58th Update, Verlag C.H. Beck. München 2016, Art. 263 TFEU, para. 82.

[181] Art. 10 (1), sub-para. 1 and Art. 15 (1) sub-para. 1 ESA Regulations.

[182] Cremer, in: Calliess/Ruffert, EUV/AEUV, 5th Edn., Verlag C.H. Beck, München 2016, Art. 263 TFEU, para. 36.

[183] Cremer, in Calliess/Ruffert, EUV/AEUV, 5th Edn., Verlag C.H. Beck, München 2016, Art. 263 TFEU, para. 36.

[184] Cremer, in Calliess/Ruffert, EUV/AEUV, 5th Edn., Verlag C.H. Beck, München 2016, Art. 263 TFEU para. 36.

[185] Dörr, in: Grabitz/Hilf/Nettesheim, Das Recht der Europäischen Union, 58th Update, Verlag C.H. Beck, München 2016, Art. 263 TFEU, para. 84 et seq.

[186] Art. 263 (2) TFEU.

provides the most important grounds for an action.[188] Despite the narrow wording, the legal test constitutes "the entire written and unwritten law" of the EU.[189]

An infringement of the principle of the legality of administration can thus be grounds for an action because it is recognised by the ECJ as a general principle of law.[190] It covers the principle of no acting without law under which the administration cannot act without a statutory basis and the principle of the supremacy of law whereby the administration is bound by the law. Thus, in the context of an action for annulment, the ECJ can examine whether an RTS or an ITS satisfies the requirements of the delegation of power and other Level 1 rules and therefore "adheres to the mandate".

An action for annulment can also be based on an infringement of the principle of subsidiarity under Art. 5 (3) TEU. Although the principle of subsidiarity protects the Member States, its infringement can be censured "incidentally in any proceedings by all those entitled to bring an action".[191]

The action for annulment also allows a measure to be challenged on the grounds that it is disproportionate. The principle of proportionality has long been recognised by the ECJ and academic literature as an element of the Rule of Law and part of the protection of fundamental rights.[192] The principle of proportionality as regards the use of competences is laid down in Art. 5 (1), sentence 2 in conjunction with (4) TEU.

Where the action is well founded, the ECJ declares the act concerned to be void.[193] The declaration takes effect erga omnes.[194]

2.2.1.2 Interim measures under Art. 278 and 279 TFEU

Actions before the ECJ do not have suspensory effect.[195] The claimant may, however, apply for interim measures.[196] In this regard, it should be noted, inter alia, that an application is only admissible where a fully substantiated action on the main issue has been brought.[197]

An application is substantiated where an order for interim measures is necessary and there is urgency.[198] In addition, according to the case law, the balancing of interests between the claimant,

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187 Cremer, in: Calliess/Ruffert, EUV/AEUV, 5th Edn., C.H. Beck Verlag, München 2016, Art. 263 TFEU, para. 95; Ehricke, in: Streinz, EUV/AEUV, 2nd Edition, C.H. Beck Verlag, München 2012, Art. 263 TFEU, para. 84.

188 Thiele, in: Leible/Terhechte, Enzyklopädie Europarecht, Europäisches Rechtsschutz- und Verfahrensrecht, § 9 Die Nichtigkeitsklage, Nomos Verlagsgesellschaft mbH & Co. KG, Baden-Baden 2014, para. 71.

189 Ibid.

190 Streinz/Michl, in: Streinz, EUV/AEUV, 2nd Edn., C.H. Beck Verlag, München 2012, Art. 6 TEU, para. 31.

191 Streinz, in: Streinz, EUV/AEUV, 2nd Edn., C.H. Beck Verlag, München 2012, Art. 5 TEU, para. 24.

192 Streinz, in: Streinz, EUV/AEUV, 2nd Edn., C.H. Beck Verlag, München 2012, Art. 5 TEU, para. 41.

193 Art. 264 (1) TFEU.

194 Cremer, in: Calliess/Ruffert, EUV/AEUV, 5th Edn., Verlag C.H. Beck ,München 2016, Art. 264 TFEU, para. 2 with further references.

195 Art. 278, sentence 1 TFEU.

196 Art. 278, sentence 2 and Art. 279 TFEU.

197 Wegener, in: Calliess/Ruffert, EUV/AEUV, 5th Edn., C.H. Beck Verlag, München 2016, Art. 279 TFEU, para. 8.

on the one side, and the interests of the EU and third parties, on the other, must come out in favour of the claimant.[199]

An interim order is necessary where the main claim appears, prima facie, to be well founded. Urgency exists where interim measures are necessary in order to protect the claimant from serious and irreparable loss. According to the ECJ, financial loss can be reimbursed subsequently and so does not generally justify an interim order.[200] In this regard, the ECJ is referring to the possibility of compensation *in concreto*.[201] This means that "the mere fact" that an action for damages is available under EU law is not sufficient to show that the alleged loss is recoverable.[202] The ECJ balances the "immediate adverse effects of the Union act" against "the possibility of future compensation for the loss".[203] The ECJ, however, "never examines the actual chances of success of an action for damages".[204] "General legal uncertainty regarding the assertion of a right to damages" is not therefore to be taken into consideration.[205] This case law of the ECJ is regarded by some as "too restrictive".[206]

Non-contractual liability claims against the EU for loss caused by its institutions or servants in the exercise of their official duties are governed by Art. 340 TFEU. Since its crucial decision in the case of *Schöppenstedt*[207], the ECJ has also recognised legislative acts as relevant under the law on liability.[208] Nevertheless, it must be noted that for such liability to arise, EU institutions must have exceeded their powers "manifestly and gravely".[209] If we classify the decision on whether an infringement of the law is "manifest and grave" as general legal uncertainty, an application for interim measures would be unsuccessful under the aforementioned ECJ case law since, in principle, compensation is possible.

2.2.2 Bringing of actions

As far as can be ascertained, no actions for annulment have yet been brought against RTS or ITS. This leads to several conclusions. It is possible that, as a result of political scrutiny, at least the controversial requirements have been mitigated or prevented so that ex post scrutiny no longer seems necessary. It is also possible, however, that the duration of the procedure or the fear of damage to reputation prevents those affected from bringing an action.

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198 Art. 156 (4) Rules of Procedure of the General Court of 4 March 2015.

