Problem-adequate decisions through functional differentiation?
Institutional incentives and constraints within the European financial services regulation

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1. Introduction

In 2001, a comitology procedure, the so-called Lamfalussy procedure, was established for the European securities regulation. This procedure is named according to the chairman of a committee of wise men who proposed it, Baron Alexandre de Lamfalussy. In 2005, this procedure was extended to the field of banking, insurance and occupations and financial conglomerates. It is one of the latest and most innovative of a steadily growing number of European comitology procedures in the field of risk regulation (Bergström 2005), which transfer regulatory decisions from the national to the European level. This bears a potential to mitigate policy problems of the nation state, notably that more and more problems which are perceived as urgent can no longer be solved by the nation state (Dehousse 1997). This problem is of particular importance in the field of financial services, because the market in this field is highly internationalised and is hardly regulated and controlled adequately by the nation state (Lütz 2001). The Lamfalussy procedure is characterised by a high degree of complexity and functional differentiation. Like many other comitology procedures, it is characterised by the logic of the so-called new approach: The ends and principles of regulation are laid down in a framework directive, whereas implementing measures are delegated to subordinated committees (comitology prodecure). The empirical research in this field has shown that this type of functional differentiation may seriously restrain the scope for action of rational actors, and, in certain circumstances, induce them to act deliberatively instead of power-based (Joerges/Neyer 2006, 1997; Gehring et al. 2005). This is caused by the special institutional design and the functional differentiation of the decision-making procedure. At best, this enables them to enter a discourse about the most adequate problem-solutions. But when compared to conventional comitology-procedures, the Lamfalussy-procedure is characterised by some institutional innovations which have been left largely unexplored by political scientists.[1] This paper begins here. Its purpose is to examine from an institutional perspective what impact the Lamfalussy procedure has on the involved actors concerning the incentives and constraints for their actions, what expectations can therefore be held for their interaction, and what the assumed results of the procedure are. The paper aims at clarifying whether incentives to act deliberatively and restraints of bargaining power also come into effect in the Lamfalussy procedure, in particular consideration of its institutional peculiarities.

The paper is organised as follows: Firstly, it is elucidated on an abstract level which institutional arrangements have the potential to prevent rational actors from using their bargaining power and respectively induce them to deliberate instead. In a second part, the institutional design of the Lamfalussy procedure is analysed in order to clarify its impact on the influence resources of the

[1]Studies of this procedure are mainly conducted by researcher in finance and law, see for example Moloney 2002, Ferran 2004, Lannoo / Levin 2004, Lastra 2004, Karpf 2005

actors involved and how it constraints their options of action. This allows for the formulation of the research questions for the following empirical studies, which are exemplary answered by a case study of the market abuse directive, two of its implementing directives, and one implementation recommendation.

2. Incentives for and constraints of action within functionally differentiated decision-making systems – bargaining and arguing in international negotiations

In the current academic debate, the prominent assumption is that two complementary modes of interaction exist in international negotiations[2]. The most basic form is the mode of bargaining in which actors try to pursue their interests by using their bargaining power, which is, first of all, based on their alternatives to the cooperation project. In the preceding empirical research about the European Union[3] and other international organisations[4], it has been shown that states in functionally differentiated decision-making systems are also able to switch into the mode of arguing, and this tends to result in more problem-solving decisions. This is reached by the establishment of decision-making systems which systematically constrain the possibilities of the states to use their bargaining power and simultaneously allow them to accept decisions which are made on the grounds of deliberative processes. States are thereby perceived as rational actors whose capabilities of information collecting and processing are limited. In the following paragraph the mode of bargaining which is seen as baseline within international negotiations is described. This is contrasted by the mode of arguing, and the way that functional differentiated decision-making systems induce actors with bounded rationality to switch into this mode of interaction and why this may lead to more problem-adequate decisions is illustrated.

States will normally only enter international negotiations if they agree that cooperation is advantageous for them all. But in most cases they will disagree about the concrete form of the arrangement, and, first of all, about the distribution of the cooperation gains (Elster 1989:50). Bargaining allows states to enforce their interests as far as possible. Their bargaining power is thereby based on their options besides the cooperation arrangement and their importance for the creation of cooperation gains (Moravcsik 1998). In other words, this means the extent of the credibility of their exit threat in negotiations, and the dependence of other states on their cooperation. The cooperation arrangement therefore normally reflects the power distribution of the states and has a positive cost-benefit balance for all states. This allows the implementation of the cooperation arrangements even in the hostile environment of the anarchic international state

[2] e.g. Elster 1998, Saretzki 1996
[3] see first of all Gehring et al. 2005 as well as Gehring/Krapohl 2007
[4] e.g. Gehring/Ruffing 2008, Kerler 2005, Plocher 2005

system. But bargaining is burdened with two problems which may impede problem-solving decisions, in particular in the field of risk regulation: If states fight hard for their preferences they may not be able to guarantee a sufficient level of regulation. Furthermore they have strategic incentives to hold back private information in order to increase their bargaining position. This may obstruct the identification of the best problem-solving decisions by the states (Lax/Sebenius 1986). But decisions which reflect the power distribution of the negotiating actors will only by chance be the best solutions (Kratochwil 1993: 457), even though the states succeeded in identifying this solution.

Actors may, in certain circumstances, be able to use a different mode of interaction, which facilitates their search for adequate problem-solutions and allows for reasonable decision-making. This mode has been introduced into the academic debate as 'arguing', and it has recently become more and more prominent[5]. Arguing is characterised by deliberation, i.e. the exchange of well-founded arguments. This means that the actors enter a discourse about norms and empirical facts and have to back up their claims with reasonable arguments. Ideally, the actors will judge these arguments against superior criteria, which they have already agreed on (Saretzki 1996). Therefore, interacting in the mode of arguing does not mean that the actors have no strategic preferences or do not pursue them, but that they do so by using arguments instead of bargaining power (Risse 2000). This means that positions which cannot be backed up with convincing arguments are no longer maintainable. It is important to mention that the concept of arguing applied in this paper springs from the assumption that actors will use the mode of arguing only if they are prevented by the institutional setting from doing otherwise, which might seem to be a worst case assumption to some readers.

Arguing has different advantages as well as disadvantages for the actors. An important benefit of arguing is that it empowers actors much more than bargaining to identify adequate solutions. The exchange of all available information and the collective judgement thereof eases the identification and solving of collective problems (Adler/Haas 1992). This is of particular importance in the field of risk regulation, because actors in this field are burdened with enormous uncertainties and informational problems (Dehousse et al. 1992). But in order to use this advantage to full capacity, the decisions must reflect the recognised problem-solutions which may not be Pareto-optimal. But it is nevertheless possible for rational actors to accept them if they are either part of a package deal, or if actors engage in a credible commitment to accepting the result of the discourse before they enter it. In the following paragraph it will be sketched how this might work.

