TRANSATLANTIC MUTUAL RECOGNITION IN THE FIELD OF GLOBAL FINANCIAL REGULATION

Lessons We Can Learn from the Experience with the Inter-European Mutual Recognition Approach Developing from ISD to MiFID

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Abstract

International cooperation and coordination among countries is a highly sought after goal for many. In that regard, in order to achieve international cooperation and coordination, this Article focuses on the concept of mutual recognition and the key areas of global financial regulatory reform to which the concept could be applied. The benefits of mutual recognition are increased market liberalization, facilitation of private cross-border movement, and increased regulatory standards. To discuss the concept of mutual recognition, this Article examines the European Union/European Economic Area approach provided by the Markets in Financial Instruments Directive ("MiFID"). This Article reviews the EU's idea of a single European Market based on fundamental freedoms. Further, it concludes that in order to establish a system of mutual recognition between two countries in a particular field of financial regulation, the countries must have some form of regulatory coordination or harmonization.

I. Introduction

In the course of the global financial regulatory reform following the recent financial crisis, one could frequently read and hear, in particular from the G-20, about the importance of devices such as global guidelines, global regulatory frameworks, international cooperation, and international coordination or harmonization.[1] Increasingly, a strong case is also made for the concept of mutual

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1. *See* G-20, Leaders' Statement at the Pittsburgh Summit, (Sept. 24–25, 2009), *available at* https://www.g20.org/sites/default/files/g20_resources/library/Pittsburgh_Declaration.pdf; G-20, Toronto Summit Declaration, (June 26–27, 2010), *available at* https://www.g20.org/sites/default/files/g20_resources/library/Toronto_Declaration_eng.pdf; Charter of the Fin. Stability Bd., *available at* http://www.financialstabilityboard.org/publications/r_090925d.pdf; Letter from Mario Draghi, Chairman of the Fin. Stability Bd., to the G-20 Leaders (June 24, 2010), *available at* http://www.financialstabilityboard.org/publications/r_100627a.pdf?noframes=1; Communiqué, Meeting of the G-20 Fin. Ministers and Cent. Bank Governors (Apr. 14–15,

recognition or a similar device.[2] While broad consensus existed as to the need for joint efforts towards sustainable reform, the coordinating effect of the actual efforts taken by the G-20 members turns out to be at least less than the well-intentioned statements once suggested.[3] Some authors even argue that the

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2011), *available at* http://www.mof.go.jp/english/international_policy/convention/g20/g20_110415.htm; Press Release, Council on Global Fin. Regulation ("CGFR"), Council Calls on the G20 to Enhance International Financial Regulatory Coordination (Apr. 14, 2011), *available at* http://cgfr.org/; TRANSATLANTIC COAL. ON FIN. REGULATION, INTER-JURISDICTIONAL REGULATORY RECOGNITION: FACILITATING RECOVERY AND STREAMLINING REGULATION 12 (June 2012), *available at* http://www.sifma.org/workarea/downloadasset.aspx?id=8589939089 ("overwhelming importance"); *Addressing the Global Dimension of Capital Markets Regulation and Solving Third-Country Access to the EU and Extra-Territoriality Issues*, EUROFI (Mar. 29, 2012), *available at* http://www.eurofi.net/wp-content/uploads/2012/09/Extra_territoriality.pdf ("has become a priority"); Edward F. Greene & Ilona Potiha, *Examining the Extraterritorial Reach of Dodd-Frank's Volcker Rule and Margin Rules for Uncleared Swaps—A Call for Regulatory Coordination and Cooperation*, 7 CAPITAL MKTS. L.J. 271, 272, 308–11, 316 (2012); Edward F. Greene & Omer S. Oztan, *The Attack on National Regulation: Why We Need a Global Framework for Domestic Regulation*, 4 CAPITAL MKTS. L.J. 6, *passim* (2009); Edward F. Greene & Joshua L. Boehm, *The Limits of "Name-and-Shame" in International Financial Regulation*, 97 CORNELL L. REV. 1083, *passim* (2012); Edward F. Greene, *Dodd-Frank and the Future of Financial Regulation,* 2 HARV. BUS. L. REV. ONLINE 79, 79–80 (2011), *available at* http://www.hblr.org/wp-content/uploads/2011/10/HBLR-Greene_Symposium1.pdf; Edward F. Greene, Syllabus of the Seminar *Issues on Global Regulatory Reform*, Columbia Law School 3, 14 (Fall 2013) (on file with Columbia Law School, Courseweb); STEFFEN KERN, TRANSANTLANTIC ACAD., THE REAL G2: AMERICANS, EUROPEANS, AND THEIR ROLE IN THE G20, (Feb. 2011), *available at* http://www.transatlanticacademy.org/sites/default/files/publications/Kern%20G20.pdf; *see also* CGFR, INITIAL REPORT: PRACTICAL MEASURES FOR ENHANCING INTERNATIONAL FINANCIAL REGULATORY COORDINATION 5, 19 (Apr. 14, 2011); *cf. also* Edward F. Greene, *Resolving Regulatory Conflicts Between the Capital Markets of the United States and Europe*, 2 CAPITAL MKTS. L.J. 5, 39 (2007) (explaining already in 2007 that, "[a]lthough political factors may impede changes in the regulation of cross-border activities, the markets themselves and the institutions that participate in them will continue to become more global" so that it "will be incumbent on the regulators of the various jurisdictions involved in these markets to view regulation more globally").

2. *See generally* TRANSATLANTIC COAL. ON FIN. REGULATION, IOSCO: FACILITATING MUTUAL RECOGNITION AND SUBSTITUTED COMPLIANCE (Nov. 2012), *available at* http://www2.isda.org/attachment/NTIzMA==/IOSCO%20paper%20-%20FINAL%20091112.pdf; TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1; Steven Maijoor, Chairman of ESMA, EVCA Investor's Forum Keynote Speech, at 3 (Mar. 15, 2012), *available at* http://www.esma.europa.eu/system/files/2012-195.pdf; Eddy Wymeersch, Chairman of CESR, *Global and Regional Financial Regulation: The Viewpoint of a European Securities Regulator*, 1 GLOB. POLICY J. 201, 203 (2010); Edward F. Greene, *Beyond Borders: Time to Tear Down the Barriers to Global Investing*, 48 HARV. INT'L L.J. 85, *passim* (2007); Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 5–6; Edward F. Greene, *Dodd-Frank: A Lesson in Decision Avoidance*, 6 CAPITAL MKTS. L.J., 29, 79 (2011); Greene & Oztan, *supra* note 1; Greene & Boehm, *supra* note 1, at 108687, 113334, 1136–37; Ethiopis Tafara & Robert J. Peterson, *A Blueprint for Cross-Border Access to U.S. Investors: A New International Framework*, 48 HARV. INT'L L.J. 31, *passim* (2007); Howell E. Jackson, *A System of Selective Substitute Compliance*, 48 HARV. INT'L L.J. 105, *passim* (2007); Eric J. Pan, *A European Solution to the Regulation of Cross-Border Markets*, 2 BROOK. J. CORP. FIN. & COM. L. 133, 161–62 (2007); Jerry Ellig & Houman B. Shadab, *Talking the Talk, or Walking the Walk? Outcome-Based Regulation of Transnational Investment*, 41 N.Y.U. J. INT'L L. & POL. 265, 265–66 (2009); Leonard Ng, *"Third country" Issues in Current EU Financial Services Regulation*, 27 BUTTERWORTHS INT'L BANKING & FIN. L.J. 287, 289 (2012); Nicholas W. Turner, *Dodd-Frank and International Regulatory Convergence: The Case for Mutual Recognition*, 57 N.Y.L. SCH. L. REV. 391, 417–22; *see also* Pierre-Hugues Verdier, *Mutual Recognition in International Finance*, 52 HARV. INT'L L.J. 55, 58, 62–63 (2011); Ellen Davis, *Protectionism Brings Trouble at the Border* (Feb. 22, 2012), *available at* http://www.efinancialnews.com/story/2012-02-20/protectionism-brings-trouble-at-the-border ("Lobby groups and trading firms are campaigning for . . . better forms of mutual recognition"); *cf. also* President Barack Obama, 2013 State of the Union Address (Feb. 12, 2013), *available at* http://www.whitehouse.gov/the-press-office/2013/02/12/remarks-president-state-union-address (explaining that there will be talks on a comprehensive Transatlantic Trade and Investment Partnership with the European Union "because trade that is fair and free across the Atlantic supports millions of good-paying American jobs").

3. *Cf.* CGFR Press Release, *supra* note 1; TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 3, 8; Greene, *Dodd-Frank and the Future of Financial Regulation*, *supra* note 1, at 79–80; Greene, *Dodd-Frank*, *supra* note 2, at 78–79; Greene, *Seminar Syllabus*, *supra* note 1, at 4, 13; Greene & Boehm, *supra* note 1, at 1086; *cf. also* FIN. STABILITY BD., OVERVIEW OF PROGRESS IN THE IMPLEMENTATION OF THE G20 RECOMMENDATIONS FOR STRENGTHENING FINANCIAL STABILITY (June 19, 2012), *available at*

global financial regulatory reform is increasingly becoming protectionist.[4]

This Article focuses on the concept of mutual recognition. Because the exact meaning of mutual recognition is not always clear, this Article will first look for a definition and explanation of mutual recognition, contrasting it with other concepts as a means to achieve reform. It will also show the significance of mutual recognition and potentially important fields in which mutual recognition could be applied in the course of the global financial regulatory reform. Then, this Article will present a discussion on the question of which requirements should be met before mutual recognition can reasonably be established. This discussion will be presented in light of Professor Pierre-Hugues Verdier's conclusion that commentators outside Europe "were increasingly advocating mutual recognition agreements as a substitute for substantive harmonization."[5]

In order to analyze the issue, this Article will examine the inter-European Union ("EU")/European Economic Area ("EEA")[6] mutual recognition approach provided by the Markets in Financial Instruments Directive ("MiFID")[7] and its predecessor, the Investment Services Directive ("ISD").[8] At the moment, the final version of the MiFID II and its implementing measures are in the process of being finalized. However, the final measures will likely not change the inter-EU/EEA harmonization and mutual recognition approach of the MiFID.[9] The inter-EU/EEA model of the MiFID and its genesis may shed some light on the reasonable minimum requirements for establishing mutual recognition by, among other things, delivering some experience in dealing with mutual recognition and by demonstrating difficulties inherent in such an approach. The MiFID will be used to illustrate the concept of mutual recognition because of its importance within the EU/EEA. The MiFID was the cornerstone of implementing the forty-two measures which make up the Financial Services Action Plan ("FSAP") of 1999 aiming at the creation of a single market for financial services in the EU/EEA.[10] Moreover, the MiFID applies to securities intermediaries and securities exchanges, one of the first fields in which the United States and the EU could work toward a mutual recognition agreement.[11]

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http://www.financialstabilityboard.org/publications/r_120619a.pdf (explaining that much further work is needed); Turner, *supra* note 2, at 392 ("coordinating financial regulations is much easier said than done").