199 Cf. Wegener, in: Calliess/Ruffert, EUV/AEUV, 5th Edn., C.H. Beck Verlag, München 2016, Art. 278, 279 TFEU, para. 24.

200 Wegener, in: Calliess/Ruffert, EUV/AEUV, 5th Edn., C.H. Beck Verlag, München 2016, Art. 279 TFEU, para. 22.

201 Wegener, in: Rengeling/Middeke/Gellermann, Handbuch des Rechtsschutzes in der Europäischen Union, 3rd Edn., C.H. Beck Verlag, München 2014, § 19 para. 30.

202 ECJ, Case No. 232/81 R, Order of 21 August 1981, ECLI:EU:C:1981:191, Olio, para. 9

203 Wegener, in: Rengeling/Middeke/Gellermann, Handbuch des Rechtsschutzes in der Europäischen Union, 3rd Edn., C.H. Beck Verlag, München 2014, § 19 para. 30 with reference to ECJ Case No. 174/80 R, Order of 21 August 1981, ECLI:EU:C:1980:205, Reichardt, para. 6 and ECJ Case No. 232/81 R, Order of 21 August 1981, ECLI:EU:C:1981:191, Olio, para. 9.

204 ECJ, Case No. C 404/01 P(R), Order of 14 December 2001, ECLI:EU:C:2001:710, Commission v Euroalliages and Others, para. 70.

205 Cf. Wegener, in: Calliess/Ruffert, EUV/AEUV, 5th Edn., C.H. Beck Verlag, München 2016, Art. 279 TFEU, para. 22.

206 Wegener, in: Calliess/Ruffert, EUV/AEUV, 5th Edn., C.H. Beck Verlag, München 2016, Art. 279 TFEU, para. 22.

207 ECJ, Case No. C-5/71, Judgement of 2 December 1971, ECLI:EU:C:1971:116, Schöppenstedt.

208 Gellermann, in: Streinz, EUV/AEUV, 2nd Edn., Verlag C.H. Beck, München 2012, Art. 340 TFEU, para. 16.

209 Ruffert, in: Calliess/Ruffert, EUV/AEUV, 5th Edn., C.H. Beck Verlag, München 2016, Art. 340 TFEU, para. 19.

In addition, as described above, there are significant hurdles to proceedings for interim measures. Furthermore, they only have a "very low success rate". [210]

2.2.3 Conclusion

The action for annulment and interim measures constitute two instruments for the judicial scrutiny of RTS and ITS. In practice, however, they play no role in examining Level 2 measures before the ECJ to determine whether they adhere to the mandate and comply with the principles of subsidiarity and proportionality.

2.3 Political Scrutiny at Level 3

2.3.1 At EU Level

The ESA Regulations do not provide for the EP and Council to deal with the content of ESA guidelines. By way of Level 1 measures, the Council and EP can expressly commission the ESAs to develop guidelines; this does not prevent the ESAs from developing guidelines outside such mandates as well. Although the non-binding nature of guidelines makes the broad scope of the mandate and the lack of material scrutiny at EU level justifiable, this is increasingly being called into question, probably as a result of the comprehensive implementation of guidelines by national regulatory authorities (cf. page 12).

Criticism of the practice of the ESAs regarding guidelines has come, in particular, from the European Parliament which is not involved in the development of guidelines - unlike the Member States who are indirectly involved via the national supervisory experts in the ESAs.

On the one hand, the EP certainly regards guidelines as a useful supervisory instrument. Such as "where no powers for the ESAs were provided for in the sectoral legislation, guidelines have proven to be a useful and necessary tool to fill gaps in regulation."[211]

At the same time, the EP "clarifies that guidelines to improve common standards for the whole internal market (...) can be issued only based on the respective empowerment in sectoral legislation (...) which can secure democratic legitimacy."[212]

In the Discharge regarding ESA budgets it is mentioned annually that every ESA "given its limited resources, must stick to the tasks assigned to it (...), must not seek to go beyond its mandate (...) and should check the necessity of drafting guidelines and recommendations;"[213]

In earlier Discharge reports, however, the criticism was softer. Every ESA "when drafting implementing legislation, guidelines, questions and answers or similar measures, must always

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[210] Wegener, in: EUV/AEUV, 5th Edn., C.H. Beck Verlag, München 2016, Art. 279 TFEU, para. 1.

[211] EP Resolution on European System of Financial Supervision Review (ESFS-Review) of 11.03.2014, P7_TA(2014)0202, Recital BA.

[212] Ibid, p. 14.

[213] Here, for example, from the European Parliament' s Discharge Decision 2013 for the EBA of 29.04.2015, P8_TA(2015)0138, No. 24.

respect the mandate attributed by the Union legislator and (...) not seek to set standards in areas where legislative processes are still pending".[214]

Only at the end of 2015 did the EP once again make itself clear when it called on the ESAs "to adopt a careful approach to the extent and number of guidelines, particularly where they are not explicitly empowered in the basic act."[215]

2.3.2 In Germany

The comply-or-explain mechanism in the guidelines provides for a decision to be made by the national authorities as to whether or not to comply with the ESA guidelines. The ability to exert political influence at national level therefore has less to do with the content of the guideline than with the question of (non-)compliance.

On 18 February 2016, the Bundestag adopted a resolution calling on the Federal Government to work towards ensuring adequate scrutiny of the ESAs at EU level.[216] Increased transparency of BaFin's involvement in the ESAs will give the Bundestag a better understanding of BaFin's work.[217] This is primarily relevant to the ESAs' Level 3 work (and therefore that of BaFin). In the case of Level 3 measures which do not correspond to the Bundestag's objectives "BaFin should be requested not to implement them and to say, at European level, that this is not possible in Germany".[218]

The political will of the Bundestag is made even clearer in the report by Bundestag Members Radwan and Zöllmer on the act to transpose the Deposit Guarantee Directive 2014/49/EU.[219] BaFin "is requested to refrain from applying" guidelines to assess the contributions to deposit guarantee schemes insofar as they fail to conform to the perceptions of the coalition parties. "Where, contrary to this request, BaFin nevertheless wants to apply the guidelines, it must submit its reasons to the Finance Committee of the German Bundestag".[220]

