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ESMA as a Residual Lawmaker: The Political Economy and Constitutionality of ESMA’s Product Intervention Measures on Complex Financial Products

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Abstract
This article proposes that product intervention constitutes a form of residual law-making by ESMA that allows it to tackle aspects of investor protection not addressed by EU incomplete financial laws. Whilst product intervention may bring about certain advantages and may contribute to mitigating regulatory arbitrage problems, it constitutes a highly intrusive regulatory mechanism that raises important questions concerning: (a) ESMA’s rationale and motivations for its use; (b) its compliance with the EU constitutional framework; and (c) its adequacy for the regulation of complex financial products. This article addresses these questions through an analysis of the rationale and consequences of ESMA’s product intervention measures on binary options and contracts for differences of May 2018–July 2019, and of recent reforms of ESMA’s powers. It offers three main contributions to the existing literature. First, it contributes to the literature on administrative discretion and agencies’ rulemaking through an analysis of the political economy of ESMA’s deployment of product intervention powers and, also, of what this reveals about the relationships between ESMA and the EU Institutions, on the one side, and ESMA and National Competent Authorities, on the other. Second, it contributes to the literature on the constitutionality of EU agencies through an examination of the compliance of ESMA’s product intervention measures with EU constitutional law and requirements. Third, it examines whether product intervention constitutes an adequate mechanism to address problems pertaining to investor protection in complex financial products markets and, in doing so, it contributes to the scholarly discussion on complex financial products’ regulation.

Keywords ESMA · Product intervention · Complex financial products · Incomplete law · Agency theory · Meroni
1 Introduction

The Markets in Financial Instruments Regulation (‘MiFIR’)\(^{1}\) confers product intervention powers on the European and Securities Markets Authority (‘ESMA’), which allow it to temporarily restrict or prohibit the marketing, distribution and/or sale of a financial product in the European Union (‘EU’). On 22 May 2018, ESMA made use of product intervention powers for the first time since its creation, with two decisions that imposed restrictions on two complex financial products, namely binary options (‘BOs’) and contracts for differences (‘CFDs’), respectively. From the point of view of administrative discretion, these decisions are of major relevance as they mark a shift from a system of regulating complex financial products based on supervisory convergence and investor warnings to a much more intrusive model based on restrictions and prohibitions. Likewise, they evidence a proactive and increasingly assertive approach by ESMA in the field of investor protection.

This article proposes that product intervention constitutes a form of residual law-making by ESMA that allows it to tackle aspects of investor protection not addressed by EU incomplete financial laws. Whilst product intervention may bring about certain advantages and may contribute to mitigating regulatory arbitrage problems, it constitutes a highly intrusive regulatory mechanism that raises important questions concerning: (a) ESMA’s rationale and motivations for its use; (b) its compliance with the EU constitutional framework; and (c) its adequacy for the regulation of complex financial products. This article addresses these questions through an analysis of the rationale and consequences of ESMA’s product intervention measures on BOs and CFDs of May 2018–July 2019, and of recent reforms of ESMA’s powers. It offers three main contributions to the existing literature. First, it contributes to the literature on administrative discretion and agencies’ rulemaking through an analysis of the political economy of ESMA’s deployment of product intervention powers and, also, of what this reveals about the relationships between ESMA and the EU Institutions, on the one side, and ESMA and National Competent Authorities (NCAs), on the other. Second, it contributes to the literature on the constitutionality of EU agencies through an examination of the compliance of ESMA’s product intervention measures with EU constitutional law and requirements. Third, it examines the question of whether product intervention constitutes an adequate mechanism to address problems pertaining to investor protection in complex financial products markets and, in doing so, it contributes to the scholarly discussion on complex financial products’ regulation.

The remainder of this article proceeds as follows:

Section 2 examines the concept and regulation of complex financial products in the EU with a focus on the Markets in Financial Instruments Directives (I and II) regimes and their product governance provisions. It also examines ESMA’s approach to the regulation and supervision of complex financial products which, until 2018, was based on supervisory convergence and investor warnings. This section explains

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Section 3 uses the concepts of incomplete law, signalling and principal-agent to explain and assess the political economy of ESMA’s product intervention measures. It proposes that product intervention is, first, a form of residual lawmaking which allows ESMA to overcome flaws in investor protection resulting from incomplete EU financial laws and, second, a signalling mechanism through which ESMA indicates to the EU legislator its readiness and willingness to assume increasing responsibilities and a preeminent role in the field of investor protection. It also argues that, in a product intervention process, the relationship between ESMA and NCAs corresponds to a model of an agency with an informed principal; in such a relationship, ESMA uses product intervention to signal NCAs’ expected domestic product intervention measures that the latter may adopt to avoid an EU-wide product intervention or its renewal. This section concludes with an assessment of the constitutionality of ESMA’s product intervention measures on BOs and CFDs. It argues that these are in breach of the EU constitutional framework because they involve the exercise of discretionary powers involving wide margins of discretion by ESMA and, hence, they do not comply with the Meroni constraints.

Section 4 offers a critical assessment of the expansion of the temporal scope of ESMA’s product intervention measures operated by Regulation 2019/2175 and of ESMA’s proposal, from February 2020, for the consolidation of such measures. It also proposes an alternative consolidation model based on the ordinary legislative procedure and where ESMA develops technical aspects of the relevant prohibitions or restrictions through technical standards. This section concludes by highlighting the dangers of the increasing relevance of ESMA’s product intervention as a regulatory mechanism.

Section 5 briefly summarizes the main findings.

2 Complex Financial Products and Their Regulation in the EU

The term ‘complex financial products’ is an elusive one and its characterization varies across jurisdictions. The International Organization of Securities Commissions (IOSCO) defines them as ‘financial products, whose terms, features and risks are not reasonably likely to be understood by a retail customer […] because of their complex structure […] and which may be difficult to value’; 2 Although EU Financial Law does not offer a single, precise, all-embracing definition of the term, Article 25(4)(a) of the Markets in Financial Instruments Directive II (‘MiFID II’) 3 gives some guidance on the nature and features of complex financial products. It does so by defining two conditions that generally render a financial product complex. First,
financial products that embed a derivative are deemed to be complex. Second, financial products whose structure makes it difficult for the investor⁴ to understand the risks linked to them are also considered as complex. Hence, the notions of customers’ knowledge, bounded rationality and risk are the main pillars that underlie MiFID II’s characterization of complex financial products. Whilst MiFID II does not make any reference to specific complex financial products, it provides a non-exhaustive list of non-complex financial products; these include equity and debt securities traded in regulated markets, money-market instruments, certain shares or units in undertakings for the collective investment in transferable securities (‘UCITS’) and structured deposits, as long as these do not fulfil any of the two conditions referred to above.⁵

In the EU, the early directives in the securities field were silent on the issue of complex financial products. One of the first EU policy documents to suggest the possibility of introducing the regulation of complex financial products was the Green Paper on Financial Services, published in May 1996,⁶ in which the European Commission (‘Commission’) pointed to the need to adopt measures to guarantee investor protection in an increasingly complex European financial sector.⁷ This coincided in time with the inception of the retail market for structured products in Europe in that very same year.⁸ Whereas the Commission acknowledged the increasing complexity of the EU financial sector, and the need to enhance the information provided to investors on the financial products and services they purchased,⁹ it nonetheless refrained from legislative intervention, advocating, instead, for a self-regulatory approach based on dialogues between the financial services industry and stakeholders in the investor realm so as to avoid ‘unnecessarily onerous requirements on financial institutions in terms of information provision’.¹⁰ As a result, complex financial products remained largely unregulated at the EU level and subject to the domestic laws of the various Member States.

The first EU law to specifically address complex financial products was the Markets in Financial Instruments Directive I (‘MiFID I’)¹¹; in addition to providing certain guidance on the legal notion of complex financial products, MiFID I established

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⁴ Policy documents and academic scholarship tend to use the terms ‘investor’, ‘consumer’, ‘client’ and ‘customer’ interchangeably. This article uniformly uses the term ‘investor’ to refer to clients or potential clients of firms that market, distribute and/or sell complex financial products. The dictionary definition of an investor as ‘someone who puts money in a bank, business, etc. in order to make a profit’ is consistent with the ‘consumers’ of complex financial products addressed in this article. For a discussion on the differences between the notions of a ‘retail investor’ and a ‘consumer of financial services’ see Moloney (2012).

⁵ Art. 25(4)(a) MiFID II.


⁷ Ibid., pp 4, 9. The Green Paper also contemplated the possibility of bringing commodity derivatives within the purview of the Community—ibid., p 11.

⁸ Célérier and Vallée (2014), pp 8, 10.


¹⁰ Ibid., pp 5–7.

obligations applicable to investment firms that provide investment services in relation to such products.\textsuperscript{12} The MiFID I regime on complex financial products was largely replicated by MiFID II,\textsuperscript{13} which amended and repealed MiFID I. MiFID II acknowledged the increasing participation of investors in financial markets and the greater complexity of the financial services and products being offered to them.\textsuperscript{14} Likewise, it noted that the financial crisis evidenced shortcomings in the functioning and transparency of the financial markets, which required reforms targeted at better protecting investors.\textsuperscript{15} MiFID II does indeed contain rules aimed at addressing various problems that may appear when investment firms offer financial products or services—notably, whenever these are complex—to investors, so as to guarantee the fairness and honesty of the former towards the latter.

First, because of their very own nature, complex financial products may aggravate information asymmetries between investment firms and their clients and, hence, lead to higher risks of misselling.\textsuperscript{16} Complexity and informational asymmetries may also exacerbate opportunistic behaviour by investment firms; for example, research shows that the advertisement of complex financial products often highlights their alleged benefits but downplays their potential risks.\textsuperscript{17} This may mislead investors about the nature of the product that they are purchasing and its associated risks. Thus, MiFID II requires investment firms to provide ‘fair, clear and not misleading’ information to their clients and to potential clients—e.g. through marketing communications.\textsuperscript{18} The scope of these disclosure duties refers, not only to the nature of the products and investment strategies being offered, but also to information about the investment firm and the services it provides, the venues used for execution, as well as the costs and charges associated with the relevant products and services.\textsuperscript{19} Disclosure obligations also incorporate a requirement of presenting the information in a comprehensible manner so as to guarantee that investors are able to understand the nature and risks of the investments and, hence, make informed investment decisions.\textsuperscript{20}

Second, complex financial products possess features which may render them inadequate for a number of potential investors. On the one side, they have a complex design, often involving derivatives instruments whose understanding requires specialized financial knowledge. On the other side, unlike most non-complex financial products, where losses are limited to the amount of the investment, complex

\begin{itemize}
  \item \textsuperscript{12} See e.g. Art. 19(6) MiFID I.
  \item \textsuperscript{13} Another relevant EU law adopted in that very same year was Regulation (EU) No. 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs) [2014] OJ L 352/1. PRIIPs are complex financial products and Regulation (EU) No. 1286/2014 addresses relevant aspects pertaining to their marketing, sale and distribution.
  \item \textsuperscript{14} Recital 70 MiFID II.
  \item \textsuperscript{15} Recital 4 MiFID II. Complex financial products, notably those that incorporate derivatives, played a major role in the global financial crisis—see e.g. Crotty (2009), pp 572–574.
  \item \textsuperscript{16} Financial Conduct Authority (FCA) (2017a), p 25.
  \item \textsuperscript{17} On this issue see e.g. Célérier and Vallée (2016), p 11.
  \item \textsuperscript{18} See e.g. Art. 24(3) MiFID II (Art. 19(2) MiFID I).
  \item \textsuperscript{19} See Art. 24(4) MiFID II (Art. 19(3) MiFID I).
  \item \textsuperscript{20} Art. 24(5) MiFID II (Art. 19(3) MiFID I).
\end{itemize}
financial products may lead to losses well beyond the original investment.\textsuperscript{21} MiFID II addresses this problem by requiring investment firms to assess whether the investments that they recommend and/or provide are adequate for their clients.\textsuperscript{22} The extent and scope of an investment firm’s obligations depends on the type of investment services offered as well as the nature of the products and services to which they relate. When an investment firm offers investment advice or portfolio management, it must carry out a suitability test that involves an analysis of the client’s relevant financial knowledge and experience, financial situation and investment objectives.\textsuperscript{23} The purpose of this test is to enable the investment firm to recommend investment products and services to the client that are suitable for its profile—particularly in respect of risk tolerance and resilience to losses.\textsuperscript{24} For other investment services, an investment firm is only required to assess the client’s relevant financial knowledge and experience, in order to determine whether the investment products or services offered are appropriate for the client (the appropriateness test)—issuing a warning to the client when a determination on appropriateness cannot be made, or if the product or service is found to be inappropriate.\textsuperscript{25} MiFID II generally exempts investment firms from the obligation to carry out the appropriateness test when they provide investment services merely consisting of the reception, transmission or execution of client orders,\textsuperscript{26} unless the latter relate to complex products,\textsuperscript{27} which are always subject to the suitability and/or appropriateness test.

