JUDGMENT OF THE COURT
11 February 2014

(Failure by a Contracting Party to fulfil its obligations – Directive 2009/111/EC – Failure to implement – Failure to notify)

In Case E-12/13,

EFTA Surveillance Authority, represented by Xavier Lewis, Director, Clémence Perrin, Officer, and Catherine Howdle, Temporary Officer, Department of Legal & Executive Affairs, acting as Agents,

applicant,

v

Iceland, represented by Anna Katrín Vilhjálmsdóttir, Ministry for Foreign Affairs, acting as Agent,

defendant,

APPLICATION for a declaration that by failing to implement correctly Article 1 paragraphs 15 to 18, 19(a), 21, 22(a), 23 to 29, 36, 37, 39 to 42 and Article 2(5) and (6) of the Act referred to at points 14, 16e and 31 of Annex IX to the Agreement on the European Economic Area (Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements and crisis management), as adapted to the EEA Agreement by Protocol 1 thereto, and by failing to notify the Authority of the text of such measures, Iceland has failed to fulfil its obligations arising under that Act and under Article 7 of the EEA Agreement.

THE COURT,

composed of: Carl Baudenbacher, President and Judge-Rapporteur, Per Christiansen and Páll Hreinsson, Judges,

Registrar: Gunnar Selvik,

having regard to the written pleadings of the parties,

having decided to dispense with the oral procedure,

gives the following

Judgment

I Introduction

1 By an application lodged at the Court's Registry on 3 July 2013, the EFTA Surveillance Authority ("ESA") seeks a declaration that by failing to implement correctly Article 1 paragraphs 15 to 18, 19(a), 21, 22(a), 23 to 29, 36, 37, 39 to 42 and Article 2(5) and (6) of the Act referred to at points 14, 16e and 31 of Annex IX to the Agreement on the European Economic Area (Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 as regards banks affiliated to central institutions, certain own funds items, large exposure supervisory arrangements and crisis management (OJ 2009 L 302, p. 97) ("Directive")), as adapted to the EEA Agreement by Protocol 1 thereto, and by failing to notify ESA of the text of such measures, Iceland has failed to fulfil its obligations arising under that Act and under Article 7 EEA.

II Relevant law

EEA law

2 Article 2 of the Directive reads as follows:

> *Amendments to Directive 2006/49/EC*
>
> *Directive 2006/49/EC is hereby amended as follows:*
>
> …
>
> *5. in Article 32(1), the first subparagraph is replaced by the following:*
>
> *'1. The competent authorities shall establish procedures to prevent institutions from deliberately avoiding the additional capital requirements that they would otherwise incur, on exposures exceeding the limit laid down in Article 111(1) of Directive 2006/48/EC once those exposures have been maintained for more than 10 days, by means of temporarily transferring the exposures in question to another company, whether within the same group or not, and/or by undertaking artificial transactions to close out the exposure during the 10-day period and create a new exposure.';*
>
> *6. in Article 35, the following paragraph is added:*

‘6. Investment firms shall be covered by the uniform formats, frequencies and dates of reporting referred to in Article 74(2) of Directive 2006/48/EC.’;

3 Article 3(1)(b) of Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions (recast) (OJ 2006 L 177, p.201) provides that:

‘investment firms’ means institutions as defined in Article 4(1)(1) of Directive 2004/39/EC, which are subject to the requirements imposed by that Directive, excluding:

(i) credit institutions;

(ii) local firms as defined in point (p); and

(iii) firms which are only authorised to provide the service of investment advice and/or receive and transmit orders from investors without holding money or securities belonging to their clients and which for that reason may not at any time place themselves in debt with those clients;

4 Article 3(1)(p) of Directive 2006/49/EC defines local firms in the following way:

‘local firm’ means a firm dealing for its own account on markets in financial futures or options or other derivatives and on cash markets for the sole purpose of hedging positions on derivatives markets, or dealing for the accounts of other members of those markets and being guaranteed by clearing members of the same markets, where responsibility for ensuring the performance of contracts entered into by such a firm is assumed by clearing members of the same markets;

5 Article 4(1)(1) of Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC (OJ 2004 L 145, p.1) defines investment firm in the following way:

‘Investment firm’ means any legal person whose regular occupation or business is the provision of one or more investment services to third parties and/or the performance of one or more investment activities on a professional basis;

Member States may include in the definition of investment firms undertakings which are not legal persons, provided that:

(a) their legal status ensures a level of protection for third parties’ interests equivalent to that afforded by legal persons, and

(b) they are subject to equivalent prudential supervision appropriate to their legal form.