In both cases, the Bundestag expresses complete self-confidence and indicates a certain desire to be involved in BaFin's decision on whether to "comply". There is no express statement, however, on whether the Bundestag (or the Finance Committee itself) or the Federal Ministry of Finance (BMF) will "request" BaFin to comply with a guideline. Admittedly, a direct request by the Bundestag would not automatically comply with the BMF's principles on legal and technical supervision of BaFin.[221] BaFin is subject to legal and technical supervision by the Ministry[222] which bears political

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214 European Parliament's Discharge report 2014 for the EBA of 28.04.2016, P8_TA-PROV(2026)0167

215 Balz Report of the EP on "EU Financial Services Regulation", PE564.921, of 9.12.2015, No. 54

216 Plenary discussion on 18/7539 of 18.02.2016, vote on the motion and adoption in 15273 A.

217 Motion proposed by the CDU/CSU, parliamentary report no. 18/7539, No.6 and 11

218 Thus Bundestag Member Radwan (CSU) during the plenary discussion about 18/7539 of 18.02.2016 in 15266 B, C.

219 Parliamentary report no. 18/4451 Section V; thus also Radwan in the plenary discussion of 26.03.2015 on the act to transpose the Deposit Guarantee Directive 2014/49/EU.

220 Parliamentary report no. 18/4451 Section V.

221 Principles governing the exercise of legal and technical supervision of BaFin by the BMF, https://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Aufsichtsrecht/Satzung/aufsicht_bmf_bafin_en.html last accessed on 28.07.2016.

responsibility for BaFin's work. The subject matter of supervision is the legality and practicality of BaFin's administrative actions.[223] According to the principles governing the exercise of legal and technical supervision of BaFin by the BMF, the BMF is responsible for answering queries from the parliamentary arena *about ongoing legislative projects*. BaFin itself can only answer queries *on existing supervisory rules*.[224] Since the proposal by the governing parties is aimed at the ex-ante scrutiny of BaFin's decision on compliance with guidelines, a supervisory regulation has not quite come into existence and thus the legislative proceedings are still just about ongoing. Thus there is nothing to prevent the Bundestag from addressing a query to the Ministry which holds a position decided on in consultation with BaFin. A parliamentary question addressed to BaFin representatives would currently constitute uncharted waters as regards legal and technical supervision by the BMF.

2.3.3 Conclusion

The ESA Regulations do not provide for political scrutiny of ESA guidelines at EU level. The European Parliament has, however, repeatedly expressed its unease at the scale and number of guidelines. In Germany, the Bundestag will request BaFin to refrain from implementing guidelines which do not correspond with the desired political objectives.

2.4 Judicial Scrutiny at Level 3

2.4.1 Proceedings before the ECJ

Guidelines and recommendations are not legally binding. They cannot therefore be subject to an action for annulment before the ECJ under Art. 263 TFEU due their lack of legal force vis à vis third parties.

Guidelines have however assumed de facto binding force. Some attempt has been made to remove this contradiction by allowing such an action for annulment (under certain circumstances). Thus it is argued that guidelines may "actually give rise to noticeable de facto disadvantages" so that, as a result of the principle of effective judicial protection, possibilities for redress against "soft measures" could be necessary.[225] Therefore "affected parties should be entitled to appropriate redress via the action for annulment under Art. 263 (4) TFEU".[226] It is also argued that "[the] de facto binding force [of guidelines] as well as the impact which they have beyond the individual case and their (intended) legal consequences for third parties, brings [them] significantly closer to sub-statutory standards which apply as "regulatory acts", and therefore an action for annulment under

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222 S. 2 FinDAG; Principles governing the exercise of legal and technical supervision of BaFin by the BMF, https://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Aufsichtsrecht/Satzung/aufsicht_bmf_bafin_en.html last accessed on 28.07.2016.

223 Section I, para. 2 of the Principles governing the exercise of legal and technical supervision of BaFin by the BMF, https://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Aufsichtsrecht/Satzung/aufsicht_bmf_bafin_en.html last accessed on 28.07.2016.

224 IV. No. 6 (1) and (2) of the Principles governing the exercise of legal and technical supervision of BaFin by the BMF, https://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Aufsichtsrecht/Satzung/aufsicht_bmf_bafin_en.html last accessed on 28.07.2016.

225 Sonder, Rechtsschutz gegen Maßnahmen der neuen Finanzaufsichtsagenturen, BKR 2012, p. 8 (11).

226 Ibid.

Art. 263 TFEU could be brought.[227] Financial institutions would thus be entitled to bring an action under Art. 263 (4) para. 3 TFEU against guidelines addressed directly to them, but not against guidelines addressed to the competent authorities, because in such cases, national implementing acts are required.[228]

This approach is however contradicted by the words "legal effects vis-à-vis third parties" in Art. 263 (1) sentence 2 TFEU.[229] In addition, although the last treaty amendment, brought in by the Lisbon Treaty, extended individual redress by way of the action for annulment,[230] the requirement of legal force vis à vis third parties in Art. 263 (1) sentence 1 TFEU was retained and also applied to the new basis of an action "acts of bodies, offices or agencies of the Union" in sentence 2. Even if financial institutions feel this result to be "unsatisfactory" due to the "noticeable de facto disadvantages", a right of action can only be created by way of a treaty amendment.[231]

2.4.2 Proceedings in national courts

Even if guidelines and recommendations do not have legal force vis à vis third parties, they apply indirectly to financial institutions/financial market players as a result of the decisions of the competent national authorities for which they form a basis.

Claimants against these decisions have recourse to the national administrative courts.[232] In Germany, these decisions are not generally binding administrative acts which rules out any right of appeal under Section 42 (1) para. 1 VwGO. They are usually adopted as BaFin circulars with no formally binding force vis à vis the financial institutions/financial marker players. The question therefore arises as to whether it is in fact possible to claim at national level. Some argue that there is, in such cases, a right to bring an action for a declaratory judgement under Section 43 VwGO.[233] In practice, such actions appear to be rare.[234]

Where an action is admissible, a guideline which forms the basis of a decision by the competent authority may form the subject matter of a preliminary ruling procedure in the ECJ under Art. 267 TFEU, if a national court considers a ruling by the ECJ to be necessary to enable it to give judgement.[235]

Admissible questions are, firstly, questions, which are relevant to the issue, on the interpretation of the treaties (primary law) and of acts by the institutions, bodies, offices or agencies of the Union (secondary and tertiary law).[236] Secondly, questions, which are relevant to the issue, relating to the

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227 Michel, Institutionelles Gleichgewicht und EU-Agenturen, Duncker & Humblot GmbH, Berlin 2015, p. 278.