Third, conflicts of interest may arise in the offer and sale of complex financial products, notably when the seller is the issuer of the product or the counterparty in the transaction.\textsuperscript{28} MiFID II requires investment firms to identify and avoid or manage conflicts of interest,\textsuperscript{29} and to act in the best interest of their clients.\textsuperscript{30} For example, inducement policies\textsuperscript{31} may incentivize investment firms to sell specific complex financial products to their clients, even when these are not the most suitable for them.\textsuperscript{32} MiFID II generally prohibits inducements, excluding those which may enhance the quality of the services provided to clients, are of a size and nature that do not impair the compliance of investment firms with their duty to act in the best interest of their clients, and are clearly disclosed to them.\textsuperscript{33} The duty to act in the

\textsuperscript{21} See e.g. ESMA and EBA (2013), p 3.
\textsuperscript{22} Art. 25 MiFID II.
\textsuperscript{23} Art. 25(2) MiFID II (Art. 19(4) MiFID I).
\textsuperscript{24} Art. 25(2) MiFID II.
\textsuperscript{25} Art. 25(3) MiFID II (Art. 19(5) MiFID I).
\textsuperscript{26} Art. 25(4) MiFID II (Art. 19(6) MiFID I).
\textsuperscript{27} Art. 25(4)(a)(vi) MiFID II (Art. 19(6) MiFID I).
\textsuperscript{28} See e.g. ESMA (2014a), p 4.
\textsuperscript{29} Art. 23 MiFID II (Art. 18 MiFID I).
\textsuperscript{30} Art. 24(1) MiFID II (Art. 19(1) MiFID I).
\textsuperscript{31} These relate to forms of remuneration, such as fees, commissions or monetary benefits, provided by a third party to an investment firm in relation to investments offered to clients—see e.g. CESR (2009a), p 5.
\textsuperscript{32} See e.g. FCA (2013), pp 9–10.
best interest of their clients also requires investment firms to execute orders in the terms that are most favourable to them.\textsuperscript{34} Order execution is, indeed, subject to the above-mentioned inducement prohibitions.\textsuperscript{35}

MiFID I and II relied substantially on regulatory and supervisory harmonization actions at the EU administrative level. The MiFID I Implementing Directive\textsuperscript{36} entrusted the Committee of European Securities Regulators (‘CESR’)\textsuperscript{37} with the adoption of guidelines aimed at guaranteeing a convergent application of MiFID I.\textsuperscript{38} CESR made active use of such delegation with regard to complex financial products, particularly by providing technical advice to the Commission on the concept, scope and types of complex financial products.\textsuperscript{39} The creation of ESMA in 2010, which took over the CESR’s functions but with an expanded mandate and powers, led to a greater centralization of regulatory and supervisory functions pertaining to complex financial products at the EU administrative level.\textsuperscript{40} Before 2018, ESMA’s work on complex financial products relied, primarily, on two types of mechanisms. On the one hand, ESMA made use of supervisory convergence instruments, such as questions and answers,\textsuperscript{41} guidelines,\textsuperscript{42} peer reviews,\textsuperscript{43} and opinions,\textsuperscript{44} aimed at building a common supervisory culture among the Member States as regards complex financial products. On the other hand, ESMA issued warnings addressed to investors aimed at highlighting the risks of complex financial products.\textsuperscript{45} In 2018, ESMA shifted its supervisory approach to complex financial products through the use of product intervention powers, which resulted in a series of temporary restrictions to the marketing, distribution and sale of two complex financial products, namely BOs and CFDs.\textsuperscript{46}

Footnote 33 (continued)
requirements and operating conditions for investment firms and defined terms for the purposes of that Directive [2006] OJ L 241/26).
\textsuperscript{34} Art. 27 MiFID II (Art. 21 MiFID I).
\textsuperscript{35} Art. 27(2) MiFID II.
\textsuperscript{36} Commission Directive 2006/73/EC.
\textsuperscript{38} Recital 12 MiFID I Implementing Directive.
\textsuperscript{39} See e.g. CESR (2005, 2009b).
\textsuperscript{41} See e.g. ESMA (2017a).
\textsuperscript{42} See e.g. ESMA (2016a).
\textsuperscript{43} See e.g. ESMA (2016b).
\textsuperscript{44} See e.g. ESMA (2014a).
\textsuperscript{45} See e.g. ESMA (2014b).
\textsuperscript{46} ESMA (2018a).
The next section examines ESMA’s work on complex financial products before 2018, with particular emphasis on the reasons for the failure of the model of supervisory convergence and investor warnings in achieving the objective of investor protection. This failure was one of the reasons alleged by ESMA to make use of its product intervention powers, which constitutes the focus of the analysis from Sect. 3 onwards.

2.1 ESMA’s Treatment of Complex Financial Products from 2010 to 2018: The Limitations of the Model of Supervisory Convergence and Investor Warnings

2.1.1 ESMA’s Supervisory Convergence Instruments and Their Limitations

Whilst both MiFID I and II brought about greater degrees of harmonization of the rules applicable to complex financial products and their supervision across the EU, they delegated important tasks to NCAs from the Member States. Despite ESMA’s efforts in achieving consistency and convergence in this area, the regulation and supervision of core aspects thereof remained largely decentralized and subject to diverging domestic rules and approaches. This, in turn, resulted in an inconsistent treatment of complex financial products and the emergence of forms of regulatory arbitrage.

First, as has been referred above in Sect. 2, MiFID II does not offer a straightforward definition of complex financial products. Instead, it provides a non-exhaustive list of non-complex financial products. A financial instrument not included in this list will be deemed as complex unless it fulfils certain criteria determined by the MiFID II Delegated Regulation. In this respect, MiFID II largely follows the approach of MiFID I, which sometimes resulted in inconsistencies across Member States. Whereas ESMA has been entrusted with the development of guidelines on the criteria to be used for the assessment of whether a financial product is complex or otherwise, its guidelines are non-binding and NCAs have some freedom to decide whether and how to implement them. More generally, the latter traditionally held different views about the nature of complex financial products and, more in particular, whether these were financial products or gambling products.

47 Art. 25(4)(a) MiFID II.
49 See e.g. European Banking Federation (2014), p 2.
50 See e.g. Art. 25(10)-(11) MiFID II.
51 See Art. 16(3) ESMA Regulation. For an example of ESMA’s guidelines on complex financial products see e.g. ESMA (2015a, 2016a).
52 For example, data on the implementation of ESMA’s Guidelines on complex debt instruments and structured deposits (2015a) shows that, as of 10 March 2020, there were still NCAs that had not implemented them; see ESMA (2020a).
53 For a discussion on the nature of certain complex financial products—investment, insurance or gambling—see e.g. Barnes (2019).
a number of years, the NCAs from Cyprus, Malta and the United Kingdom (‘UK’) considered certain complex financial products—e.g. binary options—to be gambling products and these were consequently under the oversight of gambling regulators and, hence, subject neither to the MiFID regime nor to Member States’ financial-sector laws. In 2012, the Cyprus Securities and Exchange Commission (‘CySEC’) included binary options among the list of financial instruments under its remit and took over the regulation of the providers of such products. The Malta Financial Services Authority (‘MFSA’) followed suit in 2013 and brought binary options under its supervision. In the UK, binary options were supervised by the Gambling Commission until 3 January 2018, when the FCA became their regulator.

Second, when it comes to supervision, both MiFID I and MiFID II give NCAs flexibility in how to comply with their supervisory obligations. This approach has the advantage of allowing for a supervision tailored to the domestic conditions in each Member State. However, at the same time, it bears the risk of an inconsistent application of EU law. An example of an area that has evidenced supervisory inconsistencies is the oversight of marketing communications of investment firms to clients. Article 19(2)-(3) of MiFID I defined clearly the obligations of investment firms with respect to market communications but did not provide indications of how NCAs were expected to monitor compliance with them. Although Article 19 of MiFID I entrusted the Commission with the development of implementing measures aimed at guaranteeing its ‘uniform application’, the Commission’s implementing Directive did little to clarify the role of NCAs in respect of marketing communications. This led to very different supervisory approaches with a potential impact on investor protection. For instance, whereas in some Member States NCAs pre-approved all marketing communications relating to products offered to the public, in others such pre-screening only related to marketing communications of complex products. Also, in the majority of Member States, the review was ex-post and potentially limited in scope—e.g. limited to instances when there were suspected irregularities. Although ESMA clarified important aspects pertaining to the role of NCAs in the oversight of marketing communications, MiFID’s non-prescriptive

54 CySEC (2012).
55 MFSA (2013).
56 FCA (2017b, 2018).
57 See e.g. Art. 21(2) MiFID II: ‘Member States shall require competent authorities to establish the appropriate methods to monitor that investment firms comply with their obligation […]’—with regard to the monitoring of compliance with the conditions for initial authorization of investment firms (see also Art. 16(2) MiFID I).
58 See e.g. ESMA (2014c), p 12.
59 See also Art. 24(3)-(4) MiFID II.
60 ‘Nothing in this Directive requires competent authorities to approve the content and form of marketing communications. However, neither does it prevent them from doing so […].’ Recital 43, MiFID I Implementing Directive (see also recital 62 of MiFID II Delegated Regulation).
62 Ibid.
63 See e.g. ESMA (2017a), p 39.
approach in this area limited substantially the ability of ESMA to contribute to the consistency of NCAs’ supervisory approaches across the EU.

The variation in supervisory practices across the EU may have, in turn, propitiated some regulatory arbitrage whereby firms offering complex financial products have incorporated in jurisdictions that were perceived as less stringent in terms of supervision and enforcement. For example, within the EU, one of the main jurisdictions of incorporation of these firms is Cyprus. ESMA’s (2014a) peer review of supervisory practices concerning MiFID’s rules on ‘Conduct of Business, fair, clear and not misleading information’ identified the CySEC as the NCA from the EU that was least compliant with good supervisory practices; for instance, of the five criteria assessed in the review, the CySEC was found non-compliant in four of them. According to ESMA, the main weaknesses of the CySEC’s supervisory approach related to, among others, an excessive focus on prudential, rather than conduct-of-business, matters, a non-intrusive approach to supervision and an inefficient sanctioning regime which relied excessively on name-and-shame but largely dismissed deterrent pecuniary sanctions. ESMA’s peer review also noted that the CySEC’s on-site inspections with regard to market communications were conducted ‘only on a limited and ad hoc basis and […] [did] […] not benefit of a regular planning prompted by predefined criteria’. Whereas in a follow-up report published in 2017, ESMA acknowledged some improvements in the frequency of monitoring market communications by CySEC, it also expressed concerns about the effectiveness of such measures, noted the continuing presence of aggressive marketing communications by investment firms, and questioned the ability of CySEC to exercise adequate monitoring of marketing materials.

### 2.1.2 ESMA’s Investor Warnings and Their Limitations

Since its inception, ESMA has been making use of warnings to caution investors about, among others, the risks of investing in complex speculative financial products. ESMA has the power to issue warnings to investors when it deems that a financial activity poses a serious threat to any of its objectives, which include, among others, the protection of the public interest and the enhancement of investor protection.

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64 See e.g. Financial Times (2015)—reporting that, of 73 firms using single passport rights to provide forex in the UK, 54 were based in Cyprus.
65 ESMA (2014c).
66 The criteria addressed in the peer review related to the approaches of NCAs with regard to their organization, supervisory stances, monitoring, thematic reviews, and complaints by investors—ibid., pp 16-18.
67 Ibid., p 15.
68 Ibid., p 27.
69 ESMA (2017b), pp 8–9.
70 Art. 9(3) ESMA Regulation.
71 Art. 1(5) ESMA Regulation.
The focus of ESMA’s warnings has been on complex, speculative, highly risky financial products that are offered to retail investors. ESMA’s first product-related warnings, issued in 2011 and 2013, addressed forex and CFDs respectively. In 2014, ESMA published a general warning on complex financial products, which largely replicated the concerns previously expressed by the EU regulator with respect to forex and CFDs.

The increase in the offer of complex speculative financial products and in the number of complaints by investors who experienced losses after investing in them led to another warning being issued by ESMA in 2016. According to ESMA, these products are a threat to investor protection for various reasons. First, they are highly risky and, very often, they result in investors losing their invested money; for example, a study published in 2014 by the Polish Komisja Nadzoru Finansowego (‘KNF’) showed that, in 2013, 81% of clients of online forex trading platforms suffered a loss; similarly, a study published in the same year by the French Autorité des Marchés Financiers (‘AMF’) evidenced that, in the years 2009–2013, 89.4% of forex providers’ clients and CFD trading experienced a loss—with an average value of Euro 10,887 per client.

