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'BENDING TO UNIFORMITY': EU FINANCIAL REGULATION WITH AND WITHOUT THE UK

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ABSTRACT

This article considers how the United Kingdom has shaped EU financial regulation. It suggests that the United Kingdom might best be described as the 'grit in the oyster' – an occasionally irritating presence, which has prompted the production of a harmonized regulatory system which, to a workable extent, serves the needs of the EU's integrated financial system. It also speculates as to how EU financial regulation is likely to develop without the United Kingdom. It concludes that, while prediction is a fraught exercise, the European Union can be expected to bend ever more sharply towards uniformity with respect to regulatory governance for the single market. The United Kingdom is likely to leave a moderating legacy, however, in the form of an embedded institutional commitment to proportionality and to evidence-based regulatory design. It is more difficult to predict how the EU's regulatory governance in relation to the international market is likely to evolve. Here, geo-politics and international trade relations are likely to be determinative.

I. INTRODUCTION

On March 29, 2017, the United Kingdom, under Article 50 of the Treaty on European Union, notified the European Council of its intention to leave the European Union.[1] On April 29th, negotiating guidelines were issued by European Council; these guidelines set the EU's position for the negotiations, which are being led by the European Commission, through the chief EU negotiator, Michel Barnier.[2] After months of speculation as to possible outcomes, the negotiation process, which started formally on June 19, 2017, is underway. The nature of the UK/EU settlement governing financial services (assuming one is agreed) can be expected to form a significant part of the discussions. The scale of the interdependencies between the EU and UK financial systems means that workable access arrangements are a concern to both parties, even if the distinct incentives and preferences of the European Union and United

1. *See* Letter from UK Prime Minister May to European Council President Tusk (Mar. 29, 2017) [hereinafter Article 50 Letter], https://www.gov.uk/government/publications/prime-ministers-letter-to-donald-tusk-triggering-article-50.

2. *See* European Council (Art. 50) Guidelines for Brexit Negotiations, COUNCIL OF THE EUROPEAN UNION, Press Release 220/17 (Apr. 29, 2017) [hereinafter Guidelines for Brexit Negotiations], http://www.consilium.europa.eu/en/press/press-releases/2017/04/29-euco-brexit-guidelines/.

Kingdom are asymmetric.[3] UK Prime Minister Theresa May's formal letter of notification specifically notes financial services, proposing that financial services market access be dealt with in a Free Trade Agreement and alluding to the two potentially intractable issues that financial services access raises: how to manage future regulatory divergence between the European Union and United Kingdom so that a stable form of market access and related mutual recognition of standards can be designed; and how to deal with dispute resolution, given the UK's insistence on avoiding the jurisdiction of the Court of Justice of the European Union.[4] Notably, the European Council guidelines are silent on this issue. However, there are signs of disagreement to come in that, although the guidelines indicate a readiness to finalize and conclude a Free Trade Agreement once the United Kingdom is no longer an EU Member State, they also note that any future partnership must include appropriate enforcement and dispute resolution settlement mechanisms that do not affect the EU's autonomy or, in particular, its decision-making procedures, and should safeguard financial stability in the Union and respect its regulatory and supervisory regime and standards and their application.[5]

The Brexit negotiations and the management of the implications of Brexit can be expected to dominate UK policy and political discourse and to consume the machinery of the UK government over the next two years and beyond. Domestically, a Reform Act will be deployed to ensure most of EU law, including EU financial regulation, continues to operate in the United Kingdom on the UK's withdrawal to avoid the gaping regulatory holes that would otherwise yawn in UK public law and regulation:[6] administrative law in the United Kingdom has in many respects become a function of EU law and is often administered through EU agencies. Much of UK financial

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3. On the distinct issues raised by financial services access, see John Armour, *Brexit and Financial Services*, 33 OX. REV. ECON. POL. S54 (2017); Niamh Moloney, *The EU and its Investment Banker: Rethinking Equivalence for the EU Capital Market*, LSE Law Society and Economy Working Paper Series, WP No 5/2017 (2017), *available at* https://ssrn.com/abstract=2929229; Eilis Ferran, *The UK as a Third Country in EU Financial Services Regulation*, J. FINANC. REGUL. 40 (2017).

4. *See* Article 50 Letter, *supra* note 1, at 5.

5. Guidelines for Brexit Negotations, *supra* note 2, ¶¶ 21 & 23.

6. The Reform Bill was published on July 13, 2017. *See* European Union (Withdrawal) Bill (HC Bill 5), *available at* https://publications.parliament.uk/pa/bills/cbill/2017-2019/0005/18005.pdf.

regulation derives from directly applicable EU regulations, which will fall away when the United Kingdom leaves the European Union.

The negotiations also provide a point for reflection, to ponder the question posed by this symposium: how has EU financial regulation developed with the United Kingdom and how will EU financial regulation develop without the United Kingdom?

The first part of this question, which represents the major part of this article, can be answered with a reasonable degree of confidence given the empirical evidence. The United Kingdom might best be described as the 'grit in the oyster' – an at times irritating presence which has nonetheless prompted the production of a pearl or, and perhaps stretching the metaphor too far, a regulatory system which, to a workable extent, serves the needs of the EU's integrated financial system, makes some effort to be evidence-based, and preserves a degree of national regulatory autonomy and potential for productive experimentation. In reaching this conclusion the discussion draws on the comparative political economy literature, which considers the different preferences which have shaped EU financial regulation, and on empirical observation of the UK's negotiating positions.

A satisfactory answer to the second part of the question is more elusive as it requires prediction. EU financial regulation now takes the form of a sophisticated pan-EU governance system with regulatory, supervisory, rescue/resolution, and enforcement components. This governance system is supported by a fragile but thus far resilient institutional eco-system, within which the interlocking single market (the European System of Financial Supervision) and euro area (Banking Union) institutional mechanisms uneasily co-exist. The absence of the United Kingdom will be felt across all the component elements of EU financial governance, and across the single market and euro area. This discussion narrows the wide field of inquiry by focusing on regulatory governance[7] and by considering two spheres of EU financial regulatory competence: the single market (internal); and the international market (external). Single market regulatory governance is not given the array of factors which shape EU financial

7. This article does not accordingly consider supervision or enforcement or the impact of the UK's departure on the institutional structures of EU financial governance, notably Banking Union (euro area) and the European System of Financial Supervision (single market). For an examination of the potential consequences for institutional organization, see generally Niamh Moloney, *Brexit and EU Financial Governance: Business as Usual or Institutional Change*, 42 EUR. L. REV. 112 (2017).

regulatory governance, likely to experience material Brexit-related change, but it can be expected to bend more to uniformity. In her major speech on the UK's negotiating strategy on January 17, 2017 Prime Minister May suggested that 'the EU bends towards uniformity, not flexibility.'[8] In the absence of the United Kingdom, EU financial regulation is likely to become more, and not less, harmonized. But UK legacy effects, primarily in the form of a commitment towards proportionality, should moderate the risks of EU financial regulation becoming overly standardized and insufficiently calibrated to distinct market segments. The impact of the withdrawal of the United Kingdom on the EU's approach to the international financial market is difficult to predict given the relevance of geo-politics. But a need to signal the openness of the EU financial market post Brexit can be expected to have some traction on how the EU's international posture develops.

II. SINGLE MARKET REGULATION: THE UNITED KINGDOM AND THE EUROPEAN UNION - THE ODD COUPLE?

A. The UK and EU Financial Regulation: Multiple Channels for Influencing

EU financial regulation is a highly contested sphere of EU competence. It seeks to do two things: to support the construction of an integrated, single financial system with minimal regulatory frictions;[9] and to regulate that financial system so that the pathologies of integration, notably cross-border risk transmission and financial instability, are minimized and managed. Markets are regulated and risks are managed by means of a granular, harmonized 'single rulebook,' which has highly detailed legislative, administrative, and

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8. Prime Minister Theresa May, The Government's Negotiating Objectives for Exiting the EU: PM Speech (Jan. 17, 2017), https://www.gov.uk/government/speeches/the-governments-negotiating-objectives-for-exiting-the-eu-pm-speech.

9. The ECB has described a financial market for a given set of instruments/services as fully integrated if all potential market participants with the same relevant characteristics: face a single set of rules when they decide to deal with those financial instruments/services; have equal access to such instruments/services; and are treated equally when they are active in the market. *See* European Central Bank, Financial Integration in Europe (Apr. 2016), at 4, *available at* https://www.ecb.europa.eu/pub/pdf/other/financialintegrationineurope201604.en.pdf.

soft law components.[10] Market construction is supported by means of the related regulatory 'passport,' which allows regulated financial actors to operate cross-border in the European Union on the basis of authorization and supervision in their 'home' Member State – typically the Member State in which the financial actor is registered.[11] 'Host' Member States can defer to authorization and supervision by home Member States, and accept the risks associated with cross-border financial activity, because of the harmonized single rulebook under which home supervisors must operate.[12] The regulatory and market construction functions that the single rulebook performs have a relatively straightforward and appealing logic, but the single rulebook has been forged in a crucible in which an array of competing preferences, including those of the United Kingdom, have fought for dominance.

The dense and ever-expanding nature of the single rulebook, and the organization of the EU law-making process, mean that it is possible to trace the UK's preferences and their influence on EU financial regulation – at least at the legislative level. The macro design of EU financial regulation follows the 'Lamfalussy model,' which imposes a hierarchy of norms approach. It segments financial regulation into: level 1 legislative rules; level 2 administrative rules; level 3 soft law and supervisory convergence measures; and level 4 enforcement of Member State compliance by the Commission.[13] The intergovernmental ECOFIN Council, in which the EU Member States are represented through their finance ministers, adopts level 1 legislation in the financial governance area, under a qualified majority vote (QMV),[14] with the supranational European Parliament

10. Supervisory and enforcement techniques and related institutional structures also support market construction and risk management but are not considered in this discussion.

11. On the nature and purpose of EU financial regulation, see generally EUROPEAN CAPITAL MARKETS LAW (Rudiger Veil ed., Hart, 2d. ed. 2017); Niamh Moloney, EU SECURITIES AND FINANCIAL MARKETS REGULATION (3d ed. 2014).