4. Davis, *supra* note 2; *see also* TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 2, at 3, App'x 1 (stating that "little progress has been made in the past decade in establishing substituted compliance", and that, "[u]nfortunately, the post-crisis regulatory repair programme has incorporated, in certain areas, elements of protectionism and extraterritoriality, which undermines the capacity to deliver early post-crisis economic recovery and the need for coherently-regulated and more open markets"); *cf. also* Greene, *Dodd-Frank*, *supra* note 2, at 78–79 (discussing "mutual skepticism with which regulators and markets regard one another in light of the crisis" so that "mutual recognition seems to have lost favour"); Greene, *Seminar Syllabus*, *supra* note 1, at 14; Verdier, *supra* note 2, at 87–88, 101–02.

5. Verdier, *supra* note 2, at 62, 64–65, 98–99. Some of the support Verdier offers actually refers to an exemptive approach. This Article will show that there is a significant difference between mutual recognition and an exemptive approach.

6. The European Economic Area (EEA) includes the EU zone as well as Iceland, Liechtenstein, and Norway, but not Switzerland.

7. Directive 2004/39, of the European Parliament and the Council of 21 April 2004 on Markets in Financial Instruments, 2004 O.J. (L 145) 1 (EU) ("MiFID").

8. Directive 1993/22, of the Council of 10 May 1993 on Investment Services in the Securities Field, 1993 O.J. (L 141) 27 (EC) ("ISD").

9. For discussion of third country access to EU markets under MiFID II, *see infra* § IV.B.

10. *See* Verdier, *supra* note 2, at 74.

11. Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 34.

Finally, the MiFID is a good example of how the Lamfalussy Process works. The Lamfalussy Process is a special procedure in the EU of common rulemaking, implementation, interpretation, and enforcement.[12] The Lamfalussy Process may provide for elimination of some big concerns the United States has as to fragmentation of financial laws and their inconsistent enforcement within the EU.[13] Thereby, the Lamfalussy Process could strongly contribute to the adoption of a mutual recognition approach in the relationship between the United States and the EU/EEA, instead of only between the United States and some European countries.

Once a suggestion is made as to which reasonable minimum requirements generally should be met before mutual recognition can be established, this Article will consider whether these preconditions are already fulfilled within the transatlantic relationship between the United States and the EU. Moreover, the future prospects will be considered. Finally, this Article will conclude by formulating basic recommendations recapitulating the principles found. In doing so, it must be kept in mind that the United States and the EU currently comprise the two most important financial markets in the world, standing for over seventy percent of the world's capital markets activity.[14]

II. Fundamentals

A. Definition of Mutual Recognition and Differentiation of the Concept

Mutual recognition is a concept which may be defined as an agreement among two or more states in which each state recognizes the adequacy of the other state's or states' regulation and/or prudential supervision of respective institutions, products, or activities as a substitute for its own regulation and/or supervision.[15] Mutual recognition usually means that a host country neither imposes special registration or license requirements, nor substantive double regulation on foreign products, institutions, or activities.[16] The basic principle is

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12. *See infra* § III.C.

13. *See infra* § IV.A.2.

14. *See* Press Release, SEC, Statement of the European Commission and the U.S. Securities and Exchange Commission on Mutual Recognition in Securities Markets (Feb. 1, 2008), *available at* http://www.sec.gov/news/press/2008/2008-9.htm. In the meantime, markets have not only recovered from the recent crisis but overshot all-time records, so that the figure of 2008 should still be valid. *Cf. also* TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 2; Verdier, *supra* note 2, at 101; Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 5; Greene & Boehm, *supra* note 1, at 1098; Carlo R.W. de Meijer & Michelle H.W. Saaf, *Mutual Recognition and the Transatlantic Dialogue: The Concept and its Progress*, 3 J. SEC. L., REG. & COMPL. 124, 131 (2009); KERN, *supra* note 1, at 5; EUROFI, *supra* note 1.

15. Verdier, *supra* note 2 at 57, 63; Matteo Ortino, *The Role and Functioning of Mutual Recognition in the European Market of Financial Services*, 56 INT'L & COMP. L.Q. 309, 317 (2007); Pan, *supra* note 2, at 140–41; de Meijer & Saaf, *supra* note 14, at 128; Greene, *Seminar Syllabus*, *supra* note 1, at 4; *see also* Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 6; Greene & Potiha, *supra* note 1, at 310; Greene & Oztan, *supra* note 1, at 12; Greene & Boehm, *supra* note 1, at 1137; Patrick B. Griffin, *The Delaware Effect: Keeping the Tiger in Its Cage: The European Experience of Mutual Recognition in Financial Services*, 7 COLUM. J. EUR. L. 337, 337 (2001).

16. Ortino, *supra* note 15, at 317, 319; Pan, *supra* note 2, at 140–41; de Meijer & Saaf, *supra* note 14, at 128; *see also* Verdier, *supra* note 2, at 57, 63; Greene & Potiha, *supra* note 1, at 310; Greene & Oztan, *supra* note 1, at 13; Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 6; Griffin, *supra* note 15; Kalypso Nicolaidis & Gregory Shaffer, *Transnational Mutual Recognition Regimes: Governance without Global Government*, 68 LAW & CONTEMP. PROBS. 263, 264 (2005).

that the home country's supervisory authority oversees the respective institutions or activities according to the home country's substantive rules.[17] This means that, in principle, there is no supervision by the host country's supervisory authority, and, moreover, the host country's substantive rules will not be applied by the home country's authority.

Thus, mutual recognition does not directly address the issue of achieving a common standard of regulation or prudential supervision, subject to international coordination and harmonization.[18] However, mutual recognition usually rests on a shared judgment that in both directions, the home country's regulation and prudential supervision is, at least to some extent, comparable to that of the host country.[19] Therefore, though mutual recognition does not involve direct coordination as to rulemaking, there is some relationship between mutual recognition and regulatory coordination or harmonization.[20] Arguably, the key question is which, if any, level of coordination or harmonization is necessary in order to enable regulators to prudently consider a mutual recognition agreement.

While remaining mindful of mutual recognition, the concept of "substitute compliance" is also important to note.[21] Substitute compliance is in effect similar, though not equivalent, to mutual recognition. Substitute compliance allows a competent authority to exempt foreign institutions or activities from substantive regulation if certain conditions are met. If reciprocal treatment is a prerequisite to substitute compliance,[22] an institution or activity will only be exempt if the competent authority of its home country would grant exemptions in comparable situations in the other direction as well. This is similar to what happens under a mutual recognition agreement. However, under a substitute compliance approach the institution will not necessarily be exempt from individual application or registration requirements, nor from all respective aspects of prudential supervision.

Furthermore, arguably the most important point of divergence between the concepts of mutual recognition and substitute compliance is the process of reaching market access without the burdens of double regulation. In the field of financial regulation, the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"),[23] speaks about the precondition of "comparable, comprehensive supervision and regulation" and about "appropriate system[s]."[24] The appropriate rulemaking authorities charged with implementing

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17. *Cf., e.g.*, MiFID, *supra* note 7, recital 2 (discussing the Home Country Principle).

18. *Cf.* Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 6 (defining that harmonization "seeks to achieve substantial similarity in multiple regulatory systems so that market participants face no additional burden in pursuing cross-border activities"); Greene & Potiha, *supra* note 1, at 308.

19. *See* Verdier, *supra* note 2, at 63; Greene & Potiha, *supra* note 1, at 309; Greene & Oztan, *supra* note 1, at 13; Greene, *Seminar Syllabus*, *supra* note 1, at 4; de Meijer & Saaf, *supra* note 14, at 128; *see also* Tafara & Peterson, *supra* note 2, at 59–60.

20. *See* Ortino, *supra* note 15, at 336.

21. *Cf., e.g.*, Press Release, CFTC, Proposal on Cross-Border Application Rules for Swap Provisions (June 29, 2012), *available at* http://www.cftc.gov/PressRoom/Press Releases/pr6293-12; *cf. also* Tafara & Peterson, *supra* note 2; Jackson, *supra* note 2; Greene, *Beyond Borders*, *supra* note 2.

22. *Cf.* Greene, *Beyond Borders*, *supra* note 2, at 88 ("significance of reciprocity cannot be overstated"); Tafara & Peterson, *supra* note 2, at 61–62 ("reciprocity would likely have to be the cornerstone . . . to help ensure that the framework is politically acceptable . . . and that competition is not a one-way street").

23. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1375 (2010).

24. *Cf. id.* at §§ 113(b)(2)(H), 115(b)(2)(B), 121(d), 165(b)(2), 173(a)(3) and (c), or 725(b).

the Dodd-Frank Act also referred to such comparable regulation and appropriate systems.[25] However, it is still not clear as to what exactly is required for an exemption to apply, and there is at least the risk that the standard for accepting substitute compliance may be interpreted as a very high one. Moreover, the assessment of comparability appears to be applied on a case-by-case basis, and the application of potential exemptions is revocable any time.[26] Overall, such a "limited exemptive approach" arguably provokes considerable discretion for the deciding authority and at least provokes some reluctance to recognize a foreign firm or product as sufficiently regulated and prudently overseen.[27] Even more important, this approach results in unpredictability, hence, in costly legal uncertainty in the practical deployment of cross-border activities.[28] Such uncertainty could be prevented by a joint decision made by two or more regulators stating that their standards are generally adequate and/or comparable in a certain field of regulation and finally sufficient for a mutual recognition agreement.