Second, they are non-standardized, complex products, whose features and risk may be difficult to understand by retail investors. Third, they are often advertised, marketed and offered to investors—including through online platforms—without providing adequate information and/or advice on their risks. Fourth, some providers of complex speculative financial products are unauthorized and unregulated. Finally, ESMA pointed out that providers of these products are sometimes subject to major conflicts of interest, i.e. when their profits are positively correlated to investor losses.

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72 ESMA (2011a). This warning adverted investors of the risks that may source from the potentially complex, volatile and leveraged nature of forex transactions, as well as those resulting from the misleading advertisement of forex investments and from unsafe forex trading platforms or systems.
73 ESMA and EBA (2013). With this warning, ESMA and EBA warned investors about, among others, the potential liquidity, leverage, execution and counterparty risks associated with CFDs.
74 ESMA (2014b).
75 The core messages of the warning were the following: ‘If you do not understand the key features of the product being offered, or the key risks involved, do not invest. Instead, consider seeking professional advice on what investment is suitable for you. Be aware that sometimes the name of a product may not reflect the features of the product. Be wary of promises of “high”, “guaranteed”, “hedged” or “absolute” returns. These promises often turn out to be misleading. Be careful if you need to access your money before the product is due to pay out. Before you invest, understand what the total costs are. The cost of an investment will impact the return you are likely to achieve. Also, there may be similar, less complex products—with lower costs—available’—ibid., p 1.
76 ESMA (2016c).
77 Ibid., p 1.
78 KNF (2014).
82 Ibid., p 1.
83 Ibid., p 1.
84 Ibid., p 2.
ESMA’s actions complemented warnings issued by NCAs at the Member State level, particularly in relation to unauthorized providers of complex speculative financial products.\(^{85}\) Despite the intensity of ESMA’s and NCAs’ efforts over the years to warn investors of the dangers of these products, data seems to suggest that warnings may have had insufficient deterring effects on investors. In France, the AMF has reported an exponential growth, over the years, in the number of unauthorized platforms offering complex speculative financial products as well as of related investor complaints.\(^{86}\) Likewise, in 2016, the UK’s FCA reported a rise in the number of firms offering CFDs\(^{87}\) and, in 2017, the Belgian Financial Services and Markets Authority (‘FSMA’) received 792 messages—questions or complaints—from investors regarding fraud and unlawful offers of financial services and products; this represented a 45% increase with respect to the previous year—164 of those messages concerned binary options.\(^{88}\)

### 3 Product Intervention: The Political Economy and Constitutionality of ESMA’s Residual Lawmaking

From its inception, ESMA has been given intervention powers, namely the authority to impose temporary\(^{89}\) prohibitions or restrictions concerning financial activities—this concept being broadly understood—that pose a threat to financial stability or to the good functioning of the financial markets in the EU.\(^{90}\) Ordinarily, ESMA can only exercise those powers whenever this is envisaged by specific financial-sector EU laws and according to the conditions set therein.\(^{91}\) Article 40(1) of MiFIR embraces this possibility by giving ESMA intervention powers to temporarily restrict or prohibit the advertisement, sale or distribution of specific financial instruments, activities or practices. The use of such powers is subject to strict conditionality and requires, in the first place, that the intervention measure addresses ‘a significant investor protection concern or a threat to the orderly functioning and integrity of financial markets or commodity markets or to the stability of the whole or part

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\(^{85}\) For example, in January 2018, the FCA published a list of 94 firms that offered binary options to UK investors without having an FCA authorization to do so—as required by UK law; see FCA (2018).

\(^{86}\) AMF (2016).

\(^{87}\) FCA (2016).

\(^{88}\) FSMA (2018).

\(^{89}\) Art. 9(5) ESMA Regulation; according to Art. 40(6) MiFIR, ESMA must review the product intervention decisions ‘at appropriate intervals and at least every 3 months’. If ESMA does not renew the product intervention decision, then the underlying prohibition or restriction expires. Art. 4 Regulation 2019/2175, which will apply from 1 January 2022, has expanded the temporal scope of ESMA’s MiFIR product intervention measures: ‘ESMA shall review a prohibition or restriction […] at appropriate intervals, and at least every six months. Following at least two consecutive renewals and based on proper analysis in order to assess the impact on the consumer, ESMA may decide on the annual renewal of the prohibition or restriction’.

\(^{90}\) Art. 9(5) ESMA Regulation.

\(^{91}\) Ibid.
of the financial system in the Union\textsuperscript{92}; second, that ‘regulatory requirements under Union law that are applicable to the relevant financial instrument or activity do not address the threat’\textsuperscript{93}; and, third, that ‘a competent authority or competent authorities have not taken action to address the threat or the actions that have been taken do not adequately address the threat’\textsuperscript{94}.

In a statement published in June 2017, ESMA argued that supervisory convergence mechanisms had failed to effectively guarantee investor protection in the sale and purchase of BOs\textsuperscript{95}, CFDs\textsuperscript{96}, as well as other speculative products, and raised the possibility of using product intervention measures to address this failure.\textsuperscript{97} This statement, which implicitly suggested certain limitations to the MiFID’s regime in protecting investors in complex financial products, started to pave the way for the future use of intervention powers. This was followed by the launch, on 18 January 2018, of a call for evidence where ESMA asked stakeholders about their views on potential product intervention measures.\textsuperscript{98} Although a number of respondents representing industry providers criticized the proposed measures and their potential impact on their business activities,\textsuperscript{99} ESMA contended that there persisted a significant threat to investor protection which made it necessary to introduce temporary prohibitions concerning the marketing, distribution and sale of BOs and CFDs.\textsuperscript{100} ESMA introduced such prohibitions on 22 May 2018, through two product intervention decisions (‘ESMA’s Product Intervention Decisions’), one concerning BOs (‘ESMA Decision on BOs’)\textsuperscript{101} and another pertaining to CFDs (‘ESMA Decision on CFDs’).\textsuperscript{102} These decisions, which were periodically renewed every 3 months,

\textsuperscript{92} Art. 40(2)(a) MiFIR.
\textsuperscript{93} Art. 40(2)(b) MiFIR.
\textsuperscript{94} Art. 40(2)(c) MiFIR.
\textsuperscript{95} ESMA defines a binary option as ‘any cash settled derivative in which the payment of a fixed monetary amount depends on whether one or more specified events in relation to the price, level or value of the underlying occurs at, or prior to, the derivative’s expiry’; see para. 9 ESMA Decision on BOs (\textit{infra} n. 101). In BOs, the payout depends on the fulfilment of a yes/no proposition, such as whether an underlying financial instrument will exceed a given price on a given date; see Securities and Exchange Commission (2013), p 1.
\textsuperscript{96} ESMA defines CFDs as ‘cash settled derivative contracts, the purpose of which is to give the holder an exposure, which can be long or short, to fluctuations in the price, level or value of an underlying’; see para. 8 ESMA Decision on CFDs (\textit{infra} n. 102).
\textsuperscript{97} ESMA (2017c).
\textsuperscript{98} ESMA (2018b).
\textsuperscript{99} Para. 4 ESMA Decision on BOs; para. 3 ESMA Decision on CFDs.
\textsuperscript{100} Para. 5 ESMA Decision on BOs; para. 4 ESMA Decision on CFDs.
until July 2019, \(^{103}\) constituted the first instances when ESMA made use of its MiFIR product intervention powers.

The next sections apply the concepts of incomplete law, residual lawmaking, signalling and the principal-agent relationship with an informed principal, to examine and assess the political economy and role of ESMA in a product intervention process. This analysis reveals that ESMA uses product intervention as a tool for signalling its preferences to both the EU legislator and to NCAs. Although, in many respects, product intervention constitutes an effective signalling and regulatory tool, the process of adoption and the content of ESMA’s Product Intervention Decisions raises important questions about their constitutionality.

### 3.1 The Political Economy of ESMA’s Decisions (I): Product Intervention and Incomplete Law

The last decade has witnessed major EU legislative harmonization efforts with respect to financial services. These largely constituted a response to the global financial crisis and its pernicious effects on financial stability and investor protection. \(^{104}\) MiFID II and MiFIR constitute examples of EU financial-sector laws that have led to a much more comprehensive regime on investor protection. \(^{105}\)

Despite the intensity of legislative activity and the increasing harmonization of financial rules post-crisis, EU financial-sector laws remain highly incomplete. An incomplete law is defined as one that does not ‘unambiguously stipulate(s) for all future contingencies’. \(^{106}\) On the one side, incompleteness is an intrinsic feature of directives and regulations in the financial realm; financial market relationships and transactions often involve a great deal of complexity and, consequently, EU laws cannot predict and give a solution to all the problems that may occur in them. On the other side, the EU financial services architecture acknowledges and embraces the notion of the incompleteness of the law by establishing a system of delegating rulemaking tasks to the European Supervisory Authorities (‘ESAs’). \(^{107}\) Such a system is, to a great extent, aimed at complementing and completing the EU financial services legislative framework through rules made by specialized agencies in the financial field. \(^{108}\) For example, ESMA is tasked with the creation of draft standards that develop important technical aspects of EU financial-sector laws. \(^{109}\) In addition,

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\(^{103}\) The product intervention decisions regarding BOs were the following: (EU) 2018/795, (EU) 2018/1466, (EU) 2018/2064 and (EU) 2019/509. The product intervention decisions on CFDs were the following: (EU) 2018/796, (EU) 2018/1636, (EU) 2019/155 and (EU) 2019/679. The last applicable decisions on BOs and CFDs expired on 1 July and 31 July 2019, respectively; see ESMA (2019b, c).

\(^{104}\) For an analysis of the main post-crisis reforms and their rationale see e.g. House of Lords European Union Committee (2015).

\(^{105}\) An extensive analysis of MiFID II’s investor protection-related provisions is provided by Gortsos (2018).

\(^{106}\) Pistor and Xu (2003), p 932.

\(^{107}\) The ESAs are EU agencies with decision-making powers; see Chiti (2013), p 95.

\(^{108}\) See e.g. recitals 21, 22 and 24 ESMA Regulation.

\(^{109}\) Arts. 10-15 ESMA Regulation.
ESMA plays a central role in the promotion of regulatory and supervisory convergence by developing guidelines and recommendations addressed to Member State NCAs or financial market participants.\footnote{110 Art. 16 ESMA Regulation.}

Product intervention constitutes a form of residual lawmaking\footnote{111 Pistor and Xu (2003), p 933, define ‘residual law ‑ making’ as the ‘power to interpret existing law, to adapt it to changing circumstances, and to extend its application to new cases’.} by ESMA. The core underlying rationale for granting ESMA such authority lies in the incompleteness of EU financial laws. If and when EU law is unable to foresee and effectively tackle problems affecting investor protection, product intervention powers allow ESMA to step in and overcome such incompleteness through an intervention decision; the latter may establish a ban on certain products or restrictions on their offer and sale. Although product intervention is subject to strict conditionality, it gives quasi-lawmaking powers to ESMA. First, unlike draft technical standards, guidelines and recommendations, which do not have binding force,\footnote{112 Guidelines and recommendations do not have binding force; see Art. 16(3) ESMA Regulation. Draft technical standards are not binding per se although they may be adopted by the Commission by means of regulations or decisions, therefore becoming binding; see Arts. 10(4) and 15(4) ESMA Regulation.} product intervention is binding—albeit on a temporary basis—on market participants.\footnote{113 Art. 9(5) ESMA Regulation.} In comparison to ESMA’s other rulemaking mechanisms, product intervention has a more pervasive scope and implications; whilst standards, guidelines and recommendations are primarily aimed at developing or clarifying aspects of the law,\footnote{114 See e.g. Art. 8(1)(a) ESMA Regulation.} product intervention allows ESMA to make policy choices—in the form of prohibitions and restrictions—that largely substitute, rather than develop, the law. Through product intervention, ESMA replaces a legislative choice, namely an explicit or implicit authorization to carry out a given financial activity or to market, distribute or sell a certain financial product, with a regulatory choice, namely a ban or restriction on that activity or product; whereas such a regulatory choice is authorized by the legislator through a conditional delegation to ESMA, it largely overcomes the legislator’s initial choice, and, in doing so, it embraces certain degrees of economic policy.

