JUDGMENT OF THE COURT
28 January 2013

(Directive 94/19/EC on deposit-guarantee schemes – Obligation of result – Emanation of the State – Discrimination)

In Case E-16/11,

EFTA Surveillance Authority, represented by Xavier Lewis, Director, and Gjermund Mathisen, Officer, Department of Legal & Executive Affairs, acting as Agents,

applicant,

supported by the

European Commission, represented by its Agents Enrico Traversa, Albert Nijenhuis and Karl-Philipp Wojcik,

intervener,

v

Iceland, represented by Kristján Andri Stefánsson, Agent, Tim Ward QC, Lead counsel, Jóhannes Karl Sveinsson, Co-counsel,

defendant,

APPLICATION for a declaration that by failing to ensure payment of the minimum amount of compensation to Icesave depositors in the Netherlands and in the United Kingdom provided for in Article 7(1) of the Act referred to at point 19a of Annex IX to the Agreement on the European Economic Area (Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes) within the time limits laid down in Article 10 of the Act, Iceland has failed to comply with the obligations resulting from that Act, in particular its Articles 3, 4, 7 and 10, and/or Article 4 of the Agreement on the European Economic Area.

THE COURT,

composed of: Carl Baudenbacher, President and Judge Rapporteur, Páll Hreinsson, and Ola Mestad (ad hoc), Judges,

Registrar: Gunnar Selvik,

- having regard to the written pleadings of the parties and the intervener and the written observations of the Principality of Liechtenstein, represented by Dr Andrea Entner-Koch, Director of the EEA Coordination Unit, and by Frederique Lambrecht, Legal Officer at the EEA Coordination Unit, acting as Agents;
- the Kingdom of the Netherlands, represented by Corinna Wissels, Mielle Bulterman and Charlotte Schillemans, Head and members of the European Law Division of the Legal Affairs Department of the Ministry of Foreign Affairs, acting as Agents;
- the Kingdom of Norway, represented by Kaja Moe Winther, Senior Adviser, Ministry of Foreign Affairs, and Torje Sunde, advokat, Office of the Attorney General (Civil Affairs), acting as Agents;
- the United Kingdom of Great Britain and Northern Ireland, represented by Heather Walker of the Treasury Solicitor's Department, acting as Agent, and Mark Hoskins QC,

having regard to the Report for the Hearing,

having heard oral argument of the applicant, represented by its Agents Xavier Lewis and Gjermund Mathisen; the defendant, represented by its Agent Kristján Andri Stefánsson, Lead counsel Tim Ward QC, and Co-counsel and Supreme Court Attorney Jóhannes Karl Sveinsson, assisted by Professor Miguel Poiares Maduro, State Attorney General Einar Karl Hallvarðsson, Supreme Court Attorney Reimar Pétursson, Dóra Guðmundsdóttir, Kristín Haraldsdóttir and Þóra M. Hjaltested, advisers; the intervener, represented by its Agents Enrico Traversa and Albert Nijenhuis; Liechtenstein, represented by its Agent Dr Andrea Entner-Koch; the Netherlands, represented by its Agents Corinna Wissels and Charlotte Schillemans, and Gerald Enting, Ministry of Finance, and Sander Timmerman, Netherlands Central Bank; Norway, represented by its Agents Kaja Moe Winther, Senior Adviser, and Kristin Nordland Hansen, Higher Executive Officer, Ministry of Foreign Affairs; the United Kingdom, represented by its Agent Heather Walker, and Mark Hoskins QC; at the hearing on 18 September 2012,

gives the following

Judgment

I Legal context

EEA law

1 Article 4 EEA provides:

> *Within the scope of application of this Agreement, and without prejudice to any special provisions contained therein, any discrimination on grounds of nationality shall be prohibited.*

2 The Act referred to at point 19a of Annex IX to the EEA Agreement (Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes, OJ 1994 L 135, p. 5), as amended, provides for minimum harmonised rules as regards deposit-guarantee schemes.

3 Recital 1 in the preamble to Directive 94/19 reads:

> *Whereas, in accordance with the objectives of the Treaty, the harmonious development of the activities of credit institutions throughout the Community should be promoted through the elimination of all restrictions on the right of establishment and the freedom to provide services, while increasing the stability of the banking system and protection for savers;*

4 Recital 2 in the preamble to Directive 94/19 reads:

> *Whereas, when restrictions on the activities of credit institutions are eliminated, consideration should be given to the situation which might arise if deposits in a credit institution that has branches in other Member States become unavailable; whereas it is indispensable to ensure a harmonized minimum level of deposit protection wherever deposits are located in the Community; whereas such deposit protection is as essential as the prudential rules for the completion of the single banking market;*

5 Recital 3 in the preamble to Directive 94/19 reads:

> *Whereas in the event of the closure of an insolvent credit institution the depositors at any branches situated in a Member State other than that in which the credit institution has its head office must be protected by the same guarantee scheme as the institution's other depositors;*

6 Recital 4 in the preamble to Directive 94/19 reads:

> *Whereas the cost to credit institutions of participating in a guarantee scheme bears no relation to the cost that would result from a massive withdrawal of bank deposits not only from a credit institution in difficulties but also from*

healthy institutions following a loss of depositor confidence in the soundness of the banking system;

7 Recital 7 in the preamble to Directive 94/19 reads:

Whereas a branch no longer requires authorization in any host Member State, because the single authorization is valid throughout the Community, and its solvency will be monitored by the competent authorities of its home Member State; whereas that situation justifies covering all the branches of the same credit institution set up in the Community by means of a single guarantee scheme; whereas that scheme can only be that which exists for that category of institution in the State in which that institution's head office is situated, in particular because of the link which exists between the supervision of a branch's solvency and its membership of a deposit-guarantee scheme;

8 Recital 16 in the preamble to Directive 94/19 reads:

Whereas, on the one hand, the minimum guarantee level prescribed in this Directive should not leave too great a proportion of deposits without protection in the interest both of consumer protection and of the stability of the financial system; whereas, on the other hand, it would not be appropriate to impose throughout the Community a level of protection which might in certain cases have the effect of encouraging the unsound management of credit institutions; whereas the cost of funding schemes should be taken into account; whereas it would appear reasonable to set the harmonized minimum guarantee level at ECU 20 000; whereas limited transitional arrangements might be necessary to enable schemes to comply with that figure;

9 Recital 23 in the preamble to Directive 94/10 reads:

Whereas it is not indispensable, in this Directive, to harmonize the methods of financing schemes guaranteeing deposits or credit institutions themselves, given, on the one hand, that the cost of financing such schemes must be borne, in principle, by credit institutions themselves and, on the other hand, that the financing capacity of such schemes must be in proportion to their liabilities; whereas this must not, however, jeopardize the stability of the banking system of the Member State concerned;

10 Recital 24 in the preamble to Directive 94/19 reads:

Whereas this Directive may not result in the Member States' or their competent authorities' being made liable in respect of depositors if they have ensured that one or more schemes guaranteeing deposits or credit institutions themselves and ensuring the compensation or protection of depositors under the conditions prescribed in this Directive have been introduced and officially recognized;

11 Recital 25 in the preamble to Directive 94/19 reads:

Whereas deposit protection is an essential element in the completion of the internal market and an indispensable supplement to the system of supervision of

credit institutions on account of the solidarity it creates amongst all the institutions in a given financial market in the event of the failure of any of them,

12 Article 1 of Directive 94/19 reads:

1. "deposit" shall mean any credit balance which results from funds left in an account or from temporary situations deriving from normal banking transactions and which a credit institution must repay under the legal and contractual conditions applicable, and any debt evidenced by a certificate issued by a credit institution.

...

3. "unavailable deposit" shall mean a deposit that is due and payable but has not been paid by a credit institution under the legal and contractual conditions applicable thereto, where either:

(i) the relevant competent authorities have determined that in their view the credit institution concerned appears to be unable for the time being, for reasons which are directly related to its financial circumstances, to repay the deposit and to have no current prospect of being able to do so.

The competent authorities shall make that determination as soon as possible and at the latest 21 days after first becoming satisfied that a credit institution has failed to repay deposits which are due and payable;

(ii) a judicial authority has made a ruling for reasons which are directly related to the credit institution's financial circumstances which has the effect of suspending depositors' ability to make claims against it, should that occur before the aforementioned determination has been made;

4. "credit institution" shall mean an undertaking the business of which is to receive deposits or other repayable funds from the public and to grant credits for its own account;

5. "branch" shall mean a place of business which forms a legally dependent part of a credit institution and which conducts directly all or some of the operations inherent in the business of credit institutions; any number of branches set up in the same Member State by a credit institution which has its head office in another Member State shall be regarded as a single branch.

13 Article 3 of Directive 94/19 reads:

1. Each Member State shall ensure that within its territory one or more deposit-guarantee schemes are introduced and officially recognized. ...

14 Article 4 of Directive 94/19 reads:

1. Deposit-guarantee schemes introduced and officially recognized in a Member State in accordance with Article 3(1) shall cover the depositors at branches set up by credit institutions in other Member States. ...