228 Ibid, p. 278 et seq.

229 Cf. Manger-Nestler, in: Grieser/Heemann, Europäisches Bankaufsichtsrecht, Frankfurt School Verlag GmbH, Frankfurt am Main 2016, p. 184.

230 Schwarze, in: Schwarze, EU-Kommentar, 3rd Edn., Nomos Verlagsgesellschaft mbH & Co. KG, Baden-Baden 2012, Art. 263 TFEU, para. 5.

231 Manger-Nestler, in: Grieser/Heemann, Europäisches Bankaufsichtsrecht, Frankfurt School Verlag GmbH, Frankfurt am Main 2016, p. 184.

232 Cf. Lehmann/Manger-Nestler, EuZW 2010, 87 (91).

233 Michael, Rechts- und Außenwirkung sowie richterliche Kontrolle der MaRisk VA, VersR 2010, 141 (148).

234 Cf. Schäfer, in: Boos/ Fischer/Schulte-Mattler, Kreditwesengesetz, 4. Edn., C.H. Beck Verlag, München 2012, § 6 para. 25.

235 Art. 267 (2) TFEU.

236 Art. 267 (1) (a) and (b) TFEU.

validity of secondary and tertiary law, may also form the subject matter of a preliminary ruling procedure.[237]

National courts "against whose decisions there is no judicial remedy under national law" are obliged to submit the matter to the ECJ if they consider that a decision on the matter is necessary.[238] According to ECJ case law, such courts of last instance are not simply those which constitute, in the abstract, the court of last instance in the national court structure but also those "against whose decisions there is no judicial remedy under national law" in the actual case in question.[239]

According to the treaty text, Courts which are not courts of last instance are only entitled and not obliged to submit a request for a preliminary ruling to the ECJ.[240] However, the ECJ ruled based on "[the] unity of [Union] legal order" that only the ECJ has the power to determine the invalidity of Union law.[241] National courts can however establish the validity of Union law because they are not thereby "calling into question the existence of the Community [measure]".[242] Exceptionally, therefore, courts of all instances are subject to an obligation to refer to the ECJ if they consider Union law to be invalid.[243] In questions regarding the interpretation of Union law, on the other hand, the obligation to refer to the ECJ remains reserved for the courts of last instance.

2.4.3 Conclusion

Financial institutions/financial market players cannot currently take judicial action against Level 3 guidelines and recommendations at EU level. Following a comply decision by the competent authority, they may, however, have recourse to national courts if and insofar as legal action is possible. In certain circumstances, the respective national court can or must then submit a legal question to the ECJ in the preliminary ruling procedure. In Germany, however, it seems that recourse to the courts is seldom possible.

3 Necessary additions to scrutiny mechanisms

3.1 Political Scrutiny at Level 2

3.1.1 Clear and consistent Level 1 mandate

The requirement, for effective and efficient political scrutiny of the Level 1 activities of the ESAs and the Commission by the European Parliament and Council of Ministers, is clarity with regard to the

237 Art. 267 (1) (b) TFEU.

238 Art. 267 (3) TFEU.

239 ECJ, Case No. C-99/00 of 4 June 2002, ECLI:EU:C:2002:329, Lyckeskog, para. 15.

240 Art. 267 (2) TFEU.

241 ECJ, Case No. C-314/85 of 22 October 1987, ECLI:EU:C:1987:452, Foto-Frost / Hauptzollamt Lübeck-Ost, para.15 et seq.

242 ECJ, Case No. C-314/85 of 22 October 1987, ECLI:EU:C:1987:452, Foto-Frost / Hauptzollamt Lübeck-Ost, para. 14.

243 ECJ, Case No. C-344/04 of 10 January 2006, ECLI:EU:C:2006:10, International Air Transport Association and Others / Department of Transport, para. 30; Wegener, in Calliess/Ruffert, EUV/AEUV, 5. Edn., Verlag C.H. Beck, München 2016, Art. 267 TFEU, para. 29; Ehricke, in: Streinz, EUV/AEUV, 2nd Edn., Verlag C.H. Beck, München 2012, Art. 267 TFEU, para. 45; Karpenstein, in: Grabitz/Hilf/Nettesheim, Das Recht der Europäischen Union, 58th Update, Verlag C.H. Beck, München 2016, Art. 267 TFEU, para. 62.

ESA mandate. Without such clarity on the part of the principals, the latter will subsequently find themselves unable to assess whether the agents are in fact respecting the mandate.

Sub-delegating the resolution of Level 1 political conflicts to the ESAs and Commission at Level 2, in particular, must be avoided without fail. In order to prevent damage to legislative institutions, Level 2 measures must never be anything other than technical in nature and must not be allowed to include strategic or political decisions. Parliament and the Council of Ministers should therefore - particularly during protracted trialogue negotiations - resist the temptation to seek the solution to intractable political differences by way of Level 2 clarifications.

Unclear mandates are also a double-edged sword from the ESAs' point of view. Although they allow the ESAs significant elbowroom, they can also give rise to political controversy, accompanied by allegations that the ESAs have exceeded their mandate. If the Commission subsequently has to amend a draft RTS, as a result of political pressure from Parliament or the Council, this will have a detrimental effect on the ESAs' reputation.

ESA representatives have repeatedly expressed their desire for greater involvement in Level 1 negotiations[244]. Such involvement, ideally *prior to* trialogue negotiations, could have advantages. ESA representatives could, at this early stage, already start work on formulating a mandate which would prevent errors and misunderstandings as well as unintended inconsistencies with other acts. This could involve consultative proceedings in which at least the participation of the EP negotiating team and the Council Presidency should be guaranteed.

There is no universally accepted solution to avoiding unclear mandates. It is however important that the legislator only adopts unclear mandates intentionally. Where the legislator *wishes* to allow the ESAs certain scope for discretion by way of an unclear mandate - for which there may be good reasons - he should be able to do so.

Recommendation 1 *(Principles 1 and 3)*

Political conflicts must be settled at Level 1. The European Parliament and the Council of Ministers should therefore resist the temptation to seek the solution to intractable political differences by way of Level 2 clarifications. It is advantageous for both the EU legislator and the ESAs to have mandates which are very clear as regards scope, content, purpose and objective. Consultations with ESAs at an early stage, in Parliament and the Council, promote a uniform understanding of the mandate, prevent the mandate from being exceeded and contribute to consistent regulation.