From the onset, the allocation of intervention powers to ESMA has been a matter of controversy, not equally welcomed by the different Member States. Notably, in 2012, the UK challenged the constitutionality and sought the annulment\footnote{115 Action brought on 1 June 2012—United Kingdom of Great Britain and Northern Ireland v. Council of the European Union, European Parliament (Case C‑270/12) [2012] OJ C 273/3, Application Short‑Selling case.} of Article 28 of the Short‑Selling Regulation,\footnote{116 Regulation (EU) No. 236/2012 of the European Parliament and of the Council of 14 March 2012 on short selling and certain aspects of credit default swaps [2012] OJ L 86/1.} which gives ESMA intervention powers in respect of short‑selling, including the power to prohibit it in certain scenarios and subject to strict conditions. In order for ESMA to use such intervention powers, two conditions must be satisfied. First, there must be a threat to the proper functioning of the financial markets or to the stability of the financial system of the EU
or parts thereof and with cross-border consequences. A second condition is that NCAs have not taken measures to address such a threat or that the measures adopted by them do not properly address it. In addition, when adopting short-selling prohibitions or restrictions, ESMA must consider, among others, whether those measures significantly tackle the relevant threat, do not lead to regulatory arbitrage, and are proportionate. The UK argued, *inter alia*, that ESMA enjoyed wide margins of discretion in the assessment of the occurrence of the conditions for the exercise of intervention powers and in the determination of the actual content of the intervention measures, and claimed that this entailed ESMA making economic policy choices. This, in turn, was according to the UK in breach of, among others, the *Meroni* principles and, hence, was unconstitutional.

In the *Meroni* case, one of the core issues at stake regarded the validity of a delegation of powers by the High Authority of the European Coal and Steel Community to the Joint Bureau of Ferrous Scrap and the Imported Ferrous Scrap Equalization Fund—jointly referred to as the ‘Brussels agencies’—for the putting into effect of financial arrangements concerning the supply of ferrous scrap for the Community’s Common Market. The applicant, Meroni & Co., contended *inter alia* that such delegation was illegal on the grounds that the High Authority delegated those powers, attributed to it by the Treaty establishing the European Coal and Steel Community, without conditioning their exercise by the Brussels agencies to the requirements that the Treaty would impose on the High Authority if it had exercised such powers directly. More generally, Meroni & Co. contended that the High Authority delegated powers to agencies which were ill-qualified to exercise them. As regards Meroni & Co.’s first claim, which concerned the way in which the delegation of powers was done, the Court of Justice determined that Community Institutions cannot delegate to agencies powers that they do not themselves have. In the view of the Court of Justice, the High Authority’s delegation gave...
the Brussels agencies more extensive powers than those held by the High Authority under the Treaty and, hence, such delegation was unconstitutional.\(^{128}\) When it comes to Meroni & Co.’s second claim, which addressed the extent of the delegation of powers, whilst the Court of Justice argued that it was lawful for the High Authority to delegate certain powers to third parties with distinct legal personality, such as the Brussels agencies,\(^{129}\) it also determined that such delegation must respect two important interrelated conditions. First, the delegation must be limited to ‘clearly defined executive powers the exercise of which can, therefore, be subject to strict review in the light of objective criteria determined by the delegating authority’.\(^{130}\) Second, as a result of the first condition, it is not possible to delegate a ‘discretionary power, implying a wide margin of discretion which may […] make possible the execution of actual economic policy’,\(^{131}\) the reason being that such delegation would result in a transfer of responsibility whereby the choices made by the delegator—i.e. the EU Institution—would be replaced by the choices made by a delegate—e.g. an EU agency.\(^{132}\) After assessing the delegation of powers to the Brussels agencies, the Court of Justice determined that this gave them a degree of leeway which encompassed wide margins of discretion and, hence, was unconstitutional and in breach of the principle of institutional balance.\(^{133}\)

Turning back to the *Short-Selling* case, the Court of Justice of the European Union (CJEU) did not uphold the UK’s arguments and instead contended that ESMA’s intervention powers as regards short-selling did not infringe the *Meroni* principles because those powers are clearly delineated in the Short-Selling Regulation,\(^{134}\) their exercise is subject to strict conditionality,\(^{135}\) and they are ‘amenable to judicial review’.\(^{136}\) From the point of view of the delegation doctrine, the CJEU’s decision was significant because, although it confirmed the core *Meroni* principles and rules, it nonetheless embraced their loosening,\(^{137}\) and a new paradigm whereby EU agencies may be delegated discretionary powers to adopt legally binding decisions with general application, as long as there are proper limits to the exercise of

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\(^{128}\) Ibid., p 150.

\(^{129}\) Ibid., p 151.

\(^{130}\) Ibid., p 152. According to Simoncini (2018a, p 27), through this requirement the Court of Justice indicated two core elements that must bind the exercise of administrative powers, namely discretion and accountability.

\(^{131}\) *Meroni* case, p 152.

\(^{132}\) Ibid.

\(^{133}\) Ibid., pp 152, 154. See also Lintner (2017), p 607. According to Majone (2001, pp 7–11) the principle of institutional balance indeed constituted one of the central elements behind the Commission’s traditionally strict interpretation of the non-delegation doctrine.

\(^{134}\) Case C-270/12 United Kingdom of Great Britain and Northern Ireland v. Council of the European Union, European Parliament, ECLI:EU:C:2014:18 (Short-Selling case), paras. 51 and 53.

\(^{135}\) *Short-Selling* case, paras. 47–50 and 52.

\(^{136}\) *Short-Selling* case, para. 53.

such discretion.\textsuperscript{138} In doing so, the CJEU operated an update and adaptation of Meroni to the post-Lisbon Treaty institutional and constitutional setting, in which the criteria for the allocation and delegation of powers to EU agencies became Treaty-based, hence tackling some of the concerns the Court of Justice had to address at the time of the Meroni ruling.\textsuperscript{139} From an operational standpoint, the CJEU’s decision in the \textit{Short-Selling} case widened the scope of ESMA’s use of delegated powers.\textsuperscript{140} Some scholars have pointed out that Meroni had over time become obsolete\textsuperscript{141} and untailored to the reality and scope of the tasks allocated to the ESAs, which require the exercise of important degrees of discretion.\textsuperscript{142} Hence, from this viewpoint, the relaxation of Meroni resulting from the CJEU’s decision in the \textit{Short-Selling} case may contribute to the ESAs’ functional operativity. Whilst this may have some advantages, it also poses some challenges regarding the legitimacy of ESMA’s decisions, notably, when the latter embrace the exercise of far-reaching discretionary powers. An important concern in this respect is that the accountability mechanisms applicable to ESMA may not be tailored to properly address extensive uses of discretion by it.\textsuperscript{143}

In light of the potential extensive uses that ESMA may make of its powers, an important question is how to guarantee that whenever it does so, ESMA respects the core underlying principles of Meroni. However, whilst the CJEU’s decision in the \textit{Short-Selling} case provided some clarifications as regards the scope of the Meroni restrictions, the judgement was rather vague.\textsuperscript{144} More importantly, the CJEU only addressed the legality of the delegation of intervention powers to ESMA, but it did not provide any criteria as to how to assess whether specific uses of those powers by ESMA are within the scope of the Meroni restrictions.

Intervention powers enable but do not require ESMA to take action. If ESMA finds that the conditions for product intervention apply to a given case, it can discretionally decide whether to adopt such measures or not.\textsuperscript{145} Whilst the decision of ESMA to intervene in the market on certain complex financial products evidenced a proactive and assertive approach by the EU regulator in the field of investor protection, the decisions’ timing, context and substance do however raise some questions as regards the underlying motivations of ESMA in adopting them as well

\begin{itemize}
\item \textsuperscript{138} The CJEU’s decision embraced an expansive interpretation of the scope of delegation under Meroni which may lead to more extensive delegations of regulatory powers to EU agencies; see Kelemen (2018), p 86. Scholten and van Rijssbergen (2014) indeed speak of a ‘New Delegation Doctrine’.
\item \textsuperscript{139} Nitszke (2018), p 217; Simoncini (2018b), p 171; Gabbi (2014).
\item \textsuperscript{140} Moloney (2019), p 90. Van Cleynenbreugel (2014, p 78) claims that, with its decision, the CJEU confirmed that it is possible to give discretionary powers to an EU supranational agency, such as ESMA, on the grounds of an operational support rationale.
\item \textsuperscript{141} See e.g. Pelkmans (2008), pp 40–41.
\item \textsuperscript{142} See e.g. Moloney (2019), pp 90–91; Nicolaides and Preziosi (2014), p 22. Chiti (2015, pp 316–317) advocates a non-restrictive interpretation of Meroni that allows the ESAs to exercise proper degrees of discretion and, hence, to fully exploit their qualities as highly specialized regulators.
\item \textsuperscript{143} Moloney (2019), p 91.
\item \textsuperscript{144} See e.g. Howell (2014), p 472.
\item \textsuperscript{145} Art. 9(5) ESMA Regulation and Art. 40(1)-(2) MiFIR. The only exception is emergency situations, where ESMA may be required to take action—Arts. 9(5) and 18 ESMA Regulation.
\end{itemize}
3.2 The Political Economy of ESMA’s decisions (II): Product Intervention as a Signalling Mechanism

From the very onset, the European System of Financial Supervision (‘ESFS’) has been conceived as an experimental network with a flexible governance structure to be reviewed and adapted according to its performance. The De Larosière Report\(^{146}\) recommended periodical assessments of the ESFS and foresaw the possibility of a future shift from the three-pillar sectoral approach—with three ESAs\(^{147}\)—to an EU twin-peaks model of financial supervision, with two ESAs, one in charge of banking and insurance prudential supervision and another entrusted with conduct of business supervision across the three financial sectors.\(^{148}\) Both the European Parliament’s (‘Parliament’) and the Commission’s reviews of the ESAs in 2013\(^{149}\) and 2014,\(^{150}\) respectively, acknowledged that the ESAs’ three-pillar governance model had some advantages\(^{151}\) and led to positive results\(^{152}\); however, they also recognized that certain developments at the EU level\(^{153}\) could in the future justify the adoption of a twin-peaks model or, even, an EU single supervisor.\(^{154}\)

ESMA has usually responded to the discussions and debates about its future with regulatory and supervisory assertiveness and reactiveness. Since its inception, ESMA has been proclaiming the importance of its role within the ESFS;\(^{155}\) it has also repeatedly demanded the need for an expansion of its powers in order to properly exercise its functions.\(^{156}\) ESMA has been keen to assume direct supervisory

\(^{146}\) The High-Level Group on Financial Supervision in the EU (2009).
\(^{147}\) Namely the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA). On the ESAs and their role within the ESFS see Wymeersch (2011).
\(^{148}\) The High-Level Group on Financial Supervision in the EU (2009), p 58.
\(^{150}\) European Commission (2014).
\(^{151}\) For example, in the view of the Commission, the three-pillar model ‘takes into account all elements of the financial services sector’; see European Commission (2014), p 11. The Parliament pointed out that EU financial-sector laws are largely organized along sectoral lines and, therefore, the three-pillar model seemed appropriate and consistent with such a legislative approach; see European Parliament (2013), p 111.
\(^{153}\) Such as the increasing trend towards the adoption of an EU regulatory model based on two objectives of financial supervision, namely investor protection and financial stability—see European Parliament (2013), pp 111-112—or the creation of the Banking Union—see European Commission (2014), p 11.
\(^{155}\) See e.g. ESMA (2011b).
\(^{156}\) See e.g. ESMA (2016e), pp 6, 9; ESMA (2017d), p 2.
competences and has proven to be a very active supervisor in terms of monitoring and enforcement.\textsuperscript{157}

The discussions about the ESAs’ governance gained momentum with Brexit. The latter required the relocation of the London-based EBA\textsuperscript{159} and, in the view of some commentators, this offered an opportunity to rethink the EBA’s future and, more generally, the ESFS’s governance arrangements.\textsuperscript{160} Against this background, a Commission Consultation in March 2017\textsuperscript{161} put forward the idea of a potential merger between EBA and EIOPA—the resulting entity becoming an EU prudential supervisor—and an expansion of the powers of ESMA in the field of investor protection.\textsuperscript{162} On the one side, EBA and EIOPA expressed their scepticism about the proposed framework, arguing that the three-pillar model had been working well,\textsuperscript{163} that banking and insurance required tailor-made supervision by separate entities\textsuperscript{164} and, also, that instead of merging EBA and EIOPA, there should be a strengthening of the cooperation between the three ESAs, particularly through the work of the Joint Committee.\textsuperscript{165} On the other side, ESMA, which would become an EU conduct of business supervisor with strengthened powers, welcomed the proposals.\textsuperscript{166} In September 2017, the Commission published a legislative proposal (‘Commission Proposal’)\textsuperscript{167} that provided for an extensive enlargement of ESMA’s powers—e.g. ESMA would receive direct supervision powers in areas such as prospectuses and benchmarks.\textsuperscript{168} The possibility of a widening of ESMA’s powers, as proposed by the Commission, led to a stiff reaction by the Parliament and some Member States which saw, in the Commission Proposal, an undue and excessive centralization of supervisory powers at the EU level.\textsuperscript{169}

The substance and timing of ESMA’s product intervention must be interpreted in the context of the Commission Proposal, and, in light of the likely opposition of the Parliament and the Council to the expansion of the powers of ESMA. In this respect, ESMA’s product intervention can be interpreted as a signalling mechanism\textsuperscript{170} aimed

\begin{footnotesize}
\textsuperscript{157} See e.g. ESMA (2017e), p 3: ‘ESMA stands ready to assume any new supervisory tasks should they be assigned to ESMA’.\textsuperscript{158}

\textsuperscript{158} For example, from October 2016 to September 2017, ESMA issued 23 draft technical standards, 15 guidelines, 108 opinions, advice and decisions, and published 320 questions and answers; see ESMA (2017f). More recent data, from the period between October 2019 and October 2020—15 draft technical standards, 9 guidelines, 274 opinions, advice, decisions and no-action letters, and 67 questions and answers—shows that ESMA continues to be a rather dynamic supervisor; see ESMA (2020b).

