JUDGMENT OF THE COURT

14 July 2000*

(Free movement of capital – State guarantees issued on financial loans – Different guarantee fees for foreign and domestic loans)

In Case E-1/00

REQUEST to the Court under Article 34 of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice by Héraðsdómur Reykjavíkur (Reykjavík District Court) for an Advisory Opinion in the case pending before it between

State Debt Management Agency

and

Íslandsbanki-FBA hf.

on the interpretation of Articles 4, 40, 42 and 61 of the EEA Agreement.

THE COURT,

composed of: Thór Vilhjálmsson, President, Carl Baudenbacher and Per Tresselt (Judge-Rapporteur), Judges,

Registrar: Gunnar Selvik

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* Language of the request for an Advisory Opinion: Icelandic.

after considering the written observations submitted on behalf of:

– the Plaintiff, the State Debt Management Agency, represented by Sveinn Sveinsson, Supreme Court Attorney;

– the Defendant, the Íslandsbanki-FBA hf., represented by Baldur Guðlaugsson, Supreme Court Attorney;

– the Government of Iceland, represented by Högni S. Kristjánsson, Legal Officer, Ministry of Foreign Affairs, acting as Agent;

– the Government of Norway, represented by Helge Seland, Assistant Director General, Ministry of Foreign Affairs, acting as Agent;

– the EFTA Surveillance Authority, represented by Peter Dyrberg, Director, Legal & Executive Affairs, acting as Agent;

– the Commission of the European Communities, represented by Christina Tufvesson and John Forman, Legal Advisors, Legal Service, acting as Agents.

having regard to the Report for the Hearing,

after hearing the oral observations of the State Debt Management Agency, the Íslandsbanki-FBA hf., the Government of Norway, the EFTA Surveillance Authority and the Commission of the European Communities at the hearing on 30 May 2000,

gives the following

Judgment

Facts and procedure

1 By an order dated 1 February 2000, registered at the Court 7 February 2000, Héraðsdómur Reykjavíkur (Reykjavík District Court) made a Request for an Advisory Opinion in a case pending before it between the State Debt Management Agency (Lánasýsla ríkisins) and the Icelandic Investment Bank hf. (Fjárfestingarbanka atvinnulífsins hf.). By a decision of 15 May 2000, the Icelandic Investment Bank hf. merged with Íslandsbanki hf. The merged entity, Íslandsbanki-FBA hf., assumed all rights and obligations of the Icelandic Investment Bank hf. As a result of this merger, the parties to the case pending before Héraðsdómur Reykjavíkur are now the State Debt Management Agency (hereinafter the “Plaintiff”) and Íslandsbanki-FBA hf. (hereinafter the “Defendant”).

2 The dispute before Héraðsdómur Reykjavíkur concerns the guarantee fee provisions in the Icelandic legislation establishing a system of State guarantees. Until 1998, the legal framework of this system of State guarantees was found in Act no. 37/1961 on State Guarantees, as amended by Act no. 65/1988. On 1 January 1998, a new Act no. 121/1997 on State Guarantees entered into force.

3 Article 8 of the former Act no. 37/1961 on State Guarantees provided that banks, credit funds, financial institutions and others which, by law, were entitled to a State guarantee, were obliged to pay a guarantee fee to the State Treasury on loans from foreign entities. This fee was to be paid every three months and was to be fixed at 0.0625% of the average outstanding principal of assessable obligations for the relevant period.

4 Article 6 of the new Act no. 121/1997 on State Guarantees provides that guarantee fees are payable to the State Treasury on all loans, both foreign and domestic, benefiting from State guarantees. However, the guarantee fees payable on foreign loans are to equal 0.0625% every three months on the average outstanding principal of assessable obligations, while the guarantee fees payable on domestic loans are to equal 0.0375% every three months on the average outstanding principal of assessable obligations.

