The ESM and the European Court's Predicament in *Pringle*

By Vestert Borger[*]

A. Introduction

On 27 November 2012, the European Court of Justice ("the Court") rendered its judgment in the *Pringle* case.[1] Sitting as a plenum, which is extremely rare, the Court did what had been expected. Just as the *Bundesverfassungsgericht* (German Federal Constitutional Court or *BVerfG*) had done two months earlier,[2] it gave the go-ahead for the euro area's permanent emergency instrument, the European Stability Mechanism ("ESM"). With this decision, the possibility of granting assistance to financially distressed euro area Member States has now been secured for the future.

Despite this unsurprising outcome, the Court's judgment is fascinating for several reasons. First, it informs the ordinary Treaty revision procedure of Article 48(6) TEU and the scope of the Court's jurisdiction to review European Council Decisions adopted in this context. Second, it defines the relationship between the ESM and the existing Treaty framework on Economic and Monetary Union (EMU), in particular its economic branch. Lastly, it clarifies how and to what extent Union institutions can be deployed by the Member States in the context of intergovernmental initiatives that do not have their basis in the EU legal framework.[3]

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[1] Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____, *available at* http://curia.europa.eu/juris/document/document.jsf?text=&docid=130381&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=274536.

[2] Bundesverfassungsgericht [BVerfG - Federal Constitutional Court], Case No. 2 BvR 1390/12, Sept. 12, 2012, 2012 NEUE JURISTISCHE WOCHENSCHRIFT (NJW) 3145 (Ger.).

[3] Next to the ESM Treaty, Union institutions are also used in the context of the recently concluded Treaty on Stability, Coordination and Governance in the Economic and Monetary Union. *See* Paul Craig, *The Stability, Coordination and Governance Treaty: Principles, Politics and Pragmatism*, 37 EUR. L. REV. 231 (2012). *But see* Vestert Borger & Armin Cuyvers, *Het Verdrag inzake Stabiliteit, Coördinatie en Bestuur in de Economische en Monetaire Unie: de juridische en institutionele complexiteit van de eurocrisis*, 60 TIJDSCHRIFT VOOR EUROPEES EN ECONOMISCH RECHT 370 (2012) (providing a different view).

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This case note will focus on the second of these points, namely, the relationship between the ESM and the existing framework on economic governance in the Union Treaties. In this respect the Court found itself between a rock and a hard place in *Pringle*. With the fate of the euro area hanging in the balance, it had to approve the ESM. Yet, in order to do this, it had to reconcile this new financing instrument with key provisions on EU economic policy, including the emergency exception in Article 122(2) TFEU and the no-bailout clause of Article 125 TFEU. The Court managed to achieve this goal, but only by resorting to the strained reasoning that Member States have always had the ability to provide financial assistance via an instrument such as the ESM and that nothing has changed as a result of the debt crisis. According to this reasoning, the revision of the TFEU, initiated to clear the way for the ESM, is no more than a cosmetic exercise.

B. Factual Background

The legal framework of the Economic and Monetary Union (EMU) was not built to withstand a crisis of the current proportions. When it erupted late 2009, no mechanism existed to support Member States facing debt and bond-market difficulties. Under great market pressure, the Union and the euro area Member States pursued improvised solutions. On 2 May 2010, the euro area Member States first established the *Green Loan Facility* (GLF), a set of pooled bilateral loans worth €80 billion that were coordinated and administered by the Commission.[4] Only a few days later, the Union and the euro area Member States supplemented this facility with two emergency funds. One of them is the *European Financial Stabilization Mechanism* (EFSM), an EU law construct, based on the emergency clause of Article 122(2) TFEU, with a fire power of €60 billion.[5] The other is the *European Financial Stability Facility* (EFSF), a Special Purpose Vehicle (SPV) with an effective lending capacity of €440 billion, which, however, does not have its basis in the EU legal framework.[6]

During the last several years, these funds have proven their worth as they have been used to provide financial assistance to Greece, Ireland, Portugal and Spain's ailing banking

[4] The GLF is founded on two agreements concluded on 8 May 2010, which are available at http://www.minfin.gr/content-api/f/binaryChannel/minfin/datastore/30/2d/05/302d058d2ca156bc35b0e268f9446a71c92782b9/application/pdf/sn_kyrwtikoimf_2010_06_04_A.pdf. The first concerns an inter-creditor agreement among the euro area lender Member States, containing the modalities of their involvement in the loan facility. The second forms a loan facility agreement which sets out the provisions governing the pooled bilateral loans.

[5] Council Regulation 407/2010, 2010 O.J. (L 118) 1 (EU) [hereinafter Regulation 407/2010].

[6] The basic arrangements concerning the EFSF are laid down in a framework agreement between the euro area Member States, in their capacity as shareholders, and the EFSF. *See* European Financial Stability Facility, EFSF Framework Agreement, *available at* http://www.efsf.europa.eu/about/legal-documents/index.htm [hereinafter EFSF Framework Agreement].

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sector.[7] But they could only provide a temporary solution. In order to structurally strengthen EMU, a permanent rescue facility had to be established. Realizing this, the European Council took the initiative at its meeting of 28–29 October 2010 to create a permanent crisis mechanism in order to safeguard the financial stability of the euro area as a whole. It invited its president Van Rompuy to undertake consultations with the Member States "on a limited treaty change required to that effect, not modifying Article 125 TFEU (no-bailout clause)."[8] On the basis of a proposal of the Belgian government, the European Council decided, at its meeting of 16–17 December 2010, to launch a simplified Treaty revision procedure on the basis of Article 48(6) TEU in order to add a third paragraph to Article 136 TFEU, a provision that specifically concerns euro area Member States.[9] This third paragraph reads as follows:

> The Member States whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality.[10]

After the European Parliament, the European Commission, and the European Central Bank submitted opinions on the initiative,[11] the European Council adopted Decision 2011/199 on 25 March 2011, adding this paragraph to Article 136 TFEU.[12] The Decision will only enter into force after all Member States have approved it in accordance with their respective constitutional requirements. The envisaged date of 1 January 2013 was not met because,

[7] The assistance of up to €100 billion earmarked for the Spanish banking sector—granted by the Eurogroup on 20 July 2012—was first disbursed by the EFSF but was transferred to the ESM on 29 November 2012. In addition to these existing assistance operations, Cyprus lodged an official request for assistance on 25 June 2012.

[8] European Council Conclusions, No. 25/1 REV 1 of 28–29 Oct. 2010, para. 1.

[9] European Council Conclusions, No. 30/1 REV 1 of 16–17 Dec. 2010, para. 2.

[10] *Id.* at annex I.

[11] European Parliament Resolution of 23 March 2011 on the Draft European Council Decision Amending Article 136 of the Treaty on the Functioning of the European Union with Regard to a Stability Mechanism for Member States Whose Currency is the Euro, 2012 O.J. (C 247 E) 22; Commission Opinion on the Draft European Council Decision Amending Article 136 of the Treaty on the Functioning of the European Union with Regard to a Stability Mechanism for Member States Whose Currency is the Euro, COM (2011) 70 final (Feb. 15, 2011); Opinion of the European Central Bank on a Draft European Council Decision Amending Article 136 of the Treaty on the Functioning of the European Union with Regard to a Stability Mechanism for Member States Whose Currency Is the Euro, 2011 O.J. (C 140) 8.

[12] European Council Decision 2011/199, 2011 O.J. (L 91) 1 [hereinafter Decision 2011/199].

at that time, the Czech Republic had not yet completed its approval procedure.[13] The Decision will now enter into force on the first day of the month following receipt of all notifications of approval by the Secretary General of the Council.[14]

Parallel to this simplified Treaty amendment procedure, euro area Member States also began working on an international treaty governing the *European Stability Mechanism* (ESM). The amendment of the TFEU was thought to clear the way for this international treaty that is not rooted in the EU Treaty structure. The ESM Treaty, to which all euro area Member States are party, was signed on 2 February 2011.[15] It was initially foreseen that the treaty would enter into force in July 2012.[16] Due to delays in the national ratification procedures, however, this deadline was not met. In particular, constitutional complaints against the ESM in Germany, Europe's main paymaster, delayed the treaty's entry into force. According to Article 48 of the ESM Treaty, the agreement can only take effect once the instruments of ratification have been deposited by signatories whose initial capital subscriptions represent no less than 90% of the ESM's authorized capital stock. Given that Germany's subscription to this capital stock is more than 27%, the ESM Treaty could not enter into force without German consent.[17] After the *BVerfG* gave the green light for ratification on 11 September 2012,[18] Germany finally deposited its instrument of ratification on 27 September 2012 and the ESM Treaty entered into force that day.[19] The

[13] For information about the ratification of Decision 2011/199, see Agreements Database, COUNCIL OF THE EUROPEAN UNION, http://www.consilium.europa.eu/policies/agreements?lang=en.