\textsuperscript{159} See e.g. Council of the European Union (2017), p 3.

\textsuperscript{160} See e.g. Schoenmaker and Véron (2017).

\textsuperscript{161} European Commission (2017a).

\textsuperscript{162} Ibid., pp 21–22.

\textsuperscript{163} EBA (2017), pp 2–3; EIOPA (2017), p 1.

\textsuperscript{164} EBA (2017), p 2; EIOPA (2017), pp 1–2.


\textsuperscript{166} ESMA (2017e), p 3.

\textsuperscript{167} European Commission (2017b).

\textsuperscript{168} For an overview of the main proposed changes see e.g. European Commission (2017c).

\textsuperscript{169} See e.g. Politico (2018); IFLR Practice Insight (2018).

\textsuperscript{170} In economics, signalling refers to actions taken by some players in order to convey information (not necessarily accurate or true) to other players so as to influence their behaviour in a way which is beneficial for the former; see Wilkinson and Klaes (2018), p 381.
\end{footnotesize}
at influencing the EU legislator’s views regarding the financial architecture and ESMA’s powers.

On the one side, ESMA’s Product Intervention Decisions convey a notion of the inefficiency of both EU and Member States’ laws in tackling problems pertaining to investor protection that may arise in the marketing, distribution and sale of complex financial products. At the same time, it portrays ESMA’s regulatory intervention as a superior tool for dealing with such problems. ESMA’s Product Intervention Decisions highlighted, in strong terms, alleged failures of the EU legislative framework and of Member States’ product intervention measures, it also stressed the consequential need for ESMA’s regulatory intervention so as to overcome such failures. The assessment of normative efficiency is an area where there are major informational asymmetries. Whilst ESMA, as a specialized agency in the financial field, possesses extensive knowledge and means to assess the quality, efficiency and effectiveness of EU and Member States’ laws and actions with respect to complex financial products, the Parliament lacks such a degree of technical expertise and largely relies on the work and views of ESMA in this respect. Such informational asymmetries may be strategically exploited by ESMA as a way to justify product intervention and assert the importance of its role in investor protection.

On the other side, ESMA’s Product Intervention Decisions convey a message of supervisory readiness and stringency in the realm of investor protection. This has been an area of particular concern for the Parliament, which has, on occasions, criticized the Commission’s approach, deeming it insufficient and inadequate to properly protect investors. By intervening in a market with major problems and concerns relating to investor protection—as is the case of the market for complex financial products—ESMA signals its willingness to assume a leading role in the field; also, at the same time, ESMA’s product intervention indicates a certain alignment of the EU supervisor with the Parliament’s views.

Whereas the Commission Proposal was watered down throughout the various stages of the legislative process, the text agreed by the Parliament and the Council

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171 For example, in relation to MiFID II, ESMA argued that: ‘disclosure-based rules alone—including improved information on costs—are clearly insufficient to tackle the complex risk arising from the marketing, distribution or sale of CFDs to retail clients’; para. 56 ESMA Decision on CFDs. As regards Member States’ measures, ESMA claimed that: ‘even though these measures have had some effects, the significant investor protection concern persist’; para. 77 ESMA Decision on CFDs.

172 See e.g.: ‘ESMA’s overall measure is necessary and proportionate to address the investor protection concern identified. In general, it is expected that it will reduce abnormal and significant losses experienced by retail clients on CFDs as well as enhance retail clients’ awareness of the risks related to these products’; para. 142 ESMA Decision on CFDs.

173 For example, ESMA issues opinions addressed to the Parliament (Art. 16a ESMA Regulation); see e.g. ESMA (2015b). Also, ESMA reports to the Parliament on trends, potential risks and vulnerabilities in its areas of competence (Art. 32(1) ESMA Regulation). In addition, ESMA’s Chairperson may be called to Parliamentary hearings to provide explanations and answer questions (Art. 3(4) ESMA Regulation); see e.g. ESMA (2016f).

174 See e.g. European Parliament (2016)—regarding the Parliament’s refusal to back the Commission’s proposals in the field of PRIIPs.
on 18 December 2019\textsuperscript{175} gave ESMA important powers in areas of central relevance for investor protection; for instance, on 1 January 2022, ESMA will become the direct supervisor of certain data reporting service providers, critical benchmarks, and third country benchmarks.\textsuperscript{176} This evidences the commitment of the Parliament and the Council to progressively strengthen ESMA’s investor protection role, in line with ESMA’s demands.

There are various elements that support the hypothesis about ESMA’s use of product intervention as a signalling mechanism.

First, ESMA’s Product Intervention Decisions were adopted without strong overall support from the stakeholder community. Whereas representatives from the investor realm generally supported ESMA’s measures,\textsuperscript{177} other groups expressed concerns about the prohibitions and/or their scope. Opposition came not only from the complex products industry,\textsuperscript{178} but also from other market participants. For example, while generally agreeing with product intervention, the Federation of European Securities Exchanges (‘FESE’) claimed that ESMA’s definition of certain complex products was too broad and that, as a result, it could ‘unwittingly capture financial instruments which ESMA did not intend to subject to additional investor protection measures’.\textsuperscript{179}

Second, ESMA’s decision was swift and somewhat premature, and was adopted less than 3 months after the entry into application of MiFID II and MiFIR. As has been explained, the former establishes a new regime applicable to investment services and financial products—including complex financial products; the latter gives ESMA product intervention powers. By intervening in the market for complex financial products immediately after the entry into application of MiFIR, ESMA was unable to observe the effects of the MiFID II’s regime on investor protection. The swiftness and timing of ESMA’s product intervention was indeed against the advice of ESMA’s Securities and Markets Stakeholder Group (‘SMSG’); in an own initiative opinion published on 16 June 2017\textsuperscript{180} the SMSG argued that, before adopting any ‘intrusive’ product intervention measures, ESMA should first assess the effects and effectiveness of MiFID II rules as well as of the product intervention measures.


\textsuperscript{176} Art. 7 Regulation (EU) 2019/2175; see also ESMA (2020c).

\textsuperscript{177} See e.g. BEUC (2018). Although BEUC supported ESMA’s initiative, it however demanded more stringent measures against ‘toxic financial products’.

\textsuperscript{178} See e.g. IG Group (2018).

\textsuperscript{179} FESE (2018), p 1.

\textsuperscript{180} ESMA (2017g).
taken at the Member State level.\textsuperscript{181} As will be examined in Sect. 3.4 below, the timing and swiftness of ESMA’s Product Intervention Decisions also raise questions about their constitutionality.

### 3.3 The Political Economy of ESMA’s Decisions (III): Product Intervention as a Principal-Agent Relationship with an Informed Principal

The relationship between ESMA and NCAs in a product intervention process can be described as a principal-agent relationship with an informed principal.\textsuperscript{182} ESMA acts as an informed principal that proposes a contract to NCAs, which are the agents. The object of such a contract is the adoption of product intervention measures by NCAs in their respective Member States. In this contractual relationship there are three stages, namely contract proposal, contract rejection or acceptance, and contract execution.\textsuperscript{183} In the first stage, ESMA proposes to NCAs the adoption of product intervention measures and signals their expected content through either supervisory convergence tools or an EU-wide ESMA product intervention measure. In the second stage, NCAs either accept or reject the proposed contract. In case of rejection, ESMA adopts and/or renews EU-wide product intervention measures. In case of acceptance, the process moves to the third stage, where NCAs execute the contract by adopting their own product intervention measures. An NCA will accept the contract if its expected utility exceeds its reservation utility.\textsuperscript{184} The main determinant of an NCA’s expected utility in case of contract acceptance is its ability to adapt the product intervention to its domestic conditions and, hence, to mitigate transaction costs. An ESMA product intervention imposes uniform conditions on NCAs and, hence, it may increase transaction costs at the Member State level. Hence, if and when contract rejection leads to an ESMA product intervention, and, \textit{ceteris paribus}, the reservation utility of an NCA will be lower than its expected utility in case of contract acceptance. Consequently, NCAs have strong incentives to accept the contract by adopting domestic product intervention measures that conform to ESMA’s minimum expectations and, hence, avoid an EU-wide ESMA product intervention or its indefinite renewal. Likewise, ESMA’s expected utility largely depends on its ability to signal to the EU legislator its effectiveness in facilitating and coordinating NCAs’ product intervention actions, which is one of ESMA’s tasks, according to Article 43 of MiFIR. Hence, for ESMA, the expected utility resulting from NCAs’ contract acceptance and proper execution, particularly after ESMA’s product intervention, is higher than the reservation utility resulting from contract rejection. The latter may require the renewal of product intervention measures.

\textsuperscript{181} Ibid., p 2.
\textsuperscript{182} The notion of a principal-agent relationship with an informed principal is developed in Maskin and Tirole (1990, 1992).
\textsuperscript{183} This is the three-stage game classification proposed by Maskin and Tirole (1990, 1992).
\textsuperscript{184} According to Maskin and Tirole (1992, p 2): ‘the agent accepts the contract if and only if his expected utility, given his interim beliefs, exceeds his expected reservation utility (his expected payoff if he refuses the contract)’. 
measures by ESMA and might convey a message of supervisory inefficiency—i.e. an inability to coordinate NCAs—that may ultimately affect future allocations to ESMA in aspects such as its budget or powers.

This principal-agent relationship starts prior to the adoption of actual EU-level product intervention measures, when ESMA carries out supervisory convergence actions in relation to a given financial product and/or when it expresses concerns about the limitations of the regulatory framework applicable to such a product. Through this process, ESMA signals information to NCAs about the actions that the latter need to adopt in order to avoid EU-wide product intervention. For example, in the Questions and Answers Relating to the provision of CFDs and other speculative products to retail investors under MiFID, ESMA determined the following:

The content of this document is aimed at competent authorities as defined in MiFID to ensure that in their supervisory activities, their actions are converging along the lines of the responses adopted by ESMA […] ESMA will also consider the need for any further work on this topic, in the medium term, in light of new aspects of the MiFID II framework, such as in relation to the application of product governance requirements and product intervention powers.\(^\text{185}\)

However, supervisory convergence tools provide incomplete information about ESMA’s preferences. Rather, they offer general guidance to NCAs on their expected supervisory behaviour \textit{vis-à-vis} supervised entities. As a result, there may be important informational asymmetries between ESMA and the various NCAs, and, among the latter, there may be different interpretations of ESMA’s preferences. On the basis of such limited information, NCAs may decide to take action or otherwise. Nonetheless, owing to these informational asymmetries, the probability of effective coordinated action by NCAs prior to ESMA’s product intervention is low. In the case of no action or ineffective action by NCAs, and, if the other requirements of product intervention are present, ESMA may decide to intervene. This will ultimately happen if and when a majority of the members of ESMA’s Board of Supervisors\(^\text{186}\) deem that the cost sourcing from non-intervention—e.g. the damage to investor protection in one or more Member States—is higher than the potential cost sourcing from ESMA’s uniform temporary prohibitions or restrictions. ESMA’s Product Intervention Decisions on BOs and CFDs from May 2018 noted that, whilst in the preceding years, some NCAs had been adopting a series of measures—including product interventions—that had positive effects at the level of individual Member States,\(^\text{187}\) these were often insufficient to tackle investor protection concerns,\(^\text{188}\) and inadequate to protect investors from Member States different from those where the measures were

\(^{185}\) ESMA (2017a), pp 6–7.

\(^{186}\) ESMA’s Product Intervention Decisions must be approved by a majority vote of the Board of Supervisors (Art. 44 ESMA Regulation).

\(^{187}\) Recital 74 ESMA Decision on BOs; recital 77 ESMA Decision on CFDs.

