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## SHEDDING LIGHT ON EUROPEAN FINANCIAL STABILIZATION MECHANISMS. THE NEW ROLE OF THE EURO AREA MEMBER STATES

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### 1. Introduction

The effects of the ever-increasing economic and financial crisis since 2008 in the countries of the Euro area have highlighted the need for greater economic and financial proximity among the policies of the Member States of the European Monetary Union (EMU)<sup>1</sup>, in light of the potential threat -apparent ever since the approval of the Growth and Stability Pact (GSP) in 1997<sup>2</sup>- in which the high deficit of a Member State in recession could result in the European Central Bank (ECB) losing control over its monetary policy<sup>3</sup>.

<sup>1</sup> About the history of Monetary Integration in Europe see Lastra, *Legal Foundations of International Monetary Stability*, Oxford University Press (2006), pp. 173-206.

<sup>2</sup> See Beetsma and Uhlig, “An analysis of the «Stability Pact»”, (1997) CEPR Discussion. Paper Series n. 1669, p. 1.

<sup>3</sup> In the first discussions on the creation of an Economic and Monetary Union, the topic of the economic governance within the Euro area arose. See, Dyson

In the process of harmonizing economic policies and unifying monetary policies among Member States with the aim of implementing a single currency, which began in the July of 1990, while an authentic monetary union has been achieved among the Member States of the Euro area under the direction of the ECB; a true economic union yet to emerge, since economic decisions remain within the States' competencies.

Indeed, as a result of the connections between the markets in the context of a globalized economy, problems in one part of the world quickly exert their impact on others. As the European Commission recognized in the February of 2008, "the global economic situation and outlook remain unusually uncertain at the

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and Featherstone, *The road to Maastricht: Negotiating Economic and Monetary Union*. Oxford University Press, 1999.

In the context of the action of the European Central Bank, Communication from the Commission (COM (2009) 252 final), European financial supervision, designed a new European framework of financial supervision through the European Systemic Risk Council (ESRC), which will monitor and assess potential threats to financial stability that arise from macro-economic developments and from developments within the financial system as a whole ("macro-prudential supervision"), and the European System of Financial Supervisors (ESFS), consisting of a robust network of national financial supervisors working in tandem with new European Supervisory Authorities to safeguard financial soundness at the level of individual financial firms and protect consumers of financial services ("micro-prudential supervision").

These provisions have been specified by the approval of Regulation (EU) n° 1092/2010 of the European Parliament and of the Council, of 24 November 2010, on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board (O.J. L 331/1, of 15.12.2010). This European Systemic Risk Board is controlled by the European Central Bank in the terms established by Council Regulation (EU) n° 1096/2010, of 17 November 2010 (O.J. L 331/162, of 15.12.2010).

In turn, the "micro-prudential supervision" has been put together by the creation of different European Supervisory Authorities (ESAs), such as the European Security and Markets Authority (ESMA) (Regulation (EU) n° 1095/2010 of the European Parliament and of the Council, of 24 November 2010 (O.J. L 331/84, of 15.12.2010), the European Insurance and Occupational Pensions Authority (EIOPA) (Regulation (EU) n° 1094/2010 of the European Parliament and of the Council, of 24 November 2010 (O.J. 331/8, of 15.12.2010), and the European Banking Authority (EBA) (Regulation (EU) n° 1093/2010 of the European Parliament and of the Council, of 24 November 2010 (O.J. L 331/2, of 15.12.2010).

Concerning the centralizing trend of the EU in relation to the creation of the European Supervisory Authorities (ESMA) see Moloney, "EU financial market regulation after the global financial crisis: "More Europe" or more risks?", 47 CML Rev. (2010), 1364-1371.

start of 2008, with turmoil in financial markets, a US slowdown, and soaring commodity prices, all key factors”, but in this context “the high degree of stability offered by the euro is particularly welcome” and the “financial markets are well regulated in the EU”<sup>4</sup>.

However, on the 29<sup>th</sup> of October of the same year, it was recognized that “the unprecedented crisis” in the international financial markets “has created major challenges for the EU”<sup>5</sup>, which were conducive to the design of an overall EU recovery action plan/framework which involved “a new financial market architecture at the EU level”; dealing with “the impact on the real economy” and a “global response to the financial crisis”<sup>6</sup>, and on the 9<sup>th</sup> of March, 2009 it called for “an ambitious programme of financial sector reform”<sup>7</sup>.

In this regard, exercising legal creativity—in some cases with a certain audacity—the European institutions have drawn up a set of correction mechanisms (not initially included in the original Treaties) designed to guarantee the financial stability of the EU Member States, especially the countries belonging to the Euro area which suffer from or are at risk of suffering from financial crises: namely the European Financial Stabilization Mechanism (EFSM); the European Financial Stability Facility (EFSF); the Art. 136 TFEU amendment, and the European Stability Mechanism Treaty (ESM).

At the same time, the preventive mechanisms of supervision and sanction originally included in the Stability and Growth Pact (SGP) adopted in 1997, have been reinforced through the

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<sup>4</sup> Communication from the Commission to the European Parliament and the Council. Europe’s financial system: adapting to change (COM(2008) 122 final). Available at [eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0122:FIN:EN:PDF](http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0122:FIN:EN:PDF)

<sup>5</sup> A description of the most important landmarks of the economic and monetary crisis in the European Union since 2007, in Kunstein and Wessels, “Die Europäische Union in der Währungskrise: Eckdaten und Schlüsselerscheidungen”. *Integration* 4/2011, 308-322.

<sup>6</sup> Communication from the Commission. From financial crisis to recovery: A European framework for action (COM(2008) 706 final). Available at [eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0706:FIN:EN:PDF](http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0706:FIN:EN:PDF)

<sup>7</sup> Communication for the spring European Council. Driving European recovery (COM(2009) 114 final) Volume 1. Available at [eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2009:0114:FIN:EN:PDF](http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2009:0114:FIN:EN:PDF)

“Six-Pack” and the “Two-Pack”<sup>8</sup>, and have also been laid out in the “Euro-Plus Pact”, establishing a stronger economic policy coordination for competitiveness and convergence<sup>9</sup>, developing the

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<sup>8</sup> The Stability and Growth Pact (SGP) adopted in 1997 was first modified by the Council Regulation (EC) n° 1055/2005 of 27 June 2005 (O.J. L 174/5, 7.07.2005, p. 1), and by the Council Regulation (EC) n° 1056/2005 of 27 June 2005 (O.J. L174/5, 7.07.2005, p. 6).

However, this revision did not involve a substantial alteration of the coordination model of the economic policies among the Member States of the Euro area. Therefore, to encourage the correct long-term functioning of the Monetary Union of the EU, and to develop the provisions laid out in Article 121 TFEU, the European Council approved, on 8 November 2011, the so-called “Six-Pack”.

The “Six-Pack” includes the Council Directive 2011/85/EU of 8 November 2011, on requirements of budgetary frameworks of the Member States (O.J. L 306/41, 23.11.2011); the Council Regulation (EU) n° 1177/2011 of 8 November 2011, amending Regulation (EC) n° 1467/97 (O.J. L 306/33, 23.11.2011); the Regulation (EU) n° 1173/2011 of the European Parliament and of the Council of 16 November 2011, on the effective enforcement of budgetary surveillance in the euro area (O.J. L 306/1, 23.11.2011); the Regulation (EU) n° 1174/2011 of the European Parliament and of the Council of 16 November 2011, on enforcement measures to correct excessive macroeconomic imbalances in the euro area (O.J. L 306/8, 23.11.2011); the Regulation (EU) n° 1175/2011 of the European Parliament and of the Council of 16 November 2011, amending Regulation (EC) n° 1466/97 (O.J. L 306/12, 23.11.2011), and the Regulation (EU) n° 1176/2011 of the European Parliament and of the Council of 16 November 2011, on the prevention and correction of macroeconomic imbalances (O.J. L 306/25, 23.11.2011).

Based on the provision expressed in Art. 136(1) (a) TFEU, on 23 November 2011 the European Commission (MEMO/11/822), proposed the adoption of the new Regulations (making up the “Two Pack”), with the aim of strengthening the coordination and supervision of the budgetary procedures in the Member States of the Euro area with excessive deficits, which suffer or run serious risks of suffering situations of financial instability, or which are under the application of a financial-assistance programme (see OJ of the EU, L 140, of 27 May 2013, Regulation (EU) N° 472/2013 of the European Parliament and of the Council of 21 May 2013, on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability; and Regulation (EU) N° 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area).