[14] Decision 2011/199 art. 2.

[15] Treaty Establishing the European Stability Mechanism (ESM), Feb. 2, 2012 [hereinafter ESM Treaty].

[16] Euro Area Member States, Agreed Lines of Communication by Euro Area Member States, Jan. 30, 2012, para. 2, *available at* http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/127633.pdf.

[17] ESM Treaty, *supra* note 15, at annex I–II (providing overviews of the contribution key of the ESM and of the ESM Members' respective subscriptions to the authorized capital stock).

[18] Bundesverfassungsgericht [BVerfG—Federal Constitutional Court], Case No. 2 BvR 1390/12, Sept. 12, 2012, 2012 NEUE JURISTISCHE WOCHENSCHRIFT (NJW) 3145 (Ger.). The *BVerfG* did rule, however, that ratification of the ESM would only be in compliance with the German constitution if, at the same time, two things would be ensured under international law. First, without the consent of the German representative, the amount of all payment obligations of Germany under the ESM Treaty cannot exceed its maximum subscription to the authorised capital stock. In addition, the provisions in the ESM Treaty on the inviolability of documents, professional secrecy and immunities of persons cannot stand in the way of the comprehensive information of the *Bundestag* and *Bundesrat*. Euro area Member States have complied with these requirements by adopting an interpretative declaration on the ESM Treaty.

[19] *See also* Statement, Jean-Claude Juncker, President, Eurogroup (Sept. 27, 2012), *available at* http://www.eurozone.europa.eu/documents/statement-by-the-president-of-the-eurogroup-jean-claude-juncker-on-the-entry-into-force-of-the-esm-treaty.

mechanism was subsequently inaugurated on 8 October 2012 during the first meeting of the ESM's Board of Governors.[20]

The ESM forms an international institution governed by public international law and is located in Luxembourg. It has an authorized capital stock of €700 billion,[21] which is divided in paid in shares and callable shares.[22] This arrangement should ensure that the ESM has an effective lending capacity of €500 billion.[23] The emergency mechanism can provide financial assistance via several instruments, including loans, bond purchases on the primary and secondary markets, and the indirect recapitalization of banks.[24] Any assistance granted is subject to strict conditionality.[25]

C. The Legal Background

The ESM must be understood in the context of the legal framework on economic and monetary policy. This framework is asymmetric in nature.[26] Since the introduction of the euro on 1 January 1999, monetary policy competences have been transferred to the Union level and are firmly in the hands of the European System of Central Banks (ESCB).[27] Yet, no such transfer has taken place in the area of economic policy; when it comes to economic

[20] Press Release, European Stability Mechanism (ESM) is inaugurated (Oct. 8, 2012), *available at* http://www.esm.europa.eu/press/releases/20121008_esm-is-inaugurated.htm. The Board of Governors is the ESM's highest decision-making body. The Governors are members of the governments of the ESM Members who are responsible for finance. *See* ESM Treaty, *supra* note 15, at art. 5.

[21] ESM Treaty, *supra* note 15, at art. 8(1).

[22] *Id.* at art. 8(2).

[23] *Id.* at recital 6.

[24] *See id.* at arts. 14–18 (providing an overview of the assistance instruments). The list of financial assistance instruments may be reviewed and changed by the Board of Governors. *See id.* at art. 19.

[25] *Id.* at arts. 3, 12(1), 13(3).

[26] On 13 December 2011, a six-pack of EU legislative measures, *inter alia* amending the SGP and introducing a mechanism to prevent and correct macro-economic imbalances, entered into force. These measures cannot, however, completely undo the asymmetry between economic and monetary governance as this stems from primary Treaty law. See Council Regulation (EU) 1173/2011, 2011 O.J. (L 306) 1; Council Regulation (EU) 1174/2011, 2011 O.J. (L 306) 8; Council Regulation (EU) 1175/2011, 2011 O.J. (L 306) 12; Council Regulation (EU) 1176/2011, 2011 O.J. (L 306) 25; Council Regulation (EU) 1177/2011, 2011 O.J. (L 306) 33; Council Directive (EU) 2011/85, 2011 O.J. (L 306) 41.

[27] Consolidated Version of the Treaty on the Functioning of the European Union art. 127(2), 2010 O.J. (C 83) 47 [hereinafter TFEU]; Protocol (No. 4) on the Statute of the European System of Central Banks and of the European Central Bank art. 3(1), 2010 O.J. (C 83) 230 [hereinafter Statute of the ESCB and of the ECB]. Member States that have not (yet) adopted the euro are not subject to TFEU art 127(2). *See also infra* note 39. Only the ECB and the national central banks of euro area Member States, which constitute the Eurosystem, conduct the monetary policy of the Union. *See* TFEU, at art. 282(1).

policy the Member States have retained their priority. As Articles 5(1) and 119(1) TFEU confirm, at the EU level economic policy is based on the close coordination of Member States' economic policies. For the most part, as becomes apparent from Articles 120 and 121 TFEU, EU competences in the economic sphere are limited to coordination and the adoption of guidelines. These instruments are characteristic for the Open Method of Coordination (OMC).[28]

Despite being different in nature, the Union's economic and monetary branches are strongly interrelated. Pursuit of the Union's main monetary policy goal, price stability,[29] requires that governments maintain solid budgetary policies. This inter-linkage has also found specific recognition in Article 119(3) TFEU, which states that both the Union and its Member States should be guided by the following principles when carrying out their respective competences: Stable prices, sound public finances and monetary conditions and a sustainable balance of payments.

Although the Union's economic competences are fairly limited, the TFEU sets out a legal framework to ensure that Member States comply with the principle of sound public finances. This framework relies on two mechanisms: Self-restraint and market discipline. The most important provision concerning self-restraint is Article 126(1) TFEU, which prohibits Member States from carrying excessive government deficits and debts. Article 1 of Protocol no. 12 on the excessive deficit procedure, annexed to the Union Treaties, considers a planned or actual government deficit in excess of 3% of GDP to be excessive. Similarly, debts should not exceed 60% of GDP. To ensure that Member States comply with these norms Article 126 TFEU sets out the excessive deficit procedure (EDP), which is further worked out in the corrective part of the Stability and Growth Pact (SGP).[30] Member States subject to an EDP may eventually face financial sanctions, which are to be imposed by the Council.[31]

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[28] The multilateral surveillance procedure in TFEU art. 121 is further worked out in the preventive part of the Stability and Growth Pact (SGP). *See* Council Regulation (EC) 1466/97, 1997 O.J. (L 209) 1 (*last amended by* Council Regulation (EU) 1175/2011, 2011 O.J. (L 306) 11) [hereinafter Regulation 1466/97]; *see also* Dermot Hodson & Imelda Maher, *The Open Method as a New Mode of Governance: The Case of Soft Economic Policy Coordination*, 39 J. COMMON MKT. STUDS. 719–46 (2001); Fabian Amtenbrink & Jakob de Haan, *Fiscal Policy Discipline Versus Flexibility*, 40 COMMON MKT. L. REV. 1075–106 (2003).

[29] Consolidated Version of the Treaty on European Union art. 3(3), 2010 O.J. (C 83) 13 [hereinafter TEU]; TFEU, *supra* note 27, at arts. 119(2), 127(1), 282(2); Statute of the ESCB and of the ECB, *supra* note 27, at art. 2. The Treaties do not define what is to be understood by price stability. However, the ECB has defined it as a rate of inflation below, but close, to 2% over the medium term. *See* EUROPEAN CENTRAL BANK, THE MONETARY POLICY OF THE ECB 64 (2011).

[30] Council Regulation (EC) 1467/97, 1997 O.J. (L 209) 6 (*last amended by* Council Regulation (EU) 1177/2011, 2011 O.J. (L 306) 33).

[31] TFEU, *supra* note 27, at art. 126(11).