[5] see in particular Risse 2000, Gehring 1999, Elster 1998

Two forms of functional differentiation are needed to induce actors to switch to the mode of arguing and to commit them to its results: First of all, there has to be a temporal differentiation: general norms or criteria which seriously constrain the scope for decision-making on lower levels have to be adopted at an upper level. If the norms which are set on the upper level are abstract, i.e. that only principles and general rules are set on this level, actors will be uncertain about the consequences of these on the single implementing decisions made later on and bounded by them. They will therefore also be uncertain about the question of which positions they should pursue in the negotiations concerning principles and general rules. Furthermore, the period of validity of these norms will usually not have been limited in advance. They therefore may apply to cases which are even unknown at the time they were set, for which reason actors do not know their preferences concerning these cases. Brennan and Buchannan call this phenomenon the 'veil of uncertainty'[6]. If, however, preferences concerning single cases are unknown, actors will only agree about norms which they recognise as acceptable with regard to all cases, and which are therefore in line with general interests. In the circumstance of ignorance of the own preferences, this strategy minimises the probability of negative results for each single actor[7]. Such norms cannot however be negotiated by bargaining, because actors do not even know which positions they should pursue using their bargaining power. Instead of this, they face incentives to enter a collective learning process concerning the question of which rules ensure generally acceptable results. However, this mechanism reaches its limits if the norms or criteria of the upper level are either to general and not able to give guidance and constrain the scope for the decision on the lower level, or if they are to specific, so that the actors know their preferences on the lower level. Both will cause problems later on.

Later on (and on a lower level in a hierarchy of norms) the task is to apply and / or to specify the earlier set general principles and rules. In international relations, national delegates will try to pursue their interests at this stage. How can they be prevented from bargaining? First of all, in a highly juridificated international organisation they will no longer be able to prevail with a position which exceeds the norms set before. Whether the decision is in line with superordinate norm can be controlled by judicial court ex post. Secondly, bargaining power is profoundly civilised by giving reason requirements vis à vis actors with different preferences. If actors have to give reasons for their decisions, only views which can be substantiated by convincing arguments taking recourse to the superordinate norms can be held.[8] In this way, actors can switch into the mode of arguing. Such reason requirements are particularly effective and well enforceable if the debate on

6 Brennan/Buchannan 1985
7 ibid.
8 for a similar argumentation see Shapiro 2002, p.229 and the concept of the civilising force of hypocrisy from Jon Elster (1998), who emphasised the effects of public justification.

the norm application is delegated to an independent body that has to substantiate its decision vis à vis the decision-making political body. Such independent bodies are established more and more in international regulatory organisations in the form of expert committees that cope with the huge amount of information and uncertainty problems which actors have to face when deciding about concrete regulatory measures. In these cases expert committees and political bodies form a simple decision-making chain, where the expert committee has to convincingly substantiate its decision in order to influence the decision of the political body, and it therefore has incentives to switch to the mode of arguing (Gehring 1999). It is obvious that this mechanism might work *only* if the committee is *truly independent* from the political organ. Otherwise the bargaining processes that are expected in the political organ (in undifferentiated decision-making procedures) are merely replicated in the expert committee. But if a problem-adequate decision has indeed been reached in the expert committee, it is supposedly not a Pareto-optimal solution and could therefore be overruled by the political organ. But the reasons that induced actors to delegate the norm application or specification debate can also induce them to enter a credible commitment which binds them to the expert committee's recommendation. This might be accomplished by the establishment of a strong agenda setter (Pollack 2003), e.g. if the political organ votes on the expert committee's recommendation by majority. Then no original arguing processes have to take place in the political organ, instead it is bound to the result of arguing processes which are produced at an earlier stage in the decision-making chain (Gehring/Ruffing 2008). So the independent committee has to argue to convince the political body, and at the same time the political body has to be seriously opposed to the expert committee's decision to overthrow it. This mutual dependency does not guarantee that no group of powerful actors enforces its parochial interests, but it creates a serious impedement compared to undifferentiated decision-making procedures. But this is only a basic model of functional differentiation that demonstrates theoretically what mechanisms restrict the scope for bargaining and induce actors to switch to the mode of arguing in functionally differentiated decision-making systems. The Lamfalussy-procedure is much more complex, and a broader range of actors are involved. In the next paragraph, how and to what extent the Lamfalussy-procedure influences the actors' chances will, on an abstract level, be analysed.

3. Incentives for and constraints of action within the Lamfalussy procedure: An institutionalist perspective

The Lamfalussy-procedure is highly differentiated and seriously affects the involved actors' scope for action. The procedure is comprised of four levels of decision-making. On the first level, so-called framework Directives, which lay down the basic political principles for the regulation, are adopted in the codecision procedure. On the second level, the Commission enacts implementing decisions, which are based on the recommendations of expert committees, in the so-called regulatory procedure. Three expert committees have been established, differentiated according to the several kinds of financial services, and are staffed by the national regulatory authorities. On the third level, these expert committees are concerned with the coherent implementation of the level-two measures. For this, they issue recommendations and conduct peer reviews. On the fourth level, the Commission monitors the actual implementation of the measures and opens an infringement procedure if necessary. The Lamfalussy-procedure comprises one additional level compared with the usual comitology procedures and differs, besides this, in several points from them: First of all, the Commission is obliged to conduct comprehensive consultations with all interested market participants (namely when drafting the framework Directive and the implementing measures). Secondly, the Commission assured the Parliament, that its objections concerning the implementing measures will be taken into account, and by doing so it was granted an informal right to influence the comitology procedure for the first time (Vaccari 2005). Thirdly, the framework Directives are subject to the so-called sunset-clause, which means that after a validity period of four years, the legislators (foremost the Parliament) are able to withdraw the implementing rights they granted the Commission. But these clauses will probably never come into force, because the Lamfalussy-procedure is one of the first in which the new regulatory procedure with scrutiny will be applied. The sunset clause was one of the most important tools of the Parliament when forcing the Council to grant it the formal right to influence the comitology decision, but in exchange for this the Parliament had to abstain from the sunset clause (council decision 2006/512/EG; see Bradley 2007). The existing directives are therefore currently being revised. In the following paragraphs it will be elucidated how the procedure influences the scope for action and whether one can expect that it will restrain the room for bargaining and set incentives for arguing.

3.1 Incentives for and constraints of action on the first level

The differentiation of the four levels boosts the amount of abstraction on the first level and therefore thickens the veil of uncertainty. The framework directives are adopted in the codecision-procedure according to article 251 EC-Treaty. The main involved actors are therefore the Council of Ministers, the European Parliament and the Commission. The Commission is obliged to conduct 'a comprehensive consultation with all interested market participants in an open and transparent manner'.[9] Furthermore, they may request technical advice from the expert committee at the same time. Because the results of the consultation are also public, it is possible to trace

[9] Final Report of the Committee of Wise Men on the Regulation of European Securities Markets, February 2001, p. 25

which arguments have been taken into account by the Commission and which have not. The Commission is therefore under pressure to give reasons for its decisions. Although the Commission acts as a strong agenda-setter in the codecision-procedure, the Council and the Parliament are able to change the substance of the draft. The Parliament's incentives are to establish as many details as possible in the framework Directive (Alford 2006), because so far, this the only stage in the procedure where it has a formal influence. This would curtail the expected efficiency gains of the Lamfalussy-procedure (Moloney 2003: 515 f) and diminish the Commission's scope for design on level two. Because the actors are playing an iterated game, the Parliament has a powerful tool for exerting pressure on the Commission to take its concerns on level two into account. The power constellation on level two therefore emanates, in some aspects, from the situation at level one. The member states also have a strong position in the codecision-procedure. Both, the Parliament and the Council of Ministers, have to accept the Directive. Two kinds of cleavages may therefore be important in principle: Firstly, cleavages between the member states in the Council itself, and secondly, and secondly, cleavages between the Council's and the Parliament's positions. If the actors engage in hard bargaining in order to pursue their interests, it is therefore not very likely that they will end up with a problem-adequate solution. This problem can be mitigated if the norms on level one are sufficiently general in nature and a veil of uncertainty comes into effect. This is fostered by the delegation of the legislative initiative to the Commission, whose mandate in the Lamfalussy-procedure is to lay down general principles for regulation in the Directive only. Secondly, the Commission has a self-interest in having very abstract norms at level one, because this widens its scope for action on level two. Therefore, the procedure thickens the veil of uncertainty. But if the actors differ in essence concerning the right way to regulate, they may even be unable to agree on this abstract level. In this case they may decide not to regulate the topic on the European level at all. This could hamper the building of a single European market. Secondly, they may decide to hammer out a detailed package deal, and thereby impair the efficiency gains of the procedure and may end with a lowest common denominator regulation. Thirdly, they may come to an empty compromise, which gives no substantial guidance to the actors on level two. This causes serious problems in the logic of the procedure, as will be shown in the next section.