<sup>9</sup> Signed in 2011. See the Conclusions of the Heads of State or Government of the Euro area of 11 March 2011 (available at [consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ecofin/119810.pdf](http://consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/119810.pdf)), together with the European Council Conclusions of 24-25 March 2011 in which the Euro-Plus Pact was joined by Bulgaria, Denmark, Latvia, Lithuania, Poland and Romania (available on

coordination of economic and fiscal policy planning throughout the European semester<sup>10</sup>, and a new Treaty (Treaty on Stability, Coordination and Governance-TSCG-)<sup>11</sup> has been signed, imposing stricter fiscal discipline, among other measures.

According to Moloney, there is “current consensus” supporting a European “rule book”, described “as being composed of legislative rules adopted by the Council and European Parliament, delegated Commissions acts (delegated and implementing), technical standards adopted by the Commission but proposed by the (intended) new EU supervisory authorities, and the soft guidance/recommendations adopted by those authorities”<sup>12</sup>.

Indeed, different financial-stabilization mechanisms created by the EU institutions and the Member States of the Euro area, despite their different legal nature, have the common objective to help sustain the financial stability of the Euro area as a whole. In this sense, the path towards Europe’s Economic and Monetary Union, beginning in 1990 and culminating in the creation of the single European currency, has not fully avoided the economic and financial crises of the Member States. On the contrary, while in some ways obligated by circumstance, the Euro area Member States have laid out their own permanent legal system of financial stabilization such as the ESM Treaty, based on the nexus of their union: the single currency. However, even if the ESM Treaty is regarded as an intergovernmental Treaty, the EU institutions are used as an umbilical cord to maintain the link between the new international Treaty and the primary legislation of the EU.

In this way, if one were to apply the conceptual elements of algebra in the theory of sets, until the sovereign-debt crisis was addressed with the adoption of the ESM Treaty, the Euro area

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[consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ec/120296.pdf](http://consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/120296.pdf)).

<sup>10</sup> The Commission published the first Annual Growth Survey (AGS) under the new European semester on 12 January 2011 (COM(2011)11 final) (available at [eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0011:FIN:EN:PDF](http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0011:FIN:EN:PDF)). See also the Presidency’s synthesis report of 16 March 2011 (available at [register.consilium.europa.eu/pdf/en/11/st07/st07745.en11.pdf](http://register.consilium.europa.eu/pdf/en/11/st07/st07745.en11.pdf)).

<sup>11</sup> Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, has been signed upon 25 EU Heads of State or government on 2 March 2012.

<sup>12</sup> See Moloney, “EU financial market regulation after the global financial crisis: “More Europe” or more risks?”, *op. cit.*, note 3, 1325-1326.

Member States constituted the subset B in the EU set (set A). Following adoption of the ESM Treaty the Euro area Member States have become a new legal entity (new set C) which coexists with the EU (set A).

Nevertheless, the present study is limited to the analysis of the mechanisms guaranteeing the financial stability established since 2010 by the EU institutions and the Member States, as interpreted by the recent Judgements of the German Constitutional Federal Court (Bundesverfassungsgericht) and by the European Union Court of Justice. These judgements highlight, from their respective jurisdictional spheres, aspects one must consider in relation to the political and legal meaning of the intervention of the EU and the Eurogroup in guaranteeing the financial stability of the Euro area as a whole. The Judgements also provide important legal elements for the analysis of the relationship between this new legal entity and the EU itself.

## **2. The European Financial Stabilization Mechanism (EFSM) and The European Financial Stability Facility (EFSF): The Judgement of the German Constitutional Federal Court on the 7<sup>th</sup> of September, 2011**

Given the risk for economic and financial stability<sup>13</sup> in the EU posed by the sovereign-debt crisis in Greece triggered in October, 2009, the effects of which were also manifested in other countries of the Euro area, such as Ireland, Portugal, Spain, Italy, and finally Cyprus, the European institutions began to act in early May, 2010<sup>14</sup>.

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<sup>13</sup> As Lastra puts, “financial stability” is a “broad and discretionary concept that generally refers to the safety and soundness of the financial system and to the stability of the payment and settlement systems”, *op. cit.* note 1, p. 92.

<sup>14</sup> The arrangements made between the Member States of the Euro area with Greece and between themselves (Greek Loan Facility-GLF) consist of two agreements adopted on 2 May 2010. On the one hand, the Loan Facility Agreement between the States of the Euro area and Greece essentially establishes the loan conditions and requirements for granting funds, providing bilateral loans pooled by the European Commission for a total amount of circa €80 billion (Slovakia decided not to participate in the Greek Loan Facility Agreement while Ireland and Portugal stepped down from the facility as they requested financial assistance themselves). On the other hand, in the Intercreditor Agreement among the lenders, the Member States of the Euro area

At the Euro summit of the Heads of State or Government of the Euro area on the 7<sup>th</sup> of May, 2010, it was stated that “the Commission will propose a European stabilization mechanism to preserve financial stability in Europe”. It would be submitted for decision to an extraordinary ECOFIN meeting that the Spanish presidency would convene on the 9<sup>th</sup> of May<sup>15</sup>.

In this way, with regard to Art. 122(2) Treaty of Functioning of the European Union (TFEU)<sup>16</sup>, the Commission gave the Proposal for a Council Regulation on the 9<sup>th</sup> of May, 2010<sup>17</sup>, which was finally adopted as the Council Regulation (EU) n° 407/2010, on the 11<sup>th</sup> of May, 2010, establishing a European Financial Stabilization Mechanism (EFSM)<sup>18</sup>.

Indeed, while Art. 122(2) TFEU allows the Union to grant financial assistance to a Member State that “is in difficulties or seriously threatened with severe difficulties caused by natural disasters or exceptional occurrences beyond its control”<sup>19</sup>, Regulation n° 407/2010 establishes the “conditions” and “procedures” under which the European Union financial assistance may be granted to a Member State which is experiencing, or is seriously threatened with, a severe economic or financial

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lay down the rights and duties of the Member States between themselves, as their respective contribution on the pool of loans, and the procedure to authorize the disbursement.

In addition to these measures, given that the economic scenario requires even more drastic action in the course of the current year, regarding the Art. 126(9) and 136 TFEU, the Council Decision 2010/320/EU of 10 May 2010 (O.J. 06.11.2010, L 145/6) was adopted and addressed to Greece with the aim of reinforcing and deepening fiscal surveillance as well as giving notice to Greece to take measures for the deficit reduction judged necessary to remedy the situation of excessive deficit.

<sup>15</sup> Available via [ec.europa.eu/commission\\_2010-2014/president/news/speeches-statements/pdf/114295.pdf](http://ec.europa.eu/commission_2010-2014/president/news/speeches-statements/pdf/114295.pdf)

<sup>16</sup> Art. 122(2) TFEU provides: “Where a Member State is in difficulties or is seriously threatened with severe difficulties caused by natural disasters or exceptional occurrences beyond its control, the Council, on a proposal from the Commission, may grant, under certain conditions, Union financial assistance to the Member State concerned. The President of the Council shall inform the European Parliament of the decision taken”.

<sup>17</sup> COM(2010) 2010 final

<sup>18</sup> O.J. 2010, L 118/1

<sup>19</sup> On the origin of Art. 122(2) in the negotiation of the Treaty of Maastricht, see Louis, “Guest Editorial: The no-bailout clause and rescue packages”, 47 CML Rev. (2010), p. 982-983.

disturbance “caused by exceptional occurrences” beyond its control<sup>20</sup>. Specifically, the financial assistance shall take the form “of a loan” or “of a credit line” and the Commission is empowered, in accordance with a Council decision, to contract loans on capital markets or with financial institutions on behalf of the European Union<sup>21</sup>. The Union financial assistance shall be granted by a Council Decision, adopted by a qualified majority on a proposal from the Commission<sup>22</sup>.