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As regards market discipline, Articles 123–125 TFEU are central. Together these provisions aim to discipline individual Member States through the markets to keep their budgets within acceptable parameters.[32] When the markets lose confidence in the policies of a Member State, this should result in higher risk premiums on government bonds. Article 123(1) TFEU contains a ban on monetary financing by prohibiting both the ECB and national central banks from allocating credit to the Union or Member State authorities let alone to purchase directly government bonds from them. Additionally, Article 124(1) TFEU forbids measures, not based on prudential considerations, establishing privileged access to financial institutions for Union or Member State authorities. The final piece is the "no-bailout" clause of Article 125(1) TFEU, according to which neither the Union nor the Member states shall be liable for or assume the financial commitments of another Member State's authorities. This provision is formulated as follows:

> The Union shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of any Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project. A Member State shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of another Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project.[33]

As a counterweight to the focus on budgetary discipline embodied in the "no-bailout" clause, the drafters of the Treaty of Maastricht provided Article 122 TFEU. Its second paragraph is formulated in the following terms:

> Where a Member State is in difficulties or is seriously threatened with severe difficulties caused by natural disasters or exceptional occurrences beyond its control, the Council, on a proposal from the Commission, may grant, under certain conditions, Union financial assistance to the Member State

[32] RENÉ SMITS, THE EUROPEAN CENTRAL BANK—INSTITUTIONAL ASPECTS 77–78 (1997).

[33] TFEU, *supra* note 27, at art. 125(1).

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> concerned. The President of the Council shall inform the European Parliament of the decision taken.[34]

The provision forms a compromise between strong-currency countries and those with weaker economies.[35] On the one hand, in the run-up to the Treaty of Maastricht, strong-currency countries such as Germany urged a strict system of market discipline and argued against provisions on financial assistance because they would carry the risk of creating a transfer union. On the other hand, the Commission and countries with weaker economies emphasized the need for instruments to enhance convergence of economies and grant financial assistance.[36] The assistance provisions that were eventually included in the Treaty of Maastricht can be seen as a compromise between these opposing views.[37] The stringently formulated "no-bailout" clause in Article 125 TFEU forms the basic agreement, while Articles 143(2) and 122(2) TFEU its exceptions.[38] Euro area Member States can only benefit from the latter provision,[39] the scope of which in the end has been defined more narrowly than some had argued for during the negotiations on the Treaty of Maastricht.[40]

In the *Pringle* case the Court was in essence called upon to determine how Article 136(3) TFEU and the ESM Treaty can be made fit into this existing Treaty framework on economic governance, in particular regarding the "no-bailout" clause in Article 125 TFEU and the emergency exception in Article 122(2) TFEU.

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[34] *Id.* at art. 122(2).

[35] Jörn Pipkorn, *Legal Arrangements in the Treaty of Maastricht for the Effectiveness of the Economic and Monetary Union*, 31 COMMON MKT. L. REV. 263, 273–74 (1994); Ernest Gnan, *Artikel 104b*, *in* KOMMENTAR ZUM EU-/EG-VERTRAG 96–98 (Hans von der Groeben et al. eds., 1999); Jean-Victor Louis, *Guest Editorial: The No-Bailout Clause and Rescue Packages*, 47 COMMON MKT. L. REV. 971, 982–83 (2010); Alberto de Gregorio Merino, *Legal Developments in the Economic and Monetary Union During the Debt Crisis: The Mechanisms of Financial Assistance*, 49 COMMON MKT. L. REV. 1613, 1632–35 (2012).

[36] *See* Ulrich Häde, *Haushaltdiziplin und Solidarität im Zeichen der Finanzkrise*, 20 EUROPÄISCHE ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT 399, 402–03 (2009).

[37] Pipkorn, *supra* note 35, at 273; Doris Hattenberger, *Artikel 100*, *in* EU—KOMMENTAR 1186 (Jürgen Schwarze et al. eds., 1999); Louis, *supra* note 35, at 982.

[38] Yet not exceptions in the literal sense of the word. Neither TFEU art. 143(2) nor TFEU art. 122(2) are formulated as exceptions similar to those relating to the free movement provisions—TFEU arts. 45(3), 52, 65—or internal or external security—TFEU art. 346–47.

[39] The balance of payments assistance clause in TFEU art. 143(2) only applies to Member States that have not yet adopted the euro. The legal status of these states, called "Member States with a derogation," is regulated in TFEU arts. 139–44. Special rules apply to the United Kingdom and Denmark. *See* Protocol No. 15 on Certain Provisions Relating to the United Kingdom of Great Britain and Northern Ireland, 2010 O.J. (C 83) 284; Protocol No. 16 on Certain Provisions Relating to Denmark, 2010 O.J. (C 83) 287. These latter two states can benefit from balance of payments assistance on the basis of TFEU art. 143(2) as well.

[40] Häde, *supra* note 36, at 403.

D. The National Proceedings and Preliminary Questions

Although during the months prior to the entry into force of the ESM Treaty all eyes were on Germany, preliminary questions about the ESM did not reach the Court via the *BVerfG*. Instead, they originated in Ireland. On 13 April 2012, Mr. Pringle, a member of the Irish Parliament, challenged the Irish Government's involvement in the ESM before the Irish High Court. Pringle raised two sorts of claims relating to Union law. First, he argued that the amendment of Article 136 TFEU by Decision 2011/199 constituted an unlawful change of the TFEU. More specifically, he argued that Decision 2011/199 was not lawfully adopted pursuant to the simplified treaty revision procedure of Article 48(6) TEU because the amendment entailed an alteration of the competences of the Union. Pringle further argued that Decision 2011/199 would be inconsistent with provisions of the TEU and TFEU concerning economic and monetary policy and general principles of Union law.

Second, Pringle argued that, by ratifying the ESM Treaty, Ireland would undertake obligations incompatible with Treaty provisions on economic and monetary policy and would directly encroach on the exclusive competence of the Union in relation to monetary policy. Pringle claimed that, by establishing the ESM, the Member States of the euro area are creating an autonomous and permanent international institution, thereby aiming to circumvent the prohibitions and restrictions in the TFEU in relation to economic and monetary policy. Additionally, Pringle argued that, in the ESM Treaty, the institutions of the Union are granted competences and tasks that are incompatible with the functions accorded to them by the Union Treaties. Finally, Pringle asserted that the ESM Treaty was incompatible with the general principle of effective judicial protection and with the principle of legal certainty.

After the High Court of Ireland dismissed Pringle's action in its entirety on 17 July 2012, he appealed from that judgment to the Irish Supreme Court. The Supreme Court decided to stay proceedings and referred three questions to the Court.[41]

> 1. Is Decision 2011/199 valid in so far as it amends Article 136 TFEU by providing for the insertion, on the basis of the simplified revision procedure under Article 48(6) TEU, of a third paragraph on the establishment of a stability mechanism?
>
> 2. Do the Articles 2 TEU, 3 TEU, 4(3) TEU and 13 TEU and Articles 2(3) TFEU, 3(1)(c) and (2) TFEU, 119 TFEU to 123 TFEU and 125 TFEU to 127 TFEU, as well as the general principles of effective judicial protection and

[41] The questions are presented in the way they have been reformulated by the Court.

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> legal certainty preclude a Member State of the euro area from concluding and ratifying an agreement such as the ESM Treaty?
>
> 3. May Member States conclude and ratify the ESM Treaty before the entry into force of Decision 2011/199?

The European Court's answers to these questions will be discussed below only in as far as they express its view on the relationship between the ESM and economic policy in the Union. Given the limited space available, the opinion of Advocate General (AG) Kokott will not be discussed separately.[42] However, it will be referred to where it helps to illuminate the Court's judgment and reasoning.

E. The Judgment

In answer to the first question, the Court established that it had jurisdiction to examine the validity of Decision 2011/199 in the light of the conditions of Article 48(6) TEU, which sets out the simplified Treaty revision procedure.[43] After dismissing challenges to the admissibility of the case,[44] the Court turned to its consideration of whether Decision 2011/199 complies with the conditions of Article 48(6) TEU. This means it had to do two things. First, it had to investigate whether the Treaty amendment solely concerns Part Three of the TFEU. Second, it had to make sure that the revision of the TFEU does not increase the competences of the Union.

The Court did not limit itself to the formal finding that Article 1 of Decision 2011/199, because it only adds a third paragraph to Article 136 TFEU, complies with the condition that the revision may only concern Part Three of the TFEU. Instead, it examined whether the monetary and economic policy competences are affected by the Treaty amendment. Given that the nature of the Union's monetary and economic competences are determined in Articles 2(3), 3(1)(c) and 5(1) TFEU respectively, any change in these competences would concern Part I of the TFEU and would therefore require the use of the ordinary Treaty revision procedure in Articles 48(2)–(5) TEU.