15 Article 7 of Directive 94/19 reads:

> *1. Deposit-guarantee schemes shall stipulate that the aggregate deposits of each depositor must be covered up to ECU 20 000 in the event of deposits' being unavailable.*
>
> *...*
>
> *6. Member States shall ensure that the depositor's rights to compensation may be the subject of an action by the depositor against the deposit-guarantee scheme.*

16 Article 8 of Directive 94/19 reads:

> *1. The limits referred to in Article 7(1), (3) and (4) shall apply to the aggregate deposits placed with the same credit institution irrespective of the number of deposits, the currency and the location within the Community.*
>
> *...*

17 Article 9 of Directive 94/19 reads:

> *1. Member States shall ensure that credit institutions make available to actual and intending depositors the information necessary for the identification of the deposit-guarantee scheme of which the institution and its branches are members within the Community or any alternative arrangement provided for in Article 3(1), second subparagraph, or Article 3(4). The depositors shall be informed of the provisions of the deposit-guarantee scheme or any alternative arrangement applicable, including the amount and scope of the cover offered by the guarantee scheme. That information shall be made available in a readily comprehensible manner.*
>
> *Information shall also be given on request on the conditions for compensation and the formalities which must be completed to obtain compensation.*
>
> *2. The information provided for in paragraph 1 shall be made available in the manner prescribed by national law in the official language or languages of the Member State in which the branch is established.*
>
> *3. Member States shall establish rules limiting the use in advertising of the information referred to in paragraph 1 in order to prevent such use from affecting the stability of the banking system or depositor confidence. In particular, Member States may restrict such advertising to a factual reference to the scheme to which a credit institution belongs.*

18 Article 10 of Directive 94/19 reads:

> *1. Deposit-guarantee schemes shall be in a position to pay duly verified claims by depositors in respect of unavailable deposits within three months of the date on which the competent authorities make the determination described in Article 1(3)(i) or the judicial authority makes the ruling described in Article 1(3)(ii).*

2. In wholly exceptional circumstances and in special cases a guarantee scheme may apply to the competent authorities for an extension of the time limit. No such extension shall exceed three months. The competent authorities may, at the request of the guarantee scheme, grant no more than two further extensions, neither of which shall exceed three months.

...

National law

19 Directive 94/19 was implemented into Icelandic law by Act No 98/1999 on a Deposit Guarantee and Investor Compensation Scheme (lög um innstæðutryggingar og tryggingakerfi fyrir fjárfesta).

20 Article 1 of Act No 98/1999 reads:

The objective of this Act is to guarantee a minimum level of protection to depositors in commercial banks and savings banks, and to customers of companies engaging in securities trading pursuant to law, in the event of difficulties of a given company in meeting its obligations to its customers according to the provisions of this Act.

21 Article 2 of Act No 98/1999 reads:

Guarantees under this Act are entrusted to a special institute named the Depositors' and Investors' Guarantee Fund, hereinafter referred to as the "Fund". The Fund is a private foundation operating in two independent departments, the Deposit Department and the Securities Department, with separate finances and accounting, cf. however the provisions of Article 12.

22 Article 3 of Act No 98/1999 reads:

Commercial banks, savings banks, companies providing investment services, and other parties engaging in securities trading pursuant to law and established in Iceland shall be members of the Fund. The same shall apply to any branches of such parties within the European Economic Area within the States parties to the EFTA Convention or in the Faroe Islands. Such parties, hereinafter referred to as Member Companies, shall not be liable for any commitments entered into by the Fund beyond their statutory contributions to the Fund, cf. the provisions of Articles 6 and 7. The Financial Supervisory Authority shall maintain a record of Member Companies.

23 Article 6 of Act No 98/1999 reads:

The total assets of the Deposit Department of the Fund shall amount to a minimum of 1% of the average amount of guaranteed deposits in commercial banks and savings banks during the preceding year.

…

24 Article 9 of Act No 98/1999 reads:

> *If, in the opinion of the Financial Supervisory Authority, a Member Company is unable to render payment of the amount of deposits, securities or cash upon a customer's demand for refunding or return thereof in accordance with applicable terms, the Fund shall pay to the customer of the Member Company the amount of his deposit from the Deposit Department and the value of his securities and cash in connection with securities trading from the Securities Department. The obligation of the Fund to render payment also takes effect if the estate of a Member Company is subjected to bankruptcy proceedings in accordance with the Act on Commercial Banks and Savings Banks and the Act on Securities Trading.*
>
> *The opinion of the Financial Supervisory Authority shall have been made available no later than three weeks after the Authority first obtains confirmation that the relevant Member Company has not rendered payment to its customer or accounted for his securities in accordance with its obligations. …*
>
> *Further specifications regarding payments from the Fund shall be included in a Government Regulation.*

25 Article 10 of Act No 98/1999 reads:

> *In the event that the assets of either department of the Fund are insufficient to pay the total amount of guaranteed deposits, securities and cash in the Member Companies concerned, payments from each Department [i.e. the Fund's deposits department and the Fund's securities department] shall be divided among the claimants as follows: each claim up to ISK 1.7 million shall be paid in full, and any amount in excess of that shall be paid in equal proportions depending on the extent of each Department's assets. This amount shall be linked to the EUR exchange rate of 5 January 1999. No further claims can be made against the Fund at a later stage even if losses suffered by the claimants have not been compensated in full. Should the total assets of the Fund prove insufficient, the Board of Directors may, if it sees compelling reasons to do so, take out a loan in order to compensate losses suffered by claimants.*
>
> *In the event that payment is effected from the Fund, the claims made on the relevant Member Company or bankruptcy estate will be taken over by the Fund.*

II Facts

26 On 1 January 2000, Iceland implemented Directive 94/19 (hereinafter "the Directive") through the enactment of Act No 98/1999 on a Deposit Guarantee and Investor Compensation Scheme. Act No 98/1999 set up the Depositors' and Investors' Guarantee Fund which started operating on the same day.

27 In October 2006, Landsbanki Íslands hf (hereinafter "Landsbanki") launched a branch in the United Kingdom which provided online savings accounts under the brand name "Icesave". A similar Icesave online deposit branch was launched in the Netherlands which began accepting deposits in Amsterdam on 29 May 2008.

The Icesave accounts drew in substantial deposits both from private and public investors.

28 As a part of a worldwide financial crisis, there was a run on Icesave accounts in the United Kingdom from February to April 2008.

29 In accordance with the division of responsibility laid down under the Directive, deposits at the British and Netherlands branches of Landsbanki were under the responsibility of Iceland's Depositors' and Investors' Guarantee Fund (hereinafter "TIF"), which offered a minimum guarantee of ISK 1 700 000 per depositor pursuant to Article 10 of Act No 98/1999. Iceland did not make use of the option provided for in Article 7(2) of the Directive to exclude certain categories of depositors from the guarantee scheme.

30 From May 2008, Landsbanki opted to take part in the Netherlands deposit-guarantee scheme to supplement its home scheme. At that time, the minimum amount guaranteed under the Netherlands scheme was EUR 40 000 per depositor which was later raised to EUR 100 000 per depositor. Similarly, the Landsbanki branch in the United Kingdom joined the UK deposit-guarantee scheme for additional coverage. Deposits at the British branch of Landsbanki in excess of the minimum amount guaranteed by the Icelandic TIF were later guaranteed by the UK scheme to a maximum of GBP 50 000 for each retail depositor.

31 On 3 October 2008, the UK's Financial Supervisory Authority issued a Supervisory Notice which required Landsbanki to take certain actions with regard to its London branch. The practical effect was to freeze the assets of the Landsbanki branch.

32 On 6 October 2008, Landsbanki's Icesave websites in the Netherlands and in the United Kingdom ceased to work and depositors at those branches lost access to their deposits.

33 On the same day, Althingi, the Icelandic Parliament, adopted Emergency Act No 125/2008. The Emergency Act provided for the creation of new banks and the granting of priority status in the bankruptcy to depositors with claims upon the TIF.

34 On 7 October 2008, Landsbanki collapsed and the Icelandic Financial Supervisory Authority ("Fjármálaeftirlitið", hereinafter "FME") assumed the powers of the meeting of Landsbanki's shareholders and immediately suspended the bank's board of directors. The FME appointed a winding-up committee which, with immediate effect, assumed the full authority of the board.

35 On the same day, the Netherlands Central Bank submitted a petition to the District Court of Amsterdam asking for a ruling that certain emergency regulations of Netherlands law applied.

36 Between 6 and 9 October 2008, the Icelandic Minister of Finance established new banks under the Emergency Act.

37 On 8 October 2008, the UK Government took action under its Anti-Terrorism, Crime and Security Act of 2001 to formally freeze the assets of Landsbanki, and initially also funds relating to Landsbanki owned, held or controlled by the FME and the Central Bank of Iceland (hereinafter "CBI") in the UK.

38 Between 9 and 22 October 2008, domestic deposits in Landsbanki were transferred to the new bank "New Landsbanki" which was established by the Icelandic Government. The transfer was based on a decision of the FME of 9 October 2008 that exercised its powers under the Emergency Act to achieve a restructuring of the Icelandic banks.

39 On 13 October 2008, at the request of the Netherlands Central Bank, the District Court of Amsterdam declared certain emergency regulations of Netherlands law applicable and appointed administrators to handle the affairs of the branch, including all assets and dealings with customers of the branch.

40 On 27 October 2008 and thereafter, the FME made statements that triggered an obligation for the TIF to make payments in accordance with Article 9 of Act No 98/1999 on a Deposit Guarantee and Investor Compensation Scheme to customers of Landsbanki's branches in the UK and the Netherlands. The original three-month time limit for payments was extended in accordance with Article 10(2) of the Directive to 23 October 2009.