Nevertheless, certain doubts have been expressed over whether the EU Council Regulation of the 11<sup>th</sup> of May, 2010 fits within Art. 122(2) TFEU and, specifically, whether the example of sovereign-debt crisis in Greece constitutes a “natural catastrophe” or an “exceptional event” which that State (and more specifically, its governmental authorities) “could not control”<sup>23</sup>. Such doubts seem reasonable with regard to the particular conclusions mentioned in the Report of the Commission of the 8<sup>th</sup> of January, 2010, on Greek Government deficit and debt statistics (COM(2010) 1 final) since it is clear there were: “severe irregularities” in the Excessive Deficit Procedure (EDP) notifications; the “poor cooperation” between the national services involved in the compilation of EDP figures; an “institutional setting and a public accounting system inappropriate” for the correct reporting of EDP statistics; a “lack of accountability” in the individual provision of figures used in EDP notification; and “unclear responsibility and/or lack of responsibility” on the part of the national services providing source data or compiling statistical data, combined with “unclear empowerment of officials responsible for the data”<sup>24</sup>.

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<sup>20</sup> Art. 1 Regulation (EU) n°407/2010

<sup>21</sup> Art. 2(1) Regulation (EU) n° 407/2010

<sup>22</sup> Art. 3(2) Regulation (EU) n°470/2010

<sup>23</sup> In relation to the commonly accepted interpretation of the exceptional events that a Member State could not control within the meaning of Art. 122(2), it is relevant that the notification of the sovereign-debt crisis in Greece took place after the general elections of the 9<sup>th</sup> of October, 2009, which changed the government (the PASOK replaced the majority party at that time, the New Democracy Party). Similarly, the financial crisis in Spain has been notified to European authorities by a new government of the Popular Party (PP) after general elections held on 20 November 2011.

<sup>24</sup> Available via [epp.eurostat.ec.europa.eu/cache/ITY\\_PUBLIC/COM\\_2010\\_REPORT\\_GREEK/EN/COM\\_2010\\_REPORT\\_GREEK-EN.PDF](http://epp.eurostat.ec.europa.eu/cache/ITY_PUBLIC/COM_2010_REPORT_GREEK/EN/COM_2010_REPORT_GREEK-EN.PDF)

Given that Art. 122(2) TFEU involves the non-application of Art. 125 TFEU<sup>25</sup> (so-called “no-bailout” rule/clause) which prohibits EU Member States from giving financial support to each other<sup>26</sup>, the decision to grant financial aid from the EU to a Member State in a context that does not correspond to that described by Art. 122(2) TFEU, would involve the undue non-application of the no-bailout clause and consequently an *ultra vires* intervention of the EU.

In the latter sense, it is understood that if a sovereign-debt crisis is the result of an accumulation of decisions of the State itself, then Art. 122(2) TFEU could not be applied<sup>27</sup>. By the same token, “an excessive deficit” creating a debt problem within the meaning of Art. 126 TFEU (avoiding excessive government deficits), would not be justified to activate *per se* the assistance procedure provided in Art. 122(2) TFEU<sup>28</sup>. In this way, such cases do not in themselves imply the non-application of the no-bailout clause of Art. 125 TFEU.

However, recitals 3 to 5 of the preamble to the Council Regulation (EU) n°. 407/2010 recognise that when the situation of financial crisis of a Member State - regardless of the cause -, fits within the framework of a world economic and financial crisis that seriously deteriorates the deficit and debt positions of the

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<sup>25</sup> Art. 125 TFEU provides: “1. The Union shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of any Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project. A Member State shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of another Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project.

2. The Council, on a proposal from the Commission and after consulting the European Parliament, may, as required, specify definitions for the application of the prohibitions referred to in Articles 123 and 124 and in this Article”.

<sup>26</sup> Louis states that Article 122(2) TFEU must be interpreted as a “counterweight” to the no-bailout clause (See Louis, *op. cit.*, supra note 18, p. 983); while De Witte considers that Art. 122(2) TFEU neutralises the bail-out prohibition, as a complementary norm “with the same treaty rank” (See de Witte, “The European Amendment for the Creation of a Financial Stability Mechanism” (2011:6), Sieps, p.6.

<sup>27</sup> See Townsend, *The Euro and the EMU. An historical, institutional and economic description* (Harper, 2007), p. 108.

<sup>28</sup> See Louis, *op. cit.*, supra note 18, p. 984.

Member States, having repercussions on the intrinsic financial stability of the Euro area as a whole, it becomes necessary to act towards the financial stabilization of the EU. On this basis, the Council adopted a Decision exercising a wide margin of discretion when interpreting the terms “difficulties”, “serious threat”, “severe difficulties”, “exceptional occurrences”<sup>29</sup>.

Notwithstanding, the Council Regulation of the 11<sup>th</sup> of May, 2010, has been regarded as an *ultra vires* intervention of the European Union in Germany. The monetary policy of the Federal Republic of Germany (aid for Greece) which was agreed with the other members of the Eurogroup and included the Council Regulation n° 407/2010, the EFSF Framework Agreement between the Member States of the Eurogroup and the European Financial Stability Facility (EFSF), of the 7<sup>th</sup> of June, 2010 (“euro rescue package”), was brought before the Constitutional Federal Court (Bundesverfassungsgericht).

In effect, following the Decision agreed on the 9<sup>th</sup> of May, 2010, by the ECOFIN Council<sup>30</sup>, the European Financial Stability Facility (EFSF)<sup>31</sup> was created by the Euro area Member States, as a public limited liability company (*Société Anonyme*), called the “Company”, governed by the laws of the Grand Duchy of Luxembourg<sup>32</sup>, to safeguard financial stability in Europe by providing financial assistance to Euro area Member States within the framework of a macro-economic adjustment programme<sup>33</sup>. Subsequently, on the 8<sup>th</sup> of June, 2010, the Euro area Member States concluded a “Framework Agreement” with the European Financial Stability Facility<sup>34</sup>.

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<sup>29</sup> See de Gregorio Merino, “Legal developments in the Economic and Monetary Union during the debt crisis: The mechanisms of financial assistance”, 49 CML Rev (2012), p. 1634.

<sup>30</sup> On the Council document 9614/10 of the 10<sup>th</sup> of May, 2010, so-called “Special Purpose Vehicle”. See Council document at register.consilium.europa.eu/pdf/en/10/st09/st09614.en10.pdf

<sup>31</sup> See Jansen, “What’s what in Europe. The European Financial Stability Facility (EFSF) and the European Stability Mechanism (ESM). A legal overview”. (2011/4). EUREDIA, 417-420.

<sup>32</sup> See conditions at [efsf.europa.eu/attachments/efsf\\_articles\\_of\\_incorporation\\_en.pdf](http://efsf.europa.eu/attachments/efsf_articles_of_incorporation_en.pdf)

<sup>33</sup> Available via [consilium.europa.eu/uedocs/cms\\_Data/docs/pressdata/en/misc/114977.pdf](http://consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/misc/114977.pdf)

<sup>34</sup> Available via [efsf.europa.eu/attachments/20111019\\_efsf\\_framework\\_](http://efsf.europa.eu/attachments/20111019_efsf_framework_)

Ruling outside the Treaties, as an intergovernmental mechanism, the objective of the EFSF is to collect funds and provide loans in conjunction with the International Monetary Fund (IMF), and to cover the financial needs of Euro area Member States in difficulty, subject to a “strict policy conditionality”<sup>35</sup>. The “Company” is formed for an “unlimited duration” but no new financing programme and no new loan facility agreements will be established or entered into force after the 30<sup>th</sup> of June, 2013<sup>36</sup>.

The board of the EFSF comprises of high-level representatives of the 17 Euro area Member States headed by the Chairman of the EU’s Economic and Financial Committee. As an intergovernmental mechanism, it has no specific statutory requirement for accountability to the European Parliament.

In this way, the so-called “aid for Greece” (or “rescue package”) was articulated around the Council Regulation n<sup>o</sup>. 407/2010 of the 11<sup>th</sup> of May, 2010, establishing the EFSM, and the

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<sup>35</sup> Under the EFSF rules, have been arranged the Master Financial Assistance Facility Agreement between European Financial Stability Facility, the Hellenic Republic (as a Beneficiary Member State), the Hellenic Financial Stability Fund (as Guarantor) and the Bank of Greece (available at [efsf.europa.eu/attachments/efsf\\_greece\\_fafa.pdf](http://efsf.europa.eu/attachments/efsf_greece_fafa.pdf)); the Master Financial Assistance Facility Agreement between European Financial Stability Facility, Ireland (as Beneficiary Member State) and Central Bank of Ireland (available at [efsf.europa.eu/attachments/efsf\\_ireland\\_ffa.pdf](http://efsf.europa.eu/attachments/efsf_ireland_ffa.pdf)); the Master Financial Assistance Facility Agreement between European Financial Stability Facility, the Portuguese Republic (as Beneficiary Member State) and Banco de Portugal (available at [efsf.europa.eu/attachments/efsf\\_portugal\\_ffa.pdf](http://efsf.europa.eu/attachments/efsf_portugal_ffa.pdf)); and the Master Financial Assistance Facility Agreement between European Financial Stability Facility, the Kingdom of Spain (as a Beneficiary Member State), the Fondo de Reestructuración Ordenada Bancaria (as Guarantor) and The Bank of Spain (available at [efsf.europa.eu/attachments/efsf\\_spain\\_ffa.pdf](http://efsf.europa.eu/attachments/efsf_spain_ffa.pdf)).