The Court found that neither the Union's monetary nor its economic competences are affected and that the Treaty amendment is therefore restricted to Part Three of the

[42] Opinion of Advocate Gen. Kokott, Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____.

[43] Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____, at para. 37.

[44] *Id.* at para. 43.

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TFEU.[45] With regard to the Union's exclusive monetary competence the Court examined whether the objectives and instruments of a stability mechanism, of the kind envisaged by Decision 2011/199, fall within the realm of monetary policy. It found that the mechanism's purpose of safeguarding the stability of the euro area cannot be equated with the monetary policy objective of price stability. Furthermore, the Court concluded that the instrument of granting financial assistance constitutes an economic policy competence and falls outside the area of monetary policy.[46] The Court, therefore, concluded that the stability mechanism does not belong to the area of monetary policy. Instead, explained the Court, it falls within the area of economic policy because it complements the existing economic policy framework of the Union.[47]

As far as economic policy is concerned, the Court stressed the fact that the Union merely plays a coordinating role and does not have the power to establish a stability mechanism like the one envisaged by Decision 2011/199. It explicitly differentiated between the stability mechanism referred to in Decision 2011/199 and the power to grant assistance provided by Article 122(2) TFEU. According to the Court, the latter provision can be used to grant *ad hoc* financial assistance to Member States in need; it does not enable the Union to establish a mechanism of a permanent nature focusing on the financial stability of the euro area as a whole.[48] Member States are therefore entitled to establish a stability mechanism of the kind referred to by Article 1 of Decision 2011/199 outside the EU Treaty structure. But they may not disregard Union law when exercising this competence. Yet, precisely for this reason, Article 136(3) TFEU provides that any assistance granted must be subject to strict conditionality. In the view of the Court this proviso ensures that a stability mechanism like the ESM, which is based on a legal framework outside the EU Treaty structure, complies with Union law, in particular the regulatory framework on economic policy.[49]

As far as the condition that the revision may not increase the Union's competences was concerned, the Court recalled that Member States have the competence to establish a stability mechanism of the kind envisaged by Decision 2011/199. The Court reasoned that Article 136(3) TFEU confirms this and does not entail a transfer of power to the Union. Decision 2011/199, therefore, does not create a legal basis for the Union to undertake any action that was not possible before the entry into force of the Treaty amendment.[50]

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[45] *Id.* at para. 70

[46] *Id.* at paras. 55–57.

[47] *Id.* at paras. 58–60.

[48] *Id.* at paras. 64–65.

[49] *Id.* at paras. 68–69.

[50] *Id.* at paras. 72–75.

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With regard to the second question, the Court arrived at the heart of the matter when it examined the ESM Treaty in the light of various provisions in the TFEU on economic policy. First, the Court investigated whether the ESM Treaty subverts the Union's coordinating role in this area as determined by the Articles 2(3), 119 to 121 and 126 TFEU. The Court concluded that the ESM is not concerned with the coordination of economic policies but, instead, constitutes a financing mechanism.[51] The fact that several provisions of the ESM Treaty determine that any assistance granted shall be subject to strict conditionality did not change this finding.[52] This conditionality, the Court explained, is not an instrument for the coordination of Member States' economic policies but is intended to ensure that the activities of the ESM are compatible with Article 125 TFEU and the coordinating measures adopted by the Union.[53] The ESM Treaty, therefore, also does not affect the competence of the Council to issue recommendations on the basis of Article 126(6) and 126(8) TFEU to a Member State with an excessive deficit.[54]

In relation to Article 122(2) TFEU the Court referred to its statement, made earlier, that this provision is not an appropriate legal basis for a permanent stability mechanism.[55] Furthermore, the Court found that Article 122(2) TFEU contains no indication that the Union has an exclusive competence to grant financial assistance. Member States, therefore, are free to establish the ESM, provided that the mechanism complies with Union law, in particular the measures on the coordination of Member States' economic policies.[56] Similarly, the prohibition on monetary financing in Article 123 TFEU does not preclude the conclusion and ratification of the ESM Treaty.[57]

The Court's most difficult task was to reconcile the ESM Treaty with the "no-bailout" provision in Article 125 TFEU. It pointed out that the language of the provision makes clear that the prohibition does not cover every form of financial assistance to a Member State. The Court supported this reading of Article 125 TFEU with a reference to the Articles 122(2) and 123 TFEU. It reasoned that, if Article 125 TFEU prohibits any form of financial assistance by the Union or the Member States, then Article 122(2) TFEU would have had to declare that it constitutes a derogation from this prohibition. Furthermore, the Court noted that Article 123 TFEU specifically forbids the ECB and the national central banks

[51] *Id.* at para. 110.

[52] *See* ESM Treaty, *supra* note 15, at arts. 3, 12(1), 13(3).

[53] *See* Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____, at para. 111; *see also id.* at art. 13(4).

[54] Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____, at para. 113.

[55] *Id.* at para. 116.

[56] *Id.* at paras. 120–22.

[57] *Id.* at para. 128.

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(NCB) from granting "overdraft facilities or any other type of credit facility." As this wording is much stricter than the language used in Article 125 TFEU, the Court concluded that this supports the view that the "no-bailout" clause does not prohibit all forms of assistance to a Member State.[58]

In order to find out which forms of assistance are compatible with the prohibition on bailout the Court stressed that it is necessary to look to the objective of the provision.[59] Examining the preparatory work relating to the Treaty of Maastricht, the Court concluded that the aim of Article 125 TFEU is to ensure that Member States pursue prudent budgetary policies by submitting them to the discipline of the markets. According to the Court this, in turn, contributes at the Union level to the attainment of a higher objective, namely the maintenance of the financial stability of the monetary union.[60] The Court then made two central observations. First it stated that:

> the activation of financial assistance by means of a stability mechanism such as the ESM is not compatible with Article 125 TFEU unless it is indispensable for the safeguarding of the financial stability of the euro area as a whole and subject to strict conditions.[61]

Immediately thereafter, the Court stipulated that:

> Article 125 TFEU does not prohibit the granting of financial assistance by one or more Member States to a Member State which remains responsible for its commitments to its creditors provided that the conditions attached to such assistance are such as to prompt that Member State to implement a sound budgetary policy.[62]

The Court ruled that the ESM Treaty conforms with this reading of the "no-bailout" clause. None of the instruments of assistance available to the ESM has the effect of positioning the ESM to serve as a guarantor of the debts of the recipient Member State. The Court noted that a Member State receiving aid from the ESM will remain responsible to its

[58] *Id.* at paras. 130–32.

[59] *Id.* at para. 133.

[60] *Id.* at paras. 134–35.

[61] *Id.* at para. 136.

[62] *Id.* at para. 137.

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creditors for its financial commitments.[63] Moreover, the ESM will not grant assistance as soon as a Member States suffers impaired market access. The Court noted that Articles 3 and 12(1) of the ESM Treaty provide that stability support may be granted to Member States which are coping with severe financing problems only when this is indispensable to safeguard the financial stability of the euro area as a whole and of its Member States. Furthermore, the Court pointed out that the grant of any assistance is subject to strict conditionality. This ensures that the ESM and the recipient Member State comply with Union law, in particular the measures on the coordination of national economic policies that aim to support budgetary prudence on the side of Member States.[64]

The Court also examined whether Article 25(2) of the ESM Treaty, which regulates the issue of increased capital calls, is in compliance with the "no-bailout" clause. On the basis of this provision, in case an ESM Member fails to meet a required payment under a capital call,[65] a revised capital call shall be made to the other Members in order to ensure that the ESM receives the required amount of paid-in capital. The Court found that this arrangement does not violate the "no-bailout" clause because the other ESM Members are not acting as guarantors of the debt of the defaulting Member. Articles 25(2) and 25(3) ESM Treaty make clear, the Court explained, that the defaulting ESM Member remains bound to pay its part of the capital.[66] According to the Court Article 125 TFEU, therefore, does not preclude the conclusion and ratification of the ESM Treaty.[67]

The Court only summarily treated the third question, given that it is very much linked to the first and second questions. It concluded that, because the future Article 136(3) TFEU will only confirm the existence of the power of the Member States to establish a permanent stability mechanism, the right of a Member State to conclude and ratify the ESM Treaty is not subject to the entry into force of Decision 2011/199.[68]

[63] *Id.* at paras. 138–41.

[64] *Id.* at paras. 142–43.

[65] The issue of capital calls is regulated in ESM Treaty arts. 9(2), 9(3).