However, where a natural person provides services involving the holding of third parties' funds or transferable securities, he may be considered as an investment firm for the purposes of this Directive only if, without prejudice to the other requirements imposed in this Directive and in Directive 93/6/EEC, he complies with the following conditions:

(a) the ownership rights of third parties in instruments and funds must be safeguarded, especially in the event of the insolvency of the firm or of its proprietors, seizure, set-off or any other action by creditors of the firm or of its proprietors;

(b) the firm must be subject to rules designed to monitor the firm's solvency and that of its proprietors;

(c) the firm's annual accounts must be audited by one or more persons empowered, under national law, to audit accounts;

(d) where the firm has only one proprietor, he must make provision for the protection of investors in the event of the firm's cessation of business following his death, his incapacity or any other such event;

6 Article 4(1)(2) of Directive 2004/39/EC defines investment services and activities in the following way:

'Investment services and activities' means any of the services and activities listed in Section A of Annex I relating to any of the instruments listed in Section C of Annex I;

The Commission shall determine, acting in accordance with the procedure referred to in Article 64(2):

—the derivative contracts mentioned in Section C 7 of Annex I that have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are cleared and settled through recognised clearing houses or are subject to regular margin calls

—the derivative contracts mentioned in Section C 10 of Annex I that have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are traded on a regulated market or an MTF, are cleared and settled through recognised clearing houses or are subject to regular margin calls;

7 Section A of Annex I to Directive 2004/39/EC lists the following services and activities:

(1) Reception and transmission of orders in relation to one or more financial instruments.

(2) Execution of orders on behalf of clients.

(3) Dealing on own account.

(4) Portfolio management.

(5) Investment advice.

(6) Underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis.

(7) Placing of financial instruments without a firm commitment basis

(8) Operation of Multilateral Trading Facilities.

8 Section C of Annex I to Directive 2004/39/EC lists the following instruments:

(1) Transferable securities;

(2) Money-market instruments;

(3) Units in collective investment undertakings;

(4) Options, futures, swaps, forward rate agreements and any other derivative contracts relating to securities, currencies, interest rates or yields, or other derivatives instruments, financial indices or financial measures which may be settled physically or in cash;

(5) Options, futures, swaps, forward rate agreements and any other derivative contracts relating to commodities that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event);

(6) Options, futures, swaps, and any other derivative contract relating to commodities that can be physically settled provided that they are traded on a regulated market and/or an MTF;

(7) Options, futures, swaps, forwards and any other derivative contracts relating to commodities, that can be physically settled not otherwise mentioned in C.6 and not being for commercial purposes, which have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are cleared and settled through recognised clearing houses or are subject to regular margin calls;

(8) Derivative instruments for the transfer of credit risk;

(9) Financial contracts for differences.

(10) Options, futures, swaps, forward rate agreements and any other derivative contracts relating to climatic variables, freight rates, emission allowances or inflation rates or other official economic statistics that must be settled in cash or may be settled in cash at the option of one of the parties (otherwise than by reason of a default or other termination event), as well as any other derivative contracts relating to assets, rights, obligations, indices and measures not otherwise mentioned in this Section, which have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are traded on a regulated market or an MTF, are cleared and settled through recognised clearing houses or are subject to regular margin calls.

Icelandic law

9 The English translation of Article 30(1), (2) and (4) of Act No 161/2002 on financial undertakings provided by the defendant reads:

> *Limits to large exposures*
>
> *Exposure resulting from one client, or a group of connected clients, shall not exceed 25% of a financial undertaking's capital base, cf. Articles 84 and 85. However, the provisions of the first sentence do not apply to the securities undertakings which are not licensed pursuant to subsections (c) and (f) of point 1 in the first paragraph of Article 25, securities brokerages and management companies of undertakings for collective investment in transferable securities.*
>
> *If there is any doubt as to which parties pertain to a group of connected clients a financial undertaking is required to link the parties unless the financial undertaking in question can demonstrate the contrary. The aggregate of large exposures shall not exceed 400% of the capital base; a 'large exposure' refers to any exposure amounting to 10% or more of the capital base.*
>
> …
>
> *If a financial undertaking's exposures exceed the limits provided for in the first paragraph, such exposures shall be notified to the Financial Supervisory Authority without delay. The Financial Supervisory Authority may grant the undertaking a time limit to bring its obligations into compliance. The Financial Supervisory Authority shall set detailed rules on large exposures of financial undertakings and financial conglomerates.*

10 The English translation of Article 84(3) of Act No 161/2002 on financial undertakings provided by the defendant reads:

> *The capital base requirement provided for in the first paragraph shall also apply to consolidated accounts. The Financial Supervisory Authority issues rules on the calculation of capital base and risk base for financial*

groups based on Council Directive 2002/87/EC on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate.