3.2 Incentives for and constraints of action on the second level

The functional differentiation within level two and the reasons requirements of certain actors at this level restrain the room for bargaining on this level most seriously. Three institutional actors which are engaged in a decision- making chain are involved in the procedure at this level. The procedure starts here with the drafting of an implementing measure by an expert committee.

Three of them have been established, differentiated according to different types of financial services. The experts are deputised to the committee by the member states and are usually members of the national regulatory authorities. Their self-conception is therefore built upon independence and decision-making on the ground of expertise (Moloney 2003). They prepare recommendations for the Commission and the regulatory committee, which are the next two instances in the chain, for the content of implementing measures. The expert committees draft these measures after consulting all interested market participants. If the published draft is criticised seriously by the market participants, a redrafting and second round of consultation is possible. The final draft has to be approved by the committee by way of qualified majority; positions of the minority have to be included in the recommendation. Furthermore, the expert committees publish feedback-statements which give reasons for accepting or refusing certain arguments brought forward by market participants in the consultation. This places the committee under very strong pressure for justification, makes the whole process extremely transparent, and filters out positions which cannot be backed up by good arguments, or at least aggravates to pursue them.[10] These arguments foremost have to refer to the superordinate norms of the framework Directive. If the Directive is holey and gives no guidance in this point arguing is hardly possible, because no decision-making criterion is available.

The addressee of the committee's recommendation is at first not the member states but the Commission. On the grounds of this the Commission drafts the legislative proposal for the regulatory committee and usually keeps very close to the committee's advice (Karpf 2005: 576). Although the Commission is not legally bound to the recommendation, they have to justify any deviation to the member states' representatives in the regulatory committee. Furthermore, it is difficult for the Commission to deviate from the recommendation because they lack expertise compared with the expert committee[11]. The proposal is again subject of a market participant's consultation, conducted by the Commission. But this round is much more opaque, as the Commission is not required to give reasons vis à vis the market participants (although they call for them), but only vis à vis the regulatory committee, and it is therefore unclear, why they accept some statements and reject others. Furthermore it is easier for the Commission to ignore the statements at all. The Commission sends its final draft to the European Parliament, which has three months to give its opinion, which the Commission has to take into account, according to its self-commitment. The proposal then comes to the usually final stage of the decision-making chain at level two, the regulatory committee. Four regulatory committees, which are under the rule of article 5 of Council decision 1999/468/EC, have been established-again differentiated

[10] see for a similar argumentation concerning negotiations in public Elster 1998.
[11] see Gehring/Krapohl 2007

according to different types of financial services[12]. These committees are staffed by high-standing representatives of the national ministries of finance, and are chaired by the Commission. The Commission enacts the implementing measure if the regulatory committee approves it by qualified majority. At the first sight one would expect that the national representatives in the regulatory committee engage in a bargaining process in order to pursue a decision which is in line with their parochial interests. The preceding phase of the expert committee in this case would mitigate only their information problem and help them to clarify their preferences. But it is in fact highly unlikely that they will be able to reach an agreement with a balanced cost-benefit structure for every small regulation by bargaining[13]. Furthermore, because of the intricacy of the situation and the multiplicity of the actors, which makes it unlikely to find complementary cost-benefit structures for every decision, package deals are hard to tie; this means that they are indeed in a deadlock situation and therefore have an incentive to commit themselves to the Commission's proposal and therefore to facilitate the decision-making process[14].

Two institutional features increase the probability that the committee will accept the proposal. Firstly, the Commission is a very strong agenda-setter. Although changes of single points of the proposal are possible in the regulatory committee, a complete redrafting seems unlikely. Secondly, because of the introduction of majority decisions, not every single committee member has to agree with the proposal, so this is a kind of self-commitment of the member states to the Commission's assessment of what a reasonable regulation might be. If the committee refuses to approve the measure, it can be brought to the Council. They have to reject it by simple majority in order to prevent the Commission from enacting it. In this phase, there is in fact a far-reaching delegation (Töller 2002) and member states may therefore try to avoid this phase. If one considers the whole decision-making chain, two points are important: First of all, the institutional design provides mechanisms which foster the commitment of each actor to the precedents assessment. This is the reason why the recommendation of the expert committee, which is the first instance in the chain, is like a red tape in the decision-making process. But, as has been argued above, this recommendation is very likely to be a good solution, because, in the consultation, the experts collect as much information as possible and are induced to recommend only measures which can be supported by reasonable arguments. Secondly, the engagement in a chain gives the latter instances the chance to effectively sanction the earlier ones within the procedure. This means that the Commission has the chance to sanction the expert committee by deviating from

[12] The Lamfalussy-procedure distinguishes four branches of financial services: securities, banking and insurance, occupational pensions and financial conglomerates.
[13] See for this point in complex actor constellations Scharpf 1992.
[14] See for the incentives principals have to engage in a credible commitment Majone 2001.

its recommendation if its reasons are not convincing, and the Commission may again be sanctioned by the regulatory committee if they have no good reasons for deviation by not approving.

3.3 Incentives for and constraints of action on the third level

On this level the actors face far fewer constraints by the procedure when trying to pursue their parochial interests, foremost because of the lesser internal differentiation of this level, which may be outweighed by the increased juridification at this level. The aim at the third level is to create a 'framework of enhanced and strengthened cooperation and networking between (national) regulators with a view to ensuring consistent and equivalent transposition of Level 1 and Level 2 legislation.'[15] According to this aim, the main actors on this level are representatives of the national regulatory authorities, in the capacity of members of the expert committees. They enact implementing recommendations for the level two measures (which are not legally binding) and conduct peer reviews concerning the implementation practices. They thereby decide by the rule of consensus. But the procedure is not only much less differentiated than on level two, it is also much less codified. The committees decide by themselves which procedural prerequisites they establish for their work on this level.[16] The standing orders of the three committees include the self-commitment to use the same consultation procedures as on level two. But because consultation is here self-commitment, it is not as enforceable as on level two. Furthermore, because the committees are not engaged in a decision-making chain, there are no forceful mechanisms to sanction them if they give no respectively no convincing reasons for their decisions. The weak giving-reason requirements and the lacking functional differentiation allow much more room for pursuing parochial interests than on level two. This might be mitigated by the fact that the room for manoeuvre should be much more constrained on level three compared to level two, because according to the logic of the procedure, the norms become more and more concrete in the course of the procedural stages. But it could happen that fierce conflicts remain unsolved throughout the whole procedure and leave loop-holes in the norms, as has been argued in paragraph 3.1. In this case, neither institutional incentives nor law can prevent actors from hammering out problem-inadequate compromises.