3.1.2 Council's ability to carry out scrutiny

The Council urgently needs to make organisational changes to ensure sufficient capability to carry out political scrutiny of Level 1 regulation by the ESAs. This does not currently appear to take place due to inadequate organisation.

[244] Thus Steven Maijoor in the ECON Scrutiny Slot of 28 January 2016.

The causes of this inadequacy - and thus the way to solve it - are varied and arise partly from the nature of the institution. Whereas the ECON Committee has a relatively small group of highly motivated individuals able to represent the whole committee and initiate a process of political scrutiny on an informal basis, this is not the case in the Council. A leading role - and thus also responsibility - on the part of just a few Member States (or even individuals) is not currently provided for in the Council With a large group of 28 Member States, it is often necessary to carry out time-consuming ballots.

Whilst the Council will probably never have the flexibility of the ECON Committee, it does have other advantages such as expert ministries with a large number of experts. Nor does the Council Secretariat appear to be ideally set up for taking on the Council's scrutiny role. Whereas the ECON Secretariat carries out important informational tasks and provides a certain amount of logistical support, the decision-making processes necessary to activate the Council Secretariat's (scarce) resources appear very lengthy.

Recommendation 2 *(Principles 1, 3 and 4)*

The Council's work structures are inadequate for providing sufficient political scrutiny of the Level 2 activities of the ESAs and the Commission. The Council should reflect on its strengths and develop structures which allow it to use these strengths for the scrutiny of RTS and draft RTS. The recommendations of the Financial Services Committee (FSC) should be implemented as rapidly as possible. Functioning structures in the Council are essential for overseeing compliance with the mandate, proportionality and regulatory consistence.

3.1.3 Delegate only where there is adequate scrutiny

The legislator should only delegate tasks to the ESAs and the Commission where it is capable of checking that these tasks are also in fact properly carried out. This is a massive task, especially in the (highly technical) field of financial market regulation where the amount of Level 2 regulation is huge.

It should also be borne in mind that RTS only make up a small part of the work delegated. Along with ITS and general delegated acts of the Commission, the EP and Council have a very large number of Level 2 measures to scrutinise. In light of this challenge, five additional measures are necessary which may increase the capability of the Council and EP to scrutinise Level 2 measures.

3.1.3.1 "Breathing space" between Level 1 and Level 2

Level 2 delegated acts define Level 1 legislation in more concrete terms and are frequently of huge importance for the businesses concerned. Planning the technical and organisational changes in the financial institutions concerned can often only be sensibly carried out with knowledge of the actual Level 2 measures. A "breathing space" between the entry into force of Level 2 measures and the application of the Level 1 Directive or Regulation is therefore desirable. In addition, this "breathing space" avoids the situation where the speedy application of a Directive or Regulation causes time pressure thereby impeding adequate scrutiny by Parliament and the Council of the delegated acts submitted (late) by the Commission.

Although the Level 1 text calls on the ESAs to submit draft regulatory standards by a specified date[245] this, whilst increasing the chances, does not provide a guarantee that the delegated acts will be adopted on time.

As events in the case of MiFID/MiFIR or PRIIPS have shown, such a "breathing space" can also be created "ex-post" by the Council and Parliament postponing, where necessary, the date of application of the Directive or Regulation. This, however is subject to the mandatory requirement of a legislative proposal from the EU Commission.

Alternatively, an "ex ante" requirement may be included in the Level 1 text to make the date of application of the Directive or Regulation dependent on the entry into force of the Level 2 delegated acts. For example, the Level 1 text could provide that those provisions of a Directive or Regulation which are to be defined in more concrete terms in a delegated act – and only those provisions – will not apply until 12 months after the entry into force of such delegated acts. Although this improves the negotiating position of Parliament and the Council, because a Commission proposal on postponement of the date of application of the Level 1 text is no longer necessary, in such a case there is a risk of the proposed legislation becoming fragmented. There is also a danger that political debates about the wording of the Level 1 text will be opened up because both the Council (with qualified majority) and Parliament (with absolute majority) can make their dates of application dependent on changes to the Level 1 text by threatening to challenge the delegated act.

Recommendation 3 *(Principle 3)*

Sufficient "breathing space" between the entry into force of Level 2 measures and the application of the Level 1 Directive or Regulation is desirable. It allows the Council and Parliament to adequately check the Commission's delegated acts and gives companies enough time to comply with the more detailed provisions. Ideally, this "breathing space" will be adopted ex ante - i.e. in the Level 1 measures - and the effective date of the Level 1 provisions will be dependent on entry into force of the delegated acts. Although, alternatively, an ex post postponement of the effective date of the Level 1 text is possible, it requires the Commission to submit a corresponding legislative proposal.

3.1.3.2 Cooperation between Council and EP

The Council and Parliament, as principals, commission the ESAs and Commission, as agents, to develop technical standards. Depending on the subject matter of regulation, the Council and Parliament hold different political positions which result in divergent ideas about the concrete design of technical standards. Often, however, there is a broad spectrum of opinion within the Council and the Parliament so that both institutions contain those holding similar opinions.

On that basis and in view of the fact that Council and Parliament have, as principals, a shared interest in scrutinising the agents (admittedly not always based on identical criteria), the Council

[245] Cf. e.g. Art. 12 (8) and (9) MiFID Directive 2014/65/EU.

and Parliament should consider whether they could increase their potential for Level 2 scrutiny by concerted action. Thus, on selected issues, for example, which are undisputed between the institutions, joint working groups could be set up or scrutiny coordinated. Such cooperation avoids the duplication of work and could have a positive impact, particularly on the ability to avoid disproportionate regulation. At the same time, it allows the Council and the Parliament to deploy their scant resources more effectively.

Recommendation 4 *(Principles 1 and 3)*

In view of the huge volume of Level 2 measures, the Council and the European Parliament should examine the possibility of collaborating on political scrutiny at Level 2. In particular, in the case of selected issues on which there is broad agreement between the two institutions, joint working groups could ensure efficient scrutiny of the ESAs and the Commission and ward off disproportionate regulatory conditions or prevent the ESAs and the Commission from exceeding their mandates. At the same time, the Council and the Parliament could deploy their scant resources more effectively.