Moreover, Greece has at least another two programmes assistance also agreed under the EFSF: The Master Financial Assistance Facility Agreement between European Financial Stability Facility, the Hellenic Republic (as Beneficiary Member State) and the Bank of Greece -PSI LM Facility Agreement- (extracts available at [efsf.europa.eu/attachments/efsf\\_financial\\_assistance\\_facility\\_agreement\\_greece\\_psi\\_lm.pdf](http://efsf.europa.eu/attachments/efsf_financial_assistance_facility_agreement_greece_psi_lm.pdf)), and the Financial Assistance Facility Agreement between European Financial Stability Facility, the Hellenic Republic (as Beneficiary Member State) and The Bank of Greece –Bond Interest Facility- (extracts available at [efsf.europa.eu/attachments/efsf\\_financial\\_assistance\\_facility\\_agreement\\_greece\\_bond\\_interest.pdf](http://efsf.europa.eu/attachments/efsf_financial_assistance_facility_agreement_greece_bond_interest.pdf)).

<sup>36</sup> See art. 4 of the EFSF articles of incorporation, available at [efsf.europa.eu/attachments/efsf\\_articles\\_of\\_incorporation\\_en.pdf](http://efsf.europa.eu/attachments/efsf_articles_of_incorporation_en.pdf).

“Framework Agreement” concluded by the Euro area Member States with the EFSF, on the 8<sup>th</sup> of June, 2010. Both mechanisms have been the object of analysis by the German Constitutional Federal Court in relation to the specific rules of assuming guarantees adopted by the Federal Republic of Germany (Act on Financial Stability within the Monetary Union of 7 May 2010<sup>37</sup> and Euro Stabilisation Mechanism Act of 22 May 2010)<sup>38</sup>.

In the proceedings on constitutional complaints (Judgement of the 7<sup>th</sup> of September, 2011)<sup>39</sup>, complainants argued that *ultra vires* acts of the European Union contravene the principle of democracy and infringe the complainant’s right, equivalent to a fundamental right, under Art. 38.1 of the Basic Law (Grundgesetz-GG). Those acts “involve the exercise of sovereignty in Germany” and cannot be interpreted as “democratically legitimate” through *ultra vires* acts of the European Union bodies, such as the Council Regulation (EU) n° 407/2010 of the 11<sup>th</sup> of May, 2010 which violates the bailout prohibition of Art. 125.1 TFEU<sup>40</sup>.

By mirroring the interpretation exercised in the Judgements Solange I (BVerfG 37, 271), Solange II (BVerfG 73, 339), and Solange III (BVerfG 89, 155), the German Constitutional Federal Court has considered that the various acts of cooperation of the Federal Government [including the Council Regulation (EU) n° 407/2010], “are not acts of sovereign power”<sup>41</sup>.

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<sup>37</sup> See Gesetz zur **Übernahme** von Gewährleistungen zum Erhalt der für die Finanzstabilität in der Währungsunion erforderlichen Zahlungsfähigkeit der Hellenischen Republik (Währungsunion- Finanzstabilitätsgesetz - WFStG). BGBl. I S. 537.

<sup>38</sup> See Gesetz zur Übernahme von Gewährleistungen im Rahmen eines europäischen Stabilisierungsmechanismus (StabMechG). BGBl. I S. 627.

<sup>39</sup> BVerfG, 2 BvR 987/10 vom 7.9.2011. Available at [bverfg.de/entscheidungen/rs20110907\\_2bvr098710en.html](http://bverfg.de/entscheidungen/rs20110907_2bvr098710en.html).

This Judgement took place after the rejection by the Bundesverfassungsgericht of the two previous applications for cautionary suspension by Judgements of 7 May 2010 (BVerfG, 2 BvR 1099/10) and of 7 June 2010 (BVerfG, 2 BvR 987/10). Available respectively [bverfg.de/entscheidungen/rs20100507\\_2bvr098710.html](http://bverfg.de/entscheidungen/rs20100507_2bvr098710.html); and [bverfg.de/entscheidungen/rs20100609\\_2bvr109910.html](http://bverfg.de/entscheidungen/rs20100609_2bvr109910.html)

<sup>40</sup> Para. 44. Judgement of 7.9.2011

<sup>41</sup> Para. 115. Judgement of 7.9.2011.

See, Bonini, “Dai “signori dei Trattati” al “Dominus del Bilancio”: Principio democratico, meccanismo europeo di stabilità e forma di governo parlamentare nella recente giurisprudenza del Bundesverfassungsgericht tedesco”, Rivista Associazione Italiana dei Costituzionalisti, 4/2011.

The argument by virtue of which the Bundesverfassungsgericht considers that “the challenged acts –notwithstanding other possibilities of review with regard to the right to apply them in Germany (...) are not sovereign acts of German state authority within the meaning of Art. 93.1 n°4a of the Basic Law (Grund Gesetz-GG) and §90.1 of the Federal Constitutional Court Act (...)”<sup>42</sup>, ultimately evaluates whether or not the Bundestag maintains the capacity “to dispose of its budget on its own responsibility”<sup>43</sup>, considering that this would be a violation of the right to vote recognized in Art. 38.1 of the Basic Law, “if German Bundestag relinquishes its parliamentary budget responsibility with the effect that it or a future Bundestag can no longer exercise the right to decide on the budget on its own responsibility”<sup>44</sup>.

In this sense, the German Constitutional Federal Court places itself in the classic surroundings of a Constitutional State, on the premise that “the fundamental decisions on public revenue and public expenditure are part of the core of parliamentary rights in democracy”<sup>45</sup>.

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<sup>42</sup> Para. 115. Judgement of 7.9.2011

<sup>43</sup> Para. 107. Judgement of 7.9.2011

<sup>44</sup> Para. 121. Judgement of 7.9.2011

<sup>45</sup> Para. 104. Judgement of 7.9.2011

As is known, the roots of modern budgetary practices coincide with the development of the English Constitution. In fact, P. Reuter notes the coincidence in time of the set of “prominent historical dates”: Magna Carta of 1215, the Glorious Revolution of 1668, and the political abdication of the House of Lords in 1911, with the “particular evolution” of the “English budget”. This implies, at a certain point in history, according to the statement, the recognition of “a political and judicial meaning of the budget”, which even transcends the sphere of a specific form of government by constitutional democracy, “parliamentary system”, to become the act by which the “preeminence”, the “sovereignty in political material is defined” [Reuter, “La signification juridique, politique et économique de l’acte budgétaire”, (1947) *Annales de Finances Publiques* (VI-VII), p. 103].

In fact, as L. Trotabas and J.M. Cotteret declare, the “term” and the “thing” that we called budget, come from England, where the term “budget” –meaning in the Middle French a “bouge” or “bougette” (leather bag)-, cross the Channel sometime between 1400 and 1450 and “bougette” acquires a “financial sense” as the “bag of the King and the royal treasure that it contains” (See L. Trotabas and J.M. Cotteret, *Finances Publiques*. Dalloz, Paris, 1970). Once the distinction between the national revenue and the king’s private pocket-money was introduced (see F.W. Maitland, *The Constitutional History of England*. A course of lectures delivered, Cambridge: at the University Press, 1919), in the early 18<sup>th</sup> century, the large leather bag which carried the plans of expenditure

Nevertheless, the Bundesverfassungsgericht developed an argument which could prove relevant in the future. Specifically, taking as a starting point the fact that “the purchasing power of money is included in the area of protection of the fundamental right to property of Art. 14.1 of the Basic Law”<sup>46</sup>, also considers that even though the challenged authorisations to give guarantees “entail considerable challenges for the budgetary policy of the Federal Republic of Germany”, it does not alter the fact that “the sums which have been involved to date do not as yet display such massive effects on monetary stability that a justifiable violation of the guarantee of property is possible”. Certainly, the Federal Constitutional Court feels that it is beyond its remit goes beyond the sphere of its functions “to review economic and financial policy measures to identify negative effects on monetary stability”, although it does not exclude its fiscalization “in marginal cases (...) where there is a manifest decrease of monetary value as a result of the state measures”<sup>47</sup>.