41 On 19 November 2008, the IMF approved a two-year Stand-By Arrangement of USD 2.1 billion to Iceland. Under the Arrangement, USD 827 million was made available immediately, with eight further instalments of USD 155 million to follow. An important feature of the IMF Arrangement was the requirement to introduce stringent capital controls to prevent further devaluation of the Icelandic króna. The IMF Arrangement was based upon certain projections as to the balance of payments and sustainability of debt.

42 In late 2008, compensation to depositors was paid under the Netherlands und British deposit-guarantee schemes. All retail account holders in the United Kingdom received (or in a very small number of cases, declined) compensation payments from the UK Government, to the full value of their deposits. In the Netherlands, the Netherlands Government paid all private and wholesale account holders to a maximum of EUR 100 000 per depositor.

43 On 28 November 2008, temporary capital account restrictions were imposed to prevent further depreciation of the Icelandic króna, as an important part of the economic programme Iceland followed during its cooperation with the IMF. The capital controls restricted, in general, all transnational foreign currency movements except those for the purchase of goods and services. A very limited range of other transactions, including those related to emigration, were also exempted from the controls.

44 On the same day, the Icelandic Government presented the EFTA Standing Committee and the EEA Joint Committee with notifications of protective measures under Article 43 EEA. Neither committee reacted unfavourably to the protective measures.

45 In December 2008, the Icelandic Parliament established a Special Investigation Commission (hereinafter "SIC") to investigate and analyse the processes leading to the collapse of the three main banks in Iceland. The report was delivered on 12 April 2010.

46 By March 2009, 93% of the commercial banking sector in Iceland had failed. The FME estimates that since October 2008 in total banks representing 99% of the Icelandic banking market became subject to either winding up or financial restructuring.

47 On 1 April 2009, the EFTA Standing Committee and the EEA Joint Committee were notified of developments regarding the protective measures.

48 On 9 June 2009, the freezing order in the UK was lifted.

49 On 4 October 2009, the TIF published a notice in the Icelandic Legal Gazette calling for claims to be submitted within two months. The Netherlands and UK Governments submitted claims, as did a small number of other depositors, including four institutional investors. Later the TIF wrote to all institutional investors to inform them that it was beginning to pay compensation under Act No 98/1999, and seeking an assignment of any claim against the banks themselves.

50 On 23 October 2009, the final deadline for payments expired.

51 In the autumn of 2009, controls on capital inflows in Iceland were removed. Other capital controls remained in place. Meanwhile, a strategy for gradual capital account liberalisation was introduced. These controls were in force when the facts relevant to these proceedings took place.

52 On 30 October 2009, 16 June 2010, and 1 July 2010, the EFTA Standing Committee and the EEA Joint Committee were further notified of amendments to the protective measures. None of these notifications resulted in any criticism from the committees.

53 In March 2010, the District Court of Amsterdam lifted the restrictions on the Netherlands branch of Landsbanki.

54 On 14 December 2011, in Case E-3/11 *Sigmarsson* [2011] EFTA Ct. Rep. 432, the Court held that "a national measure which prevents inbound transfer into Iceland of Icelandic krónur purchased on the offshore market is compatible with Article 43(2) and (4) of the EEA Agreement in circumstances such as those in the case before the referring court". Paragraph 50 of that judgment states that "[t]he substantive conditions laid down in Article 43(2) and (4) EEA call for a complex assessment of various macroeconomic factors. EFTA States must therefore enjoy

a wide margin of discretion, both in determining whether the conditions are fulfilled, and the choice of measures taken, as those measures in many cases concern fundamental choices of economic policy."

III Pre-litigation procedure and procedure before the Court

55 On 26 May 2010, ESA issued a letter of formal notice to Iceland alleging a failure to ensure that Icesave depositors in the Netherlands and the United Kingdom received payment of the minimum amount of compensation provided for in Article 7(1) of the Directive, as amended, within the time limits laid down in Article 10 of the Directive, in breach of the obligations resulting from the Directive and/or Article 4 EEA.

56 Iceland was requested to submit its observations within two months of the receipt of that letter. At the request of the Icelandic Government, ESA granted extensions to that deadline, first until 8 September 2010, then until 7 December 2010 and finally until 2 May 2011.

57 On 2 May 2011, the Icelandic Government replied to the letter of formal notice. In its reply, the Icelandic Government maintained that it was not in breach of its obligations under the Directive or Article 4 EEA.

58 On 10 June 2011, unconvinced by Iceland's reply to the letter of formal notice, ESA delivered its reasoned opinion to Iceland.

59 On 30 September 2011, Iceland replied to the reasoned opinion.

60 On 13 December 2011, Iceland submitted an additional letter which contained further information on the winding up of the Landsbanki estate including summaries of recent Icelandic Supreme Court judgments concerning the reordering of the priority of creditors in that winding up.

61 By application lodged at the Court on 15 December 2011, ESA brought an action under the second paragraph of Article 31 of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice (hereinafter "SCA") seeking a declaration that by failing to ensure payment of the minimum amount of compensation to Icesave depositors in the Netherlands and the United Kingdom provided for in Article 7(1) of the Act referred to at point 19a of Annex IX to the Agreement on the European Economic Area within the time limits laid down in Article 10 of the Act, Iceland had failed to comply with the obligations resulting from that Act, in particular its Articles 3, 4, 7 and 10 and/or Article 4 EEA and ordering the defendant to bear the costs of the proceedings.

62 On 3 February 2012, Iceland requested an extension of the period in which to submit its defence. That request was granted by the President on 6 February 2012, setting a time limit for the submission of the defence of 8 March 2012.

63 In its defence, lodged at the Court on 8 March 2012, Iceland contends that the Court should dismiss the application and seeks an order that ESA pay its costs.

64 On 28 March 2012, the European Commission requested leave to intervene in support of ESA.

65 On 10 April 2012, ESA submitted its reply to the defence.

66 On 23 April 2012, following observations submitted by the parties, the European Commission was granted leave to intervene by Order of the President.

67 On 7 May 2012, the Samstaða þjóðar (National Unity Coalition), an association registered in Iceland, sought leave to intervene pursuant to Article 36 of Protocol 5 to the SCA on the Statute of the EFTA Court in support of the form of order sought by Iceland.

68 On 9 May 2012, the Government of the United Kingdom submitted written observations.

69 On 11 May 2012, Iceland submitted its rejoinder. On the same date, the Government of Liechtenstein submitted written observations.

70 On 15 May 2012, the Government of the Netherlands and the Government of Norway submitted written observations. Further, Iceland submitted an urgent request to receive the written observations. This request was granted by the Registrar on 16 May 2012.

71 On 23 May 2012, the European Commission submitted its statement in intervention.

72 On 15 June 2012, the application for leave to intervene by Samstaða þjóðar was dismissed as manifestly inadmissible by Order of the President.

73 On 20 June 2012, Iceland submitted its reply to the statement in intervention by the European Commission.

74 Reference is made to the Report for the Hearing for a fuller account of the facts, the procedure, the pleas and arguments of the parties, which are mentioned or discussed hereinafter only in so far as is necessary for the reasoning of the Court.

IV The action

First plea: Obligation of result

Arguments of the parties and of the intervener

The applicant

75 The applicant's first plea is that, in failing to ensure payment of compensation to Icesave depositors holding deposits in Landsbanki's branches in the UK and the Netherlands within the time limits laid down in the Directive, the defendant has breached its obligations under Articles 3, 4, 7 and 10 of the Directive.

76 ESA submits that the Directive imposes an obligation of result on EEA States to ensure that a deposit-guarantee scheme is set up capable of guaranteeing that, in the event of deposits being unavailable, the aggregate deposits of each depositor are covered in all circumstances to the amount laid down in Article 7(1) of the Directive. Further, the obligation of result requires States to ensure that duly verified claims by depositors are paid within the deadline laid down in Article 10 of the Directive.

77 The applicant contends that Iceland has not fulfilled all its obligations simply by transposing the Directive into national law and setting up and recognising a deposit-guarantee scheme without any regard to whether the compensation of depositors is, in fact, ensured under the conditions prescribed in the Directive.

78 According to ESA, this interpretation of the Directive is in line with the case law of the Court of Justice of the European Union (hereinafter "ECJ"). In ESA's view, it follows from Case C-222/02 *Paul and Others* [2004] ECR I-9425, paragraphs 26, 27 and 30, that the ECJ considers Articles 7 and 10 of the Directive to require a clear and precise result to be achieved.

79 The applicant argues further that it is for the national authorities to determine how to achieve the result aimed at by a directive, in the manner which they deem most appropriate. In the present case, if all else fails, in order to discharge its duties under the Directive, the EEA State itself may be held responsible for the compensation of depositors to the amount provided for in Article 7 of the Directive.

80 In this regard, ESA notes that in the Impact Assessment of 12 July 2010 (see Commission Staff Working Document - Impact Assessment of 12 July 2010, SEC(2010) 834/2; hereinafter "Impact Assessment"), the Commission services set out various means of funding a deposit-guarantee fund, including ex ante contributions, ex post contributions, State loans and direct state interventions. However, the Directive itself does not specify how deposit-guarantee funds should be financed.