4. The example: The Market Abuse Directive (2003/6/EC) and its implementing measures

The aim of this case study is to make plausible how the institutional design of the Lamfalussy-procedure influences the actors' scope for action, and to confirm the assumptions made in a first

[15] Final Report of the Committee of Wise Men, p.40
[16] CESR Document Ref.: 04-527b (2004)

exemplary case. For this, the Market Abuse Directive (in short MAD) (2003/6/EC) has been chosen. As the first Directive which was adopted in the Lamfalussy-procedure, its implementation is comparatively throve, which allows for an analysis of level one, level two and level three measures. On the first level, one must examine whether or not the actors were under a veil of uncertainty. In this case, it is assumed that they could enter an arguing process in order to identify solutions which are of general interest. On the second level, the implementation of two articles of the MAD will be analysed exemplary. Theoretically, it was argued that arguing on the second level is only to be expected if a level one norm exists, which gives sufficient guidance to the actors at level two.[17] In this paper, two cases have been chosen which vary in this respect prima facie. With the first implementing measure provision, 'delay of public disclosure of inside information' (implemented by Directive 2003/124/EC), it will be examined whether the procedure is *in principle* able to induce actors to change in the mode of arguing. The second examined provision 'accepted market practices' (in short AMPs) (implemented by Directive 2004/72/EC) is on worse terms for arguing, because the MAD provides no basis on which to answer the question of what such practices might be. On the second level, the focus will be on the question of whether the expert committee enters processes of arguing, and, in particular, whether they will enter a discourse with the consulted market participants, as it is assumed because of the giving-reasons requirements of the committee. If this is confirmed, the next question is whether the Commission and the regulatory committee can be bound to the experts' recommendation. It is hypothesised that the procedure provides mechanisms to foster both. On the third level only the recommendations for the implementation of the AMP-provisions are analysed, the recommendations for the delay of disclosure were adopted to recently to be subject of this paper. In the theoretical part it was argued that the procedural restraints on this level are weak because of the flimsy giving-reasons requirements and the lacking functional differentiation. This might be outweighed if a high level of juridification had been created on level two before. Otherwise it is expected that in cases of fierce conflicts the actors' bargaining power is hardly restricted and therefore problem-adequate decisions are possible but unlikely and not to mention ensured.

4.1. The Market Abuse Directive: scope of application and conflicts

The MAD was enacted on the 28th January, 2003, after a 20-month debate, as the first Directive under the new Lamfalussy-procedure.[18] The scope of application comprises two types of market

[17] If the norm does not fulfil this condition, deliberation is not unfeasible but much more unlikely, see Gehring et al. 2005

[18] The course of action concerning this Directive and the following Prospect Directive differed slightly from the guidelines of the Lamfalussy-procedure, because no formal consultation of the market participants has been conducted by the Commission on level one. The Commission referred instead to extensive informal consultations.

abuse: insider dealing and market manipulation. Whereas insider dealing was already regulated in the European financial services regime (Directive 89/592/EEC), and therefore merely redesigned, market manipulation was added to the regime. This field was not only not harmonised before, but it was even unregulated in some member states. The definition of 'inside information' in Article 1 of the Directive is central. It states that 'inside information means information of a precise nature which has not been made public, relating, directly or indirectly, to one or more issuers of financial instruments or to one or more financial instruments and which, if it were made public, would be likely to have a significant effect on the prices of those financial instruments or on the price of related derivative financial instruments'. Furthermore the definition was extended, compared to the 1989 Directive, to derivatives of commodities and information conveyed by a client to the person charged with the execution of his orders. According to Article 2, using this information for transactions with financial instruments shall be prohibited. Article 1 (2) of the Directive defines market manipulation. Four types of market manipulation are comprised: Firstly, transactions or orders to trade which give, or are likely to give, false or misleading signals as to financial instruments, secondly, transactions which secure the price of financial instruments at an abnormal or artificial level, thirdly, those which employ fictitious devices or any other form of deception or contrivance, and, as a fourth type, the dissemination of false or misleading signals. The definition is thereby not concerned with whether or not the market manipulation has been committed intentionally (Coffey/Overett 2003).

Only if the actors also switch to the mode of arguing in contentious cases, can the theoretical assumptions made be seen as plausible. Therefore, these contentious points of the Directive are the hard cases for this paper. According to the public documents, there have been several controversial points: Firstly a set of problems as to the rights of journalists, in particular concerning the question what the legal situation should be if a journalist disseminates false or misleading information *by mistake*. A second set of problems centred about the question of whether intent has to be proven in order to hold someone accountable for insider dealing or market manipulation, or whether a negligent act is also liable to prosecution. Other conflicts concerned disclosure of conflicts of interest of persons who produce or disseminate research concerning financial instruments, and the question of whether financial intermediaries should be allowed to execute transactions when they reasonably suspect that they might constitute insider dealing or market manipulation.

Two further conflicts are analysed in the following case study: Firstly, the conflict regarding the disclosure of inside information, in particular the question of whether and when this disclosure might be delayed. Secondly, the conflict regarding the so-called accepted market practices is analysed. This conflict dealt with the provision stating that market practices which are under the definition of market manipulation according to the Directive's definition may nevertheless be lawful if legitimate reasons for them can be brought forward.

4.2 Art. 6 (2) Market Abuse Directive: Delay of the disclosure of inside information

On the grounds of the theoretical assumptions made, it is expected that the procedure ensures problem-adequate solutions in this case. The content of this provision is that inside information has to be disclosed as soon as possible to avoid insider dealing. From the very first, the Commission proposal envisaged exceptions to this rule, i.e. in particular cases no disclosure is necessary.[19] Furthermore, in exceptional circumstances a delay of disclosure should be possible. The Commission proposed the following wording: 'An issuer may at its own risk delay the public disclosure of particular information such as not to prejudice his legitimate interests provided that such omission would not be likely to mislead the public and that the issuer is able to ensure the confidentiality of this information.'[20] This provision was a specification of the disclosure norm in the 1979 Listing Conditions Directive, which was seen to include an implicit exception of the issuer's duty to disclose inside information if the issuer's interests were affected by this (Alford 2006). Undisputed was the point that there may be circumstances where legitimate interests of the issuer are at stake and therefore delay should be allowed, although it was highly controversial what these legitimate interests should comprise. Before the first reading, the Council had already discussed this article in depth.[21] The pivotal point was how far the issuer's right to delay should go and how he should be controlled. The Council discussed whether a duty of the issuer should be established to inform the prudential authority in cases of discourse delay. The result was a provision that allowed the member states to establish this duty, but did not require it. Several delegations stated that they had preferred an obligation to inform for all countries,[22] some withdrew this statement in the further negotiations. The rapporteur of the European Parliament, Robert Goebbels, proposed an amendment to oblige *all* member states to introduce the duty .to inform the prudential authority, which was highly contentious in the competent committee, with the cleavage between the social democrats and the conservatives, who preferred an optional provision. The compromise that succeeded at last was a duty to inform with a right of the authority to choose how to treat this information. A further conflict dealt with the question of in which cases the issuer should definitely not be allowed to delay the disclosure. The German conservative Thomas Mann proposed an amendment to replace the wording 'An issuer may at its own risk delay the public disclosure of particular information such as not to prejudice his legitimate inter-

