ESA's decision on net short positions – ensuring effective judicial protection?

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This contribution comments on a recent decision of the EFTA Surveillance Authority (ESA), taken by the ESA in parallel with a decision by the European Securities and Markets Authority (ESMA). It examines several questions that result from the so-called agencification in the EU and in particular from the model that the EEA Joint Committee chose to integrate the EEA/EFTA States into the European System of Financial Supervision (ESFS).

Introduction

In December 2020, the EFTA Surveillance Authority (ESA) renewed its temporary decision to lower the threshold for required reporting of net short positions, for natural and legal persons in the EEA/EFTA States for the third time.[i] The decision was reasoned with the COVID-19 situation, which constituted a "serious threat to the orderly functioning and integrity of the financial markets in the EU and in the EEA EFTA States". The wording of ESA's decisions on lowering the threshold to report net short positions is essentially identical to that of the European Securities and Markets Authority (ESMA). ESMA has adopted equivalent decisions towards market actors in the EU member states.[ii] In its reasoning, ESA refers to a "cooperation" with ESMA in reaching the conclusions that its decisions are founded upon. The parallel decisions of ESA and ESMA illustrates that the integration of the EEA/EFTA States in the European System of Financial Supervision contributes to ensure a homogenous application of the EEA financial market law, throughout the EEA. However, it can be argued that ESA's use of the term "cooperation" serves to elude the role of ESMA in ESA's decision-making-process. Article 3(1) Surveillance and Court Agreement (SCA) Protocol 8 states that ESA shall base all its decisions in the field of financial market law on "drafts" from the relevant European Supervisory Authority. There is no mention of any draft in ESA's decisions – even though this is specifically established in the decision procedure ESA follows when lowering the threshold for net short positions, according to the EEA-adapted version of article 28 of Regulation (EU) 236/2012, in accordance with article 9(5) of Regulation (EU) 1095/2010 (see Article 1(d)(iv) of JCD No. 204/2016).

The aim of this text is to raise some questions on how effective judicial protection can be ensured for EEA/EFTA market actors who are subject to legally binding decisions from ESA towards groups of private actors, like the decision lowering the threshold to report net short positions. ESA's powers are designed within the framework of the EEA two-pillar structure, which is reflected by Article 3(2) SCA Protocol 8 stating that ESA adopts its decisions "in full independence". However, the reason offered

by the EEA Joint Committee regarding the need for the draft decision procedure at all was that the "expertise" and "capacity" of the European Supervisory Authorities should be integrated to benefit the EEA/EFTA States (see recital 8 of JCD No. 204/2016). This suggests that the drafts are highly relevant for ESA's decisions, and leaves the question: does this affect the market actors that are subject to ESA's decisions in any way? In addition to this, the supranational nature of the decision, and the fact that the decision from ESA is adopted towards a group of actors, and not an individual actor, raise additional questions about effective judicial protection. These questions will be elaborated in the following. First, it is necessary to take a closer look on the role and function of the European Supervisory Authorities in the draft-decision procedure.

The role of the European Supervisory Authorities in the draft-decision procedure

In addition to ESMA, the European Insurance and Occupational Pensions Authority (EIOPA) and the European Banking Authority (EBA) are established. Aside from their sector-specific scope, they have equivalent functions, tasks and responsibilities to conduct micro-supervision towards National Competent Authorities (NCAs) and private actors.

The European Supervisory Authorities are specialised EU agencies that monitor the stability and functioning of the European financial markets and adopt necessary non-binding and binding measures. It is their role of being specialist organs that has been integrated into the EEA Agreement. Non-binding measures of the European Supervisory Authorities apply directly also for the EEA EFTA States; in constrast, binding decisions as regards the EEA EFTA States are not taken by the European Supervisory Authorities, but by ESA (see JCD No. 199/2016, 200/2016, 201/2016). The procedures that enable ESA to adopt legally binding measures towards private actors, in the field of financial market law, have in common that it is the relevant European Supervisory Authority that request introductory investigations and receives the acquired information. The European Supervisory Authorities monitor the financial markets and initiate measures to uphold the functioning and stability of the markets in the EEA/EFTA States through the issuing of drafts for ESA. ESA adopts a binding decision based on a draft from the relevant European Supervisory Authority. This is also the applicable procedure for ESA's decision to lower the threshold to report net short positions, as mentioned above.