81 Moreover, ESA argues that exceptional circumstances, such as a financial crisis of the magnitude experienced in Iceland, cannot alter the obligation to

compensate depositors in accordance with Article 7(1) of the Directive. By contrast, Article 10(2) of the Directive expressly mentions "exceptional circumstances" as allowing for certain extensions of the deadline for payment of compensation. Thus, in ESA's view, the effect of "exceptional circumstances" is limited to justifying certain payment delays.

82 ESA submits further that the TIF is an emanation of the Icelandic State within the meaning of the EEA Agreement and, consequently, any default of that institution is directly attributable to the State both in law and in fact.

83 In the applicant's view, the doctrine of *force majeure* does not apply in the present case and, in any event, does not release Iceland from its obligations under the Directive.

84 The applicant accepts that a State injection of capital to refinance a deposit-guarantee scheme may constitute State aid within the meaning of Article 61 EEA. In its view, however, this would appear to be compatible with the State aid rules. The applicant observes further that the Icelandic authorities never approached it to discuss the compatibility of any form of State intervention in this case. Furthermore, it contends that the State aid rules did not constrain the defendant from transferring national deposits to New Landsbanki.

The intervener

85 The Commission emphasises that the Directive is binding upon the EEA States and not on bodies that are created by the Member States in order to comply with their obligations under the directives concerned.

86 In this case, the Directive imposes obligations of result on the EEA States on the basis of the wording of Articles 3, 4, 7 and 10 of the Directive.

87 The intervener asserts that, following the introduction of a scheme, obligations of result include the obligation to ensure that the deposit-guarantee scheme is capable of ensuring the repayment of the covered deposits. In the event of a bank collapse, depositors are covered to a maximum of EUR 20 000. In the view of the intervener, if a deposit-guarantee scheme does not have sufficient funding, the Member State concerned must be regarded as having infringed the Directive.

88 In its view, any other interpretation would render the provision ineffective to ensure the objective of the Directive, that is, to provide a guarantee to depositors when deposits become unavailable, as depositors would not be able to rely on deposit-guarantee schemes. Such an interpretation would also fail to achieve the purpose of ensuring last resort protection.

89 The intervener shares the applicant's assessment, namely, that this interpretation is in line with the case law of the ECJ. In the intervener's view, an obligation of result can be clearly inferred from *Paul and Others* (cited above).

90 The intervener emphasises that EEA States are free to decide how deposit-guarantee schemes are funded in order to pay compensation in accordance with the Directive. In its view, a State could determine, for example, that the remaining banks, as well as newly created banks, be required to contribute to the refinancing of the scheme to the extent necessary for ensuring the repayment of depositors, or that the schemes take out long-term loans at market rates.

91 Such options would reflect the objective expressed in recital 23 in the preamble to the Directive, namely, that the costs of the schemes must, in principle, be borne by credit institutions.

92 According to the intervener, the possibility cannot be excluded, however, that an EEA State has no other choice than to resort to State funding. It reiterates that this is a matter which is within the discretion of the EEA State itself.

93 The intervener asserts that no provision of the Directive allows EEA States to disregard its rules in exceptional circumstances, such as a financial crisis. In its view, the Directive was devised precisely to deal with the exceptional occurrence of a bank failure, including circumstances in which supervision has not proved sufficient to save a bank. The European legislature did not include any additional derogation over and above what is provided for in Article 10(2) of the Directive.

94 Moreover, the intervener considers that, also on the basis of case law, the defendant's *force majeure* plea must be rejected.

95 Finally, the Commission submits that the present case concerns the obligation of an EEA State under the Directive to ensure the compensation prescribed by the Directive. Any State liability vis-à-vis individual depositors for not having ensured the compensation prescribed by the Directive is a different issue. Such liability would have to be established by a national court.

The defendant

96 The defendant submits that the Directive imposes no obligation of result on an EEA State to use its own resources in order to guarantee the pay-out of a deposit-guarantee scheme in the event that "all else fails". The obligations incumbent upon the State are limited to ensuring the proper establishment, recognition and a certain supervision of a deposit-guarantee scheme.

97 Moreover, the defendant argues that no provision of the Directive suggests that any form of State guarantee or State funding is required under the Directive, in particular where a guarantee scheme is unable to pay compensation. It places an obligation upon the State to set up and to supervise a deposit-guarantee scheme, but there is no suggestion whatsoever that it must pay compensation.

98 Recitals 4, 23 and 25 in the preamble to the Directive make clear that the funding for deposit-guarantee schemes will come from the banks. However, the

applicant's case converts the Directive from a measure funded by the banks into a measure that imposes huge potential liabilities on the State.

99 Article 7(6) of the Directive is the only operative provision that deals with the scenario that a deposit-guarantee scheme might be unable to pay duly qualified claims. However, the solution contemplated by this provision in the case of non-payment is an action against the scheme and not the EEA State.

100 The sole purpose of recital 24 in the preamble to the Directive is to exclude State liability if the compensation of depositors is ensured, as confirmed by the ECJ's judgment in *Paul and Others* and in particular by the German version of said recital.

101 With regard to the applicant's claim that it is undisputed between the parties that the TIF could not cope with the almost total failure of Iceland's banks, in the defendant's view, this does not show any failure on its part to implement the Directive properly. It contends – and claims to find particular support for its argument in the Impact Assessment – that no deposit-guarantee scheme could have coped with such a wide-scale banking failure.

102 The defendant submits that, if the obligation of result imposed by the Directive were that the State must ensure the payment of compensation, in whatever circumstances, then, if all else fails, the State would have to step in. That would be the case no matter how many hypothetical choices a State has. The logic of the applicant's argument – so the defendant contends – is that the State is left with no choice at all whether to use its resources to fund a deposit-guarantee scheme – at least where all else fails.

103 The defendant contends that any attempt to underwrite a deposit-guarantee scheme using the resources of the State creates its own problems. These include huge costs for the State, moral hazard on the part of the banks, and a linkage between the liabilities of the banks and the financial exposure of the State. That kind of link can have very serious consequences. A severe financial crisis easily turns to a possible sovereign default.

104 In the defendant's view, where widespread banking failure takes place, other policy tools are required. In that regard, it notes that the Commission is considering a package of reforms to banking supervision in Europe that aims to strengthen the measures available. State aid rules, in particular, would allow the applicant to ensure that any injection of State funds into the banking system is no more extensive than it needs to be, and that the single market is not detrimentally affected.

105 The defendant observes that the interpretation of the Directive advanced by the applicant is based on the goal of consumer protection. However, in its view, consumer protection measures must always strike a balance between costs and benefits. For this very reason, EEA law aims at a high level of consumer protection, but not the highest possible. If the applicant's approach were to

prevail, this could create serious risks and burdens for the EEA States, beyond their contemplation when the Directive was adopted. Ultimately, that could be to the detriment of consumers themselves.

106 The defendant contends that whether or not the TIF is an emanation of the State is of no relevance for the present case.

107 The defendant infers from the Impact Assessment that an injection of State resources into the banking system of the kind at issue in the present case amounts to State aid. Consequently, were an EEA State under an obligation to make payments of that kind as an automatic result of the Directive if "all else fails", the State guarantee would fall outside the scope of State aid supervision.

108 In this connection, the defendant notes that the Commission in its proposal for the original Directive and its 2010 Impact Assessment recognised that public sector funding would be subject to State aid rules and that there would be no obligation to provide such. Moreover, it contends that there is obviously scope for serious distortions of competition if a State bails out a deposit-guarantee scheme – in effect subsidising its banks. In its view, State aid rules are there to ensure that this kind of activity is regulated by the applicant.

109 In the alternative, the defendant submits that, even if the Directive were to impose strict obligations upon the State to fund the guarantee scheme in the event of its collapse, it was prevented from doing so by *force majeure*.

Other participants submitting written observations

Liechtenstein

110 Liechtenstein interprets the wording of the proposal for a Council Directive on deposit-guarantee schemes to indicate that the Directive was intended to deal with the failure of individual banks; not with the collapse of an entire banking system. Liechtenstein contends that it was not envisaged that a general and automatic State responsibility covering the costs of the failure of the whole banking system would arise from the Directive.

The Netherlands

111 The Netherlands argues that the obligation to comply with the result sought by the Directive follows both from the general obligations under EEA law and the obligation of the State in relation to a directive. The Netherlands considers that the defence of *force majeure* is not available to Iceland as it can only rely on derogations provided by the Directive itself. But even if the Directive were to allow for a *force majeure* defence, in the view of the Netherlands, Iceland cannot rely on such as it failed to notify ESA of its difficulties and did not suggest appropriate solutions. Furthermore, the Netherlands argues that financial difficulties cannot be accepted as justification under EEA law, as to allow

financial difficulties as a defence would unjustly weaken the effectiveness of the Directive.

112 In the view of the Netherlands, Iceland failed in any event to prove a *force majeure* defence on the merits as it submitted evidence which is largely general in nature and based on assertion rather than proof. Moreover, Iceland also failed to prove that there was an "absolute impossibility" of establishing any form of deposit-guarantee scheme that would have been capable of ensuring the result sought by the Directive.

Norway

113 Norway argues that a general and automatic State responsibility for compensation of depositors as a last resort would impose an extensive financial burden on EEA States. Without a clear and precise wording in the Directive, the existence of such an obligation cannot be assumed. An obligation of such kind on the part of the EEA States does not follow from the preamble to the Directive or the preparatory works. Moreover, recital 24 in the preamble to the Directive appears to exclude automatic State responsibility.