12. Host supervisors are also supported by the supervisory communication, coordination, and convergence arrangements, which apply within the European System of Financial Supervision.

13. The Lamfalussy approach was adopted by the European Union in 2001 as a means for expediting the law-making process in the financial regulation area (which was then receiving serious policy and political attention for the first time) and was refined over the crisis era. *See* Moloney, *supra* note 11, at 862-86.

14. A QMV is fifty-five percent of the currently twenty-eight Council members, comprising at least fifteen of them, and representing Member States comprising at least sixty-five percent of the EU population. A blocking minority for a measure must include at least four Council members, absent which the QMV is deemed to be attained. *See* Consolidated

(composed of directly elected representatives) as a 'co-legislator.'[15] The European Commission, the EU's supranational executive and bureaucracy, proposes legislation. This discussion focuses on the UK's direct political influence on EU financial regulation as a Member State in the ECOFIN Council. There are numerous other channels through which UK influence on legislation has been exerted, including the European Parliament.[16] The highly organized and well-resourced City of London lobbying groups have also, through a range of different portals, including through the Commission and European Parliament, shaped EU financial regulation, although the nature of this influence is more difficult to track.[17]

One of the major channels for influence is technocratic rather than overtly political and relates to the massive and fast-growing corpus of level 2 administrative law, which forms part of the single rulebook. The United Kingdom is a member of the three European Supervisory Authorities (the European Banking Authority (EBA); the European Insurance and Occupational Pensions Authority (EIOPA); and the European Securities and Markets Authority (ESMA)), which are charged with an array of quasi-regulatory and supervisory functions in relation to the single market in financial services. UK regulators (the Prudential Regulation Authority/Bank of England and Financial Conduct Authority) sit on the Boards of Supervisors of the European Supervisory Authorities (ESAs), which are composed of

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Version of the Treaty on European Union art. 16, 2012 O.J. C 362/13, at 4 [hereinafter TEU post-Lisbon].

15. Financial regulation is adopted under the multi-stage ordinary legislative procedure under which the Council and Parliament act as co-legislators in that each holds a veto. *See* Consolidated Version of the Treaty on the Functioning of the European Union art. 294, 2012 O.J. C 326/47, at 174 [hereinafter TFEU]. In practice, compromise positions are usually achieved under the informal 'fast track' process under which closed 'trilogue' negotiations, held between the Commission, Parliament and Council once the Parliament and Council have adopted negotiating positions, produce the legislative outcome. *See* Moloney, *supra* note 11, at 890.

16. Parliamentary channels include the UK MEPs on the influential European Parliament Economic and Monetary Affairs (ECON) Committee, which deals with financial governance. The UK's engagement through the European Parliament has been identified as being less effective than its engagement in other EU fora, given in part the diffusion of UK MEPs across different European Parliament political groupings. *See* Norton Rose Fulbright, SHAPING LEGISLATION: UK ENGAGEMENT IN EU FINANCIAL SERVICES POLICY-MAKING (2016).

17. It has been reported that the UK finance lobby spends over EU€34 million annually in seeking to influence EU financial regulation. *See Lobbying for the City of London: The Fire Power of the UK Financial Sector in Brussels*, CORPORATE EUROPE OBSERVATORY (2016), https://corporateeurope.org/sites/default/files/ukfinancialfirepower.pdf.

national supervisors from the EU 28 Member States and which act as the ESAs' decision-making bodies. The ESAs do not have the power to adopt level 2 administrative rules (this power rests with the Commission), but they propose administrative rules to the Commission (based on mandates contained in legislation) and advise the Commission on their content; the ESAs also adopt soft law (level 3 under the Lamfalussy model).[18] Since the establishment of the ESAs in 2011 as part of the EU's crisis-era financial governance reforms, and the related enhancement of the EU's technical capacity to adopt detailed administrative rules, EU financial regulation has become significantly more granular and administrative in nature. The ESAs have accordingly become a location for the imposition of national preferences.

The political/national influences on ESA decision-making can be difficult to track as the Boards of Supervisors, while often attuned to national rather than supranational/EU preferences,[19] tend to operate by consensus, and formal votes (ESA quasi-regulatory decision-making operates under a qualified majority vote) are relatively rare. It is nonetheless possible to conclude from the public record of Board of Supervisor decision-making[20] that the United Kingdom has been a significant influence on ESA deliberations. This influence flows from its strong technical capacity and its long experience in regulating the EU's largest financial market, as well as its support of the ESAs by means of secondments from UK regulators and its involvement in the different technical working groups through which the ESAs operate. The United Kingdom has not always been able to impose its preferences, mirroring the experience in the ECOFIN Council (discussed below). The United Kingdom was, for example, part of a minority coalition of regulators on EBA, which did not support EBA's approach to the adoption of guidelines, which would have required a restrictive approach to the EU rules that govern executive

18. On the ESAs' quasi-regulatory powers in relation to administrative rule-making and soft law, see Moloney, *supra* note 11, at 907-35; Madalina Busuioc, *Rule-Making by the European Financial Supervisory Authorities: Walking a Tight Rope*, 19 EUR. L.J. 111 (2013).

19. A frequent criticism of ESA Board of Supervisor decision-making is that it is not sufficiently supranational/EU in orientation. *See generally* Commission Public Consultation on the Operations of the European Supervisory Authorities (2017) [hereinafter Commission ESA Public Consultation].

20. Through the publicly available minutes of the three Boards of Supervisors, available on the websites of the three ESAs, http://www.eba.europa.eu/, https://www.esma.europa.eu/, https://eiopa.europa.eu/.

remuneration in banks.[21] Similarly, the United Kingdom, along with a minority group of Member State regulators, did not support guidelines which ESMA adopted in relation to short selling,[22] reflecting its distinct interests in supporting liquidity in the UK's globally-oriented trading market. Overall, it has been a key technical support to the ESAs since 2011.

B. The UK and EU Financial Regulation: Politics and Preferences

The focus of this discussion, however, is on primary level 1 legislation and on the UK's direct influence on ECOFIN Council discussions.

The Member States who, in the ECOFIN Council, adopt level 1 EU financial regulation along with the European Parliament, have long had different preferences in this area. Despite a longstanding EU policy commitment to diversify sources of funding in the EU away from the dominant bank channel,[23] patterns of financial system development still vary significantly across the European Union. Regular reviews from the European Commission and the ECB repeatedly report on, for example, diverging levels of recourse by firms across the European Union to market-based instruments for raising funds; uneven securitization patterns (an indicator for the extent to which market-based intermediation[24] is used to diversify bank funding risks); and different levels of penetration of bank-based

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21. *See* PRA and FCA statement on compliance with the EBA Guidelines on Sound Remuneration Policies, FINANCIAL CONDUCT AUTHORITY (Feb. 29, 2016) [hereinafter Statement on Compliance with EBA Remuneration Guidelines], https://www.fca.org.uk/news/statements/pra-and-fca-statement-compliance-eba-guidelines-sound-remuneration-policies.

22. *See* European Securities and Markets Authority, Guidelines Compliance Table (ESMA/2013/765) (June 19, 2013) [hereinafter ESMA Compliance Table], *available at* https://www.esma.europa.eu/sites/default/files/library/2015/11/2013-765_guidelines_compliance_table_-_market_making_guidelines.pdf.

23. This policy concern has been a decisive influence on EU financial governance policy. It has been expressed most recently in the current Capital Markets Union agenda. *See* Commission of the European Communities, Communication from the Commission to the European Parliament, The Council, The European Economic and Social Committee and the Committee of the Regions, Action Plan on Building a Capital Markets Union, COM (15) 468 Final (Sept. 2015).

24. Market intermediation refers to the process whereby actors in the financial markets 'intermediate' between suppliers and seekers of capital by, for example, providing risk management products and supporting trading in securities. On intermediation, see Moloney, *supra* note 11, at 320-25.

funding.[25] Overall, a move toward more market-based funding can be identified,[26] but the EU financial market does not have a homogeneous structure. Accordingly, distinct and typically longstanding underlying economic models and diverging patterns of financial system have shaped often sharply different national preferences[27] with respect to market construction and related financial regulation.[28] The form of capitalism which the European Union should follow; the style of regulation which should encourage or control it; the location of regulatory intervention (EU harmonization or local flexibility; euro area or single market); the extent to which related risks should be mutualized across the Member States through institutional structures - all been sharply contested politically.

The UK's distinct financial system has molded its preferences regarding EU financial regulation. Although funding to the UK domestic market remains heavily based on bank credit,[29] the United Kingdom, through the City of London, hosts the largest wholesale financial services market in the European Union, acting, in effect, as the investment banker to the EU 27. The importance of this function has been repeatedly highlighted in the current Brexit policy and political discourse in the United Kingdom, which has underlined the risks to the United Kingdom (and the European Union) if its access to the EU market is disrupted.[30] Some 37% of assets under management

25. *See, eg.*, Commission of the European Communities, Commission Staff Working Document, European Financial Stability and Integration Review (EFSIR): A focus on Capital Markets Union, SWD (16) 146 Final (Apr. 2016).

26. *See* the discussions of different Member State markets in MARKET-BASED BANKING AND THE INTERNATIONAL FINANCIAL CRISIS (Ian Hardie & David Howarth eds., 2013).

27. As the 'varieties of capitalism' literature predicts. For the foundational work, see generally VARIETIES OF CAPITALISM: THE INSTITUTIONAL FOUNDATIONS OF COMPARATIVE ADVANTAGE (Peter A. Hall & David Soskice eds., 2001).

28. For recent examples, see David Howarth & Lucia Quaglia, *Brexit and the Single European Financial Market*, 55 J. OF COMMON MKT. STUD. (2017), DOI: 10.1111/jcms.12589; David Howarth & Lucia Quaglia, *Internationalized Banking, Alternative Banks, and the Single Supervisory Mechanism*, 39 WEST EUR. POL. 438 (2016); Lucia Quaglia, David Howarth, & Moritz Liebe, *The Political Economy of European Capital Markets Union* 54 J. OF COMMON MKT. STUD. 185 (2016).