5 The Icelandic Investment Bank was established pursuant to Act No. 60/1997 and has operated since 1 January 1998. In accordance with Article 9 of Act No. 60/1997, the Icelandic Investment Bank assumed all then existing obligations of the Industrial Loan Fund, including certain loans granted by the Nordic Investment Bank, a joint financial institution established by the Governments of the five Nordic countries. The State Treasury had undertaken to guarantee all obligations of the Industrial Loan Fund and, accordingly, had issued State guarantees on the loans from the Nordic Investment Bank. Article 9 of Act No. 60/1997 provides that the State Treasury is to continue to guarantee all the obligations of the Industrial Loan Fund, which existed at the time of the establishment of the Icelandic Investment Bank, until such time as the underlying obligations are fulfilled.

6 The Plaintiff has overall responsibility for the administration of State guarantees, including the calculation, levying and collection of guarantee fees. In a letter dated 17 April 1998, the Plaintiff was informed by the Icelandic Investment Bank that the Industrial Loan Fund had not paid guarantee fees on its obligations to the Nordic Investment Bank since the middle of 1995. In the letter, the Icelandic Investment Bank expressed the view that the Nordic Investment Bank is not a foreign entity within the meaning of Article 6 of Act No. 121/1997 and that the guarantee fees payable should be those applicable to domestic loans.

7 On 23 January 1998, the Plaintiff made a request to the Ministry of Finance, asking it to decide whether obligations owed to the Nordic Investment Bank were obligations to a foreign entity for the purpose of calculating the guarantee fees. In its letter dated 9 March 1998, the Ministry of Finance confirmed that the Nordic Investment Bank should be considered a foreign entity and that the State

guarantee should be subject to the guarantee fees payable on loans from foreign entities.

8 The Icelandic Investment Bank did not accept the decision of the Ministry of Finance, and since 1 January 1998 the Icelandic Investment Bank hf. has paid guarantee fees on the obligations to the Nordic Investment Bank as if the obligations were in favour of a domestic entity.

9 The Plaintiff initiated proceedings before Héraðsdómur Reykjavíkur, making a claim for payment of guarantee fees on the assumption that the Nordic Investment Bank is a foreign entity.

10 In the proceedings before Héraðsdómur Reykjavíkur, several issues were raised concerning the compatibility of the State guarantee system imposing higher guarantee fees on loans from foreign lenders than domestic lenders with the EEA Agreement.

11 Héraðsdómur Reykjavíkur decided to submit a Request for an Advisory Opinion to the EFTA Court on the following question:

> *Is it compatible with the EEA Agreement, in particular Articles 4, 40, 42 and 61, when the national law of a Contracting Party provides:*
>
> *a. that a borrower, who is entitled to a state guarantee, shall pay a guarantee fee on loans from entities in other Contracting Parties to the EEA but not on domestic loans?*
>
> *b. that a borrower, who is entitled to a state guarantee, shall be subject to the payment of a higher guarantee fee on loans from entities in other Contracting Parties to the EEA compared to loans from domestic entities?*

12 Reference is made to the Report for the Hearing for a fuller account of the legal framework, the facts, the procedure and the written observations submitted to the Court, which are mentioned or discussed hereinafter only in so far as is necessary for the reasoning of the Court.

Findings of the Court

13 By its question, the national court is essentially asking whether the EEA Agreement, in particular Articles 4, 40, 42 and 61 EEA, precludes that entities benefiting from State guarantees are required under domestic law to pay higher guarantee fees on loans from lenders in other Contracting Parties to the EEA Agreement than from domestic lenders.

Interpretation of Article 40 EEA

14 Freedom of movement of capital is one of the fundamental principles of the EEA Agreement. Chapter 4 of the EEA Agreement contains the principal treaty provisions relating to the movement of capital within the EEA. Article 40 EEA provides as follows:

> "Within the framework of the provisions of this Agreement, there shall be no restrictions between the Contracting Parties on the movement of capital belonging to persons resident in EC Member States or EFTA States and no discrimination based on the nationality or on the place of residence of the parties or on the place where such capital is invested. Annex XII contains the provisions necessary to implement this Article."