11 The English translation of Article 1 of the Icelandic Supervisory Authority ("FME") Rules No 215/2007 on the capital requirements and risk weighted assets of financial undertakings provided by the defendant reads:

These Rules shall apply to the following:

1. *Financial Undertakings which have received an operating licence cf. Act 161/2002 on Financial Undertakings, Article 4, paragraph 1, points 1 to 2 and 5 to 7, i.e. commercial banks, savings banks, credit undertakings, securities companies, securities brokerages and management companies of UCITS.*

2. *Consolidated undertakings where the parent undertaking is one of the undertakings mentioned in item 1 above.*

The entities mentioned in paragraph 1 of this Article are called financial undertakings in the following Articles.

12 The English translation of Article 3 of FME Rules No 215/2007 on the capital requirements and risk weighted assets of financial undertakings provided by the defendant reads:

Securities companies shall each month send a solvency ratio report to the Financial Supervisory Authority and other financial undertakings shall send such a report on a quarterly basis. Financial undertakings, other than securities companies, which do not calculate separately the risk weighted exposure amounts related to trading book items, cf. the provisions of Article 6, shall, however, send a report to the Financial Supervisory Authority on a half-year basis. Provisions on the reporting of financial undertakings on less than a quarterly basis do not apply if the solvency ratio of the undertaking is less than 12% at the beginning of the year. The Financial Supervisory Authority can under certain circumstances allow a submission of reports on a yearly basis, i.e. end of year figures only.

The monthly reports from securities companies, cf. paragraph 1 of this Article, shall have reached the Financial Supervisory Authority not later than 15 days from the accounting date. The reports from financial undertakings, other than securities companies, shall have reached the Financial Supervisory Authority not later than 15 days from the accounting date. The reports from financial undertakings, other than securities companies, shall have reached the Financial Supervisory Authority not later than 30 days from the accounting date.

III Facts and pre-litigation procedure

13 Decision No 85/2010 of 2 July 2010 of the EEA Joint Committee ("Decision 85/2010") amended Annex IX to the EEA Agreement by adding the Directive to points 14 and 31 as well as to point 16e. Iceland indicated constitutional requirements for the purposes of Article 103 EEA.

14 Article 3 of Decision 85/2010 provides that it should enter into force on 3 July 2010, provided that all notifications under Article 103(1) EEA had been made to the EEA Joint Committee, or on the day of entry into force of EEA Joint Committee Decision No 65/2008 of 6 June 2008 ("Decision 65/2008") or of EEA Joint Committee Decision No 114/2008 of 7 November 2008 ("Decision 114/2008"), whichever is the latest.

15 As regards Decision 85/2010, Iceland was the final EFTA State to notify that constitutional requirements had been fulfilled on 10 November 2011. Decision 65/2008 entered into force on 1 November 2010. Decision 114/2008 entered into force on 1 November 2011.

16 Consequently, in accordance with Article 103(1) EEA, Decision 85/2010 entered into force on 1 January 2012. The time limit for EEA/EFTA States to adopt the measures necessary to implement the Directive expired on the same date.

17 On 17 January 2012, Iceland notified ESA of national measures ensuring the partial implementation of the Directive. On the basis of the notification, ESA conducted a conformity assessment.

18 ESA sent Iceland a request for information setting out the questions raised by the conformity assessment. Iceland replied on 23 January 2012. On 16 May 2012, ESA issued a letter of formal notice. ESA identified shortcomings as to the implementation of Article 1, paragraphs 7(b), 8 to 13, 15 to 18, 19(a), 20 and 21, 22(a), 23 to 29, 35 to 43 and Article 2(1), (3) and (5) to (7) of the Directive and concluded that, due to the lack of implementation of those provisions, Iceland had failed to fulfil its obligations arising under the Act and under Article 7 EEA.