3.1.3.3 Changes by the Commission

In Phase 2, the Commission can make changes to the draft RTS from the ESAs. An information system allowing the Commission to communicate to the Council at an early stage its intention to make such changes would significantly increase the capability of both institutions (but especially of the Council) to carry out scrutiny. The Level 2 procedure provides, with the ESAs on the one hand, and Commission on the other, for two agents. The Council and Parliament have to oversee the activities of both agents, not just those of the ESAs in phase 1. Consistent scrutiny applied only to the ESAs would be meaningless if the activities of the other agent, the Commission, were subsequently disregarded.

Information from the Commission on how it wants to change the results of the ESAs' work (which has ideally already been scrutinised by the Council and the EP) allows the Council and Parliament to concentrate their resources on these changes. This would be helpful, above all, for scrutinising the principles of proportionality and consistency. In addition, such information from the Commission would be useful regarding the question of whether the Council and EP has to challenge the Commission proposal within just one month or within three.[246]

Recommendation 5 *(Principles 3 and 4)*

The Commission should inform the Council and European Parliament, at an early stage, of modifications which it intends to make (or has made) to draft RTS from the ESAs. Such targeted information increases the likelihood of proportionate and consistent regulatory conditions at Level 2.

[246] As regards this question there are often differences of opinion between the Commission and the ECON Committee. The ECON Committee regularly uses even minor changes by the Commission as an opportunity to insist on an "objection period" of three months, whilst the Commission only envisages one month for this.

3.1.3.4 Reducing the hurdles to objections by the EP and the Council

The Commission passes the (amended) RTS proposals from the ESAs in the form of delegated acts. They are deemed to have been adopted provided that neither the Council (by way of qualified majority) nor the Parliament (by way of absolute majority) raises an objection.[247] In practice, these hurdles have proven to be very high and lowering them (e.g. to a simple majority in Parliament) appears to be out of the question.

The Council even assumes that the qualified majority under Art. 290 (2) TFEU is determined according to Art. 238 TFEU and thus a special majority of 72% (instead of 55%) of the Member States, representing at least 65% of the EU population, is necessary in the Council in order to revoke the delegation of power to adopt delegated acts or to pass an objection to a delegated act.

The background to the provision in Art. 238 TFEU is the fact that, in the case of Council Decisions without a proposal by the Commission, generally no preliminary examination has been carried out by an institution obliged to act in the interests of the EU.[248]

The situation is different for Level 2 Council Decisions. Firstly, the basis for the Level 2 act is the delegation of power in the Level 1 legislation. This was adopted on a proposal from the Commission so that at least there has been an examination of the delegation of power. Secondly, in the case of the adoption of delegated acts, since they are adopted by the Commission itself, the situation cannot arise whereby there is no institution involved that is obliged to act in the interests of the EU.

A clarification in the TFEU of the fact that a 55% majority of the Member States is sufficient for the qualified majority to revoke a delegation of power or pass an objection to a delegated act, is therefore desirable.

Recommendation 6 *(Principles 1, 3 and 4)*

The hurdles faced by the European Parliament and the Council when raising objections to the Commission's delegated acts (and therefore to RTS) are currently exceptionally high. A treaty amendment should make it clear that, in the Council, a qualified majority of 55% of the Member States is sufficient to revoke an empowerment or to raise an objection to a delegated act.

3.1.3.5 Bundling

In the context of the MiFID II/MiFIR framework, the Commission has bundled numerous delegations of power together. In the case of MiFIR, it adopted a delegated Regulation which

[247] Art. 290 (2) TFEU.

[248] Cf. Obwexer/Hummer, in: Streinz, EUV/AEUV, 2nd Edn., C.H. Beck Verlag, München 2012, Art. 238 TFEU, para. 5; Nettesheim/Grabitz/Hilf, in: Grabitz/Hilf/Nettesheim, Das Recht der Europäischen Union, 58th Update, C.H. Beck Verlag, München 2016, Art. 238 TFEU, para. 8; Schwarze, EU-Kommentar, 3rd Edn., Nomos Verlagsgesellschaft, Baden-Baden 2012, Art. 238 TFEU, para. 7.

bundled together 11 RTS.[249] In the case of MiFID II, it adopted a delegated Regulation in which it bundled together 19 RTS[250], and one delegated Directive in which it bundled together 2 RTS.[251] The Commission has also bundled measures together in the case of EMIR. In one case, it bundled together 17 RTS into one delegated Regulation[252] and 11 RTS into another.[253]

The Council and Parliament are critical of bundling. In a report by the ECON Committee, the MEPs call on the Commission "to fully unbundle both delegated and implementing acts and to avoid package approaches in order to allow for the timely adoption of those acts."[254] The Council, in the aforementioned FSC report, calls for the Commission to bundle Level 2 measures together only after active consultations with the Council.[255] This would create confidence and discourage subsequent rejection of the bundled acts.

Bundling certainly has its advantages. It allows the timing of several Level 2 measures to be coordinated so that they can come into effect simultaneously. This avoids the possibility of regulatory gaps or arbitrage. At the same time, bundling can contribute to consistency such as where concepts are defined centrally and then used with the identical meaning in several bundled RTS.

The criticism of bundling by the Parliament and Council relates to the question of whether it can object to the bundled delegated acts of the Commission only as a whole or separately. Thus the Council has long been of the opinion that it can also individually reject the Level 2 measures, which are bundled together into one delegated act, where there is no "objective justification" for the bundling.[256]

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249 Commission (2016): COMMISSION DELEGATED REGULATION (EU) …/... of 18.5.2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council with regard to definitions, transparency, portfolio compression and supervisory measures on product intervention and positions, C(2016) 2860 final, 18.5.2016.

250 Commission (2016): COMMISSION DELEGATED REGULATION (EU) …/... of 25.4.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive, C(2016) 2398 final, 25.4.2016

251 Commission (2016): COMMISSION DELEGATED DIRECTIVE (EU) .../… of 7.4.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits, C(2016) 2031 final, 7.4.2016.

252 COMMISSION DELEGATED REGULATION (EU) No 153/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on requirements for central counterparties.

253 COMMISSION DELEGATED REGULATION (EU) No 149/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards on indirect clearing arrangements, the clearing obligation, the public register, access to a trading venue, non-financial counterparties, and risk mitigation techniques for OTC derivatives contracts not cleared by a CCP.