In the context of the EU legal system (and the intergovernmental Treaties) directed at establishing measures to help ensure financial stability, whether for the Member States as a whole or for the individual States of the Euro area, the Federal Constitutional Court understands that “the provisions of the European treaties do not conflict with the understanding of national budget autonomy as an essential power, which cannot be relinquished, of the parliaments of the Member States which enjoy direct democratic legitimation, but instead they presuppose it”<sup>48</sup>. This implies that:

1. The Bundestag makes its budgetary decisions (revenue and expenditure) “free of other-directedness on the part of the bodies and of other Member States of the European Union”.

2. The Bundestag decides on its on behalf “while weighing current needs against the risks of medium and long-term guarantees”.

3. The Budget legislature “may not consent to an

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was called the “budget”, and in 1733, Prime Minister Robert Walpole began referring to the inauguration of the discussions on the Crown’s proposed expenditures as “to open the budget” (see R. Stourm, *Cours de Finances. Le Budget*. Paris, 1912).

<sup>46</sup> Paragr. 111. Judgement of 7.9.2011

<sup>47</sup> Para. 112. Judgement of 7.9.2011

<sup>48</sup> Para. 129. Judgement of 7.9.2011

intergovernmental or supranationally agreed automatic guarantee or performance which is not subject to strict requirements and whose effects are not limited". The Bundestag cannot give "indiscriminate authorization to a substantial degree to guarantees" which excludes the creation of "permanent mechanisms" under international treaties.<sup>49</sup>

4. If the Bundestag approves a large-scale measure of aid involving public expenditure, taken by the Federal Government "in a spirit of solidarity",<sup>50</sup> at international or European level (including supranational agreements), it must be ensured as a "counterpart" that "sufficient parliamentary influence will continue to exist in the manner in which the funds made available are dealt with".<sup>51</sup>

5. The limit to the extent of which guarantee authorizations by the budget legislature will be the "brake on debt", as established in Arts. 109.3 and 115.2 of Basic Law incorporated in 2009 by the 57<sup>th</sup> Act Amending the Basic Law<sup>52</sup>.

### **3. The Decision 2011/199/EU reforming Art. 136 TFEU and the ESM Treaty: The Judgement of the German Constitutional Federal Court of the 12<sup>th</sup> of September, 2012**

On the other hand, the European Council meeting of 24<sup>th</sup>-25<sup>th</sup> of March in 2011 had in its provisional agenda the review of the economic situation and the consensus on a special package of measures to preserve financial stability, which included the "adoption of the decision amending the TFEU with regard to the future European Stability Mechanism" (ESM), as part of a comprehensive package of measures on economic policy<sup>53</sup>. As the

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<sup>49</sup> Para. 127. Judgement of 7.9.2011

<sup>50</sup> Notice that the use of the term "solidarity" coincides, in a different context, with the expression used by Art. 122(1) TFEU: "Without prejudice to any other procedures provided for in the Treaties, the Council, on a proposal from the Commission, may decide, in a spirit of solidarity between Member States, upon the measures appropriate to the economic situation, in particular if severe difficulties arise in the supply of certain products, notably in the area of energy".

<sup>51</sup> Para. 128. Judgement of 7.9.2011

<sup>52</sup> Para. 131. Judgement of 7.9.2011.

See Gesetz vom 29 July 2009. BGBl. I S. 2247.

<sup>53</sup> See [register.consilium.europa.eu/pdf/en/11/st06/st06231.en11.pdf](http://register.consilium.europa.eu/pdf/en/11/st06/st06231.en11.pdf)

European Stability Mechanism (ESM) is designed to safeguard the financial stability of the Euro area as a whole, the European Council and the Heads of State or Government agreed “that Article 122(2) TFEU will no longer be needed/used for such purposes”<sup>54</sup>.

Regarding Art. 48(6) of the Treaty of the European Union (TEU)<sup>55</sup>, the European Council adopted the Decision 2011/199/EU suggesting the amendment of the TFEU by adding a new paragraph to Art. 136 of that Treaty<sup>56</sup>. The additional paragraph 3 runs as follows:

*“3. The Member States whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality”.*

This decision entered into force the 1<sup>st</sup> January 2013, when each Member State notified the completion of their ratification procedures (Art. 2)<sup>57</sup>.

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However, the precedents of the reform of Art. 136 TFEU may date to the Conclusions of the European Council meeting of 28-29 October 2010, where the Heads of the State or Government “agree on the need” for Member States to establish a permanent crisis mechanism to safeguard the financial stability of the Euro area as a whole, and invite the President of the European Council to undertake consultations with the members of the European Council on a limited Treaty change required to that effect, not modifying article 125 TFEU (“no bail-out” clause). Available at [consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ec/117496.pdf](http://consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/117496.pdf)

<sup>54</sup> See Conclusions of the European Council meeting of 16-17 December 2010. Available at [consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ec/118578.pdf](http://consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/118578.pdf)

<sup>55</sup> Given that the reform refers to the “internal policies” part of the TFEU and does not increase the powers of the Union, the conditions to use the simplified revision procedure of Art. 48(6) TEU are fulfilled.

<sup>56</sup> O.J. 2011, L 91/1.

About this first use of the one of the two so-called “simplified revision procedures” introduced by Lisbon Treaty (paragraphs 6 and 7 of Art. 48 TEU), see de Witte, *Op. cit. supra* note 10, p. 2-4.

<sup>57</sup> Currently ratification is been notified to EU Council by the 27 Member States: Austria (on 30/07/2012), Belgium (on 16/07/2012), Bulgaria (on 06/08/2012), Cyprus (on 03/07/2012), Czech Republic (on 05/06/2012), Denmark (on 07/05/2012), Estonia (on 07/09/2012), Finland (on 29/05/2012), France (on 02/04/2012), Germany (on 27/09/2012), Greece (on 17/04/2012), Hungary (on 19/04/2012), Ireland (on 01/08/2012), Italy (on 25/09/2012), Latvia (on 24/05/2012), Lithuania (on 06/07/2012), Luxembourg (on 24/07/2012), Malta

The European Stability Mechanism (ESM) –established by the Member States according to Art. 136(3) TFEU— will replace both the European Financial Stability Facility (EFSF)<sup>58</sup>, and the European Financial Stabilization Mechanism (EFSM) –outwith the purpose of Art. 122(2) TFEU-. Signed as an intergovernmental Treaty establishing a permanent mechanism of financial assistance involving the Euro area Member States (so called “ESM Members”) on the 2<sup>nd</sup> of February, 2012, the ESM Treaty came into force on the 27<sup>th</sup> of September, 2012<sup>59</sup>.

The ESM Treaty is an international financial institution<sup>60</sup> endowed with a capital stock of 700,000 million euros available for subscription (Annex II) according to the initial contribution key provided for in Article 11 and calculated in Annex I<sup>61</sup>. From a greater to a lesser percentage according to the Member States, the contribution is as follows:

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(on 09/10/2012), Netherlands (on 20/09/2012), Poland (on 13/11/2012), Portugal (on 06/02/2012), Romania (on 11/07/2012), Slovakia (on 13/06/2012), Slovenia (on 17/10/2012), Spain (on 15/06/2012), Sweden (on 15/06/2012), and United Kingdom (on 12/11/2012). See table on the ratification process at [europarl.europa.eu/webnp/webdav/site/myjahiasite/users/fboschi/public/Art.%20136%20ESM%20fiscal%20compact%20ratprocess.pdf](http://europarl.europa.eu/webnp/webdav/site/myjahiasite/users/fboschi/public/Art.%20136%20ESM%20fiscal%20compact%20ratprocess.pdf) (Brussels, 7/12/2012).

<sup>58</sup> Notice that the “Company” remains in operation. Its dissolution and liquidation is expected “only when its purpose is fulfilled, i.e., when the “Company” has received full payment of the financing granted to the Member States and has repaid its liabilities under the financial instruments issued and financing arrangements entered into” (art. 4 of the EFSF articles of incorporation. *Op. cit.*, on note 37).