29. *See* Ian Hardie & Sylvia Maxfield, *Market-based Banking as the Worst of all Worlds: Illustrations from the United States and the United Kingdom* in Hardie & Howarth, *supra* note 26, at 56.

30. *See, e.g.*, EUROPEAN UNION COMMITTEE, REPORT, 2016-17, HL 81, ¶ 116 (UK) (noting the UK's large trade surplus with the EU in financial services and the reliance of the wider EU economy on services provided in the UK); Simeon Djankov, *The City of London After Brexit*, LSE Financial Markets Group Discussion Paper No. 762 (2017) (outlining the

in the European Union are managed in the United Kingdom[31] and around 85% of European hedge funds are based in London.[32] Some 46% of equity funding raised in the European Union is raised in the United Kingdom,[33] and some 74% of over-the-counter trading in interest rate derivatives and 78% of foreign exchange trading takes in place in London, while twice as many euros are traded in London as in the euro area.[34] Overall, around 25% of UK financial services revenue derives from EU international and wholesale financial services business[35] and some 35% of all wholesale financial services activity in the European Union takes place in the United Kingdom.[36]

The market orientation of the UK financial system has led to the United Kingdom usually forming part of what the comparative political economy literature has termed the facilitative 'market-making' as compared to the more prescriptive 'market-shaping' coalition in the Council.[37] Membership of these coalitions is fluid, depending on the issue at stake; Germany's position in particular can vary, although as a bank-based system it might be expected to form part of the market-shaping grouping. Broadly, the market-making coalition in the Council has typically advocated for a style of EU financial regulation, which is facilitative and promotes market access and liberalization. This coalition, usually composed of Member States with stronger capital markets and a stronger international presence in their markets, and including the United Kingdom, the Nordic Member States, and the Netherlands, is also broadly sympathetic to market-based intermediation as opposed to bank-based intermediation.[38] In

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scale of the potential losses to the City, including in terms of a three percent drop in City of London employment).

31. *See* European Parliament, Briefing, M. Magnus, A. Margerit, and B. Mesnard, Brexit: the United Kingdom and EU Financial Services, PE 587.384 (Dec. 9, 2016) [hereinafter EU Briefing].

32. *See The UK: Europe's financial centre*, THECITYUK (Aug. 2016), *available for download at* https://www.thecityuk.com/research/the-uk-europes-financial-centre/.

33. *See generally* EU Briefing, *supra* note 31.

34. THECITYUK, *supra* note 32, at 3-4.

35. *See generally* Oliver Wyman, *The Impact of the UK's Exit From the EU on the UK-Based Financial Services Sector* 6 (2016), *available at* http://www.oliverwyman.com/content/dam/oliver-wyman/global/en/2016/oct/Brexit_POV.PDF.

36. *Id.* at 2.

37. *See* Quaglia & Howarth, *supra* note 28, at 2; Lucia Quaglia, The 'Old' and 'New' Politics of Financial Services Regulation in the EU, 17 NEW POL. ECON. 15 (2012); Lucia Quaglia, Completing the Single Market in Financial Services: the Politics of Competing Advocacy Coalitions, 17 J. OF EUR. PUB. POL'Y 1007 (2010).

38. *See, e.g.*, Quaglia, Howarth, & Liebe, *supra* note 28.

terms of regulatory design, although EU financial regulation has become more behaviorally-oriented and interventionist over time, the market-making coalition can be supportive of transparency and disclosure techniques over behavioral regulation, and can be more open to market substitutes for intervention. The market-making coalition also typically advocates for more national discretion and for finer calibration to the distinct features of local markets. The market-shaping coalition, by contrast, often associated with France, Spain, and Italy, typically takes a more interventionist posture and adopts a more prominent regulatory bias. In terms of financial system model, this coalition can, being composed of Member States whose financial systems have a strong bank orientation, be suspicious of intense levels of market intermediation, although this varies: France has been a prominent supporter of securitization.[39] In terms of regulatory design, this coalition can be wary of market substitutes for regulatory intervention. It also typically promotes harmonization over national discretion. Over time, and reflecting the wide range of factors that play on preference formation, the balance of power in the Council has ebbed and flowed between both coalitions.

The major themes associated with the UK's influence on EU financial regulation are considered in the following sections. But they should not be over-weighted. Distinct Member State preferences form only a part, if a significant part, of the wider, complex, and dynamic array of influences and drivers that shape EU financial law. It cannot be said that the United Kingdom has, in any real sense, been an architect of the current regulatory system. While the United Kingdom has certainly influenced it, the current system has been forged in the crucible of the financial crisis, shaped by the international reform agenda, and finessed by a complex array of EU-specific preferences and influences. The United Kingdom has nonetheless left a distinct mark on EU financial regulation. Much of the technical rigour in the single rulebook can be credited to the United Kingdom, which has brought the experience of regulating Europe's largest market to bear on rule drafting. The United Kingdom has also ensured that EU financial regulation is relatively well differentiated, tends to apply tailored rules to distinct market segment, and embeds the proportionality principle.

39. *See* David Howarth, *State Intervention and Market Based Banking in France in* Hardie & Howarth, *supra* note 26, at 128.

C. A Liberal Approach to Intervention

The United Kingdom has been a leading member of the liberally oriented, market-making coalition since EU financial regulatory governance began to mature and intensify. This point can be dated to 1999 and the EU's liberalizing Financial Services Action Plan (FSAP) agenda, a 42-measure project designed to liberalize the EU financial market and to promote market-based funding, and which can be regarded as the foundation of modern EU financial regulation.[40]

The United Kingdom has repeatedly sought to liberalize access to EU financial markets through regulatory governance techniques and to ensure that related EU financial regulation is appropriately differentiated so that it reflects the distinct risks posed by different market actors and segments. This position reflects the diversity of actors within the UK financial system and the competitive advantage of the United Kingdom in relation to wholesale market services. For example, prior to the financial crisis, the United Kingdom was a leading supporter of the FSAP agenda[41] and its imprints can be seen on several key measures from this period. The pivotal FSAP-era Prospectus Directive 2003,[42] for example, governs the disclosure document (the prospectus) required of firms (issuers) when they access the capital markets. It also liberalizes funding markets, allowing issuers to access EU markets on the basis of a single 'home' authorization of the prospectus. The United Kingdom argued strongly for differentiation in this measure and for the wholesale, professional funding markets, particularly the bond markets, to benefit from a series of exemptions. These exemptions have, over time been extended, supported by the United Kingdom. The most recent iteration of the Prospectus Directive, the recently agreed 2017 Prospectus Regulation,[43] contains numerous exemptions for the

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40. *See* Commission of the European Communities, Communication on Implementing the Framework for Financial Markets Action Plan, COM (99) 232 Final (May 1999) [hereinafter Implementation Communication].

41. *See* HM Treasury & FSA, *Strengthening the EU Regulatory and Supervisory Framework: A Practical Approach* (Nov. 2007).

42. *See* Directive 2003/71/EC of the European Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC 2003 O.J. L 345/64.

43. Regulation 2017/1129/EU of the European Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC 2017 O.J. L 168/12. For the original Commission proposal, see Proposal for a Regulation of the European Parliament and of the

wholesale markets. Over the negotiations on the 2017 amendments the United Kingdom strongly supported the raising of exemption thresholds so that offering costs were reduced for smaller issuers and a more proportionate approach adopted.[44]

Similarly, the United Kingdom opposed a prescriptive approach to the regulation of equity market trading during the negotiations on the FSAP-era Markets in Financial Instruments Directive I 2004 (MiFID I)[45] – the first major EU measure to govern investment services and trading venues. It was designed to liberalize cross-border activity by means of harmonized rules that would allow cross-border activity on the basis of 'home' authorization and supervision (home being the Member State where the actor in question was registered). The regulation of trading venues and related order execution (trading) has long been a flash-point in EU financial regulation, with France and the United Kingdom having sharply different approaches to the regulation of equity trading. France has long been suspicious of pan-EU competition between equity order execution venues, which can be traced back to early battles over the 1993 Investment Services Directive (ISD)[46] and to France's attempts then to prevent trading of French shares on the SEAQ-International trading venue in London. The United Kingdom, by contrast, has long supported competitive and multiple venues for trading, reflecting its dominance in off-venue, over-the-counter (OTC) trading, and has fought against any protection of 'national champions' in the form of dominant national stock exchanges.[47] Over the MiFID I negotiations, these longstanding differences came to a head. MiFID I was, overall, a liberalizing measure, abolishing the earlier ISD 'concentration' rule which allowed Member States to route trading to major trading venues in

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Council on the prospectus to be published when securities are offered to the public or admitted to trading, COM(2015) 583.

44. *See* Letter from HM Treasury to House of Lords European Union Committee (May 6, 2016).

45. *See* Directive 2004/39/EC of the European Parliament and of the Council on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC, 2004 O.J. L 145/1.

46. *See* Council Directive 93/22/EC on investment services in the securities field, 1993 O.J. L 141/27.

47. On the fraught history of European Union trading venue regulation, see Moloney, *supra* note 11, at 435-38.

their markets.[48] But sharp differences arose between the Member States as to how the newly liberalized order execution market should be regulated. To protect its liberal and competitive approach to trading regulation, which was based on facilitating competition between traditional stock exchanges, alternative trading venues, and other OTC execution systems, the United Kingdom fiercely resisted proposals that would have imposed the same set of stock-exchange-oriented rules (particularly transparency rules) on other execution venues, including firms dealing in securities, severely limiting their ability to compete. This position reflected intense UK market hostility to the imposition of a 'one size fits all' stock-exchange oriented-approach to trading venue regulation.[49] While the United Kingdom was not successful in achieving a fully differentiated approach to trading venue regulation under MiFID I, it succeeded in including a series of relaxations from the most onerous of the trading rules for investment firms providing dealing services in a systematic and organized manner ('systematic internalizers').[50] These differences in approaches to trading venue regulation have persisted in the Council. During the negotiations on the successor measure to MiFID I, the 2014 Markets in Financial Instruments Directive II/Markets in Financial Instruments Regulation (MiFID II/MiFIR), which comes into force in 2018,[51] the United Kingdom, in often difficult

48. The ISD concentration rule followed difficult and highly politicized negotiations which saw the 'Alliance' group of Member States (the United Kingdom, Germany, Ireland, Luxembourg, and the Netherlands) support competition in trading/order execution and the 'Club Med' group (France, Spain, Portugal, Greece, Italy, and Belgium) demand the centralization of all transactions on major stock exchanges in order to support liquidity and ensure a high level of investor protection. Protectionist undercurrents were strong during the negotiations, with certain Member States concerned to protect their markets from the then-dominant London Stock Exchange. A compromise position was finally adopted which made the concentration rule optional for Member States (the United Kingdom did not apply it) and imposed conditions on its use.