[66] Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____, at paras. 144–46.

[67] *Id.* at para. 147.

[68] *Id.* at paras. 184–85.

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F. Analysis

By approving of the ESM, the Court has not blocked the path to financial assistance to Member States in the future. The ESM will take over the tasks hitherto fulfilled by the emergency funds EFSM and EFSF.[69] Importantly, the Court's approval also enables the ECB to resume its interventions on the secondary markets for sovereign bonds on the basis of its new *Outright Monetary Transactions* programme (OMT). The ECB has linked the activation of this bond buying programme to the lodging of a formal request for stability support by a Member State to the ESM.[70]

The extensive judgment also exposes the Court's legal predicament. There was a great urgency to approve of the ESM. Legally the Court had to reconcile Article 136(3) TFEU and the ESM Treaty with the existing economic governance framework in the Union Treaties. The Court had to clear three particularly difficult hurdles. The first was that it had to find that Article 136(3) could be incorporated into TFEU via the simplified revision procedure in Article 48(6) TEU. This procedure may only be used if the amendment is confined to Part III of the TFEU and does not increase the competences of the Union. Article 136(3) TFEU, therefore, may neither affect the Union's economic competences, in particular its power to grant assistance in Article 122(2) TFEU, nor increase them. The second hurdle was that the Court had to rule that the conclusion and ratification of the ESM Treaty does not violate Union law. The ESM Treaty, therefore, had to be brought into compliance with Article 122(2) TFEU and the "no- bailout" clause in Article 125 TFEU. Finally, the Court had to confirm that the conclusion and ratification of the ESM Treaty was possible before the entry into force of Decision 2011/199, which adds Article 136(3) to the TFEU.

The Court has managed to clear these hurdles and find a way out of its predicament, but not without engaging in a mighty struggle with the economic policy provisions of the TFEU. Several aspects of this struggle will be analysed. First, the Court's view on Article 122(2) TFEU will be discussed (I). Second, the Court's interpretation of the "no-bailout" clause will

[69] *See* ESM Treaty, *supra* note 15, at recital 1. Initially, it was foreseen that the EFSF would be able to provide new stability support until the ESM entered into force. Hereafter, the EFSF would only stay involved in assistance programs in which it was already active. In accordance with ESM Treaty recital 6 and art. 39, until the complete run-down of the EFSF, the combined overall EFSF/ESM lending capacity would be set at €500 billion. However, on 30 March 2012, the Eurogroup decided that, for a transitional period until mid-2013, the EFSF may engage in new assistance programs in order to ensure a full, fresh lending capacity of €500 billion. The combined overall EFSF/ESM lending capacity was therefore set at €700 billion. After mid-2013, the maximum ESM lending volume will be €500 billion. According to Article 11(2) of the EFSF Framework Agreement, the EFSF shall be liquidated at the earliest date after 30 June 2013 on which there is no financial assistance outstanding and funding instruments and any reimbursements due to Member State guarantors have been repaid in full. EFSF Framework Agreement, *supra* note 6, at art. 11(2).

[70] *See* Press Release, European Central Bank, Technical Features of Outright Monetary Transactions (Sept. 6, 2012), *available at* http://www.ecb.int/press/pr/date/2012/html/pr120906_1.en.html.

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be considered (II). Finally, the meaning and significance of Article 136(3) TFEU and the notion of "stability of the euro area" will be examined (III).

I. Ad Hoc Assistance, Permanent Mechanisms and Article 122(2) TFEU

According to the Court Article 122(2) TFEU cannot provide a legal basis for the ESM. This conclusion seems to follow the view of the European Council, which held that the provision "should not be used for such purposes."[71] A mechanism of a permanent nature that aims to safeguard the financial stability of the euro area as a whole falls outside the scope of the provision. It only provides a legal basis for *ad hoc* financial assistance.

Why is this such an important element of the judgment? First, this was necessary to allow the Court to conclude that Decision 2011/199 does not affect the Union's economic competences which are laid down in the Treaties. And if these competences are not affected, then the simplified revision procedure is a suitable instrument for the introduction of Article 136(3) in the TFEU. Second, it forms the starting point for the Court's reasoning, which concluded that the ESM does not encroach on the powers that Article 122(2) TFEU confers on the Council.[72]

But is this conclusion legally compelling? Outside the constraints of this situation, one might wonder, on the one hand, whether Article 122(2) TFEU really only provides a legal basis for *ad hoc* financial assistance. It is true that one of the conditions to qualify for assistance under this provision is that a Member State is confronted with an "exceptional" occurrence beyond its control. As suggested by Louis, "exceptional" means "temporary."[73] Article 122(2) TFEU cannot be used to set up permanent capital flows to a Member State. But neither can the ESM! From the condition that assistance may only be granted when this is "indispensable" for the safeguarding of the financial stability of the euro area as a whole, one can conclude that assistance operations have to be stopped as soon as the threat to this stability no longer exists. Therefore, it may well be argued that a permanent mechanism, such as the ESM, can be based on Article 122(2) TFEU, provided that assistance operations to individual States only endure for as long as a threat to the financial stability of the euro area exists.

It even seems possible to use Article 122(2) TFEU for assistance that aims to safeguard the financial stability of the euro area as a whole. The emergency fund EFSM, which is based

[71] Decision 2011/199, at recital 4.

[72] Even if it would, the question would still need to be answered as to whether TFEU art. 122(2) forms an exclusive competence which excludes the possibility of Member States granting a similar kind of assistance. The Court explicitly states this in paragraph 120 of the judgment.

[73] Louis, *supra* note 35, at 985.

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on this provision, has exactly that objective,[74] although it is not limited to the financial stability of the euro area but to that of the Union.[75] Article 122(2) TFEU, however, does require that every time assistance is granted to safeguard the financial stability of the euro area as a whole, it has to be verified whether, in addition, the recipient Member State is confronted with an exceptional occurrence beyond its control.[76] Seen from this perspective Article 136(3) TFEU is actually less demanding. Even if a Member State suffers impaired market access because it has simply pursued unsound budgetary policies, which probably does not qualify as an "exceptional occurrence" within the meaning of Article 122(2) TFEU,[77] the State may qualify for assistance under Article 136(3) TFEU if its situation poses a threat to the euro area as a whole.[78]

II. The ESM and the "No Bailout" Clause

1. How to Interpret the "No Bailout" Clause?

Before the Court's judgment in *Pringle* the "no-bailout" clause in Article 125 TFEU was interpreted in various ways, which can be grouped into three basic approaches: Literal, purposive, and *ultima ratio*.

[74] *See* Regulation 407/2010, *supra* note 5, at art. 1.

[75] In order to make it a truly euro area instrument, one could consider the use of enhanced cooperation—TEU art. 20 and TFEU arts. 326–34. In this scenario, the use of enhanced cooperation for assistance targeted at the stability of the euro area has to be reconciled with the requirement of TFEU art. 328 that enhanced cooperation shall be open to all Member States subject to compliance with any conditions of participation.

[76] The EFSM satisfies this requirement because, according to Regulation 407/2010 art. 3(2), the Council has to make a decision each time it wants to grant aid to a Member State. *See* Matthias Rüffert, *The European Debt Crisis and European Union Law*, 48 COMMON MARKET L. REV. 1777, 1787 (2011). Under the ESM, this task would fall on the Board of Governors which must decide on the initiation of assistance operations. *See* ESM Treaty, *supra* note 15, art. 13(2).

[77] Louis, *supra* note 35, at 984.

[78] A different question, which the Court did not have to deal with, is whether a permanent stability mechanism based on TFEU art. 122(2) can mobilize enough funds. The EFSM's fire power is a mere €60 billion because the outstanding amount of assistance cannot exceed the margin available under the Union's own resources ceiling for payment appropriations. *See* Regulation 407/2010, *supra* note 5, at art. 2(2). Interestingly, instead of funds being disbursed by the EFSM and the EFSF in May 2010, the Commission initially proposed to establish one rescue fund on the basis of TFEU art. 122(2) which could only have been relied upon by euro area Member States. *See Commission Proposal for a Council Regulation Establishing a European Financial Stabilization Mechanism*, COM (2010) 2010 final (May 9, 2010). Similar to the arrangement that was eventually chosen for the EFSM, Union assistance would have been limited to the margin available under the Union's own resources ceiling for payment appropriations. Assistance above this ceiling would have been realized on the basis of the joint and pro-rata guarantee of euro area Member States. This construction was not chosen in the end, partly because of doubts as to whether it conforms to the Union's budget rules.