The United Kingdom

114 The United Kingdom interprets the Directive as imposing an obligation on EEA States to ensure that the relevant deposit-guarantee schemes should pay a prescribed compensation to each eligible investor within the applicable time limit in the event of unavailability of deposits within the meaning of the Directive.

115 The United Kingdom asserts that arguments related to *force majeure* should be dismissed as an EEA State may only rely on derogations provided in the Directive itself. Were *force majeure* available as a defence, the defendant would have to inform the applicant of its difficulties and suggest appropriate solutions.

116 The United Kingdom also argues that the defendant failed to prove its defence on the merits in that it failed to show that it would have been absolutely impossible for it to establish any form of deposit-guarantee scheme under the Directive. The United Kingdom submits further that the evidence offered by the defendant in support of its case was largely general in nature and based on assertions rather than evidence.

Findings of the Court

Introductory remarks

117 For the purposes of the first plea, it has to be assessed whether in a systemic crisis of the magnitude experienced in Iceland the Directive itself envisages that the defendant should have ensured payment to depositors in the Icesave branches in the Netherlands and the United Kingdom in accordance with Articles 3, 4, 7 and 10 of the Directive. Moreover, it must also be assessed whether the defendant has infringed the alleged obligation of result.

118 The Court recalls at the outset that a failure to fulfil obligations can be found only if there is, upon expiry of the period laid down in the reasoned opinion, a situation contrary to EEA law which is objectively attributable to the EEA State concerned (see, for example, Case E-8/11 *ESA* v *Iceland* [2011] EFTA Ct. Rep. 467, paragraph 34).

119 Consequently, the nature of the result to be achieved is determined by the substantive provisions of the individual directive in question.

120 As the first plea concerns the question whether the alleged obligation of result follows directly from the Directive, it must be kept in mind that, as set out in Article 7 EEA, one of the principal characteristics of directives is precisely that they are intended to achieve a specific result whilst leaving it to the EEA States and their national authorities how to achieve this objective. In any case, there is a general obligation on the EEA States to ensure that the provisions of a directive are fully effective.

121 European legislative practice shows that there may be great differences in the types of obligations which directives impose upon EEA States and therefore in the results which must be achieved. Some directives require legislative measures to be adopted at national level and compliance with those measures to be the subject of judicial or administrative review. Other directives lay down that the EEA States are to take the necessary measures to ensure that certain objectives formulated in general and unquantifiable terms are attained, whilst leaving them some discretion as to the nature of the measures to be taken. Yet other directives require the EEA States to obtain very precise and specific results after a certain period (compare Case C-60/01 *Commission* v *France* [2002] ECR I-5679, paragraphs 26 to 28, and case law and examples cited).

122 It is recalled in this respect that, pursuant to Article 1 of Protocol 1 to the EEA Agreement, preambles of the acts referred to in the Annexes are not adapted for the purposes of the Agreement. They are relevant to the extent necessary for the proper interpretation and application, within the framework of the EEA Agreement, of the provisions contained in such acts (see, for example, Case E-14/11 *DB Schenker* v *ESA*, judgment of 21 December 2012, not yet reported, paragraph 125).

123 Moreover, it should be added that the question whether an EEA State is obliged to provide for compensation for loss and damage caused to individuals as a result of breaches of obligations under the EEA Agreement for which that State can be held responsible (see, for example, Case E-9/97 *Sveinbjörnsdóttir* [1998] EFTA Ct. Rep. 95, paragraphs 62 and 63, and Case E-2/12 *HOB-vín III*, judgment of 11 December 2012, not yet reported, paragraph 117 et seq.) lies outside the scope of the present proceedings.

The Directive

124 At the outset, the Court notes that as a result of the crisis, the regulatory framework of the financial system has been subject to revision and amendment in order to enhance financial stability. As regards the Directive, those amendments dealt, *inter alia*, with the improvement of depositor protection and the maintenance of depositors' confidence in the financial safety net (see Directive 2009/14/EC of the European Parliament and of the Council of 11 March 2009 amending Directive 94/19/EC on deposit-guarantee schemes as regards the coverage level and the pay-out delay, OJ 2009 L 68, p. 3). However, the judgment in the present case must be based on the Directive as it stood at the relevant time. Then, it did not encompass those amendments and the improved protection of depositors. Those revisions are not yet part of the EEA Agreement.

125 The aim pursued by the Directive is, on the one hand, the freedom of establishment and freedom to provide services in the banking sector, and the stability of the banking system and protection for savers, on the other (compare the Opinion of Advocate General Léger in Case C-233/94 *Germany* v *Parliament and Council* [1997] ECR I-2405, point 35).

126 This dual objective is expressed in the first recital of the Directive which states that the harmonious development of the activities of credit institutions throughout the Community should be promoted through the elimination of all restrictions on the right of establishment and the freedom to provide services, while increasing the stability of the banking system and protection for savers. In this regard, the effect of the machinery established by the Directive is to prevent the EEA States from invoking depositor protection in order to impede the activities of credit institutions authorised in other EEA States (see, for comparison, *Germany* v *Parliament and Council*, cited above, paragraph 19).

127 In this regard, it must be recalled that recent European regulatory policies in the relevant field are based on the principles of mutual recognition and a "single passport" mechanism which allows financial services operators lawfully established in one EEA State to establish and/or provide their services in other EEA States without further authorisation requirements (see, for example, recitals 6 and 7 in the preamble to the Directive).

128 In light of the express reference made to the system of single authorisation, the Directive has to be considered as constituting one piece of a regulatory framework for banks and other financial institutions (see, *mutatis mutandis*, Case E-17/11 *Aresbank*, judgment of 22 November 2012, not yet reported, paragraphs 86 to 95).

129 Soundly regulated and safe financial institutions are of decisive importance for financial stability in the EEA. Therefore, the European strategy aims at establishing a common regulatory framework ensuring prudential oversight and consumer protection throughout the European internal market.

130 It follows from Article 3(1) of the Directive that an EEA State is under an obligation to ensure that within its territory one or more deposit-guarantee schemes are introduced and officially recognised.

131 The system introduced by Article 3(1) of the Directive is not one of absolute constraint. It leaves the EEA States free to introduce and recognise several deposit-guarantee schemes within their territory, thereby allowing the credit institutions to choose the model that will best suit them. The Commission's proposal for the Directive expressly states that "[a]fter receiving the assurance that the financing arrangements were sufficiently sound to pay off all depositors covered, including those at branches in another Member State, it was not considered necessary to harmonize rules which are closely linked with the management of the schemes in question" (Commission proposal for a Council Directive on deposit-guarantee schemes, COM(92) 188 final, p. 8).

132 Pursuant to Article 3(2) to (5) of the Directive, the competent national authorities that have issued authorisations to credit institutions are – in cooperation with the deposit-guarantee scheme – obliged to ensure that the credit institutions comply with their obligations as members of a scheme. Where appropriate, under the conditions specified in Article 3(5) of the Directive, they must adopt a decision revoking the authorisation of the institution in question.

133 As the ECJ held in *Paul and Others*, the purpose of those provisions is to guarantee to depositors that the credit institution in which they make their deposits belongs to a deposit-guarantee scheme and fulfils its obligations. This shall ensure protection of their right to compensation in the event that their deposits are unavailable, in accordance with the rules laid down in the Directive and more specifically in Article 7 thereof. However, Article 3(2) to (5) of the Directive relate only to the introduction and proper functioning of the deposit-guarantee scheme as provided for by the Directive (*Paul and Others*, cited above, paragraphs 28 to 29).

134 The Directive does not exhaustively regulate the unavailability of deposits under EEA law, but simply requires EEA States to provide for a harmonised minimum level of deposit protection (compare the Opinion of Advocate General Stix-Hackl in *Paul and Others*, cited above, point 117). It is therefore clear that national authorities have considerable discretion in how they organise the schemes.

135 In view of the above, pursuant to Article 3 of the Directive, EEA States have to introduce and officially recognise a deposit-guarantee scheme. Moreover, they have to fulfil certain supervisory tasks in order to ensure the proper functioning of the deposit-guarantee scheme. However, it is not envisaged in that provision that EEA States have to ensure the payment of aggregate deposits in all circumstances.

136 Article 7(1) of the Directive specifies the minimum coverage for aggregate deposits that must be provided in the event of deposits being unavailable

(compare *Paul and Others*, cited above, paragraph 27). It provides for minimum harmonisation as regards the level of coverage for individual deposits.

137 It follows from the words "[d]eposit-guarantee schemes shall stipulate..." that an obligation is imposed on EEA States to ensure that national rules are adopted or maintained which require a coverage level of at least EUR 20 000.

138 With the adoption of Directive 2009/14, the wording of Article 7(1) of the Directive has been replaced. The new version states that "Member States shall ensure that the coverage for the aggregate deposits of each depositor shall be at least EUR 50 000 in the event of deposits being unavailable". Moreover, a new paragraph 1(a) has been introduced in Article 7 which lays down that Member States shall ensure by 31 December 2010 that the coverage for the aggregate deposits of each depositor shall be set at EUR 100 000 in the event of deposits being unavailable.