254 European Parliament (2015): Balz Report on "Stocktaking and Challenges of the EU Financial Services Regulation: impact and the way forward towards a more efficient and effective EU framework for Financial Regulation and a Capital Markets Union" (2015/2106(INI)), Committee on Economic and Monetary Affairs, Rapporteur: Burkhard Balz, 9.12.2015,para. 50.

255 The Commission streamlines the Level 2 process by bundling the various Level 2 measures into one delegated act, for example because they relate to the same subject area.

256 Council of the EU (2015): FSC Report on Level 2 Processes- Endorsement, General Secretariat of the Council to Delegations, 1759/15, 23 June 2015, p. 13 et seq. In this regard, the Council refers to a report from its legal department (Doc. 8574/14) stating that "whenever a delegated act groups several empowerments of a basic act without any objective justification, the Council may regard that delegated act as a "bundle" of separate delegated acts and exercise accordingly its right to object in respect of each of them."

In fact, only being able to reject the entire bundled RTS package would probably weaken the ability of the Council and the EP to carry out scrutiny. Although bundling allows package solutions, i.e. the Council or EP can make their approval to one RTS dependent on changes being made to another, this only gives rise to increased influence if the implied threat to the agents, that RTS or delegated acts will be rejected where they are unsatisfactory, is a credible one. This is precisely what is debatable in the case of bundling however. Ultimately, bundling is likely to result in the Commission being able to extend its scope for action. Convincing arguments in favour are not in evidence. The coordinated timing and material consistency of the Level 2 measures can also be achieved with a right of rejection over each individual part of the bundled RTS. In any case, it should not be obtained at the cost of the democratic scrutiny of the ESAs and the Commission.

Recommendation 7 *(Principle 4)*

The bundling of several RTS by the Commission into a single delegated act should not reduce the ability of the European Parliament and the Council to exercise political scrutiny over the Level 2 activities of the ESAs and the Commission. They should therefore be in a position to reject individual RTS which have been bundled into a delegated act. This does not necessarily have a negative impact on the consistency of Level 2 legislation.

3.1.4 Permanently safeguard ability to scrutinise

The current scrutiny of Level 2 measures from the ESAs and the Commission is characterised, particularly in the European Parliament, by two features.

- The great importance of the commitment of just a few people for each regulatory dossier and
- the use of informal procedures

These two features are both the Parliament's strength and its weakness. Although the current constellation enables the available expertise in the Parliament to be brought together swiftly and used flexibly, in the medium term the following risks will have to be dealt with:

- Effective scrutiny of the Level 2 activities of the ESAs and Commission requires specialist knowledge which is concentrated among just a few MEPs (generally the negotiating team). It is necessary to ensure that this knowledge - and thus the Parliament's ability to effect scrutiny - is not lost when the MEPs are no longer represented in Parliament.
- Although the informal procedures make Parliament more flexible, they also make it more difficult to keep track of the process of scrutiny. Beyond the "scrutiny slots", there are no records of minutes, which makes it difficult or impossible for MEPS who are not directly involved, and the public, to follow the negotiations and the process of finding a compromises. It is therefore almost impossible to ascertain whether and to what extent packages are put together.

Greater transparency is therefore required, for example, of the meetings which take place between the MEPs or Council representatives, on the one hand, and the Commission and ESAs, on the other. Material documents or letters relating to such negotiations should also be made available ex

post.[257] At the very least, there should be a joint document register for all those involved in the scrutiny procedure, i.e. for the ESAs, Commission, Council of Ministers and European Parliament.

Recommendation 8 *(Principles 3 and 4)*

In order to maintain the ability of the European Parliament and the Council to carry out effective scrutiny of the Level 2 measures of the ESAs and the Commission, the very informal procedure which currently exists should be subject to a moderate level of formalisation. A joint register for the ESAs, Commission, Council of Ministers and Parliament would safeguard knowledge that is also necessary for future political scrutiny. In addition, greater transparency would increase the acceptance of the results of negotiations.

3.2 Judicial Scrutiny at Level 2

AT EU level, financial market players can bring an action for annulment against RTS and ITS under Art. 263 TFEU. Some argue that legal redress should also be possible with regard to draft RTS and ITS issued by the ESAs.[258] It is however settled case law of the ECJ[259] that EU acts can only be challenged "where they definitively lay down the position of the Union institution concerned". If we classify ESA drafts as similar to experts' reports, this approach would also run counter to the Olivieri Case[260] which states that acts whose purpose is to prepare for the final decision are not subject to judicial challenge.[261]

Apart from the rule that only legally binding measures should be open to challenge, there is a practical consideration which also militates against judicial scrutiny at such an early stage: When the ESA drafts are adopted, it is still not certain what changes the Commission will wish to make and what the content of the RTS and ITS will be when they are passed. Thus, in some circumstances, there would be an examination of provisions which had not yet become legally binding.

3.3 Political Scrutiny at Level 3

3.3.1 Barriers at EU Level

ESAs are currently subject to hardly any political limits when exercising their comprehensive power to adopt guidelines. Even without an explicit Level 1 mandate, the ESAs can develop such guidelines on their own initiative (cf. Section 2.1.3 on page 10). Although, officially, guidelines are non-binding, the very high level of compliance by national supervisory bodies means they have taken on much greater significance.

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[257] Cf. for example the recommendations of the European Ombudsman O'Reilly on increasing transparency in the trialogue procedure of 12/07/2016, Case OI/8/2015/JAS.

[258] Zeitler, Rechtsschutzlücken schließen, Profil – Das bayerische Genossenschaftsblatt, 1.2016, p. 28 (29).

[259] Dörr, in: Grabitz/Hilf/Nettesheim, Das Recht der Europäischen Union, 58th Update, Verlag C.H. Beck, München 2016, Art. 263 AEUV, para. 39:

[260] ECJ, Case No. T-326/99 of 18 December 2003, ECLI:EU:T:2003:351, Olivieri/KOM, para. 51 et seq.

[261] Michel, Institutionelles Gleichgewicht und EU-Agenturen, Duncker & Humblot, Berlin 2015, p. 275.