A *literal* interpretation of the bailout ban concentrates on the wording of the clause. The provision only states that neither the Union nor the Member States *shall be liable for* or *assume* the financial commitments of other Member States. As was correctly noted by AG Kokott in her opinion, in this reading a contravention of Article 125(1) TFEU would only occur when the Union or Member States guarantee the financial commitments of another Member State or when they take up these commitments.[79] An example would be a guarantee or subrogation on the side of the debtor.[80]

A *purposive* interpretation of the ban focuses on the purpose of the "no-bailout" clause and its place within the Treaty framework on economic governance, especially Articles 123–126 TFEU. As mentioned earlier, the prohibitions laid down in Articles 123–125 TFEU aim to establish market discipline. Member States need to be disciplined by the markets through the risk premiums the latter charge for buying their bonds. High premiums simply reflect the markets' lack of trust in the economic and budgetary policies of a Member State. Any form of assistance by the Union or its Member States, either direct or indirect, *ex ante* or *ex post*, would distort the functioning of this market mechanism.[81]

As a result of the crisis, a third type of reading of Article 125 TFEU has emerged.[82] This "*ultima ratio*" interpretation attributes to Article 125 TFEU a dual aim. The objective to establish market discipline so as to force Member States to pursue prudent budgetary policies and not pass on their debts to the Union or other Member States is not the only goal of the "no-bailout" clause, but must be placed within the broader perspective of maintaining the stability of the currency union itself. Normally these two objectives coincide, but the crisis pulls them apart. Leaving a Member State alone was not an option

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[79] Opinion of Advocate Gen. Kokott, Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____, paras. 114–15, 121.

[80] Cristoph Herrmann, *Griechische Tragödie—der währungsverfassungsrechtlige Rahmen für die Rettung, den Austritt oder den Ausschluss von überschuldeten Staaten aus der Eurozone*, 21 EUROPÄISCHE ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT 413, 415 (2010); Gnan, *supra* note 35, at 99–100; Phoebus Athanassiou, *Of Past Measures and Future Plans for Europe's Exit from the Sovereign Debt Crisis: What Is Legally Possible (and What Is Not)*, 36 EUR. L. REV. 558, 561 (2011).

[81] Smits, *supra* note 32; Kurt Fassbender, *Der europäische "Stabilisierungsmechanismus" im Lichte von Unionsrecht und deutschem Verfassungsrecht*, NEUE ZEITSCHRIFT FÜR VERWALTUNGSRECHT 799, 800 (2010); Vestert Borger, *De eurocrisis als katalysator voor het Europese noodfonds en het toekomstig permanent stabilisatiemechanisme*, 59 TIJDSCHRIFT VOOR EUROPEES EN ECONOMISCH RECHT 207, 212 (2011); Rainer Palmstorfer, *To Bail Out or not To Bail Out? The Current Framework of Financial Assistance for Euro Area Member States Measured Against the Requirements of EU Primary Law*, 37 EUR. L. REV. 771, 778 (2012).

[82] *See* Ulrich Häde, *Die europäische Währungsunion in der internationalen Finanzkrise—An den Grenzen europäischer Solidarität?*, 45 EUROPARECHT 854, 859–62 (2010); *Contra* Kai Hentschelmann, *Finanzhilfen im Lichte der No Bailout-Klausel—Eigenverantwortung und Solidarität in der Währungsunion*, 46 EUROPARECHT 282, 294–95 (2011); Rüffert, *supra* note 76, at 1786–87; *see also* Ulrich Jan Schröder, *Die Griechenlandhilfen im Falle ihrer Unionsrechtswidrigkeit*, 64 DIE ÖFFENTLICHE VERWALTUNG 61, 64 (2011) (dismissing the argument that TFEU art. 125 could have been modified through practice so as to allow financial assistance to safeguard stability in the euro area as a whole).

when the crisis erupted in the beginning of 2010. The risk of contagion made it impossible not to rescue Greece and other peripheral Member States. Applying Article 125 TFEU with full rigor would have threatened the stability of the currency union. In such a situation, therefore, providing financial assistance would not run counter to the "no-bailout" clause.

2. The Court's Interpretation of the "No Bailout" Clause and its Consequences

In its judgment the Court had to combine elements of all three interpretation techniques to reconcile Article 136(3) TFEU and the ESM Treaty with the "no-bailout" clause. It started from a *literal* interpretation and stated that, from the wording used in Article 125 TFEU, it is apparent that not all forms of assistance are prohibited. It supported this reading by referring to Articles 122(2) and 123 TFEU. What is prohibited, according to the text of Article 125 TFEU, is apparent from the Court's phrase that a Member State should "remain responsible for its commitments to its creditors."[83] The assistance instruments laid down in Articles 14–18 of the ESM Treaty do not have the effect that the recipient Member State is no longer responsible for its financial commitments. The same is true for Article 25(2) of the ESM Treaty, which regulates the issue of increased capital calls to ESM Members, as the defaulting ESM Member stays bound to pay its part of the capital to the ESM.

But the Court also stipulated that not all forms of assistance, even if they are not prohibited by the text of Article 125 TFEU, are allowed. Adopting a *purposive* interpretation of the "no-bailout" clause, and supporting this with a reference to the preparatory works relating to the Treaty of Maastricht, the Court acknowledged that Article 125 TFEU aims to achieve budgetary discipline on the side of Member States by subjecting them to the logic of the markets. According to the Court the "no-bailout" clause, therefore, prohibits the granting of assistance which diminishes the incentive of the recipient Member State to pursue budgetary prudence.

In addition to this *purposive* reading of the "no-bailout" clause, the Court adopted an *ultima ratio* interpretation, stating that maintenance of budgetary discipline contributes to a higher objective, namely, the maintenance of the financial stability of the monetary union. Financial assistance by means of a stability mechanism such as the ESM, the Court explained, is permitted when this is indispensable for safeguarding the financial stability of the euro area as a whole.

Only on the basis of this analysis one can find that assistance granted via a stability mechanism such as the ESM falls outside the scope of the ban on bailout in Article 125

[83] *See* Stefaan Van den Bogaert & Vestert Borger, *Rechterlijke interpretaties ESM op de pijnbank van de crisis*, HET FINANCIEELE DAGBLAD (Dec. 7, 2012), (raising the question of to what extent this requirement prohibits the Union and euro area Member States from accepting a voluntary 'haircut' on Greek debt).

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TFEU if (1) the recipient Member State remains responsible for its financial commitments to its creditors, (2) assistance is subject to strict conditions, and (3) provided that it is indispensable for the safeguarding of the financial stability of the euro area as a whole.

This interpretation of the "no-bailout" clause has several important consequences. First, from this reading it follows that the future Article 136(3) TFEU is only of a declaratory nature.[84] Member States have always had the possibility of establishing a stability mechanism such as the ESM and Article 136(3) TFEU merely confirms this. Therefore, as the Court concluded, the conclusion and ratification of the ESM Treaty is not dependent on the entry into force of Decision 2011/199, which adds Article 136(3) to the TFEU. Second, the Court's reasoning also establishes that the assistance operations carried out by the ESM's predecessor, the EFSF, do not violate the "no-bailout" clause. After all, any assistance granted by the EFSF is subject to strict conditionality and is granted with the aim of safeguarding financial the stability of the euro area as a whole.[85] Third, this explanation of the "no-bailout" clause ensures that Member States outside the euro area will also be able to participate in assistance operations.[86] Although these Member States have not (yet) introduced the euro, they are all bound by the "no-bailout" clause. Recent events suggest that it is more than an imaginary scenario that such countries will participate in assistance operations. In the fall of 2010, the United Kingdom, Denmark and Sweden[87] took part in the assistance operation relating to Ireland after the latter's financial position had deteriorated sharply as a result of the financial support it had granted to its banking sector during the financial crisis.[88] These actions will not violate the "no-bailout" clause as long as the recipient Member State remains responsible for its commitments to its creditors, as long as assistance is subject to strict conditions, and only if the action is indispensable for safeguarding the financial stability of the euro area as a whole.

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[84] The view of the Court is, therefore, in line with that of the European Council which had called for a Treaty amendment "not modifying the no-bailout clause." *See supra* note 8.

[85] EFSF Framework Agreement, *supra* note 6, at pmbl. (1). It must be admitted, however, that the EFSF Framework Agreement does not specifically state that assistance may only be granted when this is "indispensable" for safeguarding the stability of the euro area as a whole.