139 It appears that under the new version of the provision EEA States are obliged to ensure a certain level of coverage. Whether this obligation is limited to a banking crisis of a certain size would require further assessment. However, that question can be left open here since, as mentioned above (see paragraph 124), Directive 2009/14 is not applicable in the present case.

140 At any rate, the rewording of Article 7 of the Directive shows that the European legislature considered substantial change necessary to extend the responsibility of the EEA States beyond the establishment of an effective framework.

141 This supports the view that the obligation on the EEA States under the version of the provision applicable in the case at hand is limited to ensuring that national rules which require a coverage level of at least EUR 20 000 are maintained or adopted.

142 Pursuant to Article 7(6) of the Directive, EEA States have to ensure that the depositor's right to compensation may be the subject of an action by the depositor against the guarantee schemes. The scope of this provision encompasses the scenario that a deposit-guarantee scheme might be unable to pay duly qualified claims.

143 However, the obligation on the EEA States is limited to the maintenance or adoption of rules that provide for an effective right to file an action against the guarantee scheme particularly in the case of non-payment (compare *Paul and Others*, cited above, paragraph 27).

144 Consequently, it must be held that Article 7 of the Directive does not lay down an obligation on the State and its authorities to ensure compensation if a deposit-guarantee scheme is unable to cope with its obligations in the event of a systemic crisis.

145 Article 10 of the Directive establishes time limits for the payments of guarantee schemes to depositors. This follows from the exceptions provided for in Article 10(3) and (5) which refer expressly to “the time limit laid down in paragraphs (1) and (2)”.

146 However, the mandatory language of the English version of Article 10(1) of the Directive, i.e. “[d]eposit-guarantee schemes shall be in a position to pay ... within three months of the date on which the competent authorities ...”, establishes merely a procedural obligation, as it refers only to the binding nature of the three-month period prescribed therein.

147 The importance of timely payments by the guarantee scheme is further emphasised in Article 10(2) of the Directive. Under this provision, a guarantee scheme may apply to the competent authorities for an extension of the time limit set out in Article 10(1) of the Directive only in wholly “exceptional circumstances” and in “special cases”. The Directive does not contain a definition of those terms.

148 Accordingly, pursuant to Article 10(2) of the Directive, EEA States and their competent authorities are under an obligation to supervise and ensure that deposit-guarantee schemes are, as a rule, not released from the short deadline established in Article 10(1) of the Directive, which forms the general rule. However, an obligation on the State and its national authorities to ensure compensation if a deposit-guarantee scheme is unable to cope with its obligations under exceptional circumstances such as in a systemic crisis cannot be derived from that provision.

149 In view of the above, the Court finds that the obligation on EEA States under Article 10 of the Directive is limited to provide for a mandatory and effective procedural framework with respect to time limits.

150 Furthermore, reference should be had to Articles 1(3) and 9(3) and recitals 3, 10 and 25 in the preamble to the Directive. However, these provisions show that the Directive deals – at least primarily – with a failure of individual banks and not with a systemic crisis.

151 Even as regards the important objective to avoid bank runs, the wording of recital 4 in the preamble to the Directive is limited to a failure of a single credit institution that may lead to massive withdrawals also from healthy institutions.

152 It must be noted in this respect that in the 2010 Impact Assessment the Commission services stated in relation to a possible harmonised approach to a target level for deposit-guarantee funds that the “choice of a target level for the funds may be related to the capability of deposit-guarantee schemes to handle a bank failure of a specific size based on bank recapitalisation by Member States during the financial crisis…” (Impact Assessment, section 7.8, p. 53). The biggest failure envisaged by the Commission’s services is a failure of a large member bank accounting for 7.25% of eligible deposits.

153 Not even this Impact Assessment, made in the light of the financial crisis of 2007/2008 which included the failure of the Icelandic banks, contemplated the extension of the funding of deposit-guarantee schemes to cover a systemic bank failure of the magnitude experienced in Iceland. The Impact Assessment concluded: "Setting a target level for DGS [sc. deposit-guarantee scheme] funds would ensure that schemes are credible and capable to deal with medium sized bank failures. The most cost-efficient target level would be 1.96% (or simply 2%) of eligible deposits (to be achieved within 10 years) because it would increase DGS funds to cope with a medium-sized bank failure; and despite quite substantial increase in contributions, it would, on average, only moderately affect bank profits at EU level (with a stronger impact in some Member States) and lead to very limited costs for depositors. ... It would ensure a sound financing of the DGS but avoid unwanted side-effects if contributions were too high." (Impact Assessment, section 7.8, p. 58)

154 Moreover, the mechanism and level of funding of the schemes have not been harmonised. The Directive does not contain any substantive provision that deals with those organisational matters.

155 Recital 23 in the preamble states that it is not indispensable, in the Directive, to harmonise the methods of financing schemes guaranteeing deposits or credit institutions themselves. According to the same recital, this follows from the fact, *inter alia*, that the financing capacity of such schemes must be in proportion to its liabilities. The Directive contains no definition of what is considered to be proportionate funding.

156 It is clear from recital 23 in the preamble to the Directive as well as from recitals 4 and 25 that the cost of financing such guarantee schemes must be borne, in principle, by credit institutions and not the EEA States.

157 Recital 23 in the preamble to the Directive aims to strike a balance between the cost of funding a deposit-guarantee scheme, the stability of the national banking system and consumer protection. The objective is that the banking system should function in the interests of consumers and the economy as a whole.

158 However, the provision of private funding to enable the guarantee scheme to cover deposits in a systemic crisis up to the maximum coverage level would clearly undermine the objective laid down in recital 23, that is, not to jeopardise the stability of the banking system itself. Accordingly, the cost of the guarantee schemes must not be too onerous for the member credit institutions.

159 The payment obligation thus lies with the deposit-guarantee fund, and the guarantee funds are to be financed entirely by the credit institutions. In circumstances where the fund cannot meet depositors' claims in the event of a default by a member of the scheme, it is for the remaining credit institutions to make up the difference. In other words, the bankruptcy of a financial institution is covered – as in classic insurance systems – by the rest of the institutions active in the market.

160 How to proceed in a case where the guarantee scheme is unable to cope with its payment obligations remains largely unanswered by the Directive. The only operative provision that deals with non-payment is Article 7(6) of the Directive, according to which depositors must have the possibility to bring an action against the relevant scheme. However, an obligation on the State or a possible action against the State in those circumstances is not envisaged in the Directive's provisions.

161 This does not mean that depositors will necessarily remain unprotected in such a case. Depositors may fall within the remit of other parts of the safety net. They may benefit from other provisions of EEA law regarding financial services, as well as the activities of supervisors, central banks, and governments. However, the question in the present case is whether EEA States are legally responsible under the Directive in case of such an enormous event.

162 Reference should be had to the second subparagraph of Article 3(1) of the Directive. Pursuant to that rule, a credit institution may be exempted by an EEA State from its obligation to be a member of a deposit-guarantee scheme where it belongs to a system that ensures, in particular, its liquidity and solvency and it is thereby guaranteed that depositors receive protection at least equivalent to that provided by the guarantee scheme.

163 That possibility to exempt a credit institution from the obligation to belong to a deposit-guarantee scheme requires, in addition, that the alternative system fulfils certain conditions. The third of these requires the system not "to consist of a guarantee granted to a credit institution by a Member State itself or by any of its local or regional authorities". The aim of this provision is to minimise the potential to distort competition, inherent in the very nature of guarantees of that kind.

164 Were an EEA State legally obliged to ensure the compensation of depositors where a recognised deposit-guarantee scheme is unable to cope with its payment obligations, the negative effect on competition would be comparable. Consequently, it is likely that, had the European legislature sought to adopt a different approach as regards the funding of deposit-guarantee schemes, this would have been expressly stated in the Directive.

165 It is recalled in this regard that the Commission's 1992 proposal for the Directive recognised that any public sector funding would be subject to State aid rules and, moreover, that there would be no obligation to provide such. The proposal states in this respect: "The question of whether the public sector would be able to provide assistance for guarantee schemes in emergency situations of exceptional gravity and when the schemes' resources have been exhausted has been raised in order to enable them to respect their commitments to depositors. It did not seem appropriate, in the proposal for a Directive, to prohibit such assistance, which could prove necessary in practice, although it is not desirable as a general rule and could not be allowed to contravene the rules of the Treaty concerning State

aid.” (Commission proposal for a Council Directive on deposit-guarantee schemes, COM(92) 188 final, p. 8)

166 Moreover, in its 2010 Impact Assessment, the Commission noted: “DGS [sc. deposit-guarantee schemes] are financed by banks and the Commission intends to maintain this requirement. That means that the budget of Member States is not directly concerned by the DGS Directive. The recent crisis has shown that in a systemic crisis, DGS may reach their limits. However, even if in such cases governments stepped in under strict obedience of state aid rules, this would not be triggered under a legal obligation in the DGS Directive and ‘viability for Member States’ is therefore not subject of this impact assessment.” (Impact Assessment, section 3.2, pp. 8-9.)

167 An additional aspect to which regard must be had is mentioned in recital 16 in the preamble to the Directive. There, the European legislature states that it would not be appropriate to impose a level of protection “which might in certain cases have the effect of encouraging the unsound management of credit institutions”. This points to the concept of moral hazard. In economic literature the lesson of moral hazard has been described with the words that “less is more”. Professor Joseph E. Stiglitz has formulated in this respect: “[T]he more and better insurance that is provided against some contingency, the less incentive individuals have to avoid the insured event, because the less they bear the full consequences of their actions”. (“Risk, Incentives and Insurance: The Pure Theory of Moral Hazard”, *The Geneva Papers on Risk and Insurance*, 8 (No 26, January 1983), 4, at p. 6.)