15 Annex XII to the EEA Agreement refers to Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty (hereinafter the "Directive"). The Directive was in force at the material time. Article 1 of the Directive provides as follows:

> "Without prejudice to the following provisions, Member States shall abolish restrictions on movements of capital taking place between persons resident in Member States. To facilitate application of this Directive, capital movements shall be classified in accordance with the Nomenclature in Annex I."

16 The wording of Article 40 EEA is similar to that of the former Article 67(1) of the EC Treaty. The Treaty on European Union introduced new provisions on "Capital and payments" in the EC Treaty, including Article 73b which substantially reproduced the contents of Article 1 of Directive 88/361/EEC. After the Treaty of Amsterdam, Article 73b was renumbered as Article 56 EC.

17 Article 40 EEA and the Directive abolish restrictions on movements of capital between the Contracting Parties to the EEA Agreement.

18 It is firstly necessary for the Court to consider whether the making of loans such as those at issue in the main proceedings constitutes movement of capital within the meaning of Article 40 EEA.

19 The concept of movement of capital is not defined in Article 40 EEA or in the Directive. However, the Nomenclature of capital movements in Annex I of the Directive indicates the scope of capital movements for the purpose of Article 40 EEA and Article 1 of the Directive (see *inter alia* Case C-222/97 *Trummer and Mayer* [1999] ECR I-1661, at paragraph 21; and Case C-35/98 *Staatssecretaris van Financiën* v *B.G.M. Verkooijen* [2000] ECR I-0000, at paragraph 27).

20 Heading VIII of the Nomenclature lists "Financial loans and credits" as a category of capital movements. In the language of the introduction, capital movements include "- all the operations necessary for the purposes of capital movements: conclusion and performance of the transaction and related transfers."

21 In addition, as the Court of Justice of the European Communities has previously held, the borrowing of money from a bank in another Contracting Party falls within the scope of capital movement within the meaning of the Directive (see insofar Case C-484/93 *Svensson and Gustavsson* [1995] ECR I-3955).

22 The Court concludes from the foregoing that the taking of loans such as those at issue in the main proceedings constitute movement of capital within the meaning of Article 40 EEA, as read with the Directive.

23 Secondly, it is necessary for the Court to ascertain whether national rules which require entities benefiting from State guarantees to pay higher guarantee fees on loans from foreign lenders than from domestic lenders constitute a restriction on the free movement of capital.

24 National legislation that imposes higher guarantee fees in relation to loans from foreign lenders than loans from domestic lenders does not inevitably render foreign loans less attractive than domestic loans. Other factors, such as interest rates, may be decisive for borrowers when they are determining the most attractive lending offer. From the borrowers' point of view, favourable lending terms from foreign lenders may outweigh the disadvantages incurred by higher guarantee fees and consequently induce borrowers to contract loans with foreign lenders instead of domestic lenders.

25 However, the imposition of higher guarantee fees on foreign loans than those applicable to domestic loans will necessarily render the former loans more expensive for the borrower than what would have been the case if the lower guarantee fees had been applicable to those loans. The same holds true for cases in which a borrower who is entitled to a State guarantee must pay a guarantee fee on loans from foreign lenders but not on loans from domestic lenders. National provisions such as those at issue in the main proceedings provide for an inherent difference in the treatment of loans from foreign lenders and loans from domestic lenders. All other terms being equal, that difference will render foreign loans more expensive than domestic ones.

26 Such differentiated treatment may dissuade borrowers from approaching lenders established in another EEA State. Therefore, it must be held that guarantee fee provisions such as those at issue in the main proceedings constitute a restriction on the free movement of capital.

27 The Plaintiff has argued that the contested provisions of the Icelandic legislation do not constitute a restriction contrary to Article 40 EEA, since the differing guarantee fees do not, in practice, have substantial significance when borrowers are considering whether to contract loans with foreign lenders or with domestic lenders.

28 That argument cannot be accepted. The legislation in question may potentially dissuade borrowers from seeking loans in other EEA States. This is sufficient to

establish a breach of Article 40 EEA. There is no requirement that an appreciable effect on the cross-border movement of capital be demonstrated.