19 On 16 July 2012, Iceland replied to the letter of formal notice. Iceland acknowledged that changes were necessary to Icelandic law in order to fully implement the Directive. Iceland informed ESA, that it considered Article 1, paragraphs 7(b), 8 to 13, 15 to 19(a), 21, 22(a), 23 to 29, 36, 37, 39 to 43 and Article 2(1) and (3) of the Directive to be technical rules and that they would be implemented into the Icelandic legal order through rules which were being drafted at the time by the FME. Iceland stated that Article 2(5) of the Directive could be found in Articles 30(1) and (4) of Act No 161/2002 on financial undertakings and also in FME Rules No 216/2007 on large exposures incurred by financial undertakings.

20 As regards Article 2(6) of the Directive, Iceland stated that it had been partially implemented into the Icelandic legal order by Articles 117 and 84(3) of Act No

161/2002 on financial undertakings. Iceland stated that the term "investment firms" needed to be "strengthened" in that Act as well as in the FME rules on additional own funds items for financial undertakings.

21 On 15 August 2012, Iceland provided ESA with further information and as a result of which it was agreed that no changes to the Icelandic legislation were necessary for the implementation of Article 1(13), (20), (35) and (38) of the Directive. Iceland further stated that "[a]fter closely looking at FME Rules No 215/2007 and 216/2007, the Ministry agrees with ESA that a special provision or an 'anti-avoidance rule' similar to Article 2, Paragraph 5 of the Directive, can not be found in the aforementioned rules or Act No 161/2002. The Ministry is now looking into two options on how to implement a similar provision as Article 2, Paragraph 5 of the Directive. That is to implement the measure into secondary legislation or into Act No 161/2002. Either way the Article will be implemented into Icelandic legal order this autumn."

22 On 12 September 2012, ESA delivered a reasoned opinion to Iceland pursuant to the first paragraph of Article 31 of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice ("SCA"). ESA maintained that, on the basis of the information provided by Iceland up to that date, Article 1, paragraphs 7(b), 8 to 12, 15 to 18, 19(a), 21, 22(a), 23 to 29, 36, 37, 39 to 43 and Article 2(1), (3), and (5) to (7) of the Directive had not been fully implemented into the Icelandic legal order.

23 ESA concluded that by failing to correctly implement these provisions of the Act, or in any event, by failing to notify ESA forthwith of the measures it has adopted to implement the Act, Iceland had failed to fulfil its obligations arising under that Act and under Article 7 EEA. Pursuant to the second paragraph of Article 31 SCA, ESA requested Iceland to take the necessary measures to comply with the reasoned opinion within two months.

24 While Iceland did not formally reply to ESA's reasoned opinion, it did regularly update ESA on the progress made on the adoption of the various rules into the Icelandic legal order, including on 11 January 2013, 1 April 2013, and 28 May 2013.

25 ESA considered that the implementation of the following provisions remained outstanding: Article 1, paragraphs 15 to 18, 19(a), 21, 22(a), 23 to 29, 36, 37, 39 and 42 and Article 2(5) and (6) of the Act. Iceland had therefore not adopted the measures necessary to fully implement the Act within the time limit prescribed in the reasoned opinion and to notify ESA accordingly. On 29 May 2013, therefore, ESA decided to bring the matter before the Court pursuant to the second paragraph of Article 31 SCA.

IV Procedure and forms of order sought

26 On 3 July 2013 ESA lodged the present application at the Court Registry.

27 On 23 September 2013, Iceland submitted a statement of defence. On 8 October 2013, ESA submitted its reply. On 29 October 2013, Iceland submitted its rejoinder.

28 The applicant requests the Court to:

> *1. Declare that by failing to implement correctly Article 1 paragraphs 15-18, 19(a), 21, 22(a), 23-29, 36-37. 39-42 and Article 2 paragraphs 5, 6 of the Act referred to at points 14, 16e and 31 of Annex IX to the Agreement on the European Economic Area (Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements and crisis management), as adapted to the EEA Agreement by way of Protocol 1 thereto, within the time prescribed, and by failing to inform the Authority of the text of such measures, Iceland has failed to fulfil its obligations under the Act and under Article 7 of the EEA Agreement.*
>
> *2. Order Iceland to bear the costs of these proceedings.*

29 Iceland does not dispute the declaration sought by the applicant as regards Article 1 paragraphs 15 to 18, 19(a), 21, 22(a), 23 to 28, 36, 37, and 39 to 42 of the Directive.

30 However, Iceland states that, in its view, Article 1(29) and Article 2(5) and (6) of the Directive are implemented into the Icelandic legal order. ESA was informed thereof as regards Article 2(5) of the Directive. Iceland requests the Court to order each party to bear its own costs of the proceedings.