[86] *See also* ESM Treaty, *supra* note 15, at recital 9, art. 6(3) (paying specific attention to non-euro area Member States that provide financial assistance alongside the ESM on an *ad hoc* basis).

[87] Each of these three Member States is subject to a different legal regime concerning their position in the EMU, *see supra* note 39. All three states are, however, subject to the no-bailout clause in TFEU art. 125.

[88] *See* Statement by the Eurogroup and ECOFIN Ministers (Nov. 28, 2010), *available at* http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/118051.pdf. The financial rescue package consists of an Irish contribution, financed by a Treasury cash buffer and investments by the National Pension Reserve Fund, of €17.5 billion and €67.5 billion of external support. The latter is made up of €22.5 billion from the IMF, €22.5 billion from the EFSM, and €17.7 billion from the EFSF. The United Kingdom (€3.8 billion), Sweden (€0.6 billion) and Denmark (€0.4 billion) provide further support through bilateral loans totalling €4.8 billion.

3. Questioning the Court's Interpretation of the No Bailout Clause

The Court's interpretation of the "no-bailout" clause raises some interesting points. The first relates to the use of Articles 122(2) and 123 TFEU in support of a restrictive reading of Article 125 TFEU. The second has to do with the objective of safeguarding the financial stability of the euro area as a whole. The third focuses on the relationship between the no-bailout clause and market discipline.

3.1 The Reference to Articles 122(2) TFEU and 123 TFEU

The Court observed that not all forms of assistance are precluded by Article 125 TFEU. It is indeed possible to adopt such an interpretation. Yet, according to the Court, this interpretation is supported by other provisions in the TFEU, in particular Articles 122(2) and 123 TFEU. It is questionable whether these two provisions actually support the conclusion that Article 125 TFEU does not prohibit all forms of assistance.

The Court stated that if Article 125 TFEU would have been an all-encompassing prohibition, then Article 122(2) TFEU should have stated that it constituted a derogation from Article 125 TFEU. But this is not necessarily the case. Articles 122(2) and 125 TFEU are both EU Treaty provisions. Since Article 122(2) TFEU is not formulated as an exception, neither of the former provisions can take precedence over the other. Instead, they need to be reconciled with each other. This can also be deduced from declaration no. 6 to the Treaty of Nice, which specifically states:[89]

> decisions regarding financial assistance, such as are provided for in Article 100 (now Art. 122) and are compatible with the no-bailout rule laid down in Article 103 (now Art. 125) . . .[90]

The application of Article 122(2) TFEU therefore involves a delicate balancing.[91] In carrying out this exercise attention should be paid to the legislative history and the drafting process of the Treaty of Maastricht, which has been discussed above. The starting point should be that Article 125 TFEU forms the basic assumption and that the emergency clause in Article 122(2) TFEU is its exception, even though it is not literally formulated as such.

[89] *See* De Gregorio Merino, *supra* note 35, at 1633–34.

[90] Treaty of Nice Amending the Treaty on European Union, The Treaties Establishing the European Communities and Certain Related Acts, decl. 6, March 10, 2001, 2001 O.J. (C 80) 78.

[91] For an elaborate discussion of how to carry out this balancing exercise, see Louis, *supra* note 35, at 983–85.

Yet, this required balancing exercise does not lead to the conclusion that, besides assistance of the Union on the basis of Article 122(2) TFEU, other forms of assistance would be possible under Article 125 TFEU. It simply means that the Union has been granted a power to grant financial assistance and that it can only be exercised by having due regard to the "no-bailout" clause. It does not provide any further information on the scope of the "no-bailout" clause in relation to assistance granted by Member States.

Similarly, Article 123 TFEU does not provide convincing evidence in support of a restricted scope of the "no-bailout" clause. In line with AG Kokott's opinion,[92] the Court pointed to the wording of Article 123 TFEU, according to which the ECB and national central banks are prohibited from granting "overdraft facilities or any other types of credit facility" to the Member States. As this wording is stricter than that used in Article 125 TFEU the Court concluded that the "no-bailout" clause was not intended to prohibit all financial assistance.

On the one hand, given that monetary financing of public deficits and debts can have particularly harmful consequences for price stability, one can argue that the wording of Article 123 TFEU supports a restrictive reading of the "no-bailout" clause. Whereas the ECB and national central banks are not allowed to grant credit to the public sector, such a prohibition does not apply to the Union and its Member States. On the other hand, the wording of Article 123 TFEU is strongly inspired by the position of central banks prior to the launch of EMU. In several Member States central banks had certain credit arrangements in place for public authorities. The drafters of the Treaty of Maastricht specifically wanted to exclude the possibility that such practices would endure after the launch of EMU.[93] Article 123 TFEU therefore specifically addresses this issue. As the wording of the provision is so much focused on the specific nature of central banks and their position before the launch of EMU, it cannot provide strong guidance on the interpretation of Article 125 TFEU.

3.2 The Objective of Safeguarding the Financial Stability of the Euro Area as a Whole

Article 125 TFEU aims to ensure budgetary discipline by subjecting Member States to the logic of the market. From various provisions in the TFEU it is clear that budgetary prudence is not only a goal in itself. It also contributes to the higher objective of price stability. The Court has now recognized that the "no-bailout" clause pursues another higher objective: Safeguarding the financial stability of the monetary union. But, unlike

[92] Opinion of Advocate Gen. Kokott, Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____, at para. 141.

[93] *See* Smits, *supra* note 32, at 289–91.

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sound public finances and price stability,[94] this objective has to date not found specific recognition in the Treaties.[95]

It seems that by referring—very exceptionally—to the preparatory work relating to the Treaty of Maastricht, in particular the paragraphs on budgetary discipline, the Court tried to legitimize the identification of this additional objective.[96] In several instances in these paragraphs there are references to price stability as well as to broader notions such as "stability," "monetary stability," and "sustainability of the union." This may lend some support to the identification of financial stability as an objective of the "no-bailout" clause. At the same time a clear definition of this objective is lacking. What exactly does financial stability of the euro area mean and when is this so much at risk that it warrants activation of a stability mechanism such as the ESM? These uncertainties surrounding the objective make it difficult to define the scope of the "no-bailout" clause.

Yet, one cannot lose sight of the difficult position in which the Court found itself. If it had identified the safeguarding of the financial stability of the monetary union as a new objective of economic policy, to be introduced by Article 136(3) TFEU, then this would have amounted to an implicit modification of the "no-bailout" clause. Conclusion and ratification of the ESM Treaty would then have been possible only after the entry into force of Decision 2011/199.

3.3 The "No Bailout" Clause and the Objective of Market Discipline

To a certain extent the euro crisis is due to the malfunctioning of the markets. Since the start of the third stage of the EMU markets have not properly performed their disciplining role. Instead of interest rates reflecting differences in country risk, spreads between the bonds of peripheral countries and those of France and Germany narrowed.[97] Only after

[94] *See e.g.* TEU, *supra* note 29, at art. 3(3) TEU (mentioning price stability as an objective to be achieved by the Union) and TFEU, *supra* note 27, at art. 119(3) (mentioning both sound public finances and stable prices as guiding principles for the economic policies of the Union and the Member States).

[95] *See also* Jean Pisani-Ferry, *The Known Unknowns and Unknown Unknowns of EMU*, 7 (Bruegel, Bruegel Policy Contributions, No. 12, 2012), who states: *"When thinking about possible threats that EMU should be defended against, policymakers in Maastricht looked back at past experience and identified two: inflation and fiscal laxity. Financial instability was at the time perceived as being of minor importance and, even though currency unification was expected to reinforce financial integration, no provision was envisaged to deal with the effects of private credit booms-and-busts."*

[96] *Bulletin of the European Communities*, Supp. 2/91 COMMISSION OF THE EUR. COMMUNITIES (1991).

[97] Since the start of the third stage of EMU and until the first half of 2008, the spread between 10-year government bonds of euro area Member States, relative to the German bond, were 16 basis points (bps) on average. After September 2008, the spread for most euro area Member States rose sharply. The case of Greece is illustrative in this regard. Before September 2008, the average spread between Greek and German bonds was 30 bps. However, it rose dramatically after September 2008 to 270 bps in March 2009. *See* Maria-Grazia Atinnasi

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the outbreak of the financial crisis did markets seem to rediscover the differences in country risk, often overreacting given the steep, sudden surge in interest rates on mainly peripheral countries' bonds.[98] By subjecting financial assistance to strict conditions the emergency funds are meant to achieve what the markets could not: Inducing Member States to maintain budgetary discipline and pursue economic reforms. This raises the question: What role does the "no-bailout" clause's most basic objective, subjecting Member States to market discipline, still have?