29 The reply to be given to the national court must therefore be that national provisions of a Contracting Party to the EEA Agreement which provide that a borrower, who is entitled to a State guarantee, must pay a guarantee fee on loans from entities in other Contracting Parties but not on loans from domestic entities or that a borrower, who is entitled to a State guarantee, must pay a higher guarantee fee on loans from entities in other Contracting Parties compared to loans from domestic entities are incompatible with Article 40 EEA, read with Council Directive 88/361/EEC.

Article 36 EEA

30 The Government of Norway has suggested that a situation such as that in the main proceedings should be considered under Article 36 EEA. Since the Court has already concluded that the contested national legislation is contrary to Article 40 EEA, the Court will examine whether this renders Article 36 EEA inapplicable in this case.

31 Article 36 EEA requires the abolition of all restrictions on the provision of services, including financial services, within the EEA whereas Article 40 EEA prohibits all restrictions on the movement of capital within the EEA. It follows from the wording of these two provisions, as well as their placement in different chapters of the Agreement, that they were intended to regulate different situations.

32 The predominant feature of the case at hand is the free movement of capital. The provisions concerning the different guarantee fees leading to a more expensive guarantee for loans from foreign lenders constitute a national measure that directly restricts the cross-border flow of capital. They may also indirectly restrict the freedom to provide and receive services. On balance, however, the centre of gravity of the case lies with the free movement of capital.

33 Furthermore, Article 37 EEA states that activities are to be considered as "services" within the meaning of the EEA Agreement only "in so far as they are not governed by the provisions relating to freedom of movement of goods, capital and persons". One may conclude from that provision that Article 40 EEA and Article 36 EEA are, as a rule, not intended to apply simultaneously.

34 The present case must, therefore, be dealt with under Article 40 EEA.

The general prohibition of discrimination on grounds of nationality

35 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. It follows from the case law of the Court that 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-5/98 *Fagtún* [1999] EFTA Court Report 51, at paragraph 42).

36 The principle of non-discrimination has been given effect in the field of free movement of capital by Article 40 EEA. Consequently, it is not necessary to examine whether a situation such as that in the main proceedings is contrary to Article 4 EEA.

Interpretation of other provisions of the EEA Agreement

37 The national court has asked whether the contested legislation constitutes State aid contrary to Article 61 EEA. As shown by Case E-4/97 *Norwegian Bankers' Association* [1999] EFTA Court Report 1, at paragraphs 32 and 33, a State guarantee system for a publicly owned bank may constitute State aid within the meaning of Article 61 EEA. However, a national court does not have the competence to declare that State aid granted by an EFTA State is contrary to the EEA Agreement. Therefore, an answer to the part of the question relating to Article 61 EEA would not be of relevance to the national court in this case.

38 In view of the foregoing considerations on Article 40 EEA, it is not necessary to determine whether legislation such as that at issue in this case is incompatible with any of the other provisions in the EEA Agreement referred to in the Request for an Advisory Opinion or invoked by the parties in their pleadings.

Costs

39 The costs incurred by the Government of Iceland, the Government of Norway, the EFTA Surveillance Authority and the Commission of the European Communities, which have submitted observations to the Court, are not recoverable. Since these proceedings are, in so far as the parties to the main proceedings are concerned, a step in the proceedings pending before the national court, the decision on costs is a matter for that court.

On those grounds,

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THE COURT,

in answer to the question referred to it by Héraðsdómur Reykjavíkur by the reference of 1 February 2000, hereby gives the following Advisory Opinion:

National provisions of a Contracting Party to the EEA Agreement which provide

a. that a borrower, who is entitled to a State guarantee, must pay a guarantee fee on loans from entities in other Contracting Parties but not on loans from domestic entities

or

b. that a borrower, who is entitled to a State guarantee, must pay a higher guarantee fee on loans from entities in other Contracting Parties compared to loans from domestic entities

are incompatible with Article 40 EEA, read with Council Directive 88/361/EEC.

Thór Vilhjálmsson Carl Baudenbacher Per Tresselt

Delivered in open court in Luxembourg on 14 July 2000.

Gunnar Selvik
Registrar

Thór Vilhjálmsson
President