Their capacity as financial specialist organs make the European Supervisory Authorities well suited for technical economic assessments that are necessary when deciding to instigate binding measures towards private actors in the EU/EEA finance markets. ESA's role is to adopt legally binding measures addressed to the EEA EFTA market actors on the basis of the assessments of the European Supervisory Authorities, in order to uphold homogeneity between the EFTA-pillar and the EU-pillar in the EEA. The problem, from a fundamental rights perspective, is that the true extent of the role of the European Supervisory Authorities is not visible for the EEA/EFTA market actors subject to ESA's decisions. In fact, the two-pillar structure effectively removes any possibility for direct review of the work of the European Supervisory Authorities. The drafts are not meant to construe a part of ESA's decisions, or to have any legal implications towards the subjects of ESA's decisions. Instead, the market actor must address legal action either against ESA or against the national authority. The initial investigations and assessments from the European Supervisory Authorities that led to the drafts suggest on the other

hand that the drafts construe a more important part of ESA's decisions than implied. This could make it relevant for the market actors to access the drafts for a more transparent decision-making process.

Judicial remedies and effective judicial protection for EEA/EFTA market actors towards ESA's decisions

According to the case law of the EFTA Court, natural and legal persons of the EEA/EFTA States have a right to effective judicial protection against unlawful infringements in rights which they derive from EEA law, as EEA market actors (see Case E-15/10 *Posten Norge* [2012] EFTA Ct. Rep. 246, paragraph 85 and 86, and Case E-11/12 *Koch* [2013] EFTA Ct. Rep. 272 paragraph 116 and 117). In essence, the principle of effective judicial protection establishes minimum rights to ensure effective remedies towards legally binding measures, and to a fair hearing on the legality of a measure before a court. ESA and the EFTA Court are required to uphold these rights through their interpretation and application of the EEA Agreement and the SCA. It is worth mentioning that the EEA Joint Committee which initially adopted the draft decision procedure into the EEA Agreement, obligating the EEA/EFTA States to implement this into the SCA, has no formal equivalent obligation to ensure effective judicial protection to that of the EFTA Court and ESA. The EFTA Court has no competence to rule on the general legality of provisions in the EEA Agreement in the same manner as the European Court of Justice (ECJ). For instance, in Case C-270/12 *United Kingdom v. Parliament and Council*, the ECJ ruled on the legality of Article 28 of Regulation 236/2012 – the very same provision that ESMA and ESA used when lowering the thresholds to report net short positions in the abovementioned decisions. The question in this case was whether ESMA, as an EU-Agency, could hold such discretionary powers as established in the provision, which the ECJ affirmed. Admittedly, the case did not concern any questions of effective judicial protection and the action was raised by an EU Member State and not a private actor. Still, the case serves as an example of a fundamental difference between the supranational law-making in the EU and the EFTA-pillar of the EEA: there is no access to challenge the mere legality of an act in the EEA Agreement, or for the same reasons the SCA for that matter, before the EFTA Court.

That being said, an EEA/EFTA market actor can acquire effective judicial protection towards measures of ESA directly affecting the actor's legal position through access to the EFTA Court. If the draft decision procedure infringes the actor's right to effective judicial protection in any way, the result should be that the decision from ESA is invalid.

Access to the drafts?

To recall, a problem with the draft decision procedure is the elusive role of the drafts. On the one hand, the drafts constitute an obligatory and central element in the grounds for ESA's decision. On the other hand, the drafts are issued by institutions that are not subject to the jurisdiction of the EFTA Court. If the EEA/EFTA market actor in question would wish to acquaint itself with the content of the draft on which ESA is basing a decision, it would have to be given access to it. None of the relevant provisions that apply in relation to ESA's decision-making powers require ESA to give such access, explicitly. In fact, according to a non-binding "Multilateral Memorandum of Understanding on cooperation, information exchange and consultation" between ESA and the European Supervisory Authorities, the drafts are to be held confidential (see article 16). This makes it unclear whether access to the draft could be claimed in accordance with ESA's Rules on public Access to Documents.