31 In its reply, ESA indicates its agreement with Iceland that Article 1(29) of the Directive is not applicable to Iceland and therefore withdraws its request for the declaration sought in the application as regards this provision.

32 After having received the express consent of the parties, the Court, acting on a report from the Judge-Rapporteur, decided pursuant to Article 41(2) of the Rules of Procedure ("RoP") to dispense with the oral procedure.

V Arguments of the parties concerning the remaining points in dispute

ESA

33 ESA submits in its application that Article 2(5) and (6) of the Directive amends provisions of Directive 2006/49/EC on the capital adequacy of investment firms and credit institutions. ESA asserts that it is undisputed that Iceland did not inform it of the adoption of the measures necessary to fully implement the Directive before the expiry of the two-month time limit following the delivery of the reasoned opinion.

Article 2(5) of the Directive

34 In relation to Article 2(5) of the Directive, ESA submits in its reply that Iceland, following its letter of 16 July 2012 concerning the implementation of this provision, changed its opinion in an email of 15 August 2012. In that email, the Ministry of Economic Affairs stated that "after closely looking at FME rules No 215/2007 and 216/2007, the Ministry agrees with ESA that a special provision or an 'anti-avoidance rule' similar to Article 2 paragraph 5 of the Directive cannot be found in the aforementioned rules or Act No 161/2002". ESA states that since this email exchange it has received no further information concerning any measure adopted to implement Article 2(5) of the Directive. The national legislation has remained unchanged and is insufficient to implement the provision. Moreover, on a substantive comparison between Article 2(5) of the Directive and Article 30(1), (2) and (4) of Icelandic Act No 161/2002, it is clear that those provisions do not implement the provision in the Directive.

35 ESA states that it agrees with Iceland's interpretation of Article 2(5) of the Directive, namely, that it aims to ensure that the competent authorities of the State establish procedures to prevent financial undertakings from deliberately avoiding the additional capital requirements that they would otherwise incur on exposures exceeding the limit laid down in Article 111(1) of Directive 2006/48/EC once those exposures have been maintained for more than 10 days. ESA submits that the appropriate implementing measures would therefore consist, as was also suggested by Iceland in its email of 15 August 2012, in anti-avoidance rules aimed at preventing such situations from occurring.

36 ESA submits that Article 30(1) of Act No 161/2002 does not implement Article 2(5) of the Directive, but simply implements Article 111(1) of Directive 2006/48/EC into the Icelandic legal order. While Article 2(5) of the Directive refers to Article 111(1) of Directive 2006/48/EC, it sets out obligations which go beyond the mere incorporation of that article into national law.

37 Moreover, Article 30(2) and (4) of Act No 161/2002 do not contain any form of rules or procedures which aim to prevent financial undertakings from escaping the additional capital requirements that they would otherwise incur in the case of specific types of over-exposure. Article 30(4) of Act 161/2002 merely provides that the FME should be informed without delay after a financial undertaking incurs an over-exposure. ESA submits that this procedure cannot be interpreted as an anti-avoidance rule.

38 Therefore, ESA concludes that the measures listed by Iceland in its defence do not implement Article 2(5) of the Directive.

Article 2(6) of the Directive

39 In relation to Article 2(6) of the Directive, ESA notes in its reply that Iceland has submitted in its defence that this provision has been implemented by way of Article 84(3) of Act No 161/2002 and also by Articles 1 and 3 of FME Rules No

215/2007 on the capital requirements and risk weighted assets of financial undertakings. ESA observes that in the letter from the Ministry of Economic Affairs to ESA of 16 July 2012, which is relied upon by Iceland, the Ministry wrote: "Article 2 paragraph 6 has partly been implemented into Icelandic legal order with Article 117 and Article 84(3) of the Icelandic Act No 161/2002 on Financial Undertakings" and "[t]he term 'investment firm' needs to be strengthened in the Icelandic Act No 161/2002 on Financial Undertakings and the FME rules on additional own funds items for financial undertakings to fully implement the provisions of Article 2 paragraphs 6 and 7".

40 ESA submits that Iceland has done more than merely looking into the definition of the term "investment firm" and, instead, admitted that this term needs to be strengthened through the adoption of additional legislation in order to implement in full Article 2(6) of the Directive. However, the matter of the definition and interpretation of the term "investment firm" was not addressed in the subsequent correspondence.