49. Among the influential industry position papers was the one presented by a group of leading trade associations. *See* Association of Private Client Investment Managers and Stockbrokers – European Association of Securities Dealers *et. al.*, *Innovation, Competition, Diversity, Choice, A European capital market for the 21st Century* (May 21, 2002), http://www.isdadocs.org/speeches/pdf/Innovation_Competition_Diversity_Choice.pdf.

50. On preference formation in relation to EU trading venue regulation, see generally Guido Ferrarini and Niamh Moloney, *Reshaping Order Execution in the EU and the Role of Interest Groups: From MiFID I to MiFID II,* 13 EUR. BUS. ORG. L. REV. 557 (2012).

51. *See* Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU, 2014 O.J. L 173/349 (MiFID II); Regulation 600/2014/EU of the European

negotiations,[52] repeatedly raised the dangers associated with the new measure's extension of MiFID I's transparency rules to trading in asset classes beyond equity, unless the rules were carefully calibrated to address liquidity risks. This posture reflects the UK's interests as the major EU centre for trading and dealing in derivatives and bonds.[53]

Over the financial crisis, the market-shaping coalition came into the ascendant in the Council.[54] An anti-speculation agenda and a related suspicion of market intensity in some political quarters combined to give EU financial regulation a more interventionist quality. Much of EU financial regulation from this period relates to the EU's implementation of the G20 reform agenda, however, and cannot be associated entirely with Member States' political preferences. Nonetheless, there was some political pressure for a market-dampening agenda, which was resisted by the United Kingdom.

The United Kingdom opposed much of the 2012 Short Selling Regulation,[55] for example, arguing that a restrictive approach to short selling could damage market liquidity.[56] It also resisted much of the highly contested 2011 Alternative Investment Fund Managers

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Parliament and of the Council on markets in financial instruments and amending Regulation (EU) No 648/2012, 2014 O.J. L 173/84 (MiFIR).

52. The negotiations were reported as being fierce, particularly between the United Kingdom, France, and Germany. *See* Philip Stafford & James Fontanella-Khan, *UK agrees EU deal on City regulation*, FIN. TIMES 18 (June 18, 2013), https://www.ft.com/content/c9c9294a-d75b-11e2-8279-00144feab7de.

53. During the development of MiFID II/MiFIR the UK Financial Services Authority (FSA) (now Financial Conduct Authority) warned that the imposition of transparency requirements on the trading of non-equity asset classes required careful calibration if adverse impacts on liquidity were to be avoided. *See* FSA, The FSA's Markets Regulatory Agenda (2010), pp 33-34. Since then, the United Kingdom has called for careful post-implementation review of how the new rules might impact on non-equity trading. *See* HM Treasury, *Response to the EU Commission: Call for evidence on EU regulatory framework for financial services* (Feb. 2016), 16-18.

54. For measure-by-measure analysis, see Moloney, *supra* note 11; Eilis Ferran, *Crisis-driven Regulatory Reform: Where in the World is the EU Going?* in Eilis Ferran, et. al., THE REGULATORY AFTERMATH OF THE GLOBAL FINANCIAL CRISIS 1 (2012).

55. *See* Regulation 236/2012/EU of the European Parliament and of the Council on short selling and certain aspects of credit default swaps, 2012 O.J. L 86/1 [hereinafter Short Selling Regulation].

56. The United Kingdom was particularly opposed to any prohibition on 'uncovered' sovereign credit default swaps, given the potential prejudice to liquidity in the sovereign debt market, pressure on sovereign borrowing costs, damage to the ability of the European Union to recover from the financial crisis, and damage to legitimate hedging activities. *See* Ian Wishart, *Council, MEPs at odd on Short Selling and Supervision*, EUROPEAN VOICE, 7 (July 7, 2011).

Directive,[57] which imposes a new set of regulatory requirements on the previously lightly-regulated alternative investment fund sector - and which could have had a potentially disproportionate impact on the United Kingdom as the major EU centre for alternative funds, including hedge funds.[58] The UK's reluctant agreement to the Directive, after bitter negotiations, was reported as being linked to a pragmatic calculation not to deploy any further political capital on a measure that was strongly supported by France and Germany, in light of the need to keep capital for the parallel and similarly difficult negotiations on the new European Supervisory Authorities.[59] The United Kingdom did, nonetheless, achieve a number of successes, including the removal of a direct cap on fund leverage and a more proportionate approach to regulatory reporting requirements.[60] The UK's opposition to more dirigiste, market-shaping measures is similarly evident in its opposition to the 2011 proposal for a Financial Transaction Tax.[61] Most famously, perhaps, it was outvoted 27:1 on the Council vote to restrict bankers' bonuses (to a ratio of 100 percent of salary, or 200 percent with approval)[62] under the 2010 Capital Requirements Directive III.[63]

The United Kingdom was more successful in imposing its preferences on the 2012 European Market Infrastructure Regulation

57. *See* Directive 2011/61/EU of the European Parliament and of the Council on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010, 2011 O.J. L 174/1 [hereinafter Alternative Investment Fund Managers Directive].

58. On the negotiations, see generally Eilis Ferran, *After the Crisis: The Regulation of Hedge Funds and Private Equity in the EU*, 12 EUR. BUS. ORG. L. REV. 379 (2011); Barbara Sennholz-Weinhardt, *Regulatory Competition as Social Fact: Constructing and Contesting the Threat of Hedge Fund Managers' Relocation from Britain*, 21 (6) REV. OF INT'L POL. ECON. 1240 (2014).

59. *See* George Parker et al., *Osborne bows to EU Hedge Fund Rules*, FIN. TIMES (May 19, 2010), https://www.ft.com/content/319a20c4-62bb-11df-b1d1-00144feab49a.

60. *See* Norton Rose Fulbright, *supra* note 16, at 25.

61. The tax, which continues to struggle in the Council, was originally proposed in 2011 to a cacophony of protest including but not only from the United Kingdom. *See* Commission of the European Communities, Proposal for a Council Directive on a common system of financial transaction tax and amending Directive 2008/7/EC, COM (11) 594 Final (2011).

62. *See* A. Barber et al., *Brussels Deals Rare Blow to City on Bonuses*, FIN. TIMES (Mar. 28, 2013).

63. *See* Directive 2010/76/EU of the European Parliament and of the Council Amending Directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for re-securitisations, and the supervisory review of remuneration policies, 2010 O.J. L 329/3.

(EMIR),[64] one of the pillars of the EU's crisis-era reform program, which restructures how trading and clearing is organized in the OTC derivatives markets, requiring the routing of much of trading and clearing through market infrastructures. The distinct technical expertize that the United Kingdom could offer has been identified as a major determinant of the UK's successes over the negotiation of this highly complex but operationally critical measure.[65]

The UK's resistance to the crisis-era reforms, and the impact of that resistance, should not be overplayed. The incidences of opposition noted above were substantial and did shape the negotiations. But they were also exceptions in a wide-reaching reform process, which saw a vast array of financial market rules supported by the Council. The crisis-era reforms were, by and large, supported by the United Kingdom and have been shaped by the UK's technical expertise. A UK Parliament report on the crisis-era reform process concluded that while aspects of the reforms were problematic for the United Kingdom, overall the United Kingdom would have implemented the vast bulk of the reforms had it acted unilaterally; and, that, in a number of cases, the United Kingdom had gone further than the minimum required under EU law, 'gold-plating' EU rules (adding additional obligations for UK actors).[66] The report also noted the technical influence that the United Kingdom had brought to bear.[67] Presciently, it warned that the UK's influence was diminishing and could diminish further, given, inter alia, the then-ongoing debate on the UK's place in the European Union, perceptions of UK antipathy to EU intervention, and an insufficient commitment to the 'hard graft' of effective lobbying, negotiation, and alliance building.[68]

D. Local Discretion and Autonomy

The United Kingdom has not as a rule resisted the construction of the single rulebook. At an early stage of the financial crisis reforms the UK Financial Services Authority supported the construction of what has since become the detailed single rulebook for financial

64. *See* Regulation 648/2012/EU of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories, 2012 O.J. L 201/1.

65. *See* Norton Rose Fulbright, *supra* note 16, at 25.

66. *See* EUROPEAN UNION COMMITTEE, REPORT, 2014-15, HL Paper 103, ¶ 240-43 (UK).

67. *See id.* ¶ 244-46

68. *See id.* ¶ 261

services, and suggested that as between 'More Europe' and 'Less Europe,' 'More Europe' should prevail.[69] Its support has not derived primarily from a commitment to standardization, or to EU-led rule-making, but reflects a pragmatic recognition of the 'passporting' benefits that flow from the single rulebook:[70] once authorized in its home Member State (typically the State of registration), a financial actor registered in the European Union can, under the financial 'passport,' provide services and establish branches cross-border without host State regulation or supervision, subject to some limited exceptions. The passport has been widely used in the United Kingdom, with some 5,000 passports covering the export of financial services business from the United Kingdom to the European Union.[71]

The United Kingdom has, however, repeatedly championed subsidiarity and national regulatory discretion, particularly in relation to the more intrusive financial-crisis-era reforms. It advocated for greater national discretion under the 2013 Capital Requirements Directive IV/Capital Requirements Regulation (CRD IV/CRR),[72] a central pillar of EU financial regulation which contains the EU's banking rulebook and which implements the Basel III Accord. It was particularly concerned to protect domestic regulatory autonomy in relation to the application of capital and other prudential tools to manage local risks to financial stability.[73] Similarly, over the negotiations on the 2014 MiFID II/MiFIR, which provides the core of the EU's investment services/trading rulebook, the United Kingdom was a leading member of the Council coalition which successfully protected a degree of Member State autonomy and industry choice in

69. FINANCIAL SERVICES AUTHORITY, THE TURNER REVIEW, A REGULATORY RESPONSE TO THE GLOBAL BANKING CRISIS, 100-105 (Mar. 2009).