[19] No public disclosure should be necessary if inside information is only passed to persons who are bound by confidentiality vis à vis the issuer or organisations.
[20] European Commission Document (2001) 281 final, p. 19
[21] Council Document 14385/1/01 Rev 1 (2001), p. 13
[22] The document is ambiguous as to which delegations hold this view.

ests provided that such omission *would not be likely to mislead* the public' with the formulation '*does not mislead*'.[23] This amendment however was not successful in the Parliament.
With regards to the content of the provision, in particular the point, when actors are not allowed to delay the disclosure of an inside information, the actors seem to be under a veil of uncertainty. It does not allow the actors to see its consequences in singular cases. Only its impact on preferences concerning *all* cases is appraisable. Furthermore, the provision is in line with generalised interests and balances the interests of the issuer and the public. This result is interpreted as a first *hint* of deliberation, in particular because it is not necessarily an expected result in a controversial case. Beyond this, the provision is clearly in line with the Directive's goal to improve the market integrity. In the following section the implementation of article 6 (2) will be examined. The provision is on good terms to allow for arguing. It is sufficiently specific for providing guidance to the actors on level two and provides a criterion to which they can refer.

4.3 The implementation in Directive 2003/124/EC

This case makes plausible that the assumed mechanisms in principle can come into effect in the Lamfalussy-procedure. The decision-making process started here with the Commission's request for technical advice to the Committee of European Securities Regulators (CESR) with the mandate to draft a recommendation for '…factors to be taken into account when delaying the publication of inside information'[24]. CESR thereupon established a ‚Market Abuse Expert Group'[25], which developed a consultation paper[26], to give all interested parties the chance to comment on the prospective implementing measure. In this paper, the fundamental decision has already been made and substantiated not to give a definition of legitimate interests, because '[R]eality will probably be more creative than CESR can foresee and new cases will appear that will be on 'the wrong side' of the definition.'[27] Instead, only a list of examples of legitimate reasons should be adopted. Two (non-exhaustive) issues have been proposed: Matters in course of negotiation if disclosure is likely to affect the conclusion of a deal or the normal course of negotiations, and in negotiations designed to ensure the financial recovery of an issuer whose existence is endangered. An additional statement has been made in order to ensure that the issuer is only allowed to delay the disclosure if the public is not mislead by this measure and the issuer is able to guarantee the confidentiality of the inside information. Unfortunately the market participants' comments on

[23] European Parliament Document PE 307.438/51-210 (2002), p.61 seq.
[24] European Commission Document 'Provisional Request for technical advice on possible implementing measures on the future Directive on Insider Dealing and Market Manipulation (Market Abuse)' (2003), p. 4
[25] Each national prudential authority dispatches one expert, who is usually a member of this authority, to these expert groups.
[26] CESR Document Ref.: 02-089b (2002)
[27] ibid. p.30

this consultation paper have been lost.[28] In the so-called feedback-statement, which CESR publishes with regard to all consultations, the market participants' comments are summarised and CESR substantiated the acceptation or rejection of these comments. In principle, the question of whether examples or a definition should be given was contentious. Some participants favoured a list of examples, while others argued that examples would grant no legal certainty. CESR repeated its rationale, given in the consultation paper, and insisted on the list. Most participants agreed with the examples, but as a new point the issue of decisions in two-tier systems with management-board and supervisory-board was raised. It was argued that it could be misleading or erroneous to disclose a decision which has received the approval of the management-board but not yet the approval of the supervisory-board because the latter might refuse to give its assent. CESR accepted this argument and added a further example to the list, which referred to these specific situations. As rationale, CESR stated: 'The modified text now makes it clear that disclosure may be delayed in two-tier company organisations in *certain specific circumstances*, namely, when disclosure before it has been approved would be likely to prove *misleading* to the public.[29]' (my emphasis). Indeed, the reasons referred explicitly to the possible misleading of the public and clarified that a disclosure in these circumstances does not run counter to the prevention of the misleading of the public. CESR adopted this version of the recommendation paper by consensus.
Firstly, it must be stated that the limiting criterion of the MAD played an important role in the discussion concerning its implementation. Furthermore, CESR was very responsive to the consultation participants' arguments and gave convincing reasons for this. Although the reasons why CESR accepted the arguments cannot be proven, it should be stated that criterion and boundary of article 6 (2) have been recognised, and therefore the result might also have been the result of a norm application discourse. Yet it is somewhat surprising that the investor should be protected from misleading by delaying the disclosure of inside information in two-tier systems.

On the grounds of CESR's recommendation, the Commission developed a draft Directive. In doing so they accepted the notion that the list of examples should not be exhaustive and that the two further qualifications of article 6 (2) have to be satisfied in order to legitimise a delay of disclosure. The Commission adopted example one (delay to not affect the normal course of negotiations) and three (exception for two-tier systems)[30] and rejected example two (negotiations to ensure the financial recovery of an issuer). The draft was at first discussed in the European Securi-

[28] Mail from Solveig Kleiveland, CESR-Secretariat, 19.01.2007
[29] CESR Document Ref.: 02-287b (2002), p. 20
[30] ‚Decisions taken or contracts made by the management board of an issuer which need the approval of the supervisory board in order to become effective, where the organisation of such an issuer requires the separation between these boards, provided that such a public disclosure before the approval would jeopardise the correct assessment of the information by the public.' ESC Doc. 12/2003, p.9.

ties Committee (ESC), the regulatory committee for securities. The Commission substantiated, after a request of the committee's members as to why it did not follow the CESR recommendation altogether. However, this rationale is unpublished, and, according to the competent Commission staff member, no longer on hand.[31] Yet the Commission published the draft Directive on its website and again invited all market participants to comment.[32] The participation was again biased. Comments were received from banks, investment societies, issuers and a law society. Some participants asked for the resumption of CESR's example two, negotiations to ensure the financial recovery of an issuer.[33] Another central point was the disclosure in two-tier systems. One request was the inversion of the rule/exemption phrase, which means that, basically, no disclosure would be required before the supervisory-board signed off on a decision.[34] The Law Society, on the other hand, rejected the proposal to make an exemption at all for two-tier systems. They argued: ‚[W]e consider that the proviso in paragraph (2) may emasculate this particular exception - in most cases, if clear and sufficiently detailed disclosure is made, the public should be able to assess the information provided correctly - we are not clear what situation this proviso is intended to cover and why it should be felt necessary to qualify the prior wording.' This argument stands out not only because of its content, but also because it is one of only two arguments which explicitly refer to the misleading of the public as limitation for the issuer's right to delay.[35] The Commission did not vindicate vis à vis the market participants, as they do as a matter of principle, the reasons they accepted some points and rejected others. But they developed three further drafts (ESC 22/2003, Rev 1, Rev 2) before the ESC accepted the Directive; all of them with relevant corrections concerning the delay of disclosure.