In any case, and for the following reasons, the trend is towards a call for market liberalization through a device such as mutual recognition or at least substantive compliance.[29] First, a reduction of regulatory arbitrage obviously requires some form of effective global coordination. Likewise, the prevention of future major financial crises and global scandals is only possible, if at all, with increased global coordination.[30] The G-20 indicated at the Pittsburgh Summit in September 2009 that "[t]he current crisis has once again confirmed the fundamental recognition that our growth and prosperity are interconnected, and that no region of the globe can wall itself off in a globalized world economy."[31] In turn, necessary coordination or harmonization of financial rules could simultaneously provide the groundwork for reaching a mutual recognition agreement without additional efforts. Second, mutual recognition has its own significance, as explained in the following section.

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25. *Cf., e.g.*, Press Release, CFTC, *supra* note 21.

26. *See* Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 9; Comment Letter, European Comm'n to CFTC on proposed CFTC rules 5 (Aug. 24, 2012), *available at* http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=58431&SearchText=european%20commission; *cf. also* Greene & Oztan, *supra* note 1, at 13, 23.

27. *Cf.* Comment Letter, European Comm'n, *supra* note 26. "As proposed, a decision by the CFTC determining substituted compliance will not apply to jurisdictions [which is the case under EMIR in the EU] but only to specific firms after a chapter by chapter analysis and can be withdrawn from a firm at any time." *Id.* The approach "could lead to different and even discriminatory treatment between firms and jurisdictions." *Id.*

28. *Cf.* Comment Letter, European Comm'n, *supra* note 26 (discussing that the CFTC approach "will introduce legal uncertainty and higher monitoring costs").

29. *See* TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 2; TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1; Maijoor, *supra* note 2, at 3; Greene, *Resolving Regulatory Conflicts*, *supra* note 1, *passim*; Greene & Oztan, *supra* note 1, *passim*; Ellig & Shadab, *supra* note 2, at 265–66; Ng, *supra* note 2, at 289; Turner, *supra* note 2, at 417–22; *see also* Verdier, *supra* note 2, at 58, 62–63; Davis, *supra* note 2; *cf. also* President Obama, 2013 State of the Union Address, *supra* note 2.

30. *See* Leaders' Statement at the Pittsburgh Summit, *supra* note 1, at 9; Press Release, CGFR, *supra* note 1; Greene, *Seminar Syllabus*, *supra* note 1, at 14; *see also* CGFR, INITIAL REPORT, *supra* note 1, at 5, 19; Timothy Geithner, U.S. Sec'y of the Treasury, Remarks on the State of Fin. Reform (Feb. 2, 2012), *available at* http://www.treasury.gov/press-center/press-releases/Pages/tg1408.aspx; TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 12; Greene & Potiha, *supra* note 1, at 308, 316; Greene & Boehm, *supra* note 1, at 1086; *cf. also* Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 39; Tafara & Peterson, *supra* note 2, at 40.

31. Leaders' Statement at the Pittsburgh Summit, *supra* note 1, at 20.

B. Significance of Mutual Recognition and Potentially Interesting Fields of Application in the Course of the Global Financial Regulatory Reform

Broadly, mutual recognition has two main benefits. First, mutual recognition is a means of market liberalization as it facilitates private cross-border movement and transactions by eliminating hindrances on both sides, such as the need to comply with multiple and sometimes inconsistent rules.[32] This may produce further advantages. For example, the European Commission and the U.S. Securities and Exchange Commission ("SEC") jointly stated that:

> [a] mutual recognition arrangement for securities would have the potential to facilitate access of EU and U.S. investors to a broader and deeper market, increase the availability of information about foreign investment opportunities, promote greater diversification of securities portfolios, significantly reduce transatlantic trading and transaction costs,[33] and increase oversight coordination among regulators.[34]

Second, "mutual recognition is also a means of raising regulatory standards and controlling international externalities," as Professor Pierre-Hugues Verdier expressed in a recent law review article examining mutual recognition.[35] He further explained:

> Financial regulatory failures can have significant effects on other states, either directly or through contagion and other forms of systemic risk. To the extent that a mutual recognition agreement effectively conditions market access on the existence of an equivalent regulatory system in the home state, it reduces the risk that regulatory failures in the home state will affect the host state.[36]

For the reasons stated, the European Commission and the SEC have generally acknowledged the great potential of mutual recognition.[37] On the other hand, the efforts the United States and the EU have actually invested in international cooperation and coordination of financial regulatory reform are, as previously stated, at least less than originally anticipated or arguably promised, and less than desirable. The United States acted first, adopting the Dodd-Frank Act, which delegated important decision-making and new regulatory oversight to several authorities, such as the SEC, the Commodity Futures Trading

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32. Verdier, *supra* note 2, at 57, 64; Ortino, *supra* note 15, at 309, 311–12, 317, 320; Greene, *Beyond Borders*, *supra* note 2, at 96; Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 6, 34; Greene & Potiha, *supra* note 1, at 310; *see also* Maijoor, *supra* note 2, at 3; TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 2, at 3.

33. Deutsche Bank estimated in 2008 that integration of the U.S. and EU securities markets would reduce trading costs alone by more than $48 billion per year and raise the volume of securities trading from $21 trillion to $31 trillion per year. DEUTSCHE BANK, EU-US FINANCIAL MARKET INTEGRATION—A WORK IN PROGRESS 8 (June 4, 2008), http://www.dbresearch.com/prod/dbr_internet_en-prod/prod0000000000225963.pdf; *see also* de Meijer & Saaf, *supra* note 14, at 132.

34. Press Release, SEC, *supra* note 14; *see also* Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 6, 20, 34, 40; Greene & Oztan, *supra* note 1, at 29; de Meijer & Saaf, *supra* note 14, at 130.

35. Verdier, *supra* note 2, at 57, 64; *see also* Greene & Potiha, *supra* note 1, at 310–11; Greene & Oztan, *supra* note 1, at 27–29; Jan D. Luettringhaus, *Regulating Over-the-Counter Derivatives in the European Union—Transatlantic (Dis)Harmony after EMIR and Dodd-Frank: The Impact on (Re)Insurance Companies and Occupational Pension Funds*, 18 COLUM. J. EUR. L. ONLINE 19, 26 (2012); Tafara & Peterson, *supra* note 2, at 56–57.

36. Verdier, *supra* note 2, at 64.

37. *See* Press Release, SEC, *supra* note 14.

Commission ("CFTC"), or the Financial Stability Oversight Council ("FSOC").[38] With its Dodd-Frank Act, the United States did not seriously try to internationally coordinate regulation.[39] Meanwhile, Europe has acted slowly, and is at least in some fields still in the process to find its way.[40] In any case, regulation on both sides of the Atlantic does not appear to intend to consummate mutual recognition.[41] Consequently, the further part of this article is intended to analyze general minimum prerequisites for a reasonable establishment of mutual recognition in the field of financial regulation.

Though it is not the goal of this Article to predict which substantive standards on both sides of the Atlantic are likely to be comparable and therefore sufficient for a mutual recognition approach, potentially interesting fields within the area of financial regulation in which a mutual recognition approach could apply do exist. Such fields include the regulation of credit rating agencies, hedge funds, securities exchanges and investment services, over-the-counter ("OTC") derivatives, investment banking and its separation from commercial and retail banking, capital and liquidity requirements, resolution of global systemically important financial institutions ("G-SIFIs"), accounting standards, and sovereign wealth funds, among others.[42] Once both sides to a potential mutual recognition agreement established their exact standards in a particular field, and each time one side substantially changes its standard(s), it will be necessary to closely examine if the requirements for mutual recognition are eventually met. Such examination must apply to each individual field of financial regulation.

III. The Mutual Recognition Model within the EU/EEA

A. European Fundamental Freedoms

The fundament of the EU is the idea of a single European Market, also referred to as internal market or common market, based on fundamental freedoms. In this spirit, Article 26 of the Treaty on the Functioning of the European Union ("TFEU")[43] states that the Union "shall adopt measures with the aim of establishing or ensuring the functioning of the internal market" which "shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties." The black letter freedoms provided by the TFEU date back to the

38. Greene, *Dodd-Frank*, *supra* note 2, *passim*; *see also* Greene & Boehm, *supra* note 1, at1093 ("Dodd-Frank was overly reliant on this practice"); Turner, *supra* note 2, at 413 ("delegated most rulemaking tasks").

39. Greene & Potiha, *supra* note 1, at 272; Greene, *Dodd-Frank*, *supra* note 2, at 36, 78–79; Greene, *Dodd-Frank and the Future of Financial Regulation*, *supra* note 1, at 79; Greene, *Seminar Syllabus*, *supra* note 1, at 4, 13; Greene & Boehm, *supra* note 1, at 1093–94, 1097–98, 1106; *cf. also* Verdier, *supra* note 2, at 101 (SEC has recently shown disinterest in facilitating mutual recognition).

40. *Cf. also* Greene & Potiha, *supra* note 1, at 302 (stressing the duplication risk which "is clearly a significant risk in light of the fact that the USA is outpacing Europe in the regulatory sphere").

41. *Cf.* TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 2, at 3, App'x 1; Greene, *Dodd-Frank*, *supra* note 2, at 78–79; Greene, *Seminar Syllabus*, *supra* note 1, at 14; Verdier, *supra* note 2, at 87–88, 101–03; Davis, *supra* note 2.

42. *Cf.* Greene, *Seminar Syllabus*, *supra* note 1, at 4; *cf. also* Greene, *Beyond Borders*, *supra* note 2, at 95; Greene & Boehm, *supra* note 1, at 1086–87 n.18, 1136–38; Jackson, *supra* note 2, at 117–18; TRANSATLANTIC COAL. ON FIN. REGULATION Report, *supra* note 1, at 24–25.

43. The Treaty on the Functioning of the European Union, 2008 O.J. (C 115) 47 (EU) ("TFEU").

European Economic Community ("EEC") but have since been significantly developed and shaped by the European Court of Justice ("ECJ").