\(^{188}\) Recitals 77, 78 and 80 ESMA Decision on CFDs.
taken. \(^{(189)}\) ESMA pointed out that an effective protection of investors throughout the EU would require NCAs from all the Member States to adopt measures that provide a ‘common minimum level’ \(^{(190)}\) of protection. This argument was at the core of ESMA’s justification for its product intervention decisions. \(^{(191)}\)

ESMA’s product intervention measures have a temporary nature. ESMA may impose them for a limited period of time, after which ESMA must review them and decide whether to renew them or not. In the latter case, the prohibitions or restrictions expire. \(^{(192)}\) ESMA may decide not to renew a product intervention decision if the requirements that motivated it no longer apply. This would normally require either a change of relevant ‘regulatory requirements under Union law’ and/or the adoption, by NCAs, of product intervention measures that adequately address the threat that ESMA’s product intervention measures aim to tackle.

NCAs reacted to ESMA’s Product Intervention Decisions by proposing and adopting their own prohibitions and restrictions on BOs and CFDs. \(^{(193)}\) Through the latter, NCAs can adapt product intervention to the features of their own institutional setting and financial markets and, hence, reduce transaction costs that may source from a ‘one size fits all’ approach. The data concerning NCAs’ product intervention actions shows that, whilst most of these replicate ESMA’s product intervention measures, some NCAs have adapted aspects of product intervention to their own regulatory preferences. \(^{(194)}\) From the point of view of the principal-agent relationship between ESMA and NCAs, ESMA’s product intervention constitutes a much more effective signalling mechanism than supervisory convergence tools. Unlike the latter, the former sets a common minimum standard which NCAs must adopt at the domestic level in order for ESMA’s prohibitions or restrictions to be waived. This reduces informational asymmetries between ESMA and NCAs and facilitates the adoption by the latter of actions that conform to ESMA’s expectations. Indeed, ESMA’s decision not to renew its product intervention measures on BOs and CFDs was grounded on the fact that NCAs took permanent product intervention measures which were ‘at least as stringent’ as those adopted by ESMA. \(^{(195)}\) Article 43 of MiFIR stipulates that ESMA must facilitate and coordinate NCAs’ product intervention actions and issue and publish opinions on whether the measures proposed by them are justified and proportionate. This role enhances ESMA’s ability to effectively signal its preferences to NCAs.

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\(^{(189)}\) Recital 74 ESMA Decision on BOs; recital 81 ESMA Decision on CFDs.

\(^{(190)}\) Recital 75 ESMA Decision on BOs; recital 82 ESMA Decision on CFDs.

\(^{(191)}\) Ibid.

\(^{(192)}\) Art. 40(6) MiFIR.

\(^{(193)}\) Art. 42(2) of MiFIR subjects the NCAs’ power to adopt product intervention measures to strict conditionality—e.g. the existence of a threat to investor protection, proportionality and the non-discriminatory character of the measure. For a list of NCAs’ product intervention measures adopted after ESMA’s product intervention, see ESMA (2019a), pp 13–22.

\(^{(194)}\) For example, the FCA imposed a less stringent leverage limit for CFDs arguing, among other things, that ESMA’s limit was disproportionate for UK firms—see FCA (2019).

\(^{(195)}\) ESMA (2019b, c).
ESMA’s product intervention decision-making architecture mitigates the probability of non-compliant agent behaviour after ESMA imposes temporary prohibitions or restrictions. First, the adoption and renewal of ESMA’s product intervention measures is decided by the voting members of its Board of Supervisors, which comprises representatives of the Member State NCAs.\footnote{Arts. 40 and 44 ESMA Regulation.} The Board of Supervisors’ meetings where these decisions are taken constitute a peer accountability mechanism in which NCAs may be pressured to adopt product intervention measures that conform to ESMA’s expectations. Second, ESMA may decide, at any time, to reinstate product intervention measures if the applicable conditions apply. Hence, the constant threat of product intervention diminishes the incentives for NCAs to withdraw domestic product intervention measures in relation to which ESMA has already issued a positive opinion.

In its opinions on NCAs’ proposed product intervention actions, ESMA criticized some of the measures proposed by four NCAs, namely CySEC (Cyprus),\footnote{ESMA (2019d).} FCA (United Kingdom),\footnote{ESMA (2019e).} KNF (Poland),\footnote{ESMA (2019f).} and Magyar Nemzeti Bank of Hungary (‘MNB’) (Hungary).\footnote{ESMA (2019g).} As regards CySEC, FCA, and KNF, while admitting that their proposed measures generally complied with the requisites of being justified and proportionate,\footnote{ESMA (2019d), p 8; ESMA (2019e), p 10; ESMA (2019f), p 9.} ESMA disapproved of aspects of their substantive content, contending that they offered a less stringent level of protection than ESMA’s measures; for instance, some of ESMA’s criticism regarded the provision of a variable level of protection depending on the residence of the CFDs’ clients;\footnote{ESMA (2019d), pp 7-8.} the application of less strict leverage limits;\footnote{ESMA (2019e), pp 8, 10.} or the use of lower margin requirements for experienced clients.\footnote{ESMA (2019f), pp 8-9.} Despite ESMA’s criticism, neither CySEC, KNF, nor FCA withdrew the aspects of their product intervention measures censured by ESMA.\footnote{CySEC (2019); FCA (2019); KNF (2019).} When it comes to the MNB’s proposed measures on CFDs, ESMA issued a negative opinion, arguing that these were not justified and proportionate; the main reason, according to the EU supervisor, was that these were not of general application but, rather, they were addressed to individual providers of CFDs authorized in Hungary, with the result that providers of CFDs from other Member States were not covered by them.\footnote{ESMA (2019g), pp 4-6.} In contrast with its Cypriot, British and Polish counterparts, the MNB revised its position and proposed new measures which fully conformed to ESMA’s suggestions.\footnote{ESMA (2020d).} The interactions between ESMA and these NCAs, which decided to
deviate from ESMA’s signalled preferences, reveals relevant features of the principal-agent decision-making dynamics in a product intervention process.

First, the decision of an NCA to deviate from ESMA’s signalled preferences will largely depend on its assessment of ESMA’s potential reaction to such deviation. If and when a regulatory deviation is deemed as having the potential to trigger the adoption or renewal of an ESMA product intervention, an NCA may refrain from it. This is because such a deviation may ultimately result in higher cost for the NCA concerned, namely an EU-wide uniform intervention that does not permit domestic adaptations. Otherwise, if an NCA perceives that the threat of ESMA’s renewal of product intervention is weak, it may decide to adopt measures that do not fully conform to ESMA’s signalled preferences, as was the case of CySEC, KNF and FCA, whose measures were criticized but not fully censured by ESMA, and which did not result in a renewal of product intervention by the latter. The fact that CySEC, KNF and FCA did not amend their product intervention measures after the publication of ESMA’s critical opinions also suggests that ESMA’s naming and shaming of dissenting NCAs has very limited effects as a regulatory convergence tool.

Second, the comparison between ESMA’s opinion on CySEC’s product intervention, on the one side, and MNB’s product intervention, on the other, suggests that ESMA may treat similar situations differently depending on the expected reaction of the NCA to which a decision is addressed. As regards CySEC’s measures, ESMA’s main criticism was that, according to them, providers of CFDs authorized in Cyprus would afford investors different levels of protection, according to the measures applicable to CFDs in their Member States of residence; as a result, investors in Member States with less strict measures would be subject to lower degrees of protection. Likewise, with respect to MNB’s measures, ESMA criticized that these applied only to providers of CFDs authorized in Hungary, but not to those from other Member States, which, in their dealings with Hungarian investors, would be subject to the measures applicable to CFDs in their Member States; as a result, Hungarian investors might be subject to lower degrees of protection, if and when these providers from other Member States are subject to less strict measures than those applicable in Hungary. Whilst the substance of the underlying rationale for ESMA’s criticism was fairly similar in both cases, namely the application of varying degrees of protection to investors of CFDs, ESMA’s assessment of MNB’s proposed measures was harsher than that of CySEC’s, in the sense that ESMA fully censured the former, but generally deemed the latter to be justified and proportionate. An important difference between both cases lies in the reasons for the deviations of each of the NCAs from ESMA’s preferences. CySEC’s decision to apply varying degrees of protection to investors was due to a substantive difference of opinion with ESMA. Whereas the latter deemed such a measure to be detrimental to investor protection, CySEC contended that it was necessary to mitigate the risk of potential legal challenges and, also, adequate, justified and proportionate, because residents of other Member States

\[ \text{ESMA (2019d), p 6.} \]
\[ \text{ESMA (2019g), p 5.} \]
\[ \text{ESMA (2019d).} \]
would still be afforded protection according to the relevant applicable measures in their own jurisdictions. Instead, MNB’s proposal to adopt individual decrees addressed to providers of CFDs authorized in Hungary, rather than an act of general application that would also comprise those authorized in other Member States, was due to MNB’s lack of powers to adopt such acts at the time when it proposed its first product intervention measures in June 2019. MNB explicitly acknowledged this circumstance. The comparison of ESMA’s reaction in these two cases suggests that, unless it expects an NCA to modify its proposed product intervention measures after issuing its opinion—as the MNB did—or, unless the measures proposed by an NCA embrace a major deviation that flagrantly violates the principles of justification or proportionality, ESMA will likely avoid issuing negative opinions that result in a direct confrontation with and antagonization of NCAs. Such a scenario could result in an impasse situation where one or various NCAs refuse to modify their domestic measures and ESMA is forced to renew product intervention measures indefinitely until there is a change of relevant EU law requirements.

### 3.4 The Constitutionality of ESMA’s Product Intervention Decisions

The substance and timing of ESMA’s product intervention measures on BOs and CFDs raise questions about their compliance with EU law. As has been explained, according to Article 40(2) of MiFIR, the cumulative conditions for product intervention are three: first, that there is a significant threat to investor protection; second, that ‘regulatory requirements under Union law that are applicable to the relevant financial instrument or activity do not address the threat [to investor protection]’; and, third, that ‘[…] competent authorities have not taken action to address the threat [to investor protection] or the actions that have been taken do not adequately address the threat’. Whereas ESMA’s Product Intervention Decisions provided extensive justification for the occurrence of the first condition, namely a significant threat to investor protection, they failed to offer a convincing explanation about whether the second and third conditions were present and justified product intervention.

A key question to determine the compliance of ESMA’s Product Intervention Decisions with MiFIR is whether the ‘regulatory requirements’ and the ‘action[s]’ to which subsections b and c of Article 40(2) of MiFIR make reference, respectively,

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211 CySEC (2019).
212 ESMA (2019g), pp 2–3.
213 Art. 40(2)(a) MiFIR. The threat may also relate to the sound functioning of the financial markets or the stability of the financial system (ibid.).
214 Art. 40(2)(b) MiFIR.
215 Art. 40(2)(c) MiFIR.
216 See paras. 9–51 ESMA Decision on BOs; paras. 8-52 ESMA Decision on CFDs.
217 In contrast with the view presented in this article, Moloney (2018, pp 292–293) claims that ESMA provided an adequate and thorough justification for its product intervention measures on BOs and CFDs, supported by the analysis of extensive relevant data. However, Moloney’s argument is largely based on an assessment of ESMA’s justification about the existence of a significant investor protection concern, rather than the justification about the occurrence of the two other conditions of Art. 40(2) MiFIR.
are to be interpreted as those that are applicable after the entry into application of MiFID II or can also be deemed to include those adopted and/or in force under the previous regulatory regime. MiFIR’s text appears to support the former interpretation. In this respect, MiFIR applies to investment firms authorized under MiFID II\(^{218}\) and the terminology used by MiFIR is to be interpreted in accordance with the definitions provided by MiFID II.\(^{219}\) More generally, both MiFID II and MiFIR jointly substitute MiFID I’s regulatory regime.\(^{220}\) Consequently, ESMA would be entitled to adopt a product intervention decision, but only as long as there is a failure of both MiFID II’s regulatory requirements and post-MiFID II Member States’ product intervention actions, to address the threats to investor protection posed by complex financial products. In other words, ESMA’s assessments under Article 40 of MiFIR must refer to the adequacy of the applicable EU rules and Member States’ actions.

It is arguable whether ESMA’s Product Intervention Decisions were adopted in compliance with the requirement that ‘regulatory requirements under Union law […] do not address the threat [to investor protection]’. As has been explained, MiFID II sets a new regulatory regime regarding product governance and investor protection. Whereas there is evidence that MiFID I failed to properly address concerns in those areas, by the time ESMA’s Product Intervention Decisions were adopted, in the very initial stages of the application of MiFID II, it was still too early to assess, on the basis of objective data, whether the new regime introduced by MiFID II would effectively tackle threats to investor protection in the marketing, distribution and sale of complex financial products and overcome MiFID I’s weaknesses in this respect. For similar reasons, the requirement that ‘[…] competent authorities have not taken action to address the threat [to investor protection] or the actions that have been taken do not adequately address the threat’ did not seem to be applicable at the time of ESMA’s product intervention. In this respect, between 3 January 2018—the date of the entry into application of MiFIR—and 22 May 2018—the date of ESMA’s Product Intervention Decisions—, NCAs did not adopt product intervention measures in relation to BOs or CFDs;\(^{221}\) in addition, at the time of the adoption of ESMA’s Product Intervention Decisions, it was still premature to determine how NCAs’ product intervention actions taken before the entry into application of MiFIR and still applicable thereafter\(^{222}\) operated under the MiFID II regulatory environment and whether they would ‘adequately’ respond to investor protection threats.