An essential correction concerning two-tier systems was made in version 22/2003 Rev 1 of the document. The wording was then: : ‚… provided that a public disclosure of the information before such approval together with the simultaneous announcement that this approval is still pending would jeopardise the correct assessment of the information by the public;'[36] Thereby, the investor is not protected from being mislead by withholding probably misleading information, but by calling his attention to the point that the information might be misleading if he assumes

[31] Mail from Felix Flinterman, Internal Market and Services DG Securities markets Unit (G3), 29.01.07.
[32]These comments are available at http://ec.europa.eu/internal_market/securities/abuse/2003-05-contributions_de.htm
[33] Association Belge de Banques, Federation Bancaire de l'Union Europeenne, Mouvement des Enterprise de France, Zentraler Kreditausschuss. The European Saving Banks Group emphasised that situations of insolvency and takeovers should be acknowldged as legitimate interests.
[34] European Association of Public Banks, Federation Bancaire de l'Union Europeenne, Zentraler Kreditausschuss

[35]The second argument was brought forward by the Association for Investment Management and Research, who acknowledges that relevant information has to be accessible to any investor, and therefore propose a version of example one that allows delay only if the negotiations will not lead to a transaction that would have had a noticeable effect on the company's operations, financial condition or securities prices'.
[36] ESC Doc. 22/2003 Rev 1, p. 6

that the decision made by the management-board is already binding. This wording is completely for the purpose of article 6 (2) of the MAD, and is furthermore in line with the argument of the Law Society. Thereby, it is not reproducible what effect on this wording has to be ascribed to the market participants' comments and what effect to the ESC. It can only be stated that some arguments had no effect on the wording of the implementing measure. All arguments which referred to the statutory role of the supervisory board and the menace disclosure poses had no impact. In a hypothetical norm application discourse this argument need not have had an effect, because it is not in line with the aim and criterion of article 6 (2) MAD. The wording of the final provision is such that it is hardly conceivable to have empirical cases where delay of disclosure might be legitimate. Furthermore, in version 22/2003 Rev 1 of the document, CESR's second example (negotiations to ensure the financial recovery of an issuer) has been resumed, as some market participants had asked for. In this version the wording was tightened insofar as the supplement, ‚when the financial viability of the issuer is in grave and imminent danger' has been added. Furthermore, it was explicitly referred to the qualification that the delay is limited in time. This accentuation, in any case, can not be attributed to the claims of market participants, but presumably to the intention of the ESC members to tighten the eventualities for delay in such cases. Version 22/2003 Rev 2 of the draft document was adopted in the committee by consensus. Although diverse corrections had been made, the final implementing measure is very close to the CESR recommendation. All examples proposed by CESR have been resumed and beyond this no further examples have been added. The rapporteur of the European Parliament, Robert Goebbels, also commented on document 22/2003 Rev1. He criticised that the Commission did not satisfactorily incorporate the European Parliament into the decision-making process.[37] Concerning the implementation of article 6 (2), he was contended by the provisions.[38] The Commission declared in the ESC that they had taken into account all comments from the European Parliament.

All in all in concerning the provision delay of the disclosure of inside information the assumed mechanisms came into effect. CESR consulted the market participants and only accepted arguments, which were in line with the decision-making criterion of the MAD. Furthermore, it fully carried out its giving-reason duty and substantiated its decisions with reference to the superordinate norm. As was expected because of the lacking giving-reasons requirements, the Commission was far fewer responsive vis à vis the market participants. All in all, the Commission as well as the regulatory committee stayed very close to CESR's recommendation, which might be caused by a procedurally enhanced commitment mechanism.

[37] European Parliament Document PE 333.040 (2003)
[38] ibid.p.4

4.4 Article 1 (2) a) MAD: Accepted market practices

The case 'delay of disclosure of inside information' differs, in principle, from the case 'accepted market practices'. Whereas the first provision provides an objective criterion for assessing which acts can be subsumed under the norm, the second provision lacks such a criterion. The Directive is not least silent in this point, because accepted market practices constitute an exemption from market manipulation. Regarding content of these exceptions, it is only required that legitimate reasons can be brought forward for a practice and that it is reasonably expected on one or more markets. All further specification was delegated to level two.

The conflict with regard content dealt mainly with the extent of the exception[39]. The Commission draft of the Directive envisaged no exception; this was proposed as late as in the first reading by the Council, indeed in the wording which was supposed to be adopted in the final Directive later on.[40] In the European Parliament, a nearly identical version of the exception was initially proposed by the social democratic rapporteur Robert Goebbels. Furthermore, one of his amendment proposals stipulated that the Commission should be entrusted with the enacting of guidelines for accepted market practices. Because of the opposition of the conservative faction, this wording could not be adopted. Instead a compromise which seriously tightened the coverage of the exception was negotiated. According to this, only two types of market manipulation could be accepted market practices: Firstly, the conduct to secure a dominant position over the supply of or demand for a financial instrument and the buying or selling of financial instruments at the close of the market with the effect of misleading investors acting on the basis of closing prices (article 1 (2) c, first and second indent). The Council followed the will of the Parliament only with regard to the delegation to the Commission. The extent of the exception was not changed according to the Parliament claims, which accepted this.

Because the content of the provision concerning accepted market practices is so nondescript, the Parliament and the Council obviously engaged in a very wide act of delegation. It may be inferred from the analysis of the decision-making process that this wide act of delegation was not intended by the Parliament or the Council at first, but was indeed the result of an inter-institutional compromise between the two legislators. The Council launched the idea in order to create the possibility of exceptions from the definition of market manipulation, namely accepted market practices. Hereupon, the main factions of the Parliament agreed to a compromise, which seriously tightened the extent of these exceptions. Its amendment proposal linked this correction

[39] Within the Council there was, furthermore, a discussion about the question of who has to bear the burden of proof. Foremost, the Netherlands claimed that the prudential authority had to prove that the market participant had *no* legitimate reasons.

[40] 'unless the person who entered into the transactions or issued the orders to trade establishes that his reasons for so doing are legitimate and that these transactions or orders to trade conform to accepted market practices on the regulated market concerned'.

with the claim to entrust the Commission with the competence to adopt guidelines for these exceptions. This would have lead to a comprehensive harmonisation which the Council had not envisaged in its proposal, but at the same time would have limited the discretion of the Commission seriously. The Council accepted only the entrustment of the Commission, but not the limitation of the scope of accepted market practices and thereby brought this wide act of delegation into being. The Parliament abstained from challenging this wording.

Because of the vague character of the level one norm, it is expected in this case that bargaining power will have much more influence on the implementing measures than in the case 'delay of disclosure of inside information'. This is because this indistinct norm cannot deploy a civilising force on bargaining processes. This might entail a high selectivity of the chances to influence the decision-making process on level two for the benefit of powerful market participants. Concerning the member states, the evolved mechanisms which result form the differentiation of norm-setting and norm-application might not come into force. In these circumstances the decision-making procedure will not be able to *ensure* problem-adequate decision-making. Although this does not necessarily mean that the decisions are inadequate at the end, this is very likely because of the conflicting interests of the actors involved.