168 It is recalled that, in a crisis of a magnitude such as the one experienced in Iceland, an EEA State would have very limited options to ensure compensation to depositors that is, first, it could provide a State guarantee for a loan taken out by the scheme itself, or, second, it could directly fund the scheme or its depositors. Thus, moral hazard would also occur in the case of State funding, serving to immunise a deposit-guarantee scheme from the costs which have, in principle, to be borne by its members.

169 The alleged obligation of result would further run counter to the aims mentioned in recitals 2 and 3 in the preamble to the Directive, according to which consumer protection is to be achieved by means of the introduction of a minimum level of deposit protection and the guarantee that foreign and domestic deposits are protected by the same guarantee scheme irrespective of where a credit institution has its head office.

170 Accordingly, consumer protection under the Directive does not entail full protection (compare, as regards the coverage level, *Germany* v *Parliament and Council*, cited above, paragraph 48), since increasing consumer protection may reach a point where the costs outweigh the benefits.

171 Finally, the question arises whether recital 24 in the preamble to the Directive can be said to support the alleged obligation of result. That recital states that the

liability of EEA States and their competent authorities is excluded if they ensure the compensation or protection of depositors under the conditions prescribed in the Directive. The Court notes that this recital may be necessary to allow for a proper delineation of the scope of the principle of State liability.

172 As the applicant set out in its argument, recital 24 in the preamble to the Directive states that liability of a State and its competent authorities in respect of depositors is precluded "if they have ensured that one or more schemes guaranteeing deposits or credit institutions themselves and ensuring the compensation or protection of depositors under the conditions prescribed in this Directive have been introduced and officially recognized."

173 However, "the conditions prescribed in this Directive" are not further defined. As has been stated above, the funding obligation imposed on the members of a guarantee scheme is limited under the Directive and must not be too onerous in order not to jeopardize the stability of the banking system.

174 The result to be achieved by the EEA States themselves follows from their above mentioned general obligation, that is, to ensure that the provisions of the Directive are fully effective, i.e. that the specific obligations are given practical effect.

175 However, in light of the present assessment of the Directive, the result to be achieved is limited, particularly having regard to the fact that the Directive aims at minimum harmonisation in relation to the level of coverage and does not provide for any harmonisation as regards the level and mechanisms of funding.

176 Accordingly, the reservation set out in recital 24 in the preamble to the Directive aims expressly to preclude an excessive shifting to the State of the costs arising from a major banking failure. (See, by way of illustration, Michel Tison, "Do not attack the watchdog! Banking supervisor's liability after *Peter Paul*", Working Paper Series, Financial Law Institute, Universiteit Gent 2005, p. 25, including footnote 81).

177 Consequently, recital 24 in the preamble to the Directive does not support the existence of the alleged obligation of result.

178 In view of the above, the Court holds that the Directive does not envisage that the defendant itself must ensure payments to depositors in the Icesave branches in the Netherlands and the United Kingdom, in accordance with Articles 7 and 10 of the Directive, in a systemic crisis of the magnitude experienced in Iceland.

179 In any event, as the defendant correctly argued, the alleged obligation of result also cannot be derived from the ECJ's ruling in *Paul and Others*. The case at hand must be distinguished from that earlier case on the facts. *Paul and Others* dealt mainly with the alleged liability of the German authorities resulting from negligence in the conduct of banking supervision, and the question whether the supervisory obligation imposed on national authorities under Article 3(2) to (5)

of the Directive precluded a limitation of State liability under national law in relation to such supervision. Furthermore, in *Paul and Others*, the national court had already held the State concerned to be liable under the principle of State liability to the amount provided for in Article 7(1) of the Directive.

180 Finally, a comparison with other secondary law also does not confirm the existence of the alleged obligation of result. It is recalled in this regard that the content of the result to be achieved is determined by the substantive provisions of the individual directive. In any event, the ECJ's ruling in *Blödel-Pawlik* (Case C-134/11, judgment of 16 February 2012, not yet reported) does not support the applicant's plea. This case concerned the obligations of a travel organiser and its insurer. According to the ECJ, the obligation of result imposed on the State by Directive 90/314 was to ensure that a travel organiser is liable to the consumer for proper performance of the contract. However, the ECJ did not hold that there is an obligation on the State itself to pay compensation if a travel organiser is unable to meet its obligations.

Emanation of the State

181 The applicant and the intervener have argued that the TIF, a private foundation under Icelandic law, is an emanation of the State.

182 However, the case at hand concerns whether there is an obligation of result placed upon the State under the Directive, in the manner described in ESA's application.

183 Hence, the question is of no significance for the assessment of the first plea.

184 For the sake of good order, the Court simply adds that, in any event, the applicant has adduced insufficient evidence to support its claim that the TIF is directly or indirectly operated by public authorities, i.e. under the control of the Icelandic State (see, for comparison, Case C-356/05 *Farrell* [2007] ECR I-3067, paragraph 41).

Conclusion

185 In light of all of the above, the first plea is dismissed.

Second and third pleas: Discrimination contrary to the Directive and/or Article 4 EEA

Arguments of the parties

The applicant and the intervener

186 The applicant and the intervener submit that, even if, contrary to their argument, the provisions of Directive 94/19 are interpreted as not imposing an obligation of result, the defendant is in breach of Articles 4(1) and 7(1) of the Directive and/or Article 4 EEA by having failed to ensure compensation to Icesave depositors in

the Netherlands and the United Kingdom as set out in the Directive. In their view, the depositors in Iceland received full protection whereas the depositors in the Netherlands and the United Kingdom were left without any or any comparable protection.

187 The applicant and the intervener contend that the Icesave customers in branches in Iceland and their counterparts in branches in other EEA States were, in their capacity as deposit holders in Icelandic banks, in a comparable situation as regards the protection granted to them by the Directive under Article 4 thereof read in light of recital 3 in the preamble to the Directive.

188 The applicant and the intervener state that, when adopting emergency measures in response to the banking crisis in October 2008, the Icelandic Government made a distinction between domestic deposits and deposits in foreign branches. The domestic deposits were moved to new banks and were covered in full. Meanwhile, foreign depositors did not even enjoy the minimum guarantee laid down in the Directive.

189 Thus, in the view of the applicant and the intervener, the defendant has indirectly discriminated against foreign depositors on the basis of nationality, which is prohibited by the Directive read in the light of Article 4 EEA or by Article 4 EEA itself.

190 In addition, the applicant specifies that the present case does not concern whether the defendant was in breach of the prohibition on discrimination for not moving over the entirety of deposits of foreign Icesave depositors into New Landsbanki, as it did for domestic Landsbanki depositors. The breach is said to lie in the failure of the Icelandic Government to ensure that Icesave depositors in the Netherlands and the United Kingdom received payment of the minimum amount of compensation provided for in the Directive within the time limits prescribed, something it did for domestic depositors. The applicant adds that compensation of domestic and foreign depositors above and beyond that minimum amount has not been and is not at issue in the context of the present proceedings.

191 Moreover, the applicant and the intervener submit that the defendant cannot advance any viable justification for the discriminatory measures taken against the foreign deposits in the circumstances of the case.

The defendant

192 The defendant argues that the discrimination pleas are entirely misconceived and highly contrived. It observes that the applicant seeks a declaration that, in failing to ensure payment of the EUR 20 000 per depositor required under the Directive, the defendant breached EEA law. However, in the defendant’s view, this obligation cannot be derived from the principle of non-discrimination.

193 In the defendant’s view, the second plea is plainly unsustainable since it would create an obligation upon an EEA State to ensure minimum compensation under

the Directive in circumstances in which the partially harmonised regime created by the Directive does not require such.

194 In the circumstances of a bank failure, the defendant submits, it is legitimate for EEA States to intervene to rescue banks, or branches which are necessary to the functioning of the banking system, but there is no obligation to do so.

195 In the defendant's view, what is regarded as discrimination in the present case are in reality the different consequences that have flowed as a result of the fact that the domestic branches of Landsbanki were essential to the rescue of the Icelandic financial system. Although the Directive is a consumer protection measure, it does not address in any way the regulation of bank insolvency and restructuring – they are entirely beyond its scope.

196 Moreover, as regards a breach of Article 4 EEA alone, the third plea, the defendant submits that such a claim has not been made out. The applicant has simply asserted that Article 4 EEA is applicable without seeking to demonstrate that the legal conditions for its application are satisfied.

197 The defendant contends further that, in claiming that it was discriminatory not to provide the minimum compensation afforded by the Directive to the overseas depositors given that the domestic depositors were "covered" by virtue of a transfer of their deposits to the new banks, the applicant is arguing, in effect, for different treatment. Such a line of argument as a basis for a discrimination claim is, in the defendant's view, incoherent.

198 On the other hand, the defendant notes that it is not part of the applicant's case that the transfer of domestic deposits effected as part of the bank restructuring should have been extended to overseas depositors. The applicant has never questioned the fact that it was not possible to extend this rescue to the overseas branches. Thus, in the defendant's view, the applicant does not argue that the two groups should have been treated equally.