70. HM GOVERNMENT, HM TREASURY ANALYSIS: THE LONG TERM ECONOMIC IMPACT OF EU MEMBERSHIP AND THE ALTERNATIVES, Cm. 9250 (Apr. 2016).

71. *See* Letter from Andrew Bailey, FCA Chairman, to Andrew Tyrie, House of Commons Treasury Committee Chair (Aug. 17, 2016), https://www.parliament.uk/documents/commons-committees/treasury/Correspondence/AJB-to-Andrew-Tyrie-Passporting.PDF.

72. *See* Directive 2013/36/EU of the European Parliament and of the Council on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, 2013 O.J. L 176/338 (CRD IV); Regulation 575/2013/EU of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms and amending regulation (EU) No 648/2012, 2013 O.J. L 176/1 (CRR).

73. On the negotiations, see Scott James, *The Domestic Politics of Financial Regulation: Informal Ratification Games and the EU Capital Requirement Negotiations*, 21 NEW POL. ECON. 187 (2016).

relation to the otherwise extensive transparency and other rules which apply to trading in financial instruments.[74]

In the current 'open' negotiations in which the United Kingdom will participate until it leaves the European Union, its concern to protect local discretion has not diminished. It has, for example, raised concerns as to the Commission's proposal to remove many of the 'options and national discretions' (ONDs) contained in the CRD IV/CRR banking rulebook,[75] which it originally supported, and warned that it would strongly object to any proposal to reduce national discretion which was driven by the needs of the euro area.[76] The United Kingdom will, however, have limited (or no) political capital in these negotiations.

E. Regulatory Design: Proportionality and Impact Assessment

Reflecting its support for local discretion, the United Kingdom has long supported proportionality in the application of EU financial regulation. It recently called for a more proportionate approach to be adopted to EU financial regulation generally,[77] and was particularly concerned to ensure proportionality in relation to the governance requirements imposed on financial institutions, notably in relation to executive pay. The need for proportionality is a recurring theme of the UK's current approach to the open negotiations in which it will participate until it withdraws from the European Union. In the ongoing negotiations on the new securitization regime, for example, it has argued for a more proportionate approach to the new rules

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74. On the negotiations, see Moloney, *supra* note 11, at 456-57.

75. Set out in, Commission of the European Communities, Proposal for a Directive of the European Parliament and of the Council amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures, COM (16) 854 Final (Nov. 2016); Commission of the European Communities, Proposal for a Regulation of the European Parliament and of the Council, amending Regulation (EU) No 575/2013 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements and amending Regulation (EU) No 648/2012, COM (16) 850 Final (Nov. 2016).

76. *See* Letter from HM Treasury to House of Lords, European Union Committee, (Jan. 2016), *available at* http://europeanmemoranda.cabinetoffice.gov.uk/memorandum/communication-from-the-commission-to-the-european-parliament-the-council-the-european-central-bank-the-1449009130.

77. *See* HM Treasury, *supra* note 53, at 27-33. The response highlights difficulties with the proportionate application of: financial reporting rules to smaller firms; capital requirements to smaller banks; and financial rules more generally to non-financial counterparties.

proposed for due diligence, risk retention, and transparency, and has been concerned to reduce reporting burdens.[78]

The United Kingdom has also long been a champion of evidence-based policy making and of impact assessment, which, while still developing,[79] have become significantly more secure in EU financial regulation policy design in recent years.[80] This is clear from the UK's input into the Commission's major 2015-2016 review of the crisis-era reforms,[81] but has been a recurring theme of UK interventions.[82]

F. Policing the Rules of the Game: Recourse to the Referee

Finally, the United Kingdom has shaped EU financial regulation by means of its vigilance in policing the constitutional/Treaty competence of the European Union in relation to financial regulation.

EU financial regulation has not, despite its contested quality, led to many challenges before the Court of Justice of the European Union. Political and institutional differences, particularly of a technical nature, are generally addressed by means of the

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78. *See* Letter from HM Treasury to House of Lords, European Union Committee (Dec. 1, 2015), *available at* http://europeanmemoranda.cabinetoffice.gov.uk/files/2015/12/EST_to_Lords_on_securitisation_01122015.pdf.

79. While the Commission engages in impact assessment of proposals and in post implementation review, the Council and Parliament do not provide impact assessments of the revisions they make to Commission proposals. For a critical assessment of the Commission's approach to impact assessment and an analysis of related inter-institutional failures, see Andrea Renda, *Too Good to be True? A Quick Assessment of the European Commission's New Better Regulation Package*, CENTRE FOR EUROPEAN POLICY STUDIES, Special Report No 108/2015 (May 2015), https://www.ceps.eu/system/files/SR108AR_BetterRegulation.pdf.

80. As is clear from the extensive 'stock-take' of EU financial regulation which the Commission engaged in over 2015-2016 (Commission of the European Communities, Call for Evidence, EU Regulatory Framework for Financial Services (2015)) and the market assessment exercise undertaken in relation to the Capital Markets Union agenda (Commission of the European Communities, Initial reflections on the obstacles to the development of a deep and integrated EU capital markets, Staff Working Document, SWD (15) 13 Final (Feb. 18, 2015)). Institutionally, impact assessments of the different proposals developed by the Commission are reviewed by its Regulatory Scrutiny Board; rejections of assessments on quality grounds are not uncommon.

81. *See* HM Treasury, *supra* note 53, at 33-35 (highlighting the need to address excessive compliance costs and complexity); *id.* at 55-57 (on the need to monitor unexpected impacts).

82. Including those from the UK industry. *See* International Regulatory Strategy Group, *The Cumulative Impact of EU Financial Services Regulation: Better Regulation for Jobs and Growth* (June 2016), *available at* https://www.thecityuk.com/assets/2016/Reports-PDF/The-cumulative-impact-of-EU-financial-services-regulation.pdf.

compromises made over the legislative process – and often by means of a delegation to the administrative rule-making process. Challenges, to the extent they arise, are typically limited, are usually directed to technical interpretations of EU financial regulation, and tend to arise from references from national courts. They are only rarely concerned with grander constitutional questions with political implications - the most important one in this area being the competence of the European Union to act in the financial regulation sphere.[83] Competence allocation has nonetheless the potential to generate significant tensions between the European Union and its Member States in relation to financial regulation. Financial regulation is technocratic in nature, but has distributive consequences. Member States can have incentives to protect their sphere of sovereignty in this area, particularly as financial regulation can have implications for the supply of credit in an economy and, as the crisis-era has underlined, can lead to the imposition of fiscal burdens on tax-payers. The line between the EU's single-market-oriented regulatory competences, and national competences, particularly in relation to supervision and the support of financial stability, can be expected to be policed, particularly where harmonizing regulatory measures tip into the supervisory/financial stability sphere where fiscal risks to the Member States are most acute. Over the financial crisis, as political support for greater risk-sharing and related coordination of supervision at the EU-level strengthened, the United Kingdom deployed competence challenges to prevent the European Union from adopting single market measures which allowed it to intervene in national market structures or which raised the prospect of national supervisory powers been constrained. These single-market-oriented challenges reflect the UK's related decision not to participate in the euro-area-oriented Banking Union. The UK's decision was based on its characterization of Banking Union as flowing from Economic and Monetary Union and as being designed to protect the euro,[84] but also reflected its concern not to lose sovereignty over bank supervision and the support of financial stability.

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83. The challenge by Germany to the competence on which the original measure for harmonizing deposit guarantee schemes in the European Union (since repealed) was based provides an early and unusual example. *See generally* Germany v European Parliament and Council Case C-233/94, [1997] E.C.R. I-2441.

84. *See* EUROPEAN UNION COMMITTEE, REPORT, 2012-13, HL 88, ¶ 129 (UK).

EU financial regulation is almost always based on Article 114 of the Treaty on the Functioning of the EU, which contains the EU competence to adopt harmonizing measures for the purposes of the establishment and functioning of the internal market, or on similar competences related to free movement, notably the freedom to establish. The Article 114 competence has generated most controversy as it has become almost infinitely elastic in the financial regulation sphere, being deployed over the financial crisis to support an array of measures that have pushed at the boundaries of what has traditionally been characterized as a 'harmonizing' measure for the support of the single market. Chief among these were the measures used to construct institutions, notably the ESAs, which strengthened the EU's ability to shape national supervision and how financial stability was supported. Nonetheless, political exigencies over the crisis era meant that challenges to the EU's competence to adopt measures designed to address the damage caused by the financial crisis and to reduce risk were always likely to be rare - once political and institutional support for the measure in question was in place.

The United Kingdom has long been careful to monitor the competence of the European Union in financial governance over the legislative process. But it was only over the financial crisis era, when the risk of asymmetric rule impact became more acute as the single rulebook expanded and as the European Union began to stray into the national supervisory sphere to manage risk transmission, and the United Kingdom was not able to construct blocking coalitions in the Council, that it had regular recourse to the Court. In four high-profile cases, relating to the bankers' bonus rules, the proposed financial transaction tax, the powers of the new European Securities and Markets Authority (ESMA), and the 'location policy' adopted by the ECB in relation to central clearing counterparties (CCPs), it challenged the competence of the European Union to act. In all four cases, the EU measure in question had potentially material impacts for the UK market, and the ESMA case squarely raised the UK's opposition to single market measures that intervened in national supervisory autonomy. While it was unsuccessful in all apart from the ECB case, the actions underline the UK's monitoring role in relation to EU competence and the risk of over-reach.

In relation to the financial transaction tax proposal, the United Kingdom unsuccessfully challenged the spill-over effects of the proposed tax outside the 'financial transaction tax-zone' (the tax was designed to operate between the group of Member States that voluntarily opted into it under the Treaty 'enhanced cooperation' rules) and on the single market more generally.[85] In relation to the bankers' bonus rules, the UK challenge[86] was based on a number of grounds, including: that the bonus cap was not fit for purpose (to support financial stability) as it would lead to an increase in fixed salaries and fixed costs; the competence for the cap (the UK position was that the bonus cap imposed harmonized limits on pay and thus went beyond the limits of Article 53(1) TFEU (the competence deployed) which supports the freedom of establishment); and failures with respect to impact assessment and consultation. Following an opinion from the Court's Advocate General, which did not support the UK position, the action was withdrawn.