In the field of financial regulation, the freedom to provide services, the freedom of establishment, and the freedom of movement of capital are of particular importance. Article 56 *et seq.* of the TFEU[44] recognize the freedom to provide and receive cross-border services within the EU ("freedom to provide services").[45] Article 56 states that "restrictions on [the] freedom to provide services within the Union shall be prohibited in respect of nationals of Member States who are established in a Member State other than that of the person for whom the services are intended." In the broad interpretation of the ECJ, the substantive scope of application of the freedom to provide services requires:

> not only the elimination of all discrimination against a person providing services on the ground of his nationality but also the abolition of any restriction, even if it applies without distinction to national providers of services and to those of other Member States, when it is liable to prohibit or otherwise impede the activities of a provider of services established in another Member State where he lawfully provides similar services.[46]

The exercise of the freedom to provide services must not only be not prohibited but also not impeded or rendered less attractive.[47]

In light of this interpretation, if one Member State were to recognize the laws or prudential supervision of another Member State as insufficient and thus impose additional, maybe even inconsistent, requirements on cross-border activities, this would result in an illegitimate restriction on the freedom to provide services. The additional requirements would violate Article 56 of the TFEU. Hence, the ECJ's interpretation of the freedom to provide services is commonly understood as imposing an obligation of mutual recognition on the Member States.[48] The ECJ first applied such a broad interpretation in 1974 in the famous case *Procureur du Roi v. Dassonville*[49] regarding the free movement of goods, in which the ECJ held that "[a]ll trading rules enacted by Member States which are capable of hindering, directly or indirectly, actually or potentially, intra-Community trade are to be considered as measures having an effect equivalent to quantitative restrictions," thus being prohibited by Article 34 of the TFEU.[50] Since then, the ECJ has adopted a similarly broad interpretation with respect to other freedoms, such as the freedom to provide services, as explained above, and the freedom of establishment.[51]

The freedom of establishment is addressed in Article 49 *et seq.* of the TFEU.[52] Article 49 states that "restrictions on the freedom of establishment of

44. *Id.*
45. Ortino, *supra* note 15, at 311.
46. Case 76/90, Säger v. Dennemeyer, 1991 E.C.R. 4239, 4243.
47. Case 439/99, Comm'n v. Italy, 2002 E.C.R. 351, 364; Case 452/04, Fidium Finanz AG v. Bundesanstalt für Finanzdienstleistungsaufsicht, 2006 E.C.R. 9562, 9579.
48. Ortino, *supra* note 15, at 311–12, 320; *see also* Wymeersch, *supra* note 2, at 204.
49. Case 8/74, Procureur du Roi v. Dassonville, 1974 E.C.R. 838, 852.
50. The Treaty on the Functioning of the European Union, 2008 O.J. (C 115) 47 (EU).
51. *See, e.g.*, Case 76/90, Säger v. Dennemeyer, 1991 E.C.R. 4239, 4243 (regarding services); Case 439/99, Comm'n v. Italy, 2002 E.C.R. 351, 364 (regarding services and establishment); *see also* Ortino, *supra* note 15, at 311–12; Verdier, *supra* note 2, at 72.
52. The Treaty on the Functioning of the European Union, 2008 O.J. (C 115) 47 (EU).

nationals of a Member State in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State." The freedom of establishment includes "the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms . . . ."

Finally, Article 63 of the TFEU,[53] defining the freedom of capital movement, states that "all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited." In contrast to the freedom to provide services and the freedom of establishment, restrictions on the freedom of capital movement are not merely prohibited as between Member States, but also as concerning capital flows originating from the sphere of non-Member States. Article 63 thus effectively liberalizes the freedom of capital movement, also in favor of non-EU countries, and thereby attracts capital.[54]

Yet, the ECJ has held that subjects from a third country, for example service providers from Switzerland, cannot refer to the freedom of capital movement where a restriction on capital movement is just an inevitable consequence of an allowed restriction on the freedom of establishment or the freedom to provide services.[55] That is, where a situation on its merits is subject to the provisions of freedoms other than the freedom of capital movement, a restriction of the other freedoms, as is allowed against third country subjects, will prevail over a restriction on the freedom of capital movement. This is true despite that the restriction on the freedom of capital movement by itself would not be allowed. Thus, where multiple freedoms are involved, the freedom of capital movement will, in principal, not help a third country subject to overcome the scope of personal application of the other freedoms, as they are limited to subjects from the inter-EU/EEA sphere. Hence, as far as the freedom to provide services and the freedom of establishment reach substantively, the obligation of mutual recognition remains confined to the inter-EU/EEA sphere, and is not impacted by the freedom of capital movement.

B. Exceptions Justified by Imperative Reasons Relating to Public Interest, and Experiences with the ISD

Though restrictions on the freedom to provide services, freedom of establishment, and freedom of capital movement are generally prohibited, at least within the inter-EU/EEA sphere, reasons exist which justify exceptions. The reasons for such exceptions can be divided into two categories: (i) those explicitly codified and (ii) those the ECJ found in the course of interpreting the European treaties.

Black letter exceptions to the freedom to provide services and freedom of establishment can be found in Article 62 of the TFEU in conjunction with Article

53. *Id.*

54. This is subject to certain exceptions. *See* TFEU, *supra* note 43, art. 64–66.

55. *See, e.g.*, Case 452/04, Fidium Finanz AG v. Bundesanstalt für Finanzdienstleistungsaufsicht, 2006 E.C.R. 9562, 9576–81 (especially ¶¶ 34, 48–49); *see also* Case 196/04, Cadbury Schweppes v. Comm'rs of Inland Revenue, 2006 E.C.R. 8031, 8042.

51 *et seq.* of the TFEU,[56] and refer to activities which are connected to the exercise of official authority, and to special treatment for foreign nationals on grounds of public policy, public security, or public health. Precisely, Article 51 of the TFEU states: "The provisions of this Chapter shall not apply, so far as any given Member State is concerned, to activities which in that State are connected, even occasionally, with the exercise of official authority."[57] Article 52 of the TFEU holds: "The provisions of this Chapter and measures taken in pursuance thereof shall not prejudice the applicability of provisions laid down by law, regulation or administrative action providing for special treatment for foreign nationals on grounds of public policy, public security or public health."[58]

In addition to the black letter exceptions, the ECJ's broad interpretation of the freedoms triggered an expansion of potential reasons for exceptions to the freedoms. Finding that the freedoms not only prohibit discrimination of foreigners but prohibit any impediments on the freedom of cross-border movement, the ECJ also incorporated some potential reasons for exceptions to its broad interpretation. These reasons must refer to some kind of public interest the respective Member State is confronted with, and need to be imperative, meaning that the measures taken must be due to mandatory requirements relating to public interest.[59] In *Rewe-Zentral AG v. Bundesmonopolverwaltung für Branntwein ("Cassis de Dijon"),*[60] concerning the freedom of movement of goods, the ECJ prepared the ground for developing the law as to the other freedoms by stating that possible public interest reasons for exceptions to the freedoms include "the effectiveness of fiscal supervision, the protection of public health, the fairness of commercial transactions, and the defence of the consumer."

However, it is not enough that the alleged exception falls within the black letter exceptions or those interpreted by the ECJ. Instead, in order to be valid, both the explicit exceptions and exceptions as interpreted by the ECJ also need to be in line with the proportionality principle.[61] The proportionality principle entails three tests: (i) the suitability test, which verifies that one of the named valid reasons for an exception to the freedoms is actually at stake; (ii) the necessity test, which ensures that there is no less burdensome means to achieve the goal of the exception, including that no functionally equivalent standard is provided by the home Member States in which the potential cross-border movements are originated; and (iii) the proportionality stricto sensu test, which weighs the pros and cons of an exception.[62] Additionally, for a case law exception to be valid, it may not lead to any discrimination, thus, the respective measure needs to be generally applicable, including as to natives.[63]

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56. The Treaty on the Functioning of the European Union, 2008 O.J. (C 115) 47 (EU).
57. *Id.*
58. *Id.*
59. Case 120/78, Rewe-Zentral AG v. Bundesmonopolverwaltung für Branntwein, 1979 E.C.R. 650, 662 ("Cassis de Dijon"); Case 76/90, Säger v. Dennemeyer, 1991 E.C.R. 4239, 4244.; *cf. also* Ortino, *supra* note 13, at 312 ("general good exceptions").
60. Cassis de Dijon, *supra* note 59.
61. Ortino, *supra* note 15, at 312; Griffin, *supra* note 15, at 352; Gérard Hertig, *Imperfect Mutual Recognition For EC Financial Services*, 14 INT'L REV. L. & ECON. 177, 178 (1994).
62. *See* Ortino, *supra* note 15, at 313, 315.
63. *See, e.g.*, Case 76/90, Säger v. Dennemeyer, 1991 E.C.R. 4239, 4244; *see also* Griffin, *supra* note 15, at 352; Hertig, *supra* note 61, at 178.

Member States have often attempted to enact exceptions citing that host Member State's rules are insufficient because there is little comparability of standards or that the other state's standards are inadequate as to protection of investors or the market, for example. In order to diminish the occasions on which host Member States refer to exceptions, the EU is enacting directives and regulations coordinating substantive standards of law.[64] Once coordination, and thus some form of comparability of the substantive standards of law, is reached there should, in effect, only be left a narrow application range of valid exceptions to the freedoms and thus to mutual recognition. However, enacting directives and regulations is often a long lasting process, involving heavy negotiations.

The ISD of 1993 used some form of coordination and mutual recognition but did not produce only positive experiences. This was for the following reason, that for a significant period of time, directives were intended to provide no more than substantive *minimum* standards ("minimum harmonization"), for example a certain minimum level of market and investor protection. This type of directive was popular arguably because such a minimum standard was easier and quicker to reach in negotiations.[65] In this spirit, the ISD stated that the Member States must draw up rules of business conduct which implement "at least" the broad principles set out in the ISD.[66] Thus, Member States were able to adopt more severe rules if necessary because of public interest(s). This regulatory competence was accompanied by the fact that the ISD preserved significant supervisory competences for the host Member States.[67] Thus, a basis for considerable exceptions to the mutual recognition obligation in the field of financial services was incorporated in the concept of the ISD from the outset.

The exceptions created by the ISD still had to comply with the fundamental freedoms.[68] The ECJ had the power to determine at the request of a home Member State whether the preconditions for any exception used by a host Member State were actually met.[69] However, the ECJ's power is not automatically controlling but requires action of a home Member State, and the ECJ's determination is not prompt.[70] Finally, though the ISD's approach was intended to quickly reach mutual recognition, it proved to be an imperfect approach, not leading to a properly integrated European financial market and not solving the problem of protectionism which is contrary to the idea of a single market and the respective freedoms.[71]

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64. *See, e.g.,* The Treaty on the Functioning of the European Union, 2008 O.J. (C 115) 47, art. 53 (EU); *see also* Ortino, *supra* note 15, at 321–26.