199 In any event, the defendant submits, it is unclear whether the transfer of domestic deposits to the new bank led to a better position of the depositors holding such accounts. These account holders were subject to strict capital controls, and were unable to convert their (severely depreciating) Icelandic krónur into any other currency. By contrast, the priority claimants in the Landsbanki winding up now stand to be fully reimbursed in a fully convertible currency.

200 Moreover, as regards the second plea, the defendant argues that there has been no discrimination whatsoever in the manner in which the deposit-guarantee fund itself has operated. The two groups compared by ESA, depositors with domestic branches and depositors with foreign branches of Landsbanki, have been treated equally. None has received any payments under the guarantee scheme.

201 In addition, the deposits held with domestic branches never became unavailable within the meaning of Article 1(3) of the Directive. In any event, Iceland

continues, any difference in treatment between the two groups would be objectively justified. Although pure economic aims cannot constitute a sufficient justification, clear public interest objectives may constitute a legitimate aim even where that public interest has economic ends.

Other participants submitting written observations

202 The governments which submitted written observations have not addressed the issue of discrimination.

Findings of the Court

203 By its second and third pleas, the applicant contends that by covering deposits in Iceland at least to the level prescribed by the Directive, and within the time limits provided therein, and, at the same time, not providing foreign depositors with at least that same minimum guarantee, the defendant has infringed the Directive read in light of Article 4 EEA or has indirectly discriminated on the basis of nationality which is prohibited by Article 4 EEA.

Discrimination contrary to the Directive read in light of Article 4 EEA

204 Article 4 EEA provides as a general principle that, within the scope of application of the EEA Agreement, and without prejudice to any special provisions contained therein, any discrimination on grounds of nationality shall be prohibited.

205 Article 4 EEA applies independently only to situations governed by EEA law for which the EEA Agreement lays down no specific rules prohibiting discrimination (see Case E-1/00 *Íslandsbanki-FBA* [2000-2001] EFTA Ct. Rep. 8, paragraphs 35 and 36, and case law cited).

206 Pursuant to Article 4(1) of the Directive, deposit-guarantee schemes introduced and officially recognised in an EEA State in accordance with Article 3(1) of the Directive shall cover depositors at branches set up by credit institutions in other EEA States.

207 Recital 3 in the preamble to the Directive states that in the event of the closure of an insolvent credit institution the depositors at any branches situated in a Contracting Party other than that in which the credit institution has its head office must be protected by the same guarantee scheme as the institution’s other depositors.

208 It follows from Article 4 of the Directive read in light of recital 3 in the preamble that depositors at any branches established by credit institutions in other EEA States shall belong to the guarantee scheme introduced and officially recognised in the home EEA State.

209 Moreover, the treatment of foreign and domestic depositors by the deposit-guarantee scheme must be equal as regards payment of minimum compensation under the Directive in the event of the closure of an insolvent credit institution.

210 Thus, the principle of non-discrimination requires that there is no difference in the treatment of depositors by the guarantee scheme itself and the way it uses its funds. Thus, to that extent, discrimination under the Directive is prohibited.

211 In the case at hand, it is undisputed that Landsbanki collapsed on 7 October 2008. Domestic deposits were transferred to New Landsbanki which was established by the Icelandic Government between 9 and 22 October 2008. The transfer was based on an FME decision of 9 October 2008.

212 The TIF was not involved in the transfer of the deposits. The transfer was part of the restructuring of the Icelandic banks that was achieved by a series of measures under the Icelandic Emergency Act.

213 On 27 October 2008, that is, within the 21 days prescribed in Article 1(3) of the Directive, the FME made a statement that triggered an obligation for the TIF to make payments as regards foreign deposits in branches of Landsbanki.

214 Moreover, domestic deposits did not become unavailable within the meaning of Article 1(3) of the Directive. The transfer of domestic deposits to New Landsbanki was made before the FME made its declaration triggering the application of the Directive. Accordingly, depositor protection under the Directive never applied to depositors in Icelandic branches of Landsbanki.

215 As has been stated above, the principle of non-discrimination inherent in the Directive requires that there should be no difference in the way a deposit-guarantee scheme treats depositors, and the way it pays out its funds.

216 In the present case, difference in treatment of this kind was not possible. Consequently, the transfer of domestic deposits – whether it leads in general to unequal treatment or not – does not fall within the scope of the non-discrimination principle as set out in the Directive.

Conclusion

217 The second plea has to be dismissed.

Discrimination contrary to Article 4 EEA

218 As regards the third plea, it is settled case-law that the principle of non-discrimination which has its basis in Article 4 EEA requires that comparable situations must not be treated differently and that different situations must not be treated in the same way. Discriminatory treatment may be justified only if it is based on objective considerations independent of the nationality of the persons concerned and is proportionate to the objective being legitimately pursued (see,

inter alia, Case E-15/11 *Arcade Drilling*, judgment of 3 October 2012, not yet reported, paragraph 60, and case law cited).

219 At the time of the transfer, Icesave customers in the branches in the UK and in the Netherlands, and their counterparts in Iceland found themselves in their capacity as deposit holders in an insolvent Icelandic bank in a comparable situation.

220 As regards the further assessment of the third plea, it must be recalled that the application seeks only one declaration, namely, that, by failing to ensure payment of the minimum amount of compensation to Icesave depositors in the Netherlands and in the United Kingdom provided for in Article 7(1) of the Directive within the time limits laid down in Article 10 of the Directive, the defendant has infringed its obligations under EEA law. This application is based on three pleas: (i) an infringement of the alleged obligation of result under the Directive itself, (ii) an infringement of the Directive and Article 4 EEA and (iii) an infringement of Article 4 EEA alone.

221 The applicant has limited the scope of its application by stating that "the present case does not concern whether Iceland was in breach of the prohibition of discrimination for not moving over the entirety of deposits of foreign Icesave depositors into 'new Landsbanki', as it did for domestic Landsbanki depositors. The breach is constituted by the failure of the Icelandic Government to ensure that Icesave depositors in the Netherlands and the United Kingdom receive payment of the *minimum amount of compensation* provided for in the Directive within the time limits laid down in the Directive, *like it did for the domestic depositors*. The compensation of domestic and foreign depositors above and beyond that minimum amount has not and is not being discussed in the context of the present proceedings."

222 Moreover, in its application, ESA underlines "that this does not prejudge its view as to whether the discrimination relating to the compensation of depositors above and beyond the level foreseen by the Directive is justifiable".

223 Thus, having regard to the applicant's self-limitation, the Court is bound to assess whether the defendant was under a specific obligation to ensure that payments were made to Icesave depositors in the Netherlands and the UK.

224 The Court has already held that the Directive, even read in light of Article 4 EEA, imposes no obligation on the defendant to ensure that payments are made in accordance with the requirements of the Directive to Icesave depositors in the Netherlands and the UK.

225 Thus, such an obligation of result could only be deemed to exist if it were to follow directly from Article 4 EEA itself. Were this the case, the transfer of domestic deposits to New Landsbanki would have led to an obligation to ensure the payment of minimum compensation, as specifically provided for in the Directive.

226 This, however, is not required under the principle of non-discrimination. Article 4 EEA requires that comparable situations must not be treated differently. A specific obligation upon the defendant that, in any event, would not establish equal treatment between domestic depositors and those depositors in Landsbanki's branches in other EEA States cannot be derived from that principle. Consequently, this plea cannot succeed on the basis of Article 4 EEA.

227 For the sake of completeness, the Court adds that even if the third plea had been formulated differently, one would have to bear in mind that the EEA States enjoy a wide margin of discretion in making fundamental choices of economic policy in the specific event of a systemic crisis provided that certain circumstances are duly proven. This would have to be taken into consideration as a possible ground for justification. In the earlier case of *Sigmarsson*, the applicant itself underlined this point (see *Sigmarsson*, cited above, paragraphs 42 and 50).

Conclusion

228 In view of the above, also the third plea has to be dismissed.

229 Accordingly, the Court holds that, by failing to ensure payment of the minimum amount of compensation to Icesave depositors in the Netherlands and in the United Kingdom provided for in Article 7(1) of the Act referred to at point 19a of Annex IX to the Agreement on the European Economic Area (Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes) within the time limits laid down in Article 10 of the Act, Iceland has not failed to comply with the obligations resulting from that Act, in particular Articles 3, 4, 7 and 10 thereof, and/or Article 4 of the Agreement on the European Economic Area.

V Costs

230 Under Article 66(2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings. The defendant has asked that the applicant be ordered to pay the costs. Since the latter has been unsuccessful, it must be ordered to pay the costs. The costs incurred by those who have submitted observations are not recoverable.

231 In accordance with Article 66(4) of the Rules of Procedure, the European Commission, which has intervened in the proceedings, is to bear its own costs.

232 The costs incurred by the Liechtenstein, Netherlands, Norwegian and United Kingdom Governments, which have submitted observations to the Court, are not recoverable.

On those grounds,

THE COURT

hereby:

1. **Dismisses the application.**

2. **Orders the EFTA Surveillance Authority to pay its own costs and the costs incurred by Iceland.**

3. **Orders the European Commission to bear its own costs.**

Carl Baudenbacher Páll Hreinsson Ola Mestad

Delivered in open court in Luxembourg on 28 January 2013

Thomas Christian Poulsen
Acting Registrar

Carl Baudenbacher
President