41 ESA notes Iceland's change of position on the matter of the definition and interpretation of the term "investment firm". It observes that the defence states that "after further study into the aforementioned terms it was concluded that the Icelandic legal order complies with Article 2(6) of the Directive on the basis that 'verðbréfafyrirtæki' and other similar companies with limited authorisation are compatible with the term 'investment firm' in Article (6) [*sic*] of the Directive". However, ESA asserts that no additional information has been provided on the study undertaken by Iceland which could explain how it came to the conclusion that the term "investment firm" is now sufficiently clear to fully implement Article 2(6) of the Directive. ESA finds itself therefore unable to assess how well founded such a new interpretation is.

42 ESA emphasises that the need for clear and detailed reasoning is particularly important as the national legislation has remained unchanged since the letter of 16 July 2012 was sent and Iceland has not identified any other provision of national law with which to justify the conclusion that strengthening of the term "investment firm" is no longer necessary and, consequently, that Article 2(6) of the Directive is fully implemented.

43 ESA submits therefore that this plea lacks sufficient clarity and precision since Iceland has not clearly specified how the national provisions on which it relies fully implement Article 2(6) of the Directive.

44 Additionally, ESA submits Iceland's notification has come very late in the procedure and it maintains its plea that Article 2(6) was not fully implemented before the expiry of the time limit set out in the reasoned opinion.

Iceland

45 In its defence, the Iceland states that it considers Article 2(5) and (6) of the Directive to have been implemented into the national legal order and that both

provisions are, and were by 12 November 2012, so implemented. This view was communicated to ESA in the letter from the Ministry of Economic Affairs of 16 July 2012 as regards Article 2(5) of the Directive. Iceland concedes that the letter is less clear as regards the implementation of Article 2(6) of the Directive, as it notes only partial implementation.

Article 2(5) of the Directive

46 Iceland submits that, as mentioned in the letter from the Ministry of Foreign Affairs of 16 July 2012, Article 2(5) of the Directive is implemented by way of Article 30(1), (2) and (4) of Act No 161/2002 on financial undertakings.

47 Iceland submits that, according to Article 2(5) of Directive 2009/111/EC, the competent authorities shall establish procedures to prevent institutions from deliberately avoiding the additional capital requirements that they would otherwise incur, on exposures exceeding the limit laid down in Article 111(1) of Directive 2006/48/EC once those exposures have been maintained for more than 10 days, by means of temporarily transferring the exposures in question to another company, whether within the same group or not, and/or by undertaking artificial transactions to close out the exposure during the 10-day period and create a new exposure.

48 Iceland submits that Article 30(1) of Act No 161/2002 on financial undertakings *inter alia* implements Article 111(1) of Directive 2006/48/EC into the Icelandic legal order. It states that a financial undertaking cannot incur an exposure to a client or a group of connected clients that exceeds 25% of its own funds. According to Article 30(4) of the same Act, a financial undertaking must notify the FME without delay if it incurs an exposure that exceeds the 25% limit. Article 30(2) of Act No 161/2002 on financial undertakings is a rule of evidence. It states that if there is any doubt as to the parties that belong to a group of connected clients a financial undertaking is required to link the parties unless the financial undertaking can demonstrate the contrary. An exposure described in Article 2(5) of the Directive should thus be informed to the FME without delay as stated in Article 30(4) of Act No 161/2002 on financial undertakings and, should such an exposure be transferred, Article 30(2) of the same Act places the burden of proof with the financial undertaking that clients are not connected.

49 In its rejoinder, Iceland submits that the Icelandic legislation on the controlling and monitoring of large exposures already contains the elements needed to prevent the situation occurring that Article 32(1) of Directive 2006/49/EC (i.e. Article 2(5) of Directive 2009/111/EC) aims to prevent and that Iceland does not require an additional specific anti-avoidance rule of the kind described by ESA in its reply for the Icelandic legal order to comply with Article 2(5) of the Directive. Therefore, Iceland maintains that the Icelandic legal order complies with Article 2(5) of the Directive.

50 In its rejoinder, Iceland submits that a proper reading of Article 2(5) of the Directive as regards its placing in Directive 2006/49/EC implies that the

provision is not intended to prevent credit institutions from having exposures exceeding the limit laid down in Article 111(1) of Directive 2006/48/EC, but to prevent credit institutions from deliberately avoiding additional capital requirements once the 25% limit laid down in Article 111(1) of Directive 2006/48/EC has been exceeded, when those permitted exposures have exceeded the limit for more than 10 days, for example, by transferring the exposure to a special purpose vehicle or transferring it to another entity within the same group in order to close out the exposure and create another exposure.