65. *See* Verdier, *supra* note 2, at 72–73 (the model "was a compromise," a system of "'imperfect' mutual recognition," which was "praised for allowing faster integration"); Hertig, *supra* note 61, at 178–79.

66. ISD, *supra* note 8, art. 11 ¶ 1.

67. ISD, *supra* note 8, art. 11 ¶ 2, art. 19 ¶ 6.

68. *See* E. Waide Warner, *"Mutual Recognition" and Cross-Border Financial Services in the European Community*, 55 LAW & CONTEMP. PROBS. 7, 16–18 (1992).

69. *See* Verdier, *supra* note 2, at 73; Griffin, *supra* note 15, at 352; Warner, *supra* note 68, at 18.

70. *Cf. also* Ortino, *supra* note 15, at 328 ("The requirements set out by the proportionality principle, under the 'general good' doctrine, have often been disregarded.").

71. Verdier, *supra* note 2, at 73–74, 79 (describing the mutual recognition approach as "imperfect" and stating that "the results . . . were widely perceived as deficient," "mostly because of additional requirements imposed on providers by host states"; further stating that Member States "took advantage of the minimum harmonization scheme to impose additional regulatory requirements to protect their markets against foreign firms"); Pan, *supra* note 2, at 139, 148; Ortino, *supra* note 15, at 326–28; Caroline Bradley, *Consumers of Financial Services and Multi-Level Regulation in the European Union*, 31 FORDHAM INT'L L.J. 1211, 1217–20

C. The MiFID's Approach, the Lamfalussy Process, and the New ESMA

In 2004, the EU adopted the MiFID. Besides having an application range as to the encompassed kinds of financial services broader than the ISD,[72] the MiFID tries to effectively provide for mutual recognition.[73] In attempting to do so, it prescribes not only a minimum standard but simultaneously a *maximum* standard. The MiFID effectively provides a narrowly tailored regulatory framework ("maximum harmonization").[74] The exact range of the MiFID's maximum harmonization concept is still highly controversial. For example, the question exists as to whether mere domestic cases without cross-border context are also governed by MiFID instead of being governed by originary national law.[75] However, it is clear that the MiFID neither allows the imposition of more severe substantive rules nor additional prudential supervision on inter-European cross-border movement.[76]

The extent to which exceptions apply to this mutual recognition approach is not nearly as great as the extent to which exceptions to mutual recognition could be used under ISD. First, under MiFID there are basically no exceptions to mutual recognition of cross-border services.[77] Exceptions are only possibly to mutual recognition of cross-border establishment.[78] Second, where there are exceptions, a host Member State may impose its supervision on established cross-border branches, but is not allowed to impose more severe substantive rules than the deeply and strictly harmonized set of substantive rules the MiFID stipulates.[79] Third, the exceptions are coordinated and clearly defined in the directive, mainly in Article 32, paragraph 7 of the MiFID, which cross-references certain business conduct rules. Good reason exists for making host Member States supervise in this

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(2008); Griffin, *supra* note 15, at 351–53; *but cf. also* Hertig, *supra* note 61, at 180–86 (arguing "imperfect" approach has advantages).

72. *See* MiFID, *supra* note 7, at annex I: (1) Reception and transmission of orders in relation to one or more financial instruments, (2) Execution of orders on behalf of clients, (3) Dealing on own account, (4) Portfolio management, (5) Investment advice, (6) Underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis, (7) Placing of financial instruments without a firm commitment basis, and (8) Operation of Multilateral Trading Facilities.

73. *See* Verdier, *supra* note 2, at 75.

74. As to maximum harmonization, *see* Michel Tison, *Financial Market Integration in the Post FSAP Era: In Search of Overall Conceptual Consistency in the Regulatory Framework*, *in* INVESTOR PROT. IN EUROPE 443, 450–51 (Guido Ferrarini & Eddy Wymeersch eds., 2006); Peter O. Mülbert, *The Eclipse of Contract Law in the Investment-Firm-Client-Relationship: The Impact of the MiFID on the Law of Contract from a German Perspective*, *in* INVESTOR PROT. IN EUROPE 299, 318 (Guido Ferrarini & Eddy Wymeersch eds., 2006); Verdier, *supra* note 2, at 75; Danny Busch, *Why MiFID Matters to Private Law—the Example of MiFID's Impact on an Asset Manager's Civil Liability*, 7 CAPITAL MKTS. L.J. 386, 386 (2012); *cf. also* Ortino, *supra* note 15, at 337 ("[t]he degree of regulatory detail provided for by the FSAP measures adopted under the Lamfalussy approach is usually very high, and some of these measures provide for maximum harmonization"); Bradley, *supra* note 71, at 1221.

75. Another question is which consequences MiFID's prudential rules have on national contract law and—broader—civil liability. Questions of this type relating to European Harmonization Theory constitute one part of the author's Ph.D. thesis (to be published soon).

76. *See* MiFID, *supra* note 7, art. 31 ¶ 1, art. 32 ¶ 1, & art. 33 ¶ 2; Tison, *supra* note 74, at 450–51; Mülbert, *supra* note 74, at 318–19; *see also* Verdier, *supra* note 2, at 75 ("strengthen the home country principle and reduce the discretion of host states to impose additional requirements"; "host states lost control over consumer protection and other conduct of business rules").

77. *See* MiFID, *supra* note 7, art. 31.

78. *See id* art. 32.

79. Mülbert, *supra* note 74, at 318.

context. A host Member State usually can execute day-to-day supervision of the conduct of business exercised by branches established in the host Member State much more effectively and efficiently than the home Member State, since the competent authority of the host Member State "is closest to the branch, and is better placed to detect and intervene in respect of infringements of rules governing the operations of the branch."[80] Finally, to the extent that there are such coordinated exceptions to the rule that home Member States are responsible for prudential supervision, this does not place a severe burden on cross-border movement since the subject-matter of the supervision is a standard of substantive law which is deeply harmonized by MiFID. Hence, overall, the MiFID provided for an effective mutual recognition approach in the fields of securities intermediaries and securities exchanges.

The MiFID was adopted using the Lamfalussy Process which generally facilitates a more timely agreement as to regulatory projects, as well as better regulation, better and more flexible implementation, and proper enforcement.[81] The Lamfalussy reform was based on the recommendations by the Committee of Wise Men on the Regulation of European Securities Markets ("Committee"), chaired by Baron Alexandre Lamfalussy. The Committee was established in 2000 by the Economic and Financial Affairs Council ("Ecofin") with the task of evaluating the effectiveness of the European Community's ("EC's") securities regulation against the background of market integration, *inter alia*.[82] The Committee recommended that the EC adopt changes to the process of adopting, implementing, and enforcing securities legislation, resulting in the "Lamfalussy Process." In 2002, Ecofin extended the scope of the Lamfalussy Process to embrace the broader financial sector, including the fields of banking, mutual funds, and insurance and occupational pensions.[83]

The Lamfalussy Process consists of four levels.[84] At level 1, the European Parliament and the Council adopt directives, such as the MiFID, or regulations comprising fundamental policy decisions constituting a framework for measures at the next level. At level 2, the European Commission issues detailed (technical) measures to implement the fundamental policy decisions. Such measures consist of implementing directives and/or regulations, both of which were used to implement the MiFID.[85] Implementation of level 1 directives and regulations through level 2 directives and regulations is assisted by political and technical committees, such as the Committee of European Securities Regulators ("CESR"). These committees address the complexities of financial markets and the necessity of flexible and "easy-to-update" technical regulations.[86] At level 3, the technical

80. MiFID, *supra* note 7, recital 32; *see also* Ortino, *supra* note 15, at 325.

81. *See* Ortino, *supra* note 15, at 328–29; *see also* Bradley, *supra* note 71, at 1220–21.

82. Ortino, *supra* note 15, at 328–29; Bradley, *supra* note 71, at 1220.

83. Ortino, *supra* note 15, at 329.

84. *See* Final Report, Comm. of Wise Men on the Regulation of European Sec. Mkts., http://ec.europa.eu/internal_market/securities/docs/lamfalussy/wisemen/final-report-wise-men_en.pdf.

85. Commission Regulation 2006/1287, implementing Directive 2004/39 as regards recordkeeping obligations for investment firms, transaction reporting, market transparency, admission of financial instruments to trading, and defined terms, 2006 O.J. (L 241) 1 (EU); Commission Directive 2006/73, implementing Directive 2004/39 as regards organizational requirements and operating conditions for investment firms and defined terms, 2006 O.J. (L 241) 26 (EU).

86. Ortino, *supra* note 15, at 330–31; *see also* Pan, *supra* note 2, at 141.

committees, such as the CESR, issue recommendations, guidelines, and common standards, intended to ensure that Member State's supervisory authorities consistently apply level 1 and level 2 measures or the transformed national law.[87] Level 4, finally, is intended to strengthen the European Commission's power to control and enforce the Member States' compliance with EU legislation.[88]

In 2009, the EU further strengthened the technical committees working on level 3 of the Lamfalussy Process "by giving them more explicit mandates to monitor and assess financial stability, empowering them to reach decisions by qualified majority rather than consensus, and requiring national authorities to explain deviations from the committee's standards."[89] Finally, in 2011, the committees were transformed into three European Supervisory Authorities with substantially expanded powers.[90] The European Securities and Markets Authority ("ESMA") replaced the CESR; the European Banking Authority ("EBA") replaced the Committee of European Banking Supervisors; and, the European Insurance and Occupational Pensions Authority ("EIOPA") replaced the Committee of European Insurance and Occupational Pensions Supervisors.[91] These new authorities are more strongly integrated in the legislative process on Lamfalussy level 2 than their predecessors. As to Lamfalussy level 3, the new authorities' powers now encompass not only adopting recommendations for interpretation of EU measures, but also mediating disputes between national supervisors and imposing binding decisions where mediation fails, as well as adopting binding emergency measures, among other things.[92]

IV. Drawing an Analogy to the Transatlantic Relationship?

A. Analysis of the Reasonable Prerequisites for Transatlantic Mutual Recognition in the Field of Global Financial Regulation

1. Effective Substantive Coordination

The concept of the European fundamental freedoms, as explained above, suggests that the obligation of mutual recognition requires functional equivalence of the rules established by the participating parties. Within Europe, functional equivalence is either seen as a direct precondition for mutual recognition or as a negative precondition for an exception to a general mutual recognition obligation.[93] The structure of the generally applicable European freedoms,

87. Level 1 and 2 regulations comprise directly applicable substantive law. Level 1 and 2 directives, on the other side, only address the Member States, not their citizens. Directives have to be transformed into national substantive law by the Member States.