The United Kingdom also lost the ESMA case - perhaps the most closely followed of this sequence of challenges given its implications for the operation of the ESAs[87] - in which it argued that the market intervention powers granted to ESMA under the Short Selling Regulation (including the power to prohibit short selling activity by market actors in national markets) breached a number of Treaty requirements, including in relation to the Article 114 competence deployed.[88] It was successful, however, in the ECB 'location' case, although the Court's acceptance of the UK's argument was based on technical grounds, and not on the breach of

85. UK v Council and Parliament, Case C-209/13, 2014, http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A62013CJ0209. The Court of Justice rejected the challenge, primarily on grounds related to the premature nature of the action as a financial transaction taxation regime had not, at the time of the UK action, been adopted.

86. *See* UK v Parliament and Council, Case C-507/13, 2014, http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A62013CC0507.

87. See Carl F. Bergstrom, *Shaping the New System for Delegation of Powers to EU Agencies: United Kingdom v European Parliament and Council (Short Selling),* 52 COMMON MKT. L. REV. 219 (2015); Pieter Van Cleynenbrueguel, *Meroni Circumvented? Article 114 TFEU and EU Regulatory Agencies*, 21 MAASTRICHT J. OF INT'L L. 64 (2014); Valia Babis, *The Power to Ban Short-Selling: The Beginning of a New Era for EU Agencies*, University of Cambridge Faculty of Law Research Paper No 027/2014 (2014), *available at* https://ssrn.com/abstract=2420011; Miroslava Scholten & Marloes van Rijsbergen, *The ESMA Short Selling Case: Erecting a New Delegation Doctrine in the EU upon the Meroni-Romano Remnants*, 41 LEGAL ISSUES OF ECON. INTEGRATION 389 (2014).

88. *See* UK v Council and Parliament, Case C-270/12, 2014, http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A62012CJ0270.

the Treaties' non-discrimination principles which was a key aspect of the UK's argument.[89]

While the UK's scorecard before the Court of Justice is mixed, the chilling effect of potential action by the United Kingdom should not be discounted as an influence on the development of EU financial regulation. In the case of the Short Selling ruling, for example, while the United Kingdom failed to have ESMA's intervention powers over-turned, the ruling is likely to have had a moderating effect on any incentives, which the ESAs may otherwise have had to test their new powers.

III. INTERNAL EFFECTS: SINGLE MARKET REGULATION

The UK's absence is unlikely to lead to a material change to the EU's current posture on financial regulation. This prediction is based on the likely dilution of the effects of the UK's withdrawal by institutional factors, as well as on the legacy effects that will likely follow the UK's withdrawal.

Institutionally, and looked at in historical perspective, the great reforming movements in EU financial regulation have not been initiated by single Member States or even coalitions of Member States. The two most recent reforming periods (the FSAP 1999-2004 liberalizing era; and the financial crisis 2008-2014 regulatory, risk-reduction era) were driven by an interlocking array of political but also market and institutional/supranational factors, including global market conditions (which drove liberalization in the case of the FSAP era and regulatory retrenchment over the financial crisis era).

National preferences remain important. The absence of the United Kingdom may mean that the ECOFIN Council will in the future more easily adopt a more regulatory and less liberal posture. It may also be less concerned to promote market-based funding and more comfortable with the bank-based status quo. But the UK's default position has been to react on a piecemeal basis - not to steer grand regulatory designs. Its absence is unlikely to have effects that are on the scale of Germany's varying stances on EU financial governance more generally.[90] The removal of the United Kingdom as

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89. *See* Case UK v European Central Bank (ECB), T-496/11, 2015, http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A62011TJ0496 (two related challenges were subsequently withdrawn).

90. On how Germany's varying degrees of willingness to lead on financial and economic governance have shaped EU action, see Magnus G. Schoeller, *Providing Political*

the dominant non-euro-area Member State is also unlikely to have significant traction - at least in the short term, and at least in relation to regulatory governance. The United Kingdom has consistently sought to protect a 'multi-currency' form of financial market integration and to defend the integrity of the single market. The salience of this issue in the United Kingdom is clear from the pre-referendum political maneuvers in the European Union. Before the referendum, UK Prime Minister Cameron won a political commitment from the European Council (in the now defunct February 2016 'New Settlement for the UK'[91]) that euro area institutional governance measures would not be imposed on the single market. It may be (and is probably likely) that the euro area will continue to build bespoke supervisory and (although less likely) risk-sharing structures, given the distinct institutional and other incentives in the euro area.[92] But from a regulatory governance perspective, the single rulebook that governs the single market and the euro area is unlikely to become a euro area construct, at least in the short term. The Council adopts financial regulation measures through a QMV, as noted above; there is already a euro area QMV, and the related possibility for euro area caucusing and blocking, in place in the Council with nineteen of twenty-eight (soon twenty-seven) EU Member States in the euro area. Nonetheless, the political economy of Council discussions on EU financial regulation, certainly over the frenetic crisis-era period, does not suggest that the euro area speaks as one voice; coalitions are more likely to be formed on 'market-shaping/making' lines than on single market/euro area lines. In addition, different legislative negotiations have seen different coalitions form and reform, depending on the distinct issues at stake.[93] Further, all the current policy indications suggest an institutional and political commitment to preserve the regulatory integrity of the single market. There is, for example, a current concern to strengthen pan-EU

Leadership? Three Case Studies on Germany's Ambiguous Role in the Eurozone Crisis, 24 J. OF EUR. PUB. POL'Y 1 (2017).

91. Notices from European Union Institutions, Bodies, Offices and Agencies, A New Settlement for the United Kingdom within the European Union, Extract of the conclusions of the European Council of 18-19 February 2016, 2016 O.J. C 69 I/3 (Annex I).

92. From a political economy perspective, see Frank Schimmelfennig, *A Differentiated Leap Forward: Spillover, Path-dependency, and Graded Membership in European Banking Regulation,* 39 WESTERN EUR.POL. 483 (2016).

93. On the ECOFIN Council dynamics generally over the crisis reform period, see Moloney, *supra* note 11, at 891-92.

regulatory 'risk reduction' measures within the single rulebook prior to the building of further euro area risk-sharing structures, notably a European Deposit Insurance Scheme - regarded as the 'missing pillar' of Banking Union.[94]

In addition, institutional factors will dilute any effects from the withdrawal of the United Kingdom. The ECOFIN Council is a co-legislator with the European Parliament in the financial regulation sphere. The Parliament is now a force to be reckoned with in the legislative process, particularly in the 'trilogue' negotiations during which a compromise is sought between the Commission's proposal for a measure, and the Council and Parliament positions. Since the financial crisis era, the Parliament has become an increasingly mature and effective legislator and has achieved some notable victories,[95] including in relation to administrative rules, over which it has a veto power.[96] Its influence can be expected to increase, as is clear from the assertive position it is taking on the EU/UK negotiations[97] and its concern to protect the integrity of EU financial governance arrangements.[98] Similarly, the Commission[99] and the ECB,[100] who

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94. *See* ECOFIN Council, Progress Report on the European Deposit Insurance Scheme and Banking Union Roadmap, Council Document 14841/16 (Nov. 25, 2016).

95. *See* Moloney, *supra* note 11, at 893-94. *See generally* M. O'Keeffe, M. Salines & M. Wieczorek, *The European Parliament's Strategy in EU Economic and Financial Reform* 23 J. OF EUR.PUB. POL'Y 217 (2016).

96. The Parliament deployed its veto power in relation to financial administrative rules (which are adopted by the Commission and either proposed or advised on by the ESAs) for the first time in 2016, rejecting a package of administrative rules relating to disclosure requirements for packaged investment products and signaling its commitment to protecting its prerogatives in relation to administrative governance. *See* European Parliament, Objection to a delegated act: Key information documents for packaged retail and insurance-based investment products, P8_TA(2016)0347 (Sept. 14, 2016).

97. The European Parliament has a veto power over the EU/UK Article 50 agreements and has made clear its intention to influence the negotiations. *See* European Parliament, Motion for a Resolution to wind up the debate on negotiations with the United Kingdom following its notification that it intends to withdraw from the European Union, (Mar. 29, 2017) (B8-0237/2017).

98. The ECON committee, for example, held, prior to the UK's official notification of withdrawal, an 'exchange of views' with the Commission and the ESAs on how access arrangements might be configured under the current third country rules. *See* UK Parliament, House of Commons, Brussels Bulletin No. 533 (Mar. 10, 2017).

99. Although the extent to which the Commission's influence has increased is contested. *See generally* Michael W. Bauer & Stefan Becker, *The Unelected Winner of the Crisis: the European Commission's Strengthened Role in Economic Governance*, 36 J. OF EUR. INTEGRATION 213 (2014).

100. *See generally* Zdenek Kudrna, *Financial Market Regulation: Crisis-induced Supranationality*, 38 J. OF EUR. INTEGRATION 251 (2016).

played a large part in the development of the crisis-era reforms, can be expected to seek to increase their influence over EU financial regulation.

Further, there is little sign in the current policy agenda - which is primarily directed to finessing the crisis era reforms, completing Banking Union, and achieving Capital Market Union - of institutional appetite for major change to EU regulatory governance. All the indications suggest a concern to bed in and finesse the current regulatory regime.[101] Institutional energies can be expected to focus on managing the costs of and calibrating the current regime in response to market developments.[102] In addition, any appetite for radical reforms in relation to which the absence of the United Kingdom could matter will be moderated by geo-political conditions. The European Union can be expected to be wary of imposing onerous new requirements on its financial sector given current indications of large-scale deregulation in the United States and potential competitive disadvantage to the European Union.[103]

The UK's absence is also likely to be diluted by legacy effects. Strong empirical evidence has recently emerged of the embedding of an EU commitment to proportionality and differentiation. Proportionality assessments are already a feature of the single rulebook. The sharply contested remuneration requirements which apply to banks under the Capital Requirements Directive IV, for example, are to apply 'in a manner and to the extent that is appropriate to [relevant firms'] size, internal organisation and the nature, scope, and complexity of their activities' (Article 92(2)).