51 Iceland submits that, if an exposure exceeds the 25% limit allowed for in Article 31(a) to (e) of Directive 2006/49/EC, an Icelandic credit institution can apply for a written permit to hold this exposure "within a time limit laid down by the FME for up to 10 days" as stated in Article 47 of FME Rules No 215/2007.

52 Thus, according to the Icelandic legislation, all exposures exceeding the 25% limit shall be notified to the FME when they occur, a credit institution needs to have a written permit for each exposure and additional capital requirements are calculated from the time an exposure exceeds the 25% limit "but not after 10 days have passed." Consequently, according to Iceland, the Icelandic legislation is more stringent than the rules laid down in Section 4 of Chapter V of Directive 2006/49/EC, including Article 2(5) of the Directive. Furthermore, if a credit institution does not notify the FME of an exposure exceeding the limit laid down in Article 30(1) of Act No 161/2002, at the time when it is incurred, the FME can sanction the credit institution by way of fines or withdraw its authorisation.

53 Iceland submits therefore that the Icelandic legislation on the controlling and monitoring of large exposures already contains the elements needed to prevent the situation occurring that Article 2(5) of Directive 2009/111/EC aims to prevent and that Iceland does not require any additional specific anti-avoidance rule of the kind described by ESA in its reply for the Icelandic legal order to comply with Article 2(5) of the Directive.

Article 2(6) of the Directive

54 As regards Article 2(6) of the Directive, according to Iceland, it is implemented by way of Article 84(3) of Act No 161/2002 on financial undertakings and also by Articles 1 and 3 of FME Rules No 215/2007 on the capital requirements and risk weighted assets of financial undertakings. As stated in the letter of 16 July 2012 from the Ministry of Economic Affairs, the Ministry was looking into the definition of the term "investment firm". This was because of "the correlation between the Icelandic term 'verðbréfafyrirtæki' (which is translated as 'securities company/undertaking' in the unofficial translation in English) and other similar companies which have limited authorisation as described in Article 4 of Act No 161/2002 on Financial Undertakings and the term 'investment firm' mentioned in Article 2(6) of the said Directive".

55 Article 2(6) of the Directive requires "investment firms" to be covered by the uniform formats, frequencies and dates of reporting referred to in Article 74(2) of

Directive 2006/48/EC. Iceland submits that, after further study, it was concluded that the Icelandic legal order complies with Article 2(6) of the Directive on the basis that "verðbréfafyrirtæki" and other similar companies with limited authorisation are compatible with the term "investment firm" in Article 2(6) of the Directive.

56 Iceland submits, therefore, that Article 84(3) of Act No 161/2002 on financial undertakings and Articles 1 and 3 of FME Rules No 215/2007 on the capital requirements and risk weighted assets of financial undertakings are thus in compliance with Article 2(6) of the Directive, as, according to the aforementioned provisions, Icelandic securities undertakings/companies (i.e. "verðbréfafyrirtæki") shall report to the FME on capital requirements at least every month and other types of securities companies/undertakings, as described in Article 3 of FME Rules No 215/2007, shall report on capital requirements at least every quarter or at least every 6 months. Iceland acknowledges that ESA was not informed of this conclusion.

57 In its rejoinder, Iceland takes note of ESA's "call for further information" as to how Iceland came to the conclusion that the term "verðbréfafyrirtæki" and other similar companies, i.e. those companies that have limited authorisations according to Article 3(1)(6) of Act No 161/2002, are compatible with the term "investment firm" in Article 2(6) of the Directive.

58 First, Iceland contends that the English translation of Act No 161/2002 submitted with the defence is inaccurate as it does not reflect recent amendments made to the Act which changed, *inter alia*, the numbering of some of the provisions referred to in this section. Iceland thus requests that the Icelandic version of Act No 161/2002 be used for reference in this regard.

59 In its rejoinder, Iceland observes that Article 2(6) of the Directive states that "investment firms shall be covered by the uniform formats, frequencies and dates of reporting referred to in Article 74(2) of Directive 2006/48/EC". The term "investment firm" is defined in Article 3(1)(b) of Directive 2006/49/EC by reference to the institutions defined in Article 4(1)(1) of Directive 2004/39/EC and which are subject to the requirements imposed by Directive 2004/39/EC.