It can be argued that it was exactly the absence of a crisis resolution mechanism that made the "no-bailout" rule lack credibility, especially given the high degree of financial integration in the euro area.[99] A "no-bailout" clause without rules for dealing with a Member State's default is not effective because governments will try to avoid a default when a crisis hits.[100] The establishment of a mechanism that involves investors in the crisis resolution might actually bestow the "no-bailout" clause with needed credibility. The possibility of an orderly default would induce markets to care about the creditworthiness of Member States, thereby increasing the chance that differences in country risk will be reflected in interest rates.[101] The question, of course, is to what extent the structure of the ESM is fit to achieve this goal, which is an issue outside the scope of this case note.[102] For present purposes, however, it suffices to note that the Court did not address the relationship between the ESM and market discipline at all.[103]

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et al., *What Explains the Surge in Euro Area Sovereign Spreads During the Financial Crisis in 2007–09?*, 12–13 (Eur. Cent.l Bank, Working Paper Series, No. 1131, 2009).

[98] Catharina Klepsch & Timo Wollmerhäuser, *Yield Spreads on EMU Government Bonds—How the Financial Crisis Has Helped Investors to Rediscover Risk*, 46 INTERECONOMICS 169, 169–70 (2011).

[99] Daniel Gros & Thomas Mayer, *How to Deal With Sovereign Default in Europe: Create a European Monetary Fund Now!*, 2 (Centre For Eur. Policy Studies, Policy Briefs, No. 202, 2010).

[100] François Giaviti et al., A European Mechanism for Sovereign Debt Crisis Resolution: A Proposal, 9 (Bruegel, Bruegel Blueprint Series, No. 10, 2010).

[101] *Id.* at 10.

[102] *But see The European Stability Mechanism*, 7 EUR. CENTRAL BANK MONTHLY BULLETIN, 78–82 (2011). The insertion of Collective Action Clauses (CACs) in euro area Member States' government bonds, which is prescribed by ESM Treaty art. 12(3), may enhance market discipline. As such, CACs facilitate private sector involvement in the context of debt restructuring and may support an appropriate pricing of risk in government bond markets.

[103] In her opinion, AG Kokott addressed this issue. *See* Opinion of Advocate Gen. Kokott, Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____, at paras. 148, 151–52. She held the view that market discipline is ensured as long as the Union and the Member States do not directly meet the demands of the recipient Member State's creditors. As long as uncertainty exists about whether the recipient Member State will actually use the assistance to pay off its creditors, which is the case under the ESM, a sufficient degree of market discipline would be ensured. However, it is doubtful whether this uncertainty really guarantees a sufficient degree of market discipline.

Interestingly, the *BVerfG* did consider this relationship in its judgment on the ESM. In its view Article 136(3) TFEU forms an exception to Article 125 TFEU, which mitigates market discipline.[104] But the German Constitutional Court considered this acceptable because other foundations of the *Stabilitätsgemeinschaft* (stability union), which forms a precondition for the *BVerfG's* acceptance of Germany's participation in the third stage of the EMU, are still in place. The German Court was particularly comforted by the fact that there was no departure from several key elements of the *Stabilitätsgemeinschaft*, including the independence of the ECB and its focus on price stability, the prohibition on monetary financing, and the obligation to avoid excessive deficits.[105]

It would have been hard to for the European Court to reach a similar conclusion in *Pringle* because this would have meant that Article 136(3) TFEU is not only of a declaratory nature, but actually adjusts the scope and meaning of the "no-bailout" clause. Again, in that reading, the conclusion and ratification of the ESM Treaty prior to the entry into force of Decision 2011/199 would not have been possible.

III. Article 136(3) TFEU and the Stability of the Euro Area as a Whole

The Court's definition of the power of Member States to grant assistance is more limited than the actual wording of Article 136(3) TFEU. The Court reached the conclusion that assistance can be granted to safeguard the *financial* stability of the euro area, which is also specifically mentioned as the objective of the ESM in the ESM Treaty.[106] But Article 136(3) TFEU merely speaks about "stability". Given that the Court regards Article 136(3) TFEU as being declaratory in nature, it seems that the meaning of "stability" is limited to "financial stability."

In its opinion on the draft of Decision 2011/199 the European Parliament expressed its concerns about this financial conception of stability. It argued that all euro area Member States should have recourse to assistance of the ESM, even those whose economies are too small to pose a threat to the financial stability of the euro area as a whole.[107]

Interestingly, in practice it is already possible to discern a departure from this financial conception of stability. The following statement of the Heads of State and Government of

[104] Case No. 2 BvR 1390/12, *supra* note 2, at paras. 232-33.

[105] *Id.* at paras. 233–34.

[106] ESM Treaty, *supra* note 15, at art. 3.

[107] European Parliament Resolution of 23 March 2011 on the Draft European Council Decision Amending Article 136 of the Treaty on the Functioning of the European Union With Regard to a Stability Mechanism for Member States Whose Currency is the Euro, para. 6, 2012 O.J. (C 247 E) 22, 24.

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the euro area, issued shortly before they decided to establish the EFSF in May 2010, is illustrative:

> In the current crisis, we reaffirm our commitment to ensure the stability, unity and integrity of the euro area.[108]

These words reveal a different, and broader notion of stability, a notion that is no longer confined to economics and finance but is also of a political nature and relates to euro area membership. On the basis of this broader concept of stability, assistance is granted to keep Member States within the currency union, even if they do not pose a threat to the financial stability of the euro area as a whole.

Would it be possible for the Court to rule that this broader form of stability has also always been an objective of the "no-bailout" clause? Perhaps it would. From the preparatory works relating to the Treaty of Maastricht it is apparent that the interlocking of Member States' exchange rates and the accompanying introduction of the euro is an irrevocable process.[109] By inducing Member States to budgetary discipline the "no-bailout" clause intends to ensure this irreversibility. Granting assistance in order to preserve a Member State within the euro area would therefore not run counter to Article 125 TFEU. At the same time, this shows the open-ended nature of defining the scope of a prohibition by attributing to it a chain of objectives for which support may be found in preparatory works.

G. Conclusion

The euro springs from a French-German compromise. The currency itself is a French desire and a German concession.[110] For France a European single currency formed an opportunity to end the German monetary hegemony on the continent. For Germany acceptance of the euro was a means to realize the reunification of its country after the fall of the Berlin wall in 1989. By binding itself to a monetary union, it could ease fears among its European partners for renewed German dominance on the continent. But Germany was only willing to exchange its *Deutsche Mark* for a European alternative that would be at least as strong and stable. The governance framework of the EMU was, therefore, strongly focused on price stability.

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[108] Statement, Heads of State or Government of the Euro Area, (May 7, 2010).

[109] *Bulletin of the European Communities*, *supra* note 96, at 20, 64–65 (Dutch version). The irrevocability of fixing the exchange rates also becomes apparent from the provisions in the TFEU on Member States with a derogation, in particular TFEU article 140(3).

[110] André Szász, *Een Duits Dilemma: De Euro van Geloofwaardigheids-naar Vertrouwenscrisis*, 66 INTERNATIONALE SPECTATOR 137, 139 (2012).

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As a result of the crisis the euro has come to rest on a new compromise, one that is based not only on price stability, but also on financial stability. Yet, according to the Court, this compromise is not new at all but has existed in the law since the conception of EMU. Within the limits set by the Union Treaties, in particular the "no-bailout" clause, Member States have always had the possibility to grant assistance to their partners in need in order to safeguard the financial stability of the currency union. Article 136(3) TFEU only makes this explicit. Given its predicament in *Pringle* the Court could not have reached a different conclusion, but in reaching this inevitable conclusion it was forced to play a little with history as well.

Sooner rather than later this new compromise will also have to be redefined, as a consequence of the transformation the currency union is currently undergoing. The ESM is only an intermediate step. In practice, a shift in focus from financial to political stability may already be observed. But what is driving this transformation? In *Pringle*, the Court did not have to deal with this question, the importance of which reaches beyond the law. In her opinion, AG Kokott touches upon the answer: It is, probably, the development of solidarity in the Union.[111]

[111] Opinion of Advocate Gen. Kokott, Case C-370/12, Pringle v. Ir., 2012 E.C.R. I-____, paras. 142–43.

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