The criticism of guidelines is varied and not quite free of (legitimate) self-interest. The character of the guidelines is unique in that they (and their counterparts at national level), on the one hand enable supervisors to react swiftly and flexibly with a quasi-binding instrument to define unclear legal provisions. On the other hand, however, they should not evade Level 1 or Level 2 decisions by, for example, exceeding a level of regulation for which there is political consensus at Level 1 or by going so far as to contradict Level 1 decisions. In this context, the European Parliament's criticism is understandable. The criticism gains additional weight as a result of the generally high level of compliance with guidelines[262] which casts doubt on the idea that there is a culture of non-compliance with politically undesirable guidelines among national supervisors.

Below we set out two options which may prevent ESAs from overstepping their powers regarding guidelines, at EU level. Both options increase the likelihood that guidelines will be compatible with the Principle of Subsidiarity. However, since they do not provide for explicit substantive scrutiny at EU level, they are largely irrelevant for the principles of proportionality and regulatory consistency.

- *Option 1: Barrier to the mandate*

The EU legislator can amend ESA Regulations to the effect that ESAs are only able to adopt guidelines once an explicit Level 1 mandate has been issued. The legislator thereby obtains direct control over the number and scope of guidelines. The pressure to implement guidelines which arise in this way will grow as a result.

- *Option 2: Barrier to exercising the mandate*

The EU legislator can incorporate a barrier to exercising the mandate into the ESA Regulations. Thereunder, the ESAs could only pursue their plans to develop a specific guideline provided the Council or European Parliament did not object within a specific time limit (e.g. 3 months). In this regard, the ESAs should prove that the guideline has a connection to EU law, does not pre-empt regulatory proposals and is compatible with the legislator's political objectives. In this way, the legislators could exercise political scrutiny whilst the supervisory authorities are basically still able to react swiftly and consistently to close supervisory or regulatory gaps.[263]

Option 2, unlike Option 1, has the advantage that the supervisory authorities will still be able to react quickly to ambiguities by issuing guidelines.

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[262] They are not sufficient proof of this. It is also theoretically possible that the ESAs only develop those guidelines for which there is acceptance among virtually all supervisors.

[263] It cannot be ruled out that the repetition factor will allow the Council and Parliament to turn these participation rights into material influence. Thus the Council and/or EP could threaten to make their approval to ESA proposals for future guidelines dependent on the ESA guidelines corresponding with the ideas of the EP and/or Council. A better channel for material involvement would be participation by the Council and/or EP in the ESAs' public consultations on the guidelines. Initial efforts in this direction are apparent in the EP in that guidelines have become the subject of ECON scrutiny slots.

Recommendation 9 (Principle 2)

The ESAs should only be able to pursue plans to develop guidelines where the Council and the Parliament raise no objections (barrier to exercising the mandate). This increases the likelihood that guidelines will be compatible with the Principle of Subsidiarity.

3.3.2 Control of implementation at national level

Due to their unique character, restraint is advisable at the national political level when it comes to designing European guidelines. A certain amount of political scrutiny is however perfectly legitimate where it relates to whether a guideline passed at EU level must also be followed at national level (and is thus de facto binding). The efforts of the German Bundestag in this direction are therefore to be welcomed.

Such national political scrutiny may take place, depending on the national legal system, at parliamentary level and/or the level of the competent ministry. It may help to ensure that guidelines which have become binding de facto - as a consequence of national compliance - do not obviously offend against the national political will In addition, it may supplement the monitoring of regulatory proportionality and consistency.

Above all, the prospect of such political scrutiny is likely to encourage greater discipline on the part of the ESAs. Both the ESAs and national supervisors are likely to regard any rejection of their guidelines at national level due to political pressure, as damaging to their reputation. This will probably have an impact on the development of the guidelines. The challenge will be to allow national supervisors the necessary scope to carry out their work whilst at the same time preventing serious political differences.

Recommendation 10 *(Principles 3 and 4)*

At national level, political scrutiny - by Parliament or the responsible ministry - of whether EU guidelines should in fact be complied with, is perfectly legitimate. This scrutiny should provide national supervisors with the necessary room for manoeuvre but at the same time prevent guidelines from offending against the national political will. This scrutiny can also be helpful for overseeing the proportionality and consistency of legislation. In Germany, the increased transparency, demanded by the Bundestag, regarding BaFin's Level 3-collaboration with the ESAs, requires a continuous flow of information between the Finance Committee, Federal Finance Ministry and BaFin.

3.4 Judicial Scrutiny at Level 3

Up to now, it has been much more difficult to obtain redress in the case of ESA guidelines than in the case of RTS and ITS in the form of delegated acts; an action for annulment under Art. 263 TFEU is ruled out since officially guidelines are non-binding. Some people therefore want to introduce an

"examination procedure" for guidelines.[264] Judicial examination of guidelines at EU level may be introduced by an amendment to the EU Treaties. One possible route would be to extend the causes of action for an action for annulment.

In return, however, the comply-or-explain procedure for guidelines should then have to be abolished because, firstly, it is the only way to comply with the case law of the ECJ [265] which states that only the definitive version of an act can be challenged. Secondly, it is the only way to avoid the judicial scrutiny of guidelines which a competent national authority would not even have adopted. This solution would, however, have the disadvantage that the competent national authorities could also no longer reject guidelines which, although lawful, are not tailored to the respective national situation.

Alternatively, one could consider extending redress against BaFin circulars, and thereby incidentally against ESA guidelines, at the level of the Member States; in Germany, for example, by way of a declaratory action under Section 43 VwGO. This would have the major advantage that the comply-or-explain procedure could remain in place and the competent national authorities could thus continue to differentiate between guidelines that are suitable and those that are less suitable for their Member States.

[264] Zeitler, Rechtsschutzlücken schließen, Profil – Das bayerische Genossenschaftsblatt, 1.2016, p. 28 (29).

[265] Dörr, in: Grabitz/Hilf/Nettesheim, Das Recht der Europäischen Union, 58th Update, Verlag C.H. Beck, München 2016, Art. 263 TFEU, para. 39.

3.5 Summary of Recommendations

	Limits of the Mandate		Subsidiarity		Proportionality		Consistency	
	Level 2	Level 3	Level 2	Level 3	Level 2	Level 3	Level 2	Level 3
Recommendation 1	X						X	
Recommendation 2	X				X		X	
Recommendation 3			X					
Recommendation 4	X				X			
Recommendation 5					X		X	
Recommendation 6	X				X		X	
Recommendation 7							X	
Recommendation 8					X		X	
Recommendation 9				X				
Recommendation 10						X		X