<sup>59</sup> Currently ratification is been notified to EU Council by all 17 Member States signatories: Austria (on 30/07/2012), Belgium (on 26/06/2012), Cyprus (on 28/06/2012), Estonia (on 3/10/2012), Finland (on 29/06/2012), France (on 2/04/2012), Germany (on 27/09/2012), Greece (on 10/05/2012), Ireland (on 1/08/2012), Italy (on 14/09/2012), Luxembourg (on 31/07/2012), Malta (on 19/07/2012), Netherlands (on 13/07/2012), Portugal (on 4/07/2012), Slovakia (on 29/06/2012), Slovenia (on 30/05/2012), and Spain (on 2/07/2012). See table on ratification process *Op. cit.* on note 54.

<sup>60</sup> Art. 1(1) ESM Treaty.

<sup>61</sup> Art. 8(1) ESM Treaty

ESM State Member	ESM key (%)
Federal Republic of Germany	27,1464
French Republic	20,3859
Italian Republic	17,9137
Kingdom of Spain	11,9037
Kingdom of the Netherlands	5,7170
Kingdom of Belgium	3,4771
Hellenic Republic	2,8167
Republic of Austria	2,7834
Portuguese Republic	2,5092
Republic of Finland	1,7974
Ireland	1,5922
Slovak Republic	0,8240
Republic of Slovenia	0,4276
Grand Duchy of Luxembourg	0,2504
Republic of Cyprus	0,1962
Republic of Estonia	0,1860
Malta	0,0731
<b>Total</b>	<b>100</b>

The Member State subscription stock capital of Annex II, arranged from a greater to a lesser amounts:

ESM State Member	Capital subscription (EUR)
Federal Republic of Germany	190 024 800 000
French Republic	142 701 300 000
Italian Republic	124 395 900 000
Kingdom of Spain	83 325 900 000
Kingdom of the Netherlands	40 019 000 000
Kingdom of Belgium	24 339 700 000
Hellenic Republic	19 716 900 000
Republic of Austria	19 483 800 000
Portuguese Republic	17 564 400 000

Republic of Finland	12 581 800 000
Ireland	11 145 400 000
Slovak Republic	5 768 000 000
Republic of Slovenia	2 993 200 000
Grand Duchy of Luxembourg	1 752 800 000
Republic of Cyprus	1 373 400 000
Republic of Estonia	1 302 000 000
Malta	511 700 000
<b>Total</b>	<b>700 000 000 000</b>

In contrast to the EFSM, which demands the concurrence of “a severe economic or financial disturbance” caused by “exceptional occurrences” beyond the control of the Member State, the ESM mobilized funding and provided stability support under strict conditionality, for the benefit of ESM Members which are experiencing, or are threatened by, severe financial problems, “if indispensable to safeguard the financial stability of the Euro area as a whole and of its Member States”<sup>62</sup>. The stability support under strict conditionality may range from “a macro-economic adjustment programme” to continuous compliance with pre-established eligibility conditions<sup>63</sup>.

The instruments for stability support take the form of a credit line<sup>64</sup>, loans<sup>65</sup>, the purchase by the ESM of bonds issued by an ESM Member on the primary market<sup>66</sup>, and the purchase on the secondary market of bonds issued by an ESM Member<sup>67</sup>.

The ESM bodies are the Board of Governors, composed of the Finance Ministers of each ESM member<sup>68</sup> (i.e. the Board of Directors). Each Governor appoints a Director of high training in economic and financial matters<sup>69</sup>, Managing Director and other

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<sup>62</sup> Art. 3 ESM Treaty.

<sup>63</sup> Art. 12(1) ESM Treaty.

<sup>64</sup> Art. 14 ESM Treaty.

<sup>65</sup> Arts. 15 and 16 ESM Treaty.

<sup>66</sup> Art. 17 ESM Treaty.

<sup>67</sup> Art. 18 ESM Treaty.

<sup>68</sup> Art. 5(1) ESM Treaty.

<sup>69</sup> Art. 6(1) ESM Treaty.

dedicated staff if considered necessary<sup>70</sup>.

The Board of Governors, by mutual agreement (i.e. unanimously)<sup>71</sup>, decide on the activation of financial assistance and establish the choice of measures and the financial terms and conditions<sup>72</sup>. In addition, the Board of Governors can review the list of financial assistance instruments<sup>73</sup>, the maximum lending volume of the authorized capital stock of the ESM, or change the authorised capital stock amending Article 8 and Annex II, accordingly<sup>74</sup>.

In relation to the financial assistance scheduled in the ESM Treaty, the Judgement of the German Constitutional Federal Court of the 12<sup>th</sup> of September, 2012<sup>75</sup> outlined a condition to the ratification of the ESM Treaty by the Federal Republic of Germany; if at the same time it is ensured under international law that:

1°. The provision under Article 8(5)(1) of the Treaty establishing the ESM “limits the amount of all payment obligations arising to the Federal Republic of Germany from this treaty to the amount stipulated in Annex II to the treaty” in the sense that “no provision of this treaty may be interpreted in a way that establishes higher payment obligations for the Federal Republic of Germany without the agreement of the German representative”;

2°. The provisions under Article 32(5), Article 34 and Article 35(1) of the ESM Treaty “do not stand in the way of the comprehensive information of the Bundestag and of the Bundesrat”.

On the sidelines of the informal Eurogroup meeting in Nicosia the 14<sup>th</sup> of September, 2012, the Euro area partners, in consultation with the responsible Ministries, agreed on an interpretative declaration according to the conditions set by the German Federal Constitutional Court on Judgement of the 12<sup>th</sup> of September, 2012. The declaration does not amend the ESM Treaty or introduce new ratification requirements.

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<sup>70</sup> Art. 4(1) ESM Treaty.

<sup>71</sup> Art. 5(6) together with Art. 4(3) ESM Treaty.

<sup>72</sup> Art. 5(6)(f) ESM Treaty.

<sup>73</sup> Art. 19 ESM Treaty

<sup>74</sup> Art. 10(1) ESM Treaty.

<sup>75</sup> BVerfG, 2 BvR 1390/12 vom 12.9.2012. Available at [bverfg.de/entscheidungen/rs20120912\\_2bvr139012.html](http://bverfg.de/entscheidungen/rs20120912_2bvr139012.html)

This implies that the interpretative declaration, adopted in Brussels on the 26<sup>th</sup> of September, 2012, signed by the signatory States' Ambassadors and deposited with the Council Secretariat, has not received the approval of any organization representative of the Member States; rendering the German Constitutional Federal Court a legislator of the Euro area.

The interpretative declaration goes as follows:

*Article 8(5) of the Treaty Establishing the European Stability Mechanism ("the Treaty") limits all payment liabilities of the ESM Members under the Treaty in the sense that no provision of the Treaty may be interpreted as leading to payment obligations higher than the portion of the authorized capital stock corresponding to each ESM Member, as specified in Annex II of the Treaty, without prior agreement of each Member's representative and due regard to national procedures.*

*Article 32(5), Article 34 and Article 35(1) of the Treaty do not prevent providing comprehensive information to the national parliaments, as foreseen by national regulation.*

*The above-mentioned elements constitute an essential basis for the consent of the contracting States to be bound by the provisions of the Treaty*<sup>76</sup>.

On the other hand, the functioning of the ESM Treaty, in political terms, poses the problem of democratic legitimacy of the choices adopted under regulatory framework of the ESM. As a new international Treaty, there is no possibility that the European Parliament will play any role<sup>77</sup>. It is an established feature of international law, that democratic legitimacy usually resides in the prior authorization of the Treaty by the representative of the States or in the subsequent ratification of the Treaty by the representative of the States, according to the respective constitutional or legal provisions, and not in the democratic nature of the bodies created by the international Treaty.

In all events, in legal terms, the ESM State Members fall outside the regulatory framework of the EU, perhaps giving rise to the assumption of obligations incompatible with the EU Treaties as a consequence of the ratification of the ESM Treaty.

<sup>76</sup> Available at [dipbt.bundestag.de/dip21/btd/17/107/1710767.pdf](http://dipbt.bundestag.de/dip21/btd/17/107/1710767.pdf)

<sup>77</sup> See Editorial comments, "Debt and democracy: "United States then, Europe now"?, 49 CML Rev. (2010), 1835.