ESMA relied on two main arguments to justify the occurrence of the condition of Article 40(2)(b) of MiFIR. First, it contended that several of MiFID II’s and MiFIR’s regulatory requirements relating to investor protection were similar to those of MiFID I, and, consequently, the new regime would replicate the weaknesses and

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\(^{218}\) Art. 1(2) MiFIR.

\(^{219}\) Art. 2(1) MiFIR.

\(^{220}\) See e.g. recitals 3–4 MiFIR.

\(^{221}\) The only exception was the Portuguese Comissão do Mercado de Valores Mobiliários, which, in February 2018, adopted certain restrictions in relation to derivatives linked to cryptocurrencies; see para. 72(v) ESMA Decision on BOs; para. 73(x) ESMA Decision on CFDs.

\(^{222}\) As was the case of certain measures adopted by Belgium, France and Spain; see para. 72(i-iii) ESMA Decision on BOs.
limitations of the former. Second, ESMA argued that the changes introduced by MiFID II and MiFIR were insufficient to adequately protect retail investors in the sale of complex financial products.

Whereas the Commission has developed comprehensive guidance on the factors to be assessed by ESMA when determining the existence of threats to investor protection for the purposes of product intervention under MiFIR, it has not provided criteria on how to assess the effectiveness of EU regulatory requirements and Member States’ measures in addressing such threats. Therefore, according to Article 40 of MiFIR, ESMA could theoretically ground its product intervention measures on a preliminary qualitative assessment of MiFID II’s content and potential effects—as ESMA indeed did in its product intervention decisions—rather than on practical or empirical data regarding its effectiveness in dealing with threats to investor protection. Such an exercise of discretion by ESMA does however raise some concerns about its compatibility with the Meroni doctrine constraints.

In the first place, granting ESMA the authority to exercise such a preliminary judgment would imply a delegation of discretionary powers involving wide margins of discretion, to the extent that ESMA would be making assessments according to its own subjective criteria rather than according to objective criteria developed by a delegating authority and actual data regarding investor protection with regard to complex financial products after the entry into application of MiFID II and MiFIR. Moreover, on the basis of such a discretionary power and subjective judgment, ESMA would be able to substitute EU law requirements applicable to complex financial products for its own requirements, as contained in the product intervention decision; this would largely imply an economic policy decision.

As regards the condition that ‘[…] competent authorities have not taken action to address the threat [to investor protection] or the actions that have been taken do not adequately address the threat’, ESMA argued that the system of fragmented and uncoordinated measures by NCAs does not constitute an effective tool to address investor protection concerns; this, because complex financial products are often marketed, distributed and sold on a cross-border basis through online platforms and, therefore, according to ESMA, a restriction or a ban in one Member State only protects investors in that Member State but not in others. Whilst ESMA’s reasoning as regards the cross-border effectiveness of individual NCA measures on BOs and CFDs has some foundation, such a lack of effectiveness would not per se result in a fulfilment of Article 40(2)(c) of MiFIR. Notably, whereas ESMA provided examples of allegedly ineffective NCAs’ product intervention actions, the vast majority

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223 Para. 54 ESMA Decision on BOs; para. 55 ESMA Decision on CFDs.
224 Para. 54 ESMA Decision on BOs; para. 55 ESMA Decision on CFDs.
226 Paras. 74–76 ESMA Decision on BOs; paras. 80–82 ESMA Decision on CFDs.
227 Para. 74 ESMA Decision on BOs; para. 81 ESMA Decision on CFDs.
of these had been taken before the entry into application of MiFID II and MiFIR.\textsuperscript{228} However, Article 40 of MiFIR requires that when ESMA decides whether to adopt a product intervention measure, it assesses the adequacy and effectiveness of NCAs’ actions in light of and within the context of the applicable EU legislative and regulatory framework at the time of ESMA’s decision. ESMA received product intervention powers with the entry into application of MiFIR and, therefore, the exercise of such powers, including the assessment of the condition set in Article 40(2)(c) of MiFIR, must be made in view of the EU legislative regime applicable to complex financial products applicable at the time of ESMA’s product intervention, namely MiFID II. Moreover, Article 42(2)(b) of MiFIR makes NCAs’ product intervention dependent on the satisfaction of the condition that “existing regulatory requirements under Union law applicable to the financial instrument, structured deposit or activity or practice do not sufficiently address the risks”; therefore, NCAs’ product intervention measures must be a response to \textit{inter alia} the weaknesses of the applicable EU regulatory framework when they are adopted and, hence, they must be assessed in accordance thereto. Consequently, Article 40(2)(c) of MiFIR would require that ESMA made either an assessment of the adequacy of NCAs’ actions adopted after the entry into application of MiFID II—the applicable regime at the time of ESMA’s Product Intervention Decisions—or, alternatively, an assessment of how NCAs’ actions adopted before the entry into application of MiFID II operate and are or are not effective under the latter’s framework.\textsuperscript{229} ESMA’s Product Intervention Decisions on BOs and CFDs complied with neither of these conditions.

An even more problematic issue is that, as explained above, ESMA’s claim about the applicability of Article 40(2)(c) of MiFIR was largely based on the assumption that a system of uncoordinated NCA measures is inadequate for addressing the threats to investor protection posed by BOs and CFDs, rather than on an actual assessment of such measures.\textsuperscript{230} ESMA’s approach would justify an expansive application of its product intervention powers to almost any instance where Member States follow different regulatory approaches to tackle problems relating to investor protection sourcing from a given financial product. This, in turn, runs counter to the principle of subsidiarity of Article 5 TEU as well as to the MiFIR’s requirement that ESMA’s product intervention must be ‘exceptional’.\textsuperscript{231}

Although the CJEU’s decision in the \textit{Short-Selling} case determined that ESMA’s intervention powers complied with the \textit{Meroni} requirements, it nonetheless determined that, in exercising such powers, ESMA must ‘examine a significant number of factors’\textsuperscript{232} and provide ‘evidence supporting the reasons why it [a product

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\textsuperscript{228} Para. 72 ESMA Decision on BOs; para. 73 ESMA Decision on CFDs.
\textsuperscript{229} Whereas the NCAs’ measures referred to by ESMA may not have been effective under MiFID I, those very same measures may have had a different effect under MiFID II.
\textsuperscript{230} In its product intervention decisions, ESMA merely listed and provided a general description of measures taken by the NCAs of various Member States, aimed at limiting the marketing, distribution or sale of BOs and CFDs (para. 72 ESMA Decision on BOs; para. 73 ESMA Decision on CFDs).
\textsuperscript{231} Recital 29 MiFIR—on the condition of exceptionality for the use of product intervention powers see also IG Group (2018), p 4.
\textsuperscript{232} \textit{Short-Selling} case, para. 48.
\end{flushleft}
intervention measure] must be adopted’. The above analysis evidences that none of these conditions would appear to have been fulfilled in ESMA’s Product Intervention Decisions, as they failed to properly justify the occurrence of the conditions set out in Article 40(2) of MiFIR; by not doing so, ESMA largely exceeded the powers granted to it. This, in turn, questions the constitutionality of ESMA’s actual exercise of product intervention powers with regard to BOs and CFDs.

4 A Lawmaker in the Making? Some Reflections and Proposals on ESMA’s Product Intervention Powers

Until May 2018, ESMA’s regulatory approach to investor protection in the marketing, distribution and sale of complex financial products was largely based on supervisory convergence actions in relation to MiFID I’s product governance regime as well as investor warnings. ESMA’s Product Intervention Decisions on BOs and CFDs mark a shift towards a much more pervasive regulatory approach based on detailed prohibitions and restrictions. Since then, ESMA has continued to make an active use of its intervention powers as evidenced, for instance, in its temporary measures of 16 March 2020, later renewed, concerning transparency obligations on short-selling. Recent regulatory reforms and reform proposals for ESMA’s product intervention powers strongly suggest a move towards a system in which ESMA’s role in product intervention will become more ubiquitous both in temporal and substantive terms and in which ESMA would de facto perform, to a certain extent, a quasi-legislative role. The next paragraphs explain these reforms, question their adequacy and propose an alternative model.

Regulation (EU) 2019/2175 has expanded the temporal scope of ESMA’s product intervention measures. This has been done through an amendment of Article 9(5) of the ESMA Regulation, whereby ESMA’s product intervention measures are to be reviewed, at least, every 6 months—instead of every 3 months, as was the case under the former system. Moreover, after two consecutive renewals, ESMA may decide to review the measures on a yearly basis. From an efficiency point of view, the rationale for this reform is questionable. One of the advantages of ESMA’s

233 Short-Selling case, para. 50.
234 According to Moloney (2018, p 292), ESMA’s deployment of Art. 40 MiFIR constitutes ‘a material extension of ESMA’s influence and an important staging-post in its evolution as a supervisor’.
235 European Securities and Markets Authority Decision (EU) 2020/525 of 16 March 2020 to require natural or legal persons who have net short positions to temporarily lower the notification thresholds of net short positions in relation to the issued shares capital of companies whose shares are admitted to trading on a regulated market above a certain threshold to notify the competent authorities in accordance with point (a) of Article 28(1) of Regulation (EU) No. 236/2012 of the European Parliament and of the Council [2020] OJ L 116/5.
237 Art. 3 Regulation (EU) 2019/2175.
238 Ibid.
quarterly reviews is that they require ESMA to continually reassess its product intervention measures. This, in turn, allows ESMA to timely adapt product intervention to new available information by withdrawing, extending or amending existing measures. The extension of the temporal validity of product intervention measures reduces the incentives for ESMA to timely review them and to amend and adapt their content accordingly, if necessary. Moreover, such an extension may result in a delay in the withdrawal of ESMA’s measures, even in cases when NCAs have taken action and there is no longer a threat that justifies ESMA’s product intervention.

On 3 February 2020 ESMA published a report (‘ESMA Report’) addressed to the Commission with technical advice on product intervention issues. Its content, which provides an overview of the impact of product intervention measures and makes certain related policy recommendations, evidences that ESMA seeks an expansion of its product intervention powers, both in substantive and temporal terms.

When it comes to the substantive scope of product intervention measures, ESMA proposed that its powers be expanded so as to cover fund management companies authorized under the Alternative Investment Fund Managers Directive (‘AIFMD’) and the Undertakings for Collective Investment in Transferable Securities Directive (‘UCITSD’). ESMA justified its proposal arguing that, otherwise, there could be unlevel playing field situations because a product intervention decision in relation to a given financial instrument might not apply to it when such instrument is marketed, distributed and/or sold by these companies.

As regards the temporal scope of product intervention powers, ESMA proposed the introduction of mechanisms aimed at making product intervention decisions permanent. This proposal raises important constitutional and legitimacy concerns. The idea of permanent product intervention measures was already propositioned by the SMSG in November 2019, in an advisory opinion addressed to ESMA. According to the SMSG: ‘A better alternative would be that ESMA can, for instance after

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239 For example, in the renewal of its product intervention measures on CFDs of 23 October 2018, ESMA introduced amendments in relation to the form of risk warnings made by CFD providers; these amendments were in response to certain technical difficulties experienced by the latter. See recitals 12–14 ESMA Decision (EU) 2018/1636.

240 ESMA (2020e).

241 The ESMA Report summarizes the responses to ESMA’s call for evidence on the effects of product intervention measures regarding CFDs and binary options on market participants and clients, of September 2019; see ESMA (2020e), pp 5–19. The ESMA Report noted that ESMA’s Product Intervention Decisions had a positive effect on certain aspects relating to investor protection, such as a decrease in the costs incurred by CFDs’ retail clients; see ESMA (2020e), p 9.


245 ESMA (2020e), para. 86.

246 ESMA (2019h).
two renewals, take a permanent measure, but is required to submit the necessity of this measure to a yearly review’ and ‘MiFIR should be changed in this respect’.247 The SMSG’s proposal largely disregarded the legal and constitutional constraints that such a reform—in the specific terms proposed by the SMSG—would entail. In the first place, as regards the suggestion that ESMA could take a ‘permanent measure, but is required to submit the necessity of this measure to a yearly review’, it is unclear whether the SMSG referred to a measure that would expire after 1 year if not renewed or to a measure that may be dropped after revision but which would otherwise continue to apply indefinitely. The former would de facto be a system of temporary product intervention measures. The latter, which seems to be closer to the SMSG’s proposal,248 would constitute a system of permanent ESMA product intervention measures. Such a model would most likely be deemed as contravening Meroni and, hence, it would be unconstitutional. In this respect, in the Short-Selling case, the CJEU clearly ruled that one of the factors that limits ESMA’s margins of discretion in the exercise of intervention powers—and, hence, determines its compliance with Meroni—is the temporary nature of the measures adopted by virtue of those powers.249 Therefore, a system where those measures have a permanent nature ab initio, regardless of whether ESMA decides to withdraw them at a later time, would not comply with such a requirement. Moreover, the SMSG’s assumption that ESMA could be empowered to adopt permanent product intervention measures as regards complex financial products through a mere reform of MiFIR, neglected the fact that such empowerment would first require a reform of Article 9(5) of the ESMA Regulation, which determines that ESMA’s product intervention powers are temporary.