4.5 The implementation in Directive 2004/72/EC: The definition of accepted market practices

4.5.1 CESR's recommendation

Accepted market practices have been the most contented point in the ESC when discussing the mandate for the second set of implementing measures of the MAD. Unfortunately, according to the new policy of the Commission, only a summary record of the session is available, which gives no details about the conflict with regard to content. [41] The mandate for CESR included the development of factors to be taken into account when deciding whether a market practice is acceptable or not and the development of guidelines for the review of existing and emerging practices.[42] On the grounds of this mandate, CESR drafted a consultation paper which consisted of three parts of rules the national authorities should take into account when deciding whether a market practice is acceptable [43]: Firstly, general principles, secondly, a non-exhaustive list with factors to be taken into account, and thirdly, procedural rules for the national decision-making process. The general principles included the basic decision against a general registration require-

[41] ESC Document 9/2003, p. 2.
[42] European Commission Document ‚Formal Request for Technical Advise on Possible Implementing Measures on the Directive on Insider Dealing and Market Manipulation (Market Abuse)' (2002)
[43] CESR Document Ref.: 03-103b (2003)

ment for practices, which means that market participants do not have to register a practice before they are allowed to use it. Furthermore, CESR proposed seven factors to be taken into account. Each factor is a kind of a continuum, which means that a practice is more likely to be acceptable, the better a practice fits a factor (or the other way round). These factors could not be educed from the MAD, but for an earlier implementing measure, CESR had identified signals of market manipulation. [44] The factors were transparency, the extent to which the practice in question enables market participants to react properly to the said practice, prevalence, risks for the integrity of the wider market inherent in the practice, the extent to which a practice breaches existing rules or regulations designed to prevent market manipulation on the market in question, structural characteristics of the market in question including the type of financial instruments and extent of retail participation in the market, and the degree to which the practice has an impact on market liquidity and efficiency.[45] The factor conformance with national anti-market-manipulation law is of crucial importance. On the one hand, it inhibits a far-reaching European harmonisation. On the other hand, it is a safeguard against a regulatory race to the bottom, as it forestalls the possibility that practices become accepted in one market only because they are accepted in another one, although they breach existing national law against market manipulation. Besides these factors, CESR submitted three procedural rules: Firstly, national authorities should consult market participants when deciding about a specific practice. Secondly, they should make their decision public. And thirdly, they should pay attention to new developments on the market.

In the following consultation, CESR was very responsive vis à vis the market participants. Almost all participant comments (participants again mainly being issuers, banks, investment firms and exchanges) were accepted by CESR and included in the final recommendation.[46] The most contentious topic was the level of harmonisation that should be sought.[47] Some participants claimed that the national authorities should come to consent regarding the acceptability of market practices.[48] Others stressed that no uniform list of accepted market practices should be created, because the characteristics of the national markets are too different to allow a uniform treat-

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[44] see Directive 2003/124/EC

[45] CESR Document Ref.: 03-103b (2003), p. 9

[46] In one case, antagonistic arguments were brought forward by the market participants. CESR followed the majority and vindicated its decision in this way. In a second case, an argument was brought forward which was in open conflict with the aim and provisions of the MAD. It was therefore rejected.

[47] In the Feedback-Statement, they acknowledged: 'The key issue that emerged from the feedback was the appropriate degree of harmonisation that should be sought at level 2 or level 3. It was accepted that harmonisation and convergence of views on particular practices was desirable, but it was also recognised that there would be occasions when the same practice would be regarded as acceptable by one competent authority and not by another. Detailed discussions on particular practices should therefore be left to level 3 rather than level 2.'
see CESR Document Ref.: 03-213b (2003), p.5

[48] Association Francaise des Entreprises d'Investissement, BNP Paribas, Italian Association of Financial Intermediaries, Nederlandse Vereniging van Banken, Italian Bankers Association (claimed that an authority should accept a practice if the majority of national regulatory authorities accepts it)

ment.[49] CESR took both positions into account. Its final recommendation, it invited the national authorities to consult each other in order to reach a consensus with regard to the acceptability of a practice, but did not require this consensus for its acceptation in a single market. In addition to this, a multiplicity of minor corrections was made. Nearly all factors were specified and the duties to consult market participants on the national level were strengthened. To sum up, no hints for a selective influence of powerful market participants could be found. The problem was much more the selective participation of market participants. CESR's rationale for accepting or rejecting arguments was much less reproducible, because no criterion it could refer to was at hand. Therefore, the risk of capture was much higher than in the 'delay of disclosure of inside information' case.

4.5.2 The Commission's draft and the regulatory committee

The Commission's draft[50] was very close to CESR's final advice.[51] One of the most interesting things is the deletion of the requirement that the national authorities should consult each other in order to reach a consensus. The concerned national authorities had proposed, in their capacity, as CESR members had previously proposed this obligation.[52] The Commission again consulted on the grounds of this working document. The document was criticised for the deletion of the coordination requirement and, in general, the low level of harmonisation it envisaged.[53] Furthermore, the Commission was attacked for not giving reasons for its deviations from the CESR recommendation, because a rationale would enable interested parties 'to make a more focused and informed contribution to the Commission's draft'.[54] The Commission made no corrections on the grounds of this consultation, and the draft was discussed in the ESC for the first time in November 2003. The Commission gave reasons for its deviations from the CESR recommendation only with regard to those points that delegations had explicitly asked for.[55] AMPs were not among them, so the corrections concerning this point were obviously not contentious. This allows the assumption that the Commission did not try to exploit its agenda-setting power by deleting the

[49] Association of British Insurers, Association of German Banks
[50] working document ESC/38/2003
[51] CESR Document Ref.:03-212c (2003)
[52] Because the Commission does not substantiate its decisions publicly, it is unknown what motivated the Commission to delete this phrase. This deletion may result in a lower level of harmonisation, because less coordination between the national authorities is required. If one presumes that the Commission favours a high level of harmonisation in general, one might infer that the Commission saw no chance of success for this provision in the ESC.
[53] Particularly by the Association Francaise des Entreprises d'Investissement. The Italian Banking Association claimed 'a complete redrafting of the said provisions in order to ensure an undoubted consistency between the aforesaid Directive goals and the factors as well as the factors to be accordingly taken into account.' Comment p.1
[54] Comment of the European Banking Federation, p. 1
[55] documented in the summary record of the meeting

coordination requirement, but acted with the consent of the member states' delegations.
In the ESC, the factors as the material part of the provisions were hardly disputed at all in contrast to the procedural rules. The coordination obligation for national authorities had no majority in the committee. A coalition of several national delegations, the representative of CESR and the rapporteur of the European Parliament successfully pushed a compromise to use CESR as a forum for discussion in cases when national authorities are discordant on the acceptability of a market practice.[56] This provision was relegated to the recitals of the Directive. Furthermore, two delegations challenged whether there should be an obligation to consult the market participants on the national level. This resulted in a provision to abstain from consultations if an investigation concerning market manipulation is under way. The committee members further agreed to involve CESR in the publication of the national acceptability decisions, which resulted in a central register for AMPs.

The final Directive (2004/72/EC) is very close to the CESR recommendation. All factors CESR proposed were adopted. Furthermore, the giving-reasons requirements for national authorities (when deciding about AMPs) have gained approval, and are of particular importance if the authorities are discordant about them. But the deletion of the coordination requirement for national authorities could result in a lower harmonisation level than CESR intended. The level of harmonisation is further determined by the factor 'congruence with existing anti-market-manipulation law or codes of conducts, which, not least of all, means national law. The unspecific and wide exemption on level one, which seemed, at the first sight, to result in maximum harmonisation, was caught on level two by the acceptance of national law as a standard. De facto, this rule results in a reaquiring of the competences by the member states and a comparatively low level of harmonisation. In order to come to an evaluation of the effect of the institutional setting on this stage, it must be stated that the assumption that the Commission and the ESC lack the expertise to deviate from the CESR recommendation in technical matters has been justified by the fact that only procedural rules were disputed and revised by these two organs. Furthermore, the Commission was not at all responsive vis à vis the consultation participants, which was not to costly for the Commission, because it is not engaged in giving-reasons requirements at this stage.