#### **4. The Judgement of the Court of Justice of the European Union of the 24<sup>th</sup> of November, 2012 (the Pringle Case). Considerations on the ESM Treaty in the context of the Treaty on the Functioning of the European Union.**

In relation to the previous point, the Judgement of the Court of Justice of the 27<sup>th</sup> of November, 2012, on preliminary ruling under Article 267 TFEU from Supreme Court (Ireland)<sup>78</sup>, gave an opinion on whether the revision of the TFEU concerned solely the provisions of Part Three of that Treaty and consequently proceeded to use the simplified revision procedure established in Art. 48(6) TFEU.

Firstly, the Court of Justice considers that TFEU, “contains no definitions of monetary policy”. Its provisions on that policy “refer to the objectives, rather than to the measures”<sup>79</sup>.

The primary objective of the Union’s monetary policy -under Articles 127 (1) and 282 (2) TFEU- “is to maintain price stability”. From these premises, it considers that the intended aim pursued by the European Stability Mechanism (ESM) -to safeguard the stability of the Euro area as a whole (an economic policy measure)- is clearly distinct from the objective of maintaining price stability (a monetary-policy measure)<sup>80</sup>, and Council Decision 2011/199/EU granting financial assistance to a Member State “does not fall within monetary policy”<sup>81</sup>.

Moreover, the Court of Justice distinguishes between the nature of these measures, including, on the one hand, the various regulations of the European Parliament and the Council (adopted on the 8<sup>th</sup> and the 16<sup>th</sup> of November, 2011) establishing “closer coordination and surveillance of the economic and budgetary policies conducted by the Member States” and intending “to consolidate macroeconomic stability and the sustainability of public finances”<sup>82</sup> and, on the other hand, the provisions in the chapter of the TFEU relating to economic policy (Articles 123 and 125 TFEU), which are meant “to reduce as far as possible the risk

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<sup>78</sup> Case C-370/12, *Pringle v. Ireland* [2012].

<sup>79</sup> Para. 53. Judgement Court of Justice 27.11.2012.

<sup>80</sup> Para. 56 with regard to the Paragraphs. 93-98. Judgement Court of Justice 27.11.2012.

<sup>81</sup> Para. 57. Judgement Court of Justice 27.11.2012.

<sup>82</sup> Para. 58. Judgement Court of Justice 27.11.2012.

of public-debt crisis”. In addition, there are corrective measures, such as the stability mechanism, intended for “the management of financial crises which, notwithstanding such preventive action as might have been taken, might nonetheless arise”<sup>83</sup>.

From this perspective, given that “the close link” between the objectives to be achieved by the corrective measures can be associated with the preventive aim of the TFEU Treaty relating to economic policy and the regulatory framework for a strengthened economic governance of the European Union, the Court of Justice concludes that the adoption of the ESM Treaty “falls within the area of economic policy”<sup>84</sup> in which the EU does not have exclusive power. Consequently, Article 1 of Decision 2011/119/EU, which envisages the establishment of a stability mechanism, “is not capable of affecting the exclusive power held by the Union under Article 3(1)(c) TFEU” in the area of monetary policy for the Member States whose currency is the euro<sup>85</sup>.

With respect to the possible infringement by the Decision 2011/119/EU of the power of the EU in the ambit of the coordination of the Member States’ economic policies; the Court of Justice considers that the EU and TFEU Treaties do not confer “any specific power on the Union to establish a stability mechanism” of the kind stipulated by Decision 2011/199/EU<sup>86</sup>. Article 122(2) TFEU “does not constitute an appropriate legal basis” for the establishment of this sort of stability mechanism<sup>87</sup>. In fact, nothing in Art. 122 TFEU indicates that the Union has exclusive power to grant financial assistance to a Member State<sup>88</sup>, and Article 143(2) TFEU enables the Union to only grant mutual assistance to a Member States whose currency is not the euro<sup>89</sup>.

On the other hand, as “a financial mechanism”, the ESM is not concerned with the coordination of the economic policies of the Member States<sup>90</sup>, which implies that the EU has not act-

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<sup>83</sup> Para. 59. Judgement Court of Justice 27.11.2012.

<sup>84</sup> Para. 60. Judgement Court of Justice 27.11.2012.

<sup>85</sup> Para. 63. Judgement Court of Justice 27.11.2012.

<sup>86</sup> Para. 64. Judgement Court of Justice 27.11.2012.

<sup>87</sup> Para. 65. Judgement Court of Justice 27.11.2012.

<sup>88</sup> Para. 120. Judgement Court of Justice 27.11.2012.

<sup>89</sup> Para. 66. Judgement Court of Justice 27.11.2012.

<sup>90</sup> Para.110. Judgement Court of Justice 27.11.2012.

ed within the normative framework of Art. 352 TFEU, either<sup>91</sup>. Consequently, the Decision 2011/119/EU does not constitute an “appropriate measure” of the EU to attain one of the objectives set out in the Treaties “if those Treaties have not provided the necessary powers”.

By contrast, on the basis of Articles 4(1) TEU and 5(2) TEU, Member States using the euro “are entitled to conclude an agreement between themselves” to establish a stability mechanism of the kind envisaged by Art. 1 of Decision 2011/199/EU<sup>92</sup>, provided that Member States may not disregard their duty to comply with European Union law, and particularly, the “strict conditionality” established by Art. 136(3) TFEU<sup>93</sup>.

A concept of “conditionality” which is understood by the Court of Justice in the sense that it does not constitute an instrument to “the coordination” of the economic policies of the Member States, but rather “to ensure that the activities of the ESM are compatible with, *inter alia*, Article 125 TFEU and the coordinating measures adopted by the Union”<sup>94</sup>.

In fact, the Court considers that Art. 125 TFEU “is not intended to prohibit either the Union or the Member States from granting any form of financial assistance whatsoever to another Member State”<sup>95</sup>. Within the framework of the Art. 125 TFEU, financial assistance is thus possible (for an EU-State Member or State Member-State member). But for this to be compatible with Art. 125 TFEU, “it is necessary to abide by the objective pursued by that article”<sup>96</sup>, which is “to ensure that the Member States follow a sound budgetary policy”<sup>97</sup>. Given that this is the objective pursued by Art. 125 TFEU, a financial-assistance measure adopted within the ESM framework “is not compatible with Article 125 TFEU unless it is indispensable for the safeguard of the financial stability of the Euro area as a whole and subject to strict

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<sup>91</sup> Para. 67. Judgement Court of Justice 27.11.2012.

<sup>92</sup> Para. 68. Judgement Court of Justice 27.11.2012.

<sup>93</sup> Para. 69. Judgement Court of Justice 27.11.2012.

<sup>94</sup> Para. 111. Judgement Court of Justice 27.11.2012.

<sup>95</sup> Para.130. Judgement Court of Justice 27.11.2012.

<sup>96</sup> Para.133. Judgement Court of Justice 27.11.2012.

<sup>97</sup> Para.135. Judgement Court of Justice 27.11.2012.

conditions<sup>98</sup>. With regard to the ESM Treaty, both conditions are fulfilled and, consequently the Court of Justice concludes that signing on the part of Member States in the Euro area of an agreement as the ESM Treaty does not infringe Art. 125 TFEU<sup>99</sup>.

Concerning the question posed to the Court of Justice, as to whether the revision of the TFEU increases the powers conferred on the Union in the Treaties, the Court ruled that paragraph 3 of Article 136 TFEU “does not confer any new power on the Union” in the Treaties<sup>100</sup>, despite the fact that the ESM Treaty makes use of the Union’s institutions (the Commission, the ECB and the Court of Justice)<sup>101</sup>.

In relation to the role allocated to the Commission and the ECB by the ESM Treaty, the Court of Justice resorts to its own case-law<sup>102</sup> to validate the functions assigned. Thus it recalls that

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<sup>98</sup> Para.136. Judgement Court of Justice 27.11.2012.

<sup>99</sup> Para. 147. Judgement Court of Justice 27.11.2012.

<sup>100</sup> Para.73. Judgement Court of Justice 27.11.2012.

<sup>101</sup> Specifically, the ESM Treaty establishes the use of an emergency voting procedure whereby the Commission and the ECB both conclude that a failure to urgently adopt a decision to grant or implement financial assistance, “would threaten the economic and financial sustainability of the euro area” (Art. 4(4) ESM Treaty).

Likewise the Commission, in liaison with the ECB, may negotiate the economic policy conditionality attached to each financial assistance in the sense of Art. 13 (1) and (2). (Art. 5(6)(g) ESM Treaty with regard to Article 13(3) ESM Treaty), and shall be entrusted with monitoring compliance with the conditionality attached to the financial-assistance facility (Article 13(7) ESM Treaty with regard to the Art. 14(5) (6) ESM Treaty and Art. 17(5) ESM Treaty).