88. Final Report, Comm. of Wise Men on the Regulation of European Sec. Mkts., *supra* note 84, at 40.

89. Verdier, *supra* note 2, at 77.

90. Another key part of the new supervisory framework (European System of Financial Supervision, "ESFS") was the establishment of the European Systemic Risk Board ("ESRB") which has a similar macro-prudential role as the FSOC in the United States. Greene & Boehm, *supra* note 1, at 1096; *but see also* Greene, *Dodd-Frank*, *supra* note 2, at 38 (ESRB has "no regulatory authority").

91. *See* Verdier, *supra* note 2, at 77; Greene & Boehm, *supra* note 1, at 1096–97.

92. *See* Verdier, *supra* note 2, at 77–78; Greene & Boehm, *supra* note 1, at 1097; in more detail, *see* Regulation 2010/1095, of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Sec. and Mkts. Authority), 2010 O.J. (L 331) 84 (EU).

93. *See* Ortino, *supra* note 15, at 313–14.

including the interpretation of such by the ECJ, and the exceptions which must be justified by imperative reasons relating to public interest, suggest that the second view is the appropriate one.[94] The negative precondition approach means that there is a general obligation of mutual recognition, and that an exception can only be made under certain circumstances which, among other things, require that no functionally equivalent rules of the host state exist.[95]

From a transatlantic point of view, on the other hand, functional equivalence cannot be a mere negative precondition for an exception to a generally applicable mutual recognition approach. No general mutual recognition exists within the transatlantic relationship. The particular fields of regulation, such as securities intermediaries and securities exchanges, or rating agencies, must be examined one at a time. The question is under which circumstances mutual recognition can be prudently considered in such a field of regulation in the first place. An appropriate standard might be to look for functional equivalence of the substantive rules and supervision of the potential parties to a mutual recognition agreement. But, is functional equivalence in fact sufficient?

Europe's experience with the ISD teaches that effective mutual recognition may prosper only when the possibility to undermine such agreement by using broadly phrased exceptions does not exist. Rather, the development from ISD to MiFID shows that attempting to accelerate integration by establishing an imperfect mutual recognition obligation is not a good approach. To establish an effective mutual recognition approach, entirely acceptable substantive standards on both sides should first be in place, so that the mutual recognition approach, once established, is a strong one, not being undermined by various, blurrily phrased exceptions. For the transatlantic relationship, reliance on such uncertain exceptions would create even greater problems than those which existed between the European Member States under the ISD regime, since there is no common jurisprudence which could control whether the preconditions of an exception were actually fulfilled by determining whether the side which took "advantage" of an exception indeed could justify doing so.

Thus, to establish a successful system of mutual recognition, both sides to the agreement must actually trust in the entire adequacy of the other side's substantive standard.[96] Until this is reached, an effective and reasonable transatlantic mutual recognition approach cannot be established. This trust in the adequacy of each other's standards arguably necessitates comparability of the standards, even though the assessment of comparability might be difficult in practice.[97] The question then becomes, what is an appropriate level of comparability. From the basic approach of the European freedoms, the indirect answer could again be functional equivalence, as explained above. By itself, the

94. Ortino, *supra* note 15, at 314–16.

95. *See supra* §§ III.A., III.B.

96. *See* Ortino, *supra* note 15, at 323; Wymeersch, *supra* note 2, at 203.

97. For a discussion of the practical difficulties, *see* Verdier, *supra* note 2, at 93–94; Greene, *Beyond Borders*, *supra* note 2, at 90–91; Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 35; TRANSATLANTIC COAL. ON FIN. REGULATION Report, *supra* note 1, at 19–20; *cf. also* John C. Coffee, Jr., *Law and the Market: The Impact of Enforcement*, 156 U. PA. L. REV. 229, 307–11 (2007) (pointing out the difference between an emphasis on ex ante regulation and on ex post enforcement, further, that the SEC, though also using ex ante regulation, "seems more committed than other regulators to a policy of general deterrence through substantial penalties").

functional equivalence approach is a reasonable standard because it does not require strict equivalence, which would be very hard to reach, but requires at least functional equivalence which achieves a comparable degree of protection of the public interest(s) regardless of the methods used.[98] This approach allows for an assessment of comparability on a higher level, focusing on the regulatory principles and objectives, instead of a very detailed, highly technical analysis.[99]

Given that this concept generally appears to be reasonable, the experience with the desire of the European countries to make use of more severe rules than the ISD stipulated needs to be taken into account, which in cross-border contexts meant to carve-out the mutual recognition approach.[100] This experience shows that even within the EU, there often was some reservation to trust in the adequacy of the harmonized minimal standards which all Member States had to transpose and implement into their domestic law. In response to such reservation, the MiFID and its implementing measures provided for broad, deep, and maximum harmonization and, in turn, eliminated the "imperative public interest exceptions" to its mutual recognition obligation in order to make it a strict approach.[101]

In conclusion, before an effective mutual recognition approach in a particular field of financial regulation can be established, and be able to persist in the long term, at least some form of actual regulatory coordination or harmonization must exist.[102] In order to be effective and persist, this form of regulatory coordination or harmonization does not need to be as deep as that provided by the Lamfalussy Process, but it should be sufficient to take the step of eliminating at least most of the exceptions to the respective mutual recognition concept which are based on alleged imperative public interest(s), such as controlling systemic risk.[103] Any attempts of either the United States or the EU to

98. Ortino, *supra* note 15, at 315; EUROFI, *supra* note 1.

99. *See also* Greene, *Beyond Borders*, *supra* note 2, at 90–91; Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 35; Greene & Oztan, *supra* note 1, at 28, 29; TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 19–20; Ellig & Shadab, *supra* note 2, at 334; de Meijer & Saaf, *supra* note 14, at 128–29; EUROFI, *supra* note 1.

100. *See supra* § III.B.

101. *See supra* § III.C.

102. *See* Ortino, *supra* note 15, at 323–24, 334–35; *see also* DEUTSCHE BANK, *supra* note 33, at 11–13 ("an optimal, well-functioning recognition regime needs to be . . . underscored and preceded by a reasonable degree of regulatory convergence"; "the most important potential shortcoming of mutual recognition, i.e., competitive distortions in case the underlying market rules are too divergent, can in fact be mitigated by underscoring the recognition framework with a reasonable degree of convergence"); Sydney J. Key, Bd. of Gov. of the Fed. Res. Sys., *International Finance Discussion Paper no. 349* 40 (Apr. 1989), *available at* http://www.federalreserve.gov/pubs/ifdp/1989/349/ifdp349.pdf ("a crucial prerequisite for mutual recognition is harmonization of essential rules"); *cf. also* Pan, *supra* note 2, at 138–39, 161–62 (arguing MiFID's mutual recognition regime was an appropriate model for the transatlantic relationship with respect to securities exchanges, and that a substitute compliance proposal "does not go far enough to resolve the regulatory differences that exist . . . and the task of coordinating regulation and enforcement"; speaking about the "blueprint" laid out by the MiFID, meaning the passport concept combined with home country supervision, which requires at least "harmonization of certain regulatory standards"). One should have in mind that there is a distinction between mutual recognition and a limited exemptive approach with respect to the point that the latter might provide a possibility for quicker relief for specific market participants in specific areas. *See* Greene & Oztan, *supra* note 1, at 30.

103. *Cf.* Ortino, *supra* note 15, at 334–35 ("regulation must also be sufficiently wide in scope and deep in its harmonizing effects to allow the application of mutual recognition to the various aspects of financial regulation, without exceptions"); *but cf. also* James D. Cox & Edward F. Greene, *Financial Regulation in a Global Market Place: Report of the Duke Global Capital Markets Roundtable*, 18 DUKE J. COMP. & INT'L L. 239, 246–47 (2007) ("There was a view that countries must retain residual authority for the host country to carry out enforcement efforts, particularly, or perhaps solely, with respect to fraud, where it is *believed*

look for exceptions, provoked by distrust in the standard of the other side, would not only have the potential to devour a mutual recognition approach but could also lead to even deeper distrust and, finally, sustained protectionist measures by both sides. Such impact is precisely what the necessary level of coordination should prevent. A proper level of coordination needs to effectively convince both sides of the safety and soundness of the other side's standard in order to relinquish their rights to pull the trigger of unnecessary public interest exceptions.

Even if the United States and EU have difficulty establishing such a mutual recognition approach which is based on actual confidence in the adequacy of the other region's measures, the parties should not suspend their efforts towards establishing mutual recognition. Instead, the United States and the EU should concentrate on achieving the preconditions of a reasonable mutual recognition approach. A reasonable mutual recognition approach is directly linked to actually providing for some form of effective substantive coordination or harmonization. Merely declaring intentions as to effective coordination is eventually not enough. As a potential intermediate solution, quicker relief from burdens on cross-border activity might be possible with respect to specific market participants in specific areas by using a limited exemptive approach.[104]

2. Necessity of Providing For Common Interpretation and Harmonized Enforcement?

Common interpretation and harmonized enforcement of substantive rules are a logical step accompanying coordination/harmonization, at least if a system establishes such a deep form of harmonization as the MiFID and its implementing measures did.[105] However, within the transatlantic relationship there will likely not be such a strong form of substantive harmonization in the near future, meaning that such a narrowly tailored regulatory frame will likely not be achieved.[106] However, this does not mean that in the case of some smoother form of coordination there is no necessity for common interpretation of the coordinated rules as well as safeguarding proper enforcement of the rules.

As to common interpretation, it is plausible that the guidelines, frameworks, or further coordinated standards that both sides potentially adopt would have to be interpreted in a consistent way, though a mutual recognition approach arguably could survive even when there would be some form of inconsistencies as to interpretation of coordinated standards.[107] However, if such inconsistencies were to increase and have a greater impact, the possibility of one party terminating the mutual recognition agreement would also increase, because

[emphasis added] necessary for investor protection or to provide relief where otherwise the remedy is *believed* [emphasis added] inadequate."). Hopefully, this was actually meant as "solely", if at all, with respect to fraud.

104. *See* Greene & Oztan, *supra* note 1, at 30. For differentiation of the concepts, *see supra* § II.A.