It could be easier for EEA/EFTA market actors to be granted access to the draft upon which a decision from ESA is based, during proceedings before the EFTA Court to determine the legality of a decision from ESA. The EFTA Court can demand ESA to admit the draft as part of the evidence, in the proceedings. ECJ case law such as Case C-119/97 P, *Ufex and Others v. Commission* clearly shows that documents that are necessary and relevant for the outcome of the proceedings shall be made available to the other party and to the Court. In light of this, the importance of the draft as grounds for ESA's decision suggest that the it should be made part of the proceedings, and available for the applicant.

However, the possibility for EEA/EFTA market actors to access the draft in the proceedings before the EFTA Court depends on a complaint being admissible before the EFTA Court. This requires that the market actor who wishes to bring a complaint on the legality of ESA's decision before the EFTA Court has legal standing. Where ESA adopts a binding decision that is addressed to an individual EEA/EFTA market actor, this is clearly in accordance with the requirements for legal standing in Article 36(2) SCA. It may, however, be up for debate whether natural or legal persons can bring a decision addressed to EEA/EFTA market actors as a group, such as the one lowering the threshold to report net short positions, before the EFTA Court. The wording of Article 36(2) indicates that only decisions towards individuals can be brought before the EFTA Court by natural or legal persons. The provision refers to decisions from ESA addressed to "that person" or "another person, if it is of direct and individual concern to the former". This bodes the question of whether ESA's decision to report net short positions, or any other decision adopted towards natural and legal *persons* as a group, can be brought before the EFTA Court. I only aim to raise the question here. It is, however, an important one. It is unclear whether the EEA/EFTA actors are meant to address potential allegations on the legality of the measures towards ESA, or perhaps only towards the NCAs that receive the required reports on net short positions. As the measure from ESA is legally binding, the principle of effective judicial protection states that the private actors, one way or another, should have effective remedies to clarify the legality of the measure. If access to a court is only available through national procedure, this would extend the distance between the EEA/EFTA market actors subject to the measures, and the European Supervisory Authorities that can be argued to have initiated the measures even further. In addition to this, it is necessary to determine whether effective judicial protection can be ensured without access to bring the decision from ESA before the EFTA Court. After all, the initial binding measure is adopted by ESA and not by the NCAs.

Final reflections

The temporary nature of ESA's decision means that ESA will have to renew the decision in three months in order to uphold the measure lowering the threshold to report net short positions. However, regardless of whether the decision will be renewed a fourth time or not, the questions raised in this text will apply to future decisions from ESA in accordance with the powers constituted in article 9(5) of Regulation (EU) 1095/2010, or equivalently in articles 9(5) of Regulation (EU) 1093/2010 (corresponding to the powers of EBA), and of Regulation (EU) 1094/2010 (corresponding to the powers of EIOPA). Overall, this text highlights only a few of several questions that can be raised, with regard to how effective judicial protection for private actors can be ensured under the model that the EEA Joint Committee chose to integrate the EEA/EFTA States into the ESFS. The legal foundation for effective judicial protection towards binding decisions from ESA is established through the case law of the EFTA Court, while in the EU it is expressed in the European Charter of Fundamental Rights. The so-called agencification in the EU has led to the establishment of several specialised administrative EU

agencies with binding authority. The consequence is that the implementation of such EU legal acts into the EEA Agreement requires adaption to how the executive power is designed in each individual case. In the efforts to maintain a homogenous European Economic Area, it is important that the consequences for the private actors are taken into account as well. As the EFTA Court has stated in Case E-11/12 *Koch*, the goal of homogeneity can only be upheld if the private actors in the EU and EFTA pillar of the EEA have equal possibilities to uphold their EEA based rights, through effective judicial remedies (see paragraph 117). This applies irrespective of whether the administrative and supervisory functions are placed on the national or the supranational level, and with the same minimum requirements.

[i] Decision no. 167/20/COL 17 December 2020 available from ESA renews decision requiring disclosure of net short positions of 0.1% and above | ESA (eftasurv.int). First Decision no. 020/20/COL, 16 March 2020; renewed by Decision no. 056/20/COL, 11 June 2020; renewed by Decision no. 106/20/COL.

[ii] See ESMA Decision of 16 December 2020 ESMA70-155-11608. First decision ESMA Decision 16 March 2020, ESMA70-155-246; renewed by ESMA71-99-1342, 11 June 2020; renewed by ESMA70-155-11072, 16 September 2020.

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