Furthermore the Member of the European Commission in charge of economic and monetary affairs and the President of the ECB “may participate in the meetings of the Board of Governors as observers” (Art. 5(3) ESM Treaty), and they may appoint one observer each in the Board of Directors (Art. 6(2) ESM Treaty). In the same sense, the European Commission shall sign the memorandum of understanding (MoU) on behalf of the ESM (Article 13(4) ESM Treaty).

On the other hand, Art. 37(3) of the ESM Treaty provides for the intervention of the Court of Justice of the European Union if an ESM Member “contests the decision referred to in paragraph 2” adopted by the Board of Governors.

<sup>102</sup> *Parliament v. Council and Commission* (C-181/91 and C-248/91, of 30 July 1993. Rec. p. I-3685) and *Parliament v. Council* (C-316/91, of 2 March 1994. Rec. p. I-625).

Those Judgements recognize that, in matters that are not under the exclusive power of the EU, the Member States can contract commitments from third-party States collectively or individually and even jointly with the EU. Regarding the

State Members are entitled, in the areas which do not fall under the exclusive power of the Union, to entrust tasks to the institutions, outside the framework of the Union, provided that those tasks do not alter the essential character of the powers conferred on those institutions by the TEU and TFEU<sup>103</sup>. In this way, the tasks conferred to the Commission and the ECB within the ESM Treaty do not “entail any power to make decisions of its own”<sup>104</sup>, or “alter the essential character of the powers conferred on those institutions” within the TEU and the TFEU.

However, given the political and legal nature of the European Commission and the ECB, the Court does not appear to take into account that this intervention in the functioning of the ESM Treaty, involves the participation of Member States which do not belong to the Euro area, have not signed the ESM Treaty and consequently make no type of subscription on the authorized capital stock.

With respect to the duty assigned in Article 37(3) of the ESM Treaty to the European Union Court of Justice, the Court considers that it is called upon to exercise Art. 273 TFEU<sup>105</sup> -also from the perspective that the membership of the ESM consists solely of Member States-<sup>106</sup> taking as the “special agreement” that Art. 273 TFEU requires the “whole class of pre-defined disputes” by means of a provision such as Article 37(3) of the ESM Treaty<sup>107</sup>. Moreover, the disputes to be submitted to the jurisdiction of the Court “are related to the subject matter of the Treatises” within the meaning of Art. 273 TFEU<sup>108</sup>, while “a dispute linked to the interpretation or application of the ESM Treaty is likely also

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first Judgement, the Parliament brought actions under Article 173 of the EEC Treaty for the annulment of an act adopted at the 1487th session of the Council with a view to the grant of special aid to Bangladesh and of the means adopted by the Commission implementing that act. Regarding the second Judgement, the European Parliament brought action under Article 173 of the EEC Treaty for the annulment of Financial Regulation 91/491/EEC of 29 July 1991 applicable to development finance cooperation under the Fourth ACP-EEC Convention (so-called the Lome Convention).

<sup>103</sup> Para. 158. Judgement Court of Justice 27.11.2012.

<sup>104</sup> Para. 161. Judgement Court of Justice 27.11.2012.

<sup>105</sup> Para. 171. Judgement Court of Justice 27.11.2012.

<sup>106</sup> Para. 175. Judgement Court of Justice 27.11.2012.

<sup>107</sup> Para. 172. Judgement Court of Justice 27.11.2012.

<sup>108</sup> Para. 173. Judgement Court of Justice 27.11.2012.

to concern the interpretation or application of provisions of European Union law”<sup>109</sup>.

## 5. Conclusions

The sovereign-debt crisis in the Euro area has triggered the adoption of a set of political decisions and legal regulations that, among other aims, seek formulas for the financial stabilization of countries that suffer or run serious risks of suffering severe financial crises which might have repercussions for the financial stability of the entire Euro area.

In this context, the Euro area (referring specifically to the Protocol n° 14 TFEU), has become a legal subject of international law, which concerns a common interest within the context of the EU and the entire international community.

Following the revision of Article 136 TFEU, the protection of the single currency against the threats of the financial markets has required the Member States of the Euro area to adopt a permanent financial-stabilization mechanism, i.e. the ESM Treaty, declared in accordance with the EU Treaties by the Court of Justice of the EU in the Judgement of the 27<sup>th</sup> of November, 2012.

Through the adoption of the ESM Treaty, which takes on the form of an intergovernmental treaty, the Euro area responds subsidiarily to the situations of financial crisis of any of its members, while the European Commission and the ECB have been assigned the role of final guardians of the financial stability of the Euro area, giving rise to a sort of “guided decentralization” by the EU in decision making by the bodies of the functioning of the ESM Treaty.

In any case, the subscriptions to the authorized capital stock of each ESM State Member included in the ESM Treaty have been interpreted in a limited way in the Judgement of the German Constitutional Federal Court of 12 September 2012, giving rise to an interpretive Declaration of the Member States adopted outside the ratification procedure of the ESM Treaty by the Member States. However, the German Constitutional Federal Court has also, in its Judgement of the 7<sup>th</sup> of September, 2011, aired its

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<sup>109</sup> Para. 174. Judgement Court of Justice 27.11.2012.

opinion in relation to enforcing the financial-stabilization measure, whether with the legal support of EU Treatises (such as the EFSM) or as instruments established outside the order of the EU Basic law by Member States of the Euro area (such as EFSF). This highlights the need to guarantee the exercise of the sovereign powers of the Bundestag in relation to the budgetary approval of economic assistance to Member States of the EU or of the Euro area affected by the financial crisis.

### **Abstract**

*The sovereign-debt crisis affecting different countries of the European Union (EU) since 2009 has led to the articulation of different financial-stabilization mechanisms both within the EU legal system as well as through international regulations linking European Member States of the Euro area. This constitutes a set of financial stabilization mechanisms with respect to which the German Constitutional Federal Court has declared, while in a different context, its need to guarantee the exercise of the sovereign powers of the Bundestag in relation to the budget approval of economic aid to the EU or to Euro area Member States affected by the financial crisis. By signing the European Stability Mechanism Treaty, the Euro area Member States have in fact become subject to international law under a common interest, the protection of financial stability of the Euro area as a whole. However, despite having adopted the legal form of an intergovernmental treaty, thereby situating itself outside the scope of EU primary legislation, the ESM Treaty maintains a link—a sort of umbilical cord—with certain European institutions, in particular with the European Commission and the European Central Bank (ECB), which has been analysed, inter alia, in the Judgement of the Court of Justice the 27<sup>th</sup> of November, 2012 (the Pringle Case), as to engender a kind of “guided decentralization” by some of the EU Institutions in the decision making process of the ESM treaty bodies.*

La crisis de la deuda soberana que ha afectado a diversos países de la Unión Europea (UE) desde 2009 ha supuesto la articulación de diversos mecanismos de estabilización financiera, tanto en el marco jurídico de la UE como a través de normas de carácter internacional que vinculan a los Estados miembros de la Eurozona. Un conjunto de mecanismos de estabilización financiera respecto de los cuales se ha pronunciado, aunque en un contexto diferente, el Tribunal Constitucional Federal alemán, planteando la necesidad de garantizar el ejercicio de las competencias soberanas del Bundestag en relación con la aprobación pre-

supuestaria de ayudas económicas a los Estados miembros de la Unión Europea o del Eurogrupo afectados por una crisis financiera. A través de la ratificación del Tratado por el que se establece el Mecanismo Europeo de Estabilidad (MEDE). La Eurozona se ha constituido, de hecho, en sujeto de derecho internacional titular de un interés común, la defensa de la estabilidad financiera de la zona Euro en su conjunto. Sin embargo, a pesar de ser un Tratado intergubernamental ubicado, en consecuencia, al margen de los Tratados constitutivos de la Unión Europea, mantiene un vínculo de unión –a modo de cordón umbilical– con ciertas instituciones europeas, en especial con la Comisión Europea y el Banco Central Europeo (BCE), que ha sido analizado entre otros aspectos en la Sentencia del Tribunal de Justicia de 27 de noviembre de 2012 (Asunto Pringle), dando lugar a una especie de “descentralización tutelada” por algunas instituciones de la Unión Europea en el proceso de toma de decisiones por parte de los órganos de funcionamiento del Mecanismo Europeo de Estabilidad.