105. *Cf.* Ortino, *supra* note 15, at 334–35.

106. *See* Greene, *Beyond Borders*, *supra* note 2, at 90–91 ("while perhaps academically appealing, [it] is simply not realistic"); *see also* EUROFI, *supra* note 1; Griffin, *supra* note 15, at 349.

107. *But see* Ortino, *supra* note 15, at 327 (Mutual recognition requires harmonization which should not only refer to similar rules but also "include" uniform application and interpretation of such rules by national authorities.).

trust in some form of similarity of the rules once constituted a precondition for adopting a mutual recognition approach.[108]

Therefore, to counteract such inconsistencies, some form of an interpretive authority could be established at the international level. For example, pertinent power could be assigned to the international board or organization which provided the recommendations for the regulatory framework which both sides maybe adopted. Another option could be that officials of the parties participating in the mutual recognition agreement hold regular, formal meetings to determine binding interpretation. Another suggestion is that the SEC could join the ESMA by treaty, for example, at least for dispute resolution.[109]

On the other hand, a transatlantic authority with powers comparable to that of the ECJ or the European Commission will not be achievable in the near future. However, an interpretive authority does not need to have such extensive powers in order to ensure sustainable mutual recognition by providing for consistent interpretation of common standards or frameworks. Furthermore, as previously indicated, such common interpretive authority is neither an absolute precondition for the establishment of mutual recognition nor will a mutual recognition agreement fail for sure at long sight if such authority does not exist. Nevertheless, the presence of an interpretive authority would be a reasonable means to increase the likelihood that the mutual recognition agreement will sustain in the long term.

As to safeguarding proper prudential supervision and enforcement of the coordinated substantive rules,[110] an extreme possibility to ensure the longevity and success of a mutual recognition agreement would be to require some centralized form of control.[111] However, in light of the United States' and the EU's highly developed financial markets, regulators and prudential authorities,[112] the need for providing a centralized authority which controls proper supervision and enforcement of coordinated substantive standards both sides adopted should not be oppressive. Due to the advanced level of financial regulators and prudential authorities in the United States and the EU, effective supervision and enforcement of coordinated or harmonized substantive financial regulation should

108. *See* Ortino, *supra* note 15, at 334.

109. Pan, *supra* note 2, at 163–64 (as to the former CESR), *referring to* Eric J. Pan, *Authoritative Interpretation of Agreements: Developing More Responsive International Administrative Regimes*, 38 HARV. INT'L L.J. 503 (1997) (discussing need for self-interpreting international administrative bodies). As to ESMA's competences, *see supra* § III.C.

110. *Cf.* TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 2, at 6 (noting "a finding that rules are equivalent is not the same as a finding that the supervisory system or enforcement practice in a given jurisdiction is equivalent"); TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 19–20 ("it is clear that an assessment of the . . . regulatory system would necessarily involve an assessment of the effectiveness of the process by which compliance with the regulatory regime is policed and sanctioned"); Greene, *Beyond Borders*, *supra* note 2, at 90 (stating that comparable regulatory oversight and robust enforcement mechanisms are preconditions for mutual recognition); Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 35; Verdier, *supra* note 2, at 60, 67 (stating there must be comparable levels of supervision and enforcement capacities as well as enhanced cross-border cooperation; discussing institutional frameworks to achieve international cooperation in enforcement problems); *cf. also* Ortino, *supra* note 15, at 316, 323–24 (within the EU, functional equivalence of the enforcement mechanisms is a negative precondition for an exception to mutual recognition); Coffee, Jr., *supra* note 97, at 307–11 (in doubt about whether "foreign compliance systems would impose anything resembling U.S.-style enforcement discipline").

111. *See* Pan, *supra* note 2, at 164 ("CESR-like entity" implementing technical regulation and monitoring enforcement).

112. *See* Verdier, *supra* note 2, at 88.

automatically follow. However, the United States traditionally has had some concerns with respect to the question of whether there is assurance of consistent financial regulation and enforcement already within the EU itself.[113]

Because many different countries assemble the EU, the concerns of the United States once were understandable. However, since the Lamfalussy Process provided for broadly and deeply harmonized rules in the financial sector, and facilitated common interpretation and enforcement, the United States' concerns should already have diminished.[114] Moreover, the new ESMA, the new EBA, and the new EIOPA are powerful common authorities which will more strictly provide for consistent, binding interpretation and enforcement of the broadly and deeply harmonized rules within the EU.[115] This enforcement takes place within the relationship between the EU and its Member States, thereby safeguarding that the individual Member States properly enforce the rules within the relationship to the investment firms subject to their authority. MiFID II and other new legislation is intended to further strengthen enforcement directly at the second level.[116] It will likely harmonize enforcement mechanisms necessarily available to the individual authorities of the Member States in the relationship to the investment firms subject to their authority, for example, providing for stricter fines, establishing the additional mechanism of name-and-shame as a standard, and setting incentives for whistle-blowers. Overall, the United States' concerns as to inconsistencies already within the EU should be put aside.[117]

Yet, while there is no requirement of a centralized form of transatlantic control over proper supervision and enforcement of coordinated or harmonized substantive rules, this does not prevent the necessity of strengthened cooperation in oversight and enforcement matters, including a sufficient device for information exchange. In this respect, it has been pointed out that there is a need to establish an:

> enforcement, inspections, and information-sharing technical arrangement or memorandum of understanding that would enable the two partners not only to share enforcement-related information and cooperate with each other's enforcement investigations, but also to share inspections reports, conduct joint inspections, and cooperate with each other at the prudential oversight level.[118]

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113. *See* Jackson, *supra* note 2, at 114–15; Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 9–10, 17–18, 39; Greene & Oztan, *supra* note 1, at 13, 17; Verdier, *supra* note 2, at 60, 102; *cf. also* Davis, *supra* note 2 (indicating that, according to one source familiar with the situation, the US did not select the EU for the mutual recognition experiment with Australia "because of the complexity of its state-within-a-state framework").

114. *See* Ortino, *supra* note 15, at 335–36, 338; *see also* TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 15; Greene & Boehm, *supra* note 1, at 1095–96; *cf. also* Elliot Posner, *Making Rules for Global Finance: Transatlantic Regulatory Cooperation at the Turn of the Millennium*, 63 INT'L ORG. 665, 691 (2009) (arguing that the EU enhanced its "bargaining strength" by pursuing "internal financial regulatory centralization").

115. *See* TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 15; Greene & Boehm, *supra* note 1, at 1096–97.

116. *Cf.* Memo, European Commission, *Markets in Financial Instruments (MiFID): Commissioner Michel Barnier Welcomes Agreement in Trilogue on Revised European Rules* (Jan. 14, 2014), *available at* http://europa.eu/rapid/press-release_MEMO-14-15_en.pdf.

117. *See* TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 15; *cf. also* EUROFI, *supra* note 1, (creation of ESMA "should facilitate" the process of the definition, implementation and monitoring of global standards); Greene & Boehm, *supra* note 1, at 1095–97 ("very positive development").

118. Tafara & Peterson, *supra* note 2, at 58; *see also* Greene, *Beyond Borders*, *supra* note 2, at 90; Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 38–39; Greene & Oztan, *supra* note 1, at 29–30;

The establishment of a formal or institutional means for information exchange will require some discussion as well as implementation efforts, but should not constitute an actual obstacle against the background of mutual recognition's benefits.[119]

B. Status Quo and Future Prospects

The United States and the EU failed to use the chance provided by the recent financial crisis for broadly effective joint coordination and/or harmonization efforts.[120] It is possible that because of this failure, the preconditions for mutual recognition are out of reach in some fields of regulation. Nevertheless, if principles and concepts one party set out were adopted by the other party, both parties would still be able to agree to a mutual recognition agreement. But, where neither coordination was sufficiently effective nor one party adopts the standard of the other side, we end up with the question of whether the standards of both parties to a potential mutual recognition agreement are by coincidence sufficiently comparable and both adequate.

In fact, this might be the case in some fields of financial regulation. For example, before the financial crisis emerged, it has been recommended that "[o]ne of the first areas in which the EU and the [United States] should work towards a mutual recognition approach to regulation is with respect to securities intermediaries and securities exchanges."[121] In Europe, this field is governed by MiFID and its implementing measures. Whether the standards which will be set out under MiFID II and its implementing measures will be functionally equivalent to U.S. standards, is a question, though, which cannot be ultimately answered yet. Likely, there will be functional equivalent rules to a large extent. However, some fields which will be impacted by MiFID II and its implementing measures, such as OTC derivatives regulation and regulation of algorithmic trading activity (so-called high-frequency-trading), should be dealt with separately. As to the first one, the assessment is complicated.[122] As to the second one, the discussion about regulation has just started in the United States.

Apart from that, the United States and the EU could agree that they want to mutually recognize the other party's standards and prudential supervision with respect to securities intermediaries and securities exchanges in cross-border contexts. Yet, to be effective, such an agreement should include that no party shall be allowed to impose additional supervision and/or substantive rules caused by special public interest(s) according to broadly phrased exceptions. Each party's standards must be acceptable as sufficient in their entirety. Otherwise, the concept of mutual recognition would likely turn out to be significantly undermined from the outset, as occurred within the EU under the ISD regime. Whether the United States and the EU will be willing to refrain from such exception clauses, is

TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 3–4; Verdier, *supra* note 2, at 86–87, 89, 95–96; de Meijer & Saaf, *supra* note 14, at 130.

119. *See supra* § II.B.

120. *See supra* § I.

121. Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 34. For a more detailed analysis, *see id.,* at 18–24; *see also* de Meijer & Saaf, *supra* note 14, *passim*.

122. *See infra* note 127.

arguably a political question. However, whether they will refrain, is the decisive point.

MiFID II will have implications for the access of third country subjects to EU markets, which was not addressed under MiFID. Such third country access will most likely be based on an equivalence assessment of third country jurisdictions by the European Commission.[123] Thus, the decision(s) will no longer be governed by the third country regimes of the individual Member States, as was the case under MiFID. This is an improvement. However, the procedure will only apply to investment services and activities provided to professional clients and eligible counterparties, but not to retail clients.[124] Moreover, there will be a transitional period of three years during which the Member States have to transpose and implement the MiFID II into their domestic law.[125] Furthermore, it is possible that the European Commission will interpret "equivalence" as a high standard to reach. There might be some reluctance to open the European market to third countries. With respect to the United States, this might especially be true if the United States would apply a substitute compliance approach on a case-by-case basis, maybe differentiating between the Member States of the EU, so that the European Commission could have some doubt as to reciprocity of market access. Therefore, in order to reach legal certainty, the United States and the EU should work on reaching a mutual recognition agreement. Such agreement, then, could serve as a blueprint for other fields of financial regulation.