 Whilst the ESMA Report generally embraced and supported the idea of ESMA’s permanent product intervention measures, it dismissed the advice of the SMSG in this respect—an unsurprising fact in light of the latter’s major inconsistencies. Instead, ESMA proposed to the Commission the broadening of the temporal scope of its intervention powers through two alternative mechanisms. The first, and ESMA’s preferred mechanism, is one where there would be a ‘legal mechanism taken by the EC or of a legal act to consolidate the [ESMA’s] temporary measures as permanent ones’.250 The second and, alternative, mechanism251 is one where ESMA would adopt product intervention measures with an extended validity period of 18 months.252 Whilst the second mechanism would, in principle, abide by the Meroni constitutional constraints, for the reasons referred above with respect to the reform operated by Regulation (EU) 2019/2175, product intervention measures with

247 ESMA (2019h), p 5.  
248 This interpretation would be supported by the fact that the SMSG used the term ‘permanent’—in relation to ESMA’s product intervention measures—in various passages of its advice; see e.g. ESMA (2019h), pp 4-5.  
249 Short-Selling case, para. 50.  
250 ESMA (2020e), para. 96.  
251 This would apply ‘if it is not possible for the [European Commission] to consolidate temporary measures’. ESMA (2020e), para. 95.  
252 ESMA (2020e), para. 96.
an extended validity period may be suboptimal from an efficiency point of view. As regards the first mechanism, ESMA’s proposal is rather vague. The reference to a ‘legal mechanism taken by the EC or of a legal act [of the European Commission]’\textsuperscript{253} seems to imply a model where ESMA’s measures would be consolidated by the Commission. This does not imply an actual allocation of powers to ESMA to adopt permanent product intervention measures and, hence, in such regard, it is not in breach of Meroni. However, from a legitimacy perspective, this model poses important problems. Notably, because it would imply the use of delegated acts by the Commission\textsuperscript{254} and would bear some similarities with the process of the adoption of regulatory technical standards, which are proposed by ESMA and endorsed by the Commission.\textsuperscript{255} Whilst, in such a process, the Commission has the power to introduce amendments in relation to ESMA’s proposals,\textsuperscript{256} and the Council and the Parliament may object to the delegated acts submitted by the Commission, the development of these standards is led by ESMA, which, hence, exercises quasi-law-making powers. A model of consolidation of ESMA’s product intervention measures designed along these lines raises a question of legal adequacy because the purpose of delegating acts is to ‘supplement or amend certain non-essential elements of the legislative act’\textsuperscript{257} and this definition does not adequately suit the scope of a product intervention measure. The latter, as explained in Sect. 3.1, embraces the exercise of a policy choice that substitutes, rather than supplements or amends, the law. Moreover, owing to their very own nature, product intervention measures address an essential aspect of the law, namely whether a given financial product, not prohibited by the law, should be subject to prohibitions or restrictions that may affect their marketing, distribution and/or sale.

It follows that the consolidation of product intervention measures through permanent prohibitions and/or restrictions on financial products is a task that naturally falls under the remit of the EU legislator. This should be acknowledged by any future reform and could be devised through the application of a model based on the ordinary legislative procedure to the consolidation of ESMA’s product intervention measures. Here it is submitted that a potential system could be one in which whenever ESMA makes the first renewal of a product intervention measure, it is required to submit an opinion to the Council and the Parliament indicating whether such measure(s) should, in ESMA’s view, be made permanent. If the Council and/or the Parliament consider otherwise and decide that no action is required, then ESMA would be obliged to withdraw its product intervention measure(s). However, if the Council and/or the Parliament consider that there is a rationale for consolidation, they would then request the Commission to submit relevant legislative proposals.

\textsuperscript{253} ESMA (2020e), para. 95.
\textsuperscript{254} Arts. 290-291 TFEU.
\textsuperscript{255} Arts. 10-14 ESMA Regulation.
\textsuperscript{256} For example, the Commission may amend the technical standards submitted by ESMA only ‘where the Union’s interests so require’. Likewise, if the Commission amends a standard submitted by ESMA it must inform the latter about the reasons for those amendments (Arts. 10(1) and 15(1) ESMA Regulation).
\textsuperscript{257} Art. 290(1) TFEU.
In such a case, ESMA’s temporary measures would continue to apply until the legislative procedure is completed, unless the Commission decides not to formulate legislative proposals, in which case ESMA would also be required to withdraw its product intervention measures. As regards the degree of legislative intervention, the proposed system would be based on general prohibitions or restrictions formulated by the EU legislator, which would then be developed—in their more technical aspects—by ESMA through technical standards, which would be submitted to the Commission for endorsement through delegated and implementing acts. Overall, the proposed system would be consistent with the nature and entity of permanent product prohibitions or restrictions, which justify legislative consideration. At the same time, this system would still grant ESMA a relevant role in the process, through the development of standards which, if endorsed by the Commission, would become legally binding. However, ESMA’s discretion would be bound by ex-ante ad hoc, specific delegations from the EU legislator and by ex-post Commission oversight. Likewise, by conditioning the validity of ESMA’s product intervention measures to the existence of a legislative procedure aimed at their consolidation, the proposed system would also address the conceptual difficulties underlying the current system of ESMA’s temporary product intervention measures, which allows for an indefinite renewal of such measures, hence rendering them potentially permanent, de facto.

A final reflection concerns the perils of the increasing relevance of product intervention as a tool for the regulation of complex financial products and practices. ESMA’s deployment of product intervention measures on BOs and CFDs did not only attest to the failure of supervisory convergence tools and investor warnings in dealing with threats to investor protection in the marketing, distribution and sale of certain complex financial products, but also signified a shift, from a regulatory system based on transparency, disclosure and investor warnings, towards a much more pervasive system based on prohibitions or restrictions. Likewise, the extension of the temporal scope of ESMA’s product intervention measures operated by Regulation (EU) 2019/2175 and ESMA’s demands for an expansion of its product intervention powers, including the establishment of a system of consolidation of its product intervention measures, suggest that product intervention may gain weight as a regulatory tool of complex financial products that other regulatory instruments fail to address in an efficient way. A ‘prohibitionist’ or ‘restrictive’ product intervention approach may be appealing for ESMA, which, as has been explained in this paper, can use it to both signal its policy preferences to the EU legislator and to exercise

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258 Whilst ESMA could alternatively be delegated with the development of certain aspects of general legislative prohibitions or restrictions through soft law instruments, such as guidelines, the nature of technical standards and the Commission’s acts endorsing them—i.e. regulations or decisions—make the latter more effective in guaranteeing certain minimum degrees of uniformity in their domestic implementation. In this respect, although NCAs generally tend to comply with ESMA’s guidelines, there are instances of a lack of compliance (Moloney 2018, p 147) and also problems relating to consistent implementation at the Member State level (Van Rijsbergen 2014, pp 127–128). More generally, there are legitimacy concerns about the fact that guidelines and other ESMA soft-law instruments—whose adoption is subject to less stringent procedural requirements than technical standards—are often treated by NCAs as binding instruments (Moloney 2019, p 99).
control over the NCAs’ regulatory approaches at the Member State level. Likewise, for the EU legislator, ESMA’s product intervention may bring about certain perceived benefits, as it shifts a regulatory problem from the legislative arena to the administrative arena. However, the use of product intervention as an ordinary regulatory tool would be contrary to the spirit of product intervention powers, which, as has been explained, are devised as an extraordinary and temporary mechanism to address threats to, among others, investor protection, in a timely manner. In other words, product intervention powers are designed as a temporary complement rather than a substitute for ordinary regulatory mechanisms. If and when the latter fail to address a threat to investor protection in a satisfactory way, it is the task of the legislator to assess the underlying reasons for such a failure and to tackle the problem through a reform of those ordinary regulatory mechanisms.

More generally, in assessing future approaches and responses to complex financial products, the EU legislator, the Commission and ESMA should consider two important factors. The first is that, when dealing with these products, there is not necessarily a ‘one size fits all’ solution and that any approach should acknowledge the specificities of complex financial products, their providers, and investor behaviour at the Member State level. Hence, highly specific and uniform prohibitions or restrictions that leave little to no freedom for NCAs to adapt them to domestic specificities may not constitute the most appropriate response. The second factor is the notion of investor empowerment, which is strongly embraced by the Commission in its Consumer Financial Services Action Plan. Empowerment is linked to ideas of investor autonomy and assumes the possibility that, even well-informed investors, may voluntarily and legitimately enter into risky financial transactions. Hence, the application of this idea to the regulation of complex financial products would require the adoption of strategies aimed, not at discouraging investors from engaging in highly risky financial practices with complex financial products, but at guaranteeing that, if and when they decide to do so, they are fully informed of the associated risks beforehand and, also, that those who provide those products to them scrupulously abide by the applicable rules. This, in turn, would justify a reinforcement of product governance and investor warning mechanisms throughout the EU, rather than mere recourse to product intervention measures.

261 For a diverging opinion see e.g. Busch (2017, pp 137, 146), who suggests that product governance rules cannot fully address problems pertaining to the marketing of potentially harmful financial products and that this justifies the allocation to and the use of extensive product intervention powers by ESMA.
5 Conclusions

This article has examined critical questions regarding the political economy and constitutionality of ESMA’s product intervention powers and measures as well as their adequacy for the regulation of complex financial products. The main findings are the following.

First, product intervention constitutes a form of residual lawmaking whereby ESMA substitutes a legislative choice—i.e. an authorization to market, distribute and/or sell a financial product—with a regulatory choice, consisting of a prohibition or restrictions applicable to such product. Through product intervention, ESMA largely overcomes the legislator’s initial choice, and, hence, it embraces certain degrees of economic policy.

Second, ESMA’s Product Intervention Decisions on BOs and CFDs must be interpreted in light of and, partly as a response to, the policy discussions concerning ESMA’s future. Notably, ESMA has used product intervention to signal to the Parliament and the Council the inefficiencies of the EU legislative framework as well as its willingness and ability to play a prominent role in the field of investor protection.

Third, as regards the relationship between ESMA and NCAs in a product intervention process, this is one between an informed principal (ESMA) and an agent (NCA), where the former proposes to the latter a contract whose object is the adoption of domestic product intervention measures. When contract rejection results in ESMA’s product intervention, an NCA’s reservation utility is lower than its expected utility in case of contract acceptance. Therefore, NCAs have incentives to accept the proposed contract and adopt domestic product intervention measures which largely abide by ESMA’s expectations. By doing so, they mitigate the transaction costs linked to a uniform ESMA EU-wide product intervention that may not permit adaptations to the specific conditions in an NCA’s Member State.

Fourth, whilst ESMA’s Product Intervention Decisions may have contributed to mitigating some of the investor protection problems that they aimed to address, they are in breach of the EU constitutional framework and, particularly, of the Meroni requirements. In this respect, ESMA’s assessment of the occurrence of MiFIR’s conditions for product intervention involved the exercise of wide margins of discretion and the execution of actual economic policy.

This article has also assessed the expansion of the temporal scope of ESMA’s product intervention measures operated by Regulation 2019/2175, which reduces ESMA’s incentives to periodically reassess and adapt them. It has also examined ESMA’s proposal in February 2020 for the establishment of a system of consolidation for its product intervention measures. This proposal is inadequate because it would require Commission delegated acts, which do not adequately suit the scope of product intervention measures. This article has proposed an alternative model where ESMA’s product intervention measures are either consolidated by the Council and the Parliament on the basis of Commission proposals or, otherwise, withdrawn by ESMA. Such a model is more consistent with the entity of product intervention consolidation, which justifies legislative intervention, and also addresses the conceptual
problems underlying the potentially indefinite renewal of ESMA’s product intervention measures, which could render them *de facto* permanent.

This article has concluded by highlighting the perils of the increasing relevance of product intervention as a regulatory tool. Product intervention is devised as a temporary and extraordinary tool and should be used as a complement, rather than a substitute, to ordinary regulatory mechanisms. Moreover, an undue and excessive use of product intervention runs against the idea of investor empowerment which is an important pillar of the Consumer Financial Services Action Plan.

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