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101. Recent illustrations include the Commission's November 2016 'stock-take' reform agenda and the Council's focus on 'completing Banking Union.' *See* Council Conclusions on a roadmap to complete the Banking Union, COUNCIL OF THE EUROPEAN UNION, Press Release 353/16 (June 17, 2016), *available at* http://www.consilium.europa.eu/en/press/press-releases/2016/06/17-conclusions-on-banking-union/.

102. The Commission's current review of the prudential regime which applies to investment firms under CRD IV/CRR, for example, is designed to 'evaluate, recalibrate and simplify' existing EU rules. *See* European Commission, Inception Impact Assessment, Review of the appropriate prudential treatment for investment firms (Mar. 22, 2017), at 2.

103. An Executive Order of February 3, 2017 sets out core principles for regulating the US financial system, which include that regulation be efficient, effective, and appropriately tailored, and calls on all relevant agencies to report on the extent to which current laws and international obligations promote and support the core principles. President Trump has singled out the Dodd Frank Act for reform stating, in the context of the Order, that cuts to Dodd Frank could be expected. *See* Barney Jopson and Ben McLannahan, *Trump prepares to take axe to Wall St Regulation*, FIN. TIMES (Feb. 3, 2017), https://www.ft.com/content/1c5a8dd0-ea3a-11e6-967b-c88452263daf.

Proportionality requirements are, however, becoming increasingly important. The Commission's recent November 2016 report on the 'stock-take,' which it has undertaken of EU financial regulation, suggests a strong institutional commitment to the proportionality principle as a means for moderating the costs of regulation and for engaging with different market actors and segments. A recurring theme of the Commission's related reform agenda is the need for EU measures to be more proportionate and to reflect the distinct risks posed by different financial system actors.[104] Similar themes emerge from the important November 2016 package of reforms, which the Commission has proposed to the EU's banking rulebook and which will shape the banking reform agenda for some time.[105] The European Parliament's 2016 Balz Resolution on the Commission's 'stock-take' has similarly underlined that EU financial legislation should be proportionate, and highlighted a number of areas where it had disproportionate effects.[106] While the United Kingdom can be expected to have championed the cause of proportionality, recent evidence suggests considerable support within the EU institutions for an appropriately proportionate application of rules. This may significantly mitigate the effects of the UK's departure.

It can be predicted relatively safely, however, that EU financial regulation, however proportionate in design, will continue to bend towards uniformity. The Commission's November 2016 'stock-take' reform agenda repeatedly references the need to strengthen the single rulebook.[107] The ECB is emerging as a standard bearer for greater harmonization, driving the removal of 'national options and discretions' from the banking rulebook within the Banking Union zone.[108] The current Capital Markets Union regulatory reform agenda

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104. *See* Commission of the European Communities, Commission Staff Working Document on the Call for Evidence, SWD (16) 359 Final, at 29-36 (Nov. 2016) (calling for the proportionate application of rules to be enhanced on a cross-sector basis).

105. For summarization, see EUROPEAN COMMISSION, FREQUENTLY ASKED QUESTIONS: CAPITAL REQUIREMENTS (CRR/CRD IV) AND RESOLUTION FRAMEWORK (BRRD/SRM) AMENDMENTS, MEMO/16/3840 (2016).

106. *See* EUROPEAN PARLIAMENT, STOCKTAKING AND CHALLENGES OF EU FINANCIAL SERVICES REGULATION, P8_TA(2015)0268 (2016).

107. *See supra* note 80 and accompanying text.

108. *See* Regulation 2016/445/EU of the European Central Bank on the exercise of options and discretions available in Union law (ECB/2016/4), 2016 O.J. L 78/60; EUROPEAN CENTRAL BANK, BANKING SUPERVISION, ECB GUIDE ON OPTIONS AND DISCRETIONS AVAILABLE IN UNION LAW (2016), https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ecb_guide_options_discretions.en.pdf.

is in part designed to deliver greater harmonization, including in relation to areas of national law, which have not been subject to EU harmonization given their embedding in national private and procedural law, in particular insolvency law.[109] In the absence of the United Kingdom and its support for national discretion, more, and not less, harmonization can be expected.

IV. EXTERNAL EFFECTS: INTERNATIONAL FINANCIAL GOVERNANCE AND THE INTERNATIONAL MARKET

There are several dimensions to how the European Union engages with the international financial market, chief among the regulatory dimension (the process through which international standards are adopted and subsequently implemented by the European Union); and the access dimension (the EU rules which govern the extent to which and how third country actors can access the EU financial system). Both these dimensions may be influenced by the UK's withdrawal, but here again the extent of the effects may be limited.

The European Union has always engaged with the process through which standards are set for the international financial system, but since the financial crisis it has become a significant player in global financial governance, capable of imposing its preferences through multiple channels, whether political or technocratic.[110] These channels include its participation in the major international standard-setting bodies of international financial governance, such the Basel Committee, the Financial Stability Board, and the International Organization of Securities Commissions, through the Commission, the ECB, and, increasingly frequently, the ESAs – and alongside the Member States and their regulator representatives, which sit independently on these bodies (including the United Kingdom).[111] The influence of international financial governance on EU financial regulation, and the now considerable ability of the European Union to impose its preferences on international standards, are unlikely to be

109. Action Plan, *supra* note 23, at 6, 23-25.

110. For an examination of how the different preferences which shape international financial governance are formed and diffused and how 'power' is gathered and deployed, see LUCIA QUAGLIA, THE EUROPEAN UNION & GLOBAL FINANCIAL REGULATION 8-17 (2014).

111. *See generally* Niamh Moloney, *International Financial Governance, the EU, and Brexit: The Agencification of EU Financial Governance and the Implications*, 17 EUR. BUS. ORG. L. REV. 451 (2016).

changed by the absence of the United Kingdom from the European Union; these two factors will also moderate the regulatory governance effects of UK withdrawal.

Particularly since the financial crisis era, EU financial regulation has been shaped by the international standard setting bodies, and it will continue to be so. At Commission level, the November 2016 banking package reforms, for example, are in part designed to implement Financial Stability Board standards in relation to 'TLAC' – the 'total loss absorbing capacity' tool for supporting bank resolution – and to address how TLAC interacts with the parallel EU loss absorbency tool (the 'MREL' – or minimum requirement for eligible liabilities). At ECOFIN level, ECOFIN is monitoring a range of international governance developments, including the Financial Stability Board's initiatives in relation to misconduct.[112]

Any new standards adopted at the international level will be shaped by EU preferences, alongside the distinct preferences of its Member States where they sit independently on the relevant bodies. The European Union may, however, find it easier to come to a common position on international negotiations in the absence of the United Kingdom and in the coalitions and structures through which the European Union imposes its preferences – such as EBA and Banking Union's Single Supervisory Mechanism on the Basel Committee.[113]

During the subsequent implementation process, international standards will continue to be 'carved out' from by the European Union to reflect EU and Member State preferences, as was the case with the Basel III agreement. The EU's implementation of Basel III through the Capital Requirements Directive IV/Capital Requirements Regulation, and the related imposition of EU interests, particularly in relation to facilitating EU bank lending to small and medium-sized enterprises (the European Union imposed lower capital requirements on SME lending), led to a finding of 'material non-compliance' from the Basel Committee in its 2014 review of EU compliance with the

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112. *See* Financial Stability Board, Presidency Progress Report on EDIS and the Banking Union Roadmap, Council Document 14841/16 (Nov. 25, 2016).

113. For an account of the SSM's activities on the Basel Committee, see European Central Bank, Banking Supervision, Annual Report on supervisory activities 2016 (Mar. 2017), at 46-47, *available at* http://www.bankofgreece.gr/BogEkdoseis/ssmar2016en.pdf.

regime.[114] Further carve-outs can be expected. The European Union is, for example, currently resisting the finalization of the most recent suite of Basel proposals (informally termed 'Basel IV'), concerned as to their impact on the competitive position of the EU banking sector.[115] It is not clear that the withdrawal of the United Kingdom will lead to material change in relation to carve-outs. The extent to which the European Union carves out from international standards is a function of a range of different national and other interests and has not usually been dictated by the United Kingdom. For example, the EU's famous IAS 39 carve-out from what are now International Financial Reporting Standards (IFRS) was driven by France's concern to protect its national banking sector.[116] Similarly, a range of different national interests, and different banking systems, drove the EU's approach to the implementation of the Basel III accord.[117] The United Kingdom has traditionally been a supporter of compliance with international standards and is continuing to emphasize the importance of such compliance in its final months as a member of the European Union. It is, for example, concerned to ensure that the Commission's current proposal for a harmonized regime governing CCP resolution remains consistent with international standards and G20 reform commitments.[118] It may be that in the absence of the United Kingdom the Council will more easily support carve-outs from international standards. But overall, the influence of international financial governance on EU regulatory governance, and the ability of the European Union to impose its preferences and its approach to carve-

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114. *See* Basel Committee on Banking Supervision, Regulatory Consistency Assessment Programme (RCAP), Assessment of Basel III regulations – European Union (Dec. 2014), *available at* http://www.bis.org/bcbs/publ/d300.pdf.

115. *See* Caroline Binham & Emma Dunkley, *Basel postpones bank reform vote amid policy differences*, FIN. TIMES (Jan. 3, 2017), . https://www.ft.com/content/589f1ce0-d1a1-11e6-9341-7393bb2e1b51. Both the European Parliament (European Parliament, European Parliament Resolution on Finalisation of Basel III, P8_TA-PROV(2016)0439 (Nov. 23, 2016)) and the Council (Council conclusions on finalizing the post crisis Basel reforms, COUNCIL OF THE EUROPEAN UNION, Press Release 432/2016 (July 12, 2016), http://www.consilium.europa.eu/press-releases-pdf/2016/7/47244644169_en.pdf) have expressed concern and called for the Basel reforms to be calibrated and to reflect the different distribution of their impact on banking systems globally.