4.6 CESR's recommendation on level three

Accepted market practices were the first provision to be dealt with on level three of the Lamfalussy-procedure. The extremely wide discretion the actors faced on level two was narrowed con-

[56] ESC Document 8/2004 „Summary Record of the 18th Meeting of the European Securities Committee / Alternates", p. 5 as well as European Parliament Document PE 333.128/rev.1 (2004), p.3

siderably by the provisions adopted at this level. But, as has been elaborated above, the procedure on level three differs significantly from that of level two. Here CESR develops recommendations, which are not legally binding, for a coherent implementation in the member states. Thereby, it is the sole institutional actor, which means that the procedure is much less functionally differentiated, and CESR is not engaged in a decision-making chain.

A crucial point in the first draft (and as well in the final recommendation) was a form that every national authority has to fill in when deciding whether or not a market practice is acceptable. All factors laid down in the Directive 2004/72/EC are mentioned here and followed by a wild-card, where the evaluation of the practice concerning this factor has to be substantiated. In the consultation, this form was hardly contentious.[57] This is not surprising, thinking of the fact that these factors became binding law on level two. But the few comments made were all rejected by CESR without a reproducible rationale. [58] A further important part of the draft was a long blacklist, which encompassed market practices that are surely market manipulation. This list is the only part of the document that deals with concrete practices. Furthermore, it is the sole part that is truly harmonised, because it is addressed to all national authorities, whereas all further decisions must be made by the national authorities by themselves, and without a coordination obligation. In the consultation it was disputed whether or not a blacklist should be part of the recommendation, and what practices should be included. [59] Almost all practices were qualified by one or more participant as, in principle, not manipulative. CESR did not substantiate in the draft or in the feedback-statement *why* these practices are manipulative. It accepted some comments from consultation participants, rejected some, and ignored many. In its response to the consultation, CESR deleted no practices from the list, but specified many of them, what might improve the applicability of the provisions. But in the feedback-statement, no rationale exists that explains why some comments were accepted and others ignored. This prompts the question of what motivated CESR to make these selective corrections. One might assume that CESR was more responsive against potentially powerful actors. But facts do not confirm this assumption. The London Stock Exchange, for example, as a presumably powerful actor, was successful with some of its arguments and ignored with regard to others. The case also fails to substantiate the assumption that actors with the better arguments, opposed to actors with weak arguments, were able to influence the draft. Very few coherent rationales were given and neither CESR nor the participants assiduously referred to the level two factors or principles. Because the CESR made corrections to some groups of examples and left others untouched, the most convincing explanation is

[57] All public comments can be found on www.cesr-eu.org

[58] CESR Document Ref.: 05-247 (2005)

[59] Assonime (Associazione fra le società italiane per azioni) and the European Association for Listed Companies disapproved the concept of a list. The argument was that it would be difficult to identify practices that constitute market manipulation per se.

that CESR members made a package deal and were not willing to untie the package in order not to jeopardise the reached compromise.

All in all, CESR deficiently substantiated its decisions on level three, and it is therefore unclear how, and on what grounds, its decisions were accomplished. CESR neglected its self-imposed giving-reasons requirements and was much less responsive to the market participants' comments than on level two. Because of the lacking engagement in a decision-making chain, CESR is lacking the institutional incentives for this, and for the same reasons the addressees of the rationale fail to sanction CESR for this behaviour. The market participants have no formal possibility to press CESR to take their comments into account and to give convincing reasons for their decision. In contrast, the Commission and the ESC are able to sanction CESR on level two. Therefore no mechanisms exist that weaken parochial interests on level three. If CESR members find it acceptable to bargain about parochial interests, they cannot be prevented from this by the decision-making procedure. Whereas on level two adequate decisions could not be ensured because of the lack of substantial decision-making criteria on level one, on level three such criteria were available. The explored civilising mechanisms nevertheless did not come into force, because CESR absconded from its self-imposed giving-reasons requirements. CESR therefore did not tap the full potential of the procedure to improve the adequacy of the regulation. Additional information from the market participants was wasted and the failure to substantiate the decision adequately lowered the level of reflection of the decision.

5. Conclusion

The theoretical analysis of the Lamfalussy-procedure allowed for drawing the conclusion that the procedure is, in principle, able to contain the bargaining power of the actors involved and to foster problem-adequate decisions. The functional differentiation of the procedure can contribute to the intensification of the veil of uncertainty and induce the legislating actors to deliberate. But provisions which are to general and give no guidance on level two, or norms which are to specific cause problems on level two. In the first analysed case (delay of the disclosure of inside information) hints on the effect of a veil of uncertainty were found and the enacted provision seems to balance the interests of the issuer and the public, and appears to be a problem-adequate solution. In the second case (AMPs) convincing evidence was found that the core conflict dealt with was the level of harmonisation and that therefore no veil of uncertainty exists. The result was a compromise that enacted delegation without substantial constraint of the agent.

On the level of implementing measures, it was elaborated on an abstract level first how giving-reasons requirements impede the assertion of parochial interests and promote the consideration of arguments of the commenting market participants. But the acceptance of these arguments is only convincingly justifiable if they refer to the aims and criteria of the superordinate framework Directive. To judge by the result, these mechanisms worked in the first analysed case. In the second case (AMPs) no criterion was available from the framework Directive; hence it was much easier to insist on particular positions. But no hints for a selective *influence* of the market participants were found. Instead the problem in both cases was rather the selective *participation* of the market participants.

The next step in the argumentative chain was that the Commission is bound to CESRs recommendation, because of its own giving-reasons requirements vis à vis the regulatory committee and its lack of expertise compared with that of CESR. This was empirically confirmed and is also in line with the findings of Karpf (2005) who states that the Commission generally keeps the draft very close to the CESR-recommendation. With regard to the 'accepted market practices' case, it is, first and foremost, interesting to see that the Commission accepted the technical provisions, but deviated from the draft in procedural matters, where much less expertise is necessary.

Thirdly, it was argued that the member states are committed to the assessment of the Commission because of the majority rule in the regulatory committee. In both analysed cases the committee accepted the draft with consensus. But as a matter of principle this commitment will reach its limits when, for the majority of the member states, the draft implies a negative cost-benefit structure.

On level three only one case study has been conducted, so no very far reaching conclusions can be drawn. But as it was expected, CESR's behaviour on level three differed considerably from its behaviour on level two. The sole analysed case confirms the assumptions made, CESR neglected its giving reason requirements and ignored many of the comments made by the market participants. It seems plausible that some provisions were not open to the helpful suggestions of the market participants, because they were part of a package deal of the CESR members. These provisions might therefore be suboptimal regulation. The high level of juridifcation on level two had had the potential to stave off this drawback, but because of the lacking rationale it is unclear on the grounds of what factors the practices were judged as being manipulative. Although it is evident prima facie that the level two norms constrained the discretion on level three considerably, a final assessment has to be left to ex post judicial review. The assumption that the decision-making procedure on level three gives not enough incentives for argumentative processes and instead allows decisions on the grounds of bargaining power, in contrast to the procedure on level two, has to be substantiated in further empirical research.

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