However, in some fields it will be difficult to find that the United States and EU's standards are sufficiently comparable and adequate for both sides if there are no further efforts to reach effective coordination between the parties.[126] For example, concerns have generally been articulated with respect to diverging standards as to the question of separation of investment banking from commercial and retail banking, or as to the regulation of OTC derivatives.[127] As to the second one, the European Regulation on OTC derivatives, central counterparties and trade repositories, known as the European Market Infrastructure Regulation

123. *See* Memo, European Commission, *supra* note 116.

124. *See id.*

125. *See id.*

126. *Cf.* Verdier, *supra* note 2, at 103 ("Despite international efforts to coordinate regulatory reforms, new U.S. and European rules will in many areas not be identical, and the discrepancies may create substantial new obstacles to cross-border financial activity. This would be an unwelcome development, as it would contradict the Group of 20's objective to avoid protectionism and new restraints on international financial flows.").

127. *Cf.* Comment Letter from the European Comm'n, *supra* note 26 (pointing out the risk of an "uncoordinated, duplicative international regulatory framework"); Greene, *Dodd-Frank and the Future of Financial Regulation*, *supra* note 1, at 88–89 ("In particular, the US proposals to reform the derivatives market differ in important ways from the reforms under consideration in the EU."); Greene & Potiha, *supra* note 1, *passim* (dealing especially with the extraterritorial reach of Dodd-Frank's Volcker rule and margin rules for uncleared swaps); Greene & Boehm, *supra* note 1, at 1127–29 (discussing key tensions as to derivatives regulation, and concluding that there is "a number" of likely conflicts, meaning that the regulators "have not heeded the G-20 call for the development of a single, international framework"); Luettringhaus, *supra* note 35, at 26, 31 (derivatives regulations "differ in some important respects"; "As substantial disharmonies between certain parts of the respective regulations persist, it is far from certain that DFA and EMIR will be considered 'equivalent' or at least 'comparable' in every respect."); Memorandum, Shearman & Sterling LLP, *OTC Derivatives Regulation and Extraterritoriality III* (Feb. 8, 2013), *available at* http://www.shearman.com/files/Publication/79415a4f-560b-4b13-8846095b38621e0a/Presentation/PublicationAttachment/703f95c9-92c8-4afe-9e2a-95a422423a56/OTC-Derivatives-Regulation-and-ExtraterritorialityIII-FIA-020813.pdf ("Both Dodd-Frank and EMIR have some extraterritorial effect, as well as different approaches in certain other key areas which have the potential to give rise to conflicts.").

("EMIR"), was finally adopted by the European Parliament and the Council on July 4, 2012.[128] Regulatory and implementing technical standards were adopted on December 19, 2012.[129] Nevertheless, as indicated above, a final assessment is still not yet soundly possible, since MiFID II and its implementing Regulation on Markets in Financial Instruments ("MiFIR"), both still to be finalized, will amend EMIR.[130]

In any case, it is important that the United States and the EU reinforce their efforts to actually achieve some form of effective coordination or harmonization in the several fields of financial regulation.[131] This coordination should ideally include a mechanism for common interpretation of the coordinated standard(s). When adequate coordination of standards is reached, mutual recognition, as a means to avoid protectionism and new restraints on international capital flows,[132] will be comparatively easy to achieve, and, maybe more important, it will be reasonable to do so.[133]

V. Conclusion

Some form of effective regulatory coordination or harmonization is usually a prerequisite for mutual recognition. Mutual recognition has to be distinguished from the mere intermediate solution of a limited exemptive approach being applied on a case-by-case basis with respect to specific market participants in specific areas. The level of harmonization reached within the EU/EEA with the MiFID and its implementing measures, or with other directives/regulations and their implementation and enforcement in the course of the Lamfalussy Process, is likely not reachable within the transatlantic relationship in the near future. Some less extensive level of coordination or harmonization, based on recommendations of international organizations and bodies, could still justify accepting the other side's

128. Regulation 2012/648, of the European Parliament and of the Council of 4 July 2012, 2012 O.J. (L 201) 1 (EU).

129. European Comm'n, *The EU Single Market: Financial Markets Infrastructure: Derivatives* (Mar. 24, 2014), http://ec.europa.eu/internal_market/financial-markets/derivatives/index_en.htm.

130. *Cf.* Memo, European Comm'n, *supra* note 116.

131. *Cf. also* Greene, *Resolving Regulatory Conflicts*, *supra* note 1, at 33 ("an agenda, much like the FSAP and the accounting roadmap, should be created between the United States and the EU to identify and facilitate transatlantic securities regulation convergence in the short-term and longer term"; it "should adopt . . . a formal agenda with timelines for achieving each step and a formal process of progress reports"); Greene & Boehm, *supra* note 1, at 1085–89, 1098 (illustrating the limits of "name-and-shame", and advocating a stronger role of the supranational institutions, including formal or institutional mechanisms yielding binding agreements; "Because most global financial transactions still take place within the United States and the EU, it is critical that these two jurisdictions adopt a unified front in the reform process."); KERN, *supra* note 1, at 5 (arguing that the "G2", meaning the United States and the EU, must take the lead in the "harsh" reality of international financial market diplomacy, and first work on "joint policy positions between themselves", what in practice "necessitates concrete cooperation on the scheduling, design, and details of regulation"); TRANSATLANTIC COAL. ON FIN. REGULATION Paper, *supra* note 2 (suggesting that and how the process of regulatory analysis and setting standards of sufficient comparability should be "undertaken collectively and under the auspices and sponsorship of IOSCO").

132. *Cf.* Leaders' Statement at the Pittsburgh Summit, *supra* note 1, at 18–19 ("It is imperative we stand together to fight against protectionism. . . . We will not retreat into financial protectionism, particularly measures that constrain worldwide capital flows.").

133. *Cf.* Greene & Potiha, *supra* note 1, at 311 ("when there is an established framework and commitment to common principles, there is not much risk in relying on mutual recognition").

standard as sufficient, though.[134] However, the goal must be to completely convince both sides of the safety and soundness of the other side's standards, so that no party will look for unnecessary public interest exceptions to a mutual recognition agreement. As a result, mutual recognition would be a strict and effective approach.

It is advisable for a mutual recognition agreement to provide a mechanism for common interpretation of the coordinated standards, though it is not a precondition for establishing mutual recognition. Furthermore, centralized control of enforcement of such coordinated standards appears not to be a precondition within the transatlantic relationship. Looking at the inter-European level, the Lamfalussy Process, the extended powers of the newly formed, ESMA, EBA, and EIOPA, as well as the MiFID II and other new legislation should be able to eliminate some big concerns the United States has had and has as to fragmentation of financial laws and inconsistent enforcement within the European Union, thereby diminishing the United States' reluctance as to mutual recognition. However, there needs to be strengthened cooperation in oversight and enforcement matters in the transatlantic relationship, including a sufficient device for information exchange.

In the field of securities intermediaries and securities exchanges, a mutual recognition agreement should already be up for debate. In other fields, the United States and the EU need to stick to their commitment to international cooperation and coordination, and try to align their regulatory efforts more closely to the nonbinding[135] standards and recommendations of the respective international organizations and bodies, such as the Financial Stability Board ("FSB"), the Basel Committee on Banking Supervision ("BCBS") or the International Organization of Securities Commissions ("IOSCO"). On the other hand, recommendations of international organizations need to cover all significant aspects of the respective regulatory field. Furthermore, the recommendations should be more detailed than mere ambiguous principles in order to serve as a basis for an alignment of regulatory efforts sufficiently consistent for mutual recognition. However, negotiations do not always result in recommendations of such breadth and depth. Instead, international conflicts sometimes are solved by "carving out provisions that are objectionable to individual states, leading to a lowest common denominator."[136] This, therefore, emphasizes the need for additional coordination between the transatlantic "partners" if they intend to consummate transatlantic mutual recognition.

The fact that future major financial crises and global scandals can only be prevented, if at all, by sustainable joint efforts, should be enough incentive to

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134. As to the importance of the international organizations, *cf.* Greene & Potiha, *supra* note 1, at 315–16 ("A key to effective cooperation is giving force to international organizations" which "can be effective in establishing norms and best practices and facilitating communications between national regulators that are crucial to coordinating financial regulation."); TRANSATLANTIC COAL. ON FIN. REGULATION, *supra* note 1, at 12 ("The crises . . . demonstrated the overwhelming importance of international coordination in the regulation of markets and institutions and the regulatory standards and principles set by international bodies.").

135. Noncompliance gets sanctioned by not more than the mechanism of "name and shame." Greene & Boehm, *supra* note 1, at 1086.

136. Verdier, *supra* note 2, at 61; *cf. also* Greene & Potiha, *supra* note 1, at 272 ("Their principles are non-compulsory soft law and are typically quite broad, the result of which is granularity and inconsistency when implemented by national regulators.").

facilitate further coordination, at least within the transatlantic relationship, as the EU and the United States comprise the two most important markets to date. Reduction of regulatory arbitrage and the prospect of market liberalization, with all its further benefits,[137] provide additional incentives. Conversely, where a sufficient level of coordination is reached, and actual trust in comparable and adequate standards is established, mutual recognition is the logical next step, and should be taken up by the regulators without delay. Once the reasonable minimum requirements are fulfilled, mutual recognition is not a burdensome step. If the prerequisites are fulfilled, the advantages of mutual recognition clearly outweigh any objections.

It remains to overall conclude that "[w]hen dealing with entities with cross-border influence, and to enhance the confidence in and safety of financial markets, coordination and mutual recognition is key."[138] Effective regulatory coordination and mutual recognition form two sides of one precious coin, a coin which urgently needs to be invested, in order to enhance confidence in and establish safety of financial markets, facilitate private cross-border transactions and control international externalities.[139]

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137. *See supra* § II. B.
138. Greene, *Seminar Syllabus*, *supra* note 1, at 14.
139. *Cf. also supra* § II.B.