116. *See generally* further Andreas M. Fleckner, *FASB and IASB: Dependence despite Independence*, 3 VA. L. & BUS. REV 275 (2008).

117. *See* David Howarth & Lucia Quaglia, *The Comparative Political Economy of Basel III in Europe*, 35 POL'Y AND SOC'Y 205 (2016).

118. *See* HM Treasury, *Explanatory Memorandum for European Legislation and Documents* (Dec. 14, 2016).

outs, are not likely to be materially changed by the UK's withdrawal from the European Union.

The European Union also engages with the international market by bending third country regimes to EU regulation.[119] It does this by means of the 'equivalence' rules, which govern access to the EU market (a third country actor can alternatively establish a subsidiary in the European Union, in which case that subsidiary is treated as an EU actor and benefits from EU law rights). These third country rules (which are not available for all financial market segments) typically link market access to the 'equivalence' of the third country regime with the EU regime and (not always) require registration in the European Union, usually with ESMA, the EU's securities markets authority. The MiFID II/MiFIR regime, for example, provides for an equivalence-based access route for firms providing wholesale investment services into the European Union on a cross-border services basis, based on ESMA registration. Similarly, the credit rating agency regime links third country access to an equivalence process and ESMA registration, as does the regime governing CCPs. By contrast, the banking rulebook (CRD IV/CRR) does not provide specific access rights for third country firms.[120] Other equivalence rules have an internal focus. They usually either moderate the requirements which apply to transactions between EU counterparties and third country counterparties, or restrict the nature of the third country transactions in which an EU actor can engage.[121]

The United Kingdom has long been a strong supporter of the European Union adopting an open and liberal posture to access/equivalence in related ECOFIN negotiations.[122] It was, for example, influential during the Council negotiations on the MiFID

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119. On the different strategies which the European Union deploys to exert influence internationally, see generally Abraham Newman & Elliot Posner, *Putting the EU in its Place: Policy Strategies and the Global Regulatory Context*, 22 J. OF EUR. PUB. POL'Y 1316 (2015).

120. For an industry-oriented review of the different equivalence/access regimes, see *Brexit and Equivalence: Review of the Financial Services Framework Across All Sectors*, SHEARMAN & STERLING (Aug. 10, 2016), http://www.shearman.com/en/newsinsights/publications/2016/08/brexit-and-equivalence-review-of-the-financial.

121. For example, higher capital requirements apply where loan assets of EU banks are located in a jurisdiction which has not been determined to be 'equivalent,' while EU investment firms are prohibited in some circumstances from entering into transactions on trading venues in third countries whose regulatory regimes have not been declared to be equivalent. *See generally* Moloney, *supra* note 3.

122. *See generally* Lucia Quaglia, *The Politics of 'Third Country Equivalence' in Post Crisis Financial Services Regulation in the European Union*, 38 WEST EUR. POL.167 (2015).

II/MiFIR market access regime, and supported a more liberal approach to access to the EU investment fund market under the 2011 Alternative Investment Fund Managers Directive, although that regime remains complex. The future of the third country regime is highly uncertain at present.[123] But this uncertainty is not only, or even primarily, a function of the future absence of the UK's voice in ECOFIN. It is mainly a function of whether the European Union will change its approach to third country access more fundamentally as part of its response to the UK withdrawal and to any stability or efficiency risks the EU financial market may consequently face. The United Kingdom is seeking bespoke financial services access arrangements, to be included in a Free Trade Agreement, as was confirmed in the Prime Minister's March 29, 2017 Article 50 letter. In parallel, however, the European Union is contemplating revisions to its third country regime more generally.[124] Current indications suggest a concern to exert more control over third country actors operating in the European Union, including through enhanced supervision arrangements.[125] It remains to be seen how the EU's third country arrangements will develop. It is reasonable to suggest that the European Union will wish to signal its openness to global financial markets in the wake of the UK's withdrawal. It may, for example, decide to adopt a more coherent approach to access/equivalence, which replaces the current patchwork of third country arrangements, and to adopt a more liberal posture. Current indications suggest that it may deploy the proportionality principle more fully, applying a more intensive review of equivalence where market access is sought from a third country with systemic implications for the European Union, and a less intrusive review for third countries with smaller and less systemic markets.[126] It is unlikely, however, that the European Union will turn inwards at a moment when it will likely seek to signal the resilience and depth of its financial market.

One significant uncertainty attends the EU's future regulatory approach to the international market access. Third countries may come to be affected by new regulatory 'location' requirements (or

123. For analysis, see generally Armour, *supra* note 3, Moloney, *supra* note 3, and Ferran, *supra* note 3.

124. *See* Alex Barker & Jim Brunsden, *EU Review Casts Doubt on City's Hopes for 'Equivalence' as Brexit Last Resort*, FIN. TIMES (Nov. 2016).

125. *See* Commission of the European Communities, EU Equivalence Decisions in Financial Services Policy: An Assessment, SWD (17) 102 Final.

126. *See id*.

requirements that certain activities and/or transactions be located within the EU/euro area and subject to EU/euro area supervision and/or emergency liquidity/fiscal support). The dominance of the United Kingdom as the EU centre for the trading and clearing of euro-denominated instruments[127] has been a source of contention for some time, as is clear from the UK's successful challenge to the ECB's 2011 'location policy' for euro-denominated derivatives clearing;[128] this policy required that related clearing infrastructures be legally incorporated within the euro area (with managerial and operational control exercised within the euro area) and, accordingly, subject to the oversight of the ECB-located Eurosystem oversight of payment, clearing, and settlement systems and so eligible for ECB liquidity support.[129] In the wake of the ruling, the Bank of England (which supervises UK CCPs) and the ECB came to an agreement on supervisory coordination, information sharing, and liquidity support, which acknowledged the distinct financial stability interest of the ECB in UK CCPs which cleared significant volumes of euro-denominated instruments.[130] But the imminent withdrawal of the United Kingdom from the European Union has heightened tensions. Recent indications from the ECB suggest a concern to re-establish this policy.[131] Certain Member States, including France, also support

127. The fate of UK-based euro-denominated derivatives clearing has been a major feature of the Brexit policy debate given the importance of this industry to the UK financial sector and the related tensions. *See Euro-clearing and Brexit - The Practitioners' View*, FINANCIAL SERVICES NEGOTIATION FORUM (Jan. 16, 2017), http://www.fsnf.uk/2017/01/euro-clearing-and-brexit-practitioners.html.

128. Case UK v European Central Bank (ECB), T-496/11, 2015, http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A62011TJ0496.

129. *See generally* European Central Bank, Eurosystem, Eurosystem Oversight Policy Framework (July 2011), https://www.ecb.europa.eu/pub/pdf/other/eurosystemoversightpolicyframework2011en.pdf (since annulled in relation to location requirements).

130. European Central Bank, Eurosystem, ECB and Bank of England announce measures to enhance financial stability in relation to centrally cleared markets in the EU, Press Release (Mar. 29, 2015); Bank of England, European Central Bank (ECB) location policy For Central Counterparties (CCPs), News Release (Mar. 4, 2015).

131. ECB President Draghi has been reported as calling for ECB oversight of post Brexit, UK-located clearing business. *See* J Brunsden, ECB Steps Up Warning on UK-based Euro Clearing after Brexit, FIN. TIMES (Jan 23, 2017), https://www.ft.com/content/51a68c6e-e094-11e6-9645-c9357a75844a. Changes would be required to the competence of the ECB in this area as the UK's successful challenge was based on the ECB not having the power to adopt a euro area location policy. The ECB has recently recommended that related changes be made to its competence in relation to clearing systems. *See* European Central Bank, Eurosystem, ECB recommends amending Article 22 of its Statute, Press Release (June 23, 2017).

repatriating euro-denominated clearing to the euro area.[132] Some clarity was brought in June 2017 when the Commission presented a proposal for the supervision of third country CCPs; the proposal is less radical than might have been expected, adopting a staggered approach, only deploying a relocation requirement for the most systemically important CCPs, and making any such requirement dependent on a prior assessment of systemic importance.[133] At the time of writing, the fate of the proposal, which must be agreed by the European Parliament and Council, is difficult to predict. The interests and preferences swirling around the euro clearing controversy are many; location requirements serve an array of interests from the securing of competitive advantage to the protection of financial stability. The Commission's proposal is, however, nuanced, and does not imply immediate relocation, which may moderate the risk of any global regulatory retaliation.

V. CONCLUSION

EU financial regulation has been shaped by a multiplicity of interests and preferences, of which UK interests form just one component. The United Kingdom has nonetheless left a distinct imprint on EU financial regulation. It can be credited with ensuring the regime is differentiated, to at least some degree, to different market segments; is responsive to the distinct risk profiles of the sophisticated wholesale markets; leaves some room for national experimentation and for the accommodation of distinct national markets and conditions; embeds the proportionality principle; and is technically robust. The United Kingdom cannot, however, be credited with the overall design and architecture of EU financial regulation, which has been shaped by multiple internal and external interests and preferences.

It is axiomatic that it remains to be seen how EU financial regulation will develop without the United Kingdom. It can be

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132. *See* Alex Barker and Jim Brunsden, EU plan to curb City's euro clearing set to be flashpoint in Brexit talks, FIN. TIMES (Dec. 16, 2016).

133. *See* Commission of the European Communities, Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) No 1095/2010 establishing a European Supervisory Authority (European Securities and Markets Authority) and amending Regulation (EU) No 648/2012 as regards the procedures and authorities involved for the authorisation of CCPs and requirements for the recognition of third-country CCPs, COM (17) 331 Final (2017).

expected to become ever-more standardized and to bend more sharply towards uniformity. It may also become more prescriptive and less liberal in design, although international market dynamics are likely to ensure that the European Union will strive to remain competitive. The current direction of travel in regulatory policy suggests that radical changes to current regulatory designs and priorities are unlikely, not least given the influence of international financial governance and the international standard setters on EU financial regulation. The most uncertainty attaches to the EU's third country arrangements for access to the EU market. But even here, international geo-politics and trade relations are likely to have more traction than the absence of the United Kingdom from the European Union.