60 Iceland notes that Article 4(1)(1) of Directive 2004/39/EC defines investment firms as meaning any legal person whose regular occupation or business is the provision of one or more investment services to third parties and/or the performance of one or more investment activities on a professional basis. "Investment services and activities" are further defined in Article 4(2) of Directive 2004/39/EC as meaning any of the services and activities listed in Section A of Annex I to the same Directive relating to any of the instruments listed in Section C of Annex I.

61 Iceland submits that Directive 2004/39/EC was implemented into the Icelandic legal order by Act No 108/2007 on securities transactions. However, Directive 2004/39/EC also required certain additional types of financial activities

(investment activities) to obtain operating licences. The implementation of Directive 2004/39/EC thus also led to changes to Act No 161/2002 on financial undertakings.

62 Iceland observes that the scope of Act No 108/2007 on securities transactions is defined in Article 1 of that same Act. Article 1 of Act No 108/2007 is built on Section A of Annex I to Directive 2004/39/EC. According to Article 3(1)(6) of Act No 161/2002 on financial undertakings, the activities and services covered by Act No 108/2007 on securities transactions are subject to operating licences. Article 3(1)(6)(a) to (g) also lists the activities and services listed in Section A of Annex I to Directive 2004/39/EC. Article 4(1)(5) of Act No 161/2002 notes that the operating licences on the basis of Article 3(1)(6) are awarded to "verðbréfafyrirtæki".

63 Iceland states that the Icelandic authorities came to the conclusion therefore that the term "verðbréfafyrirtæki" is compatible with the term "investment firms" within the meaning of Article 4(1)(1) of Directive 2004/39/EC and, accordingly, also Article 2(6) of Directive 2009/111/EC.

64 In its rejoinder, Iceland makes submissions on the obligation to inform ESA that Article 2(5) and (6) of the Directive were implemented into the Icelandic legal order. It notes that the defence stated that ESA was informed of the implementation in relation to Article 2(5). Given the wording of the email of 15 August 2012, it acknowledges that it is understandable that confusion arose regarding the status of the implementation of Article 2(5). As regards Article 2(6), the defence acknowledges that ESA was only informed of "partial implementation".

65 Iceland requests the Court to order each party to bear its own costs of the proceedings, due to the circumstances of the case.

VI Findings of the Court

66 Article 3 EEA imposes upon the Contracting Parties the general obligation to take all appropriate measures, whether general or particular, to ensure fulfilment of the obligations arising out of the EEA Agreement (see, *inter alia*, Case E-11/13 *ESA* v *Iceland*, judgment of 15 November 2013, not yet reported, paragraph 19, and case law cited).

67 It follows from Article 7 EEA that an act corresponding to an EU directive referred to in the Annexes to the EEA Agreement or in decisions of the EEA Joint Committee shall be binding, as to the result to be achieved, upon the Contracting Parties and be made part of their internal legal order leaving the authorities of the Contracting Parties the choice of form and method of implementation. The Court notes that the implementation of a directive does not necessarily require legislative action in each EEA State, as the existence of statutory provisions and general principles of law may render the implementation

by specific legislation superfluous (see Case E-15/12 *Wahl*, judgment of 22 July 2013, not yet reported, paragraph 49).

68 An obligation to implement the Directive, and to notify ESA thereof, also follows from Article 4 of the Directive. Fulfilment of this obligation is of crucial importance for securing the two fundamental EEA law principles of homogeneity and reciprocity.

69 Accordingly, the implementation of a directive into domestic law does not necessarily require the provisions of the directive to be enacted in precisely the same words in a specific, express provision of national law and a general legal context may be sufficient provided it actually ensures the full application of the directive (see, Case E-15/12 *Wahl,* cited above, paragraph 50).

70 However, provisions of directives must be implemented with unquestionable binding force and the specificity, precision and clarity necessary to satisfy the requirements of legal certainty. EEA States must ensure full application of directives not only in fact but also in law (see, Case E-15/12 *Wahl,* cited above, paragraph 51 and case law cited).

71 It is essential that the legal situation resulting from national implementing measures be sufficiently precise and clear and that individuals be made fully aware of their rights so that, where appropriate, they may rely on them before the national courts. The latter condition is of particular importance where the directive in question is intended to confer rights on nationals of other EEA States, as is the case here, as those nationals may not be aware of provisions and principles of national law (see, Case E-15/12 *Wahl,* cited above, paragraph 52).

72 In that regard, it must also be borne in mind that it is clear from case law with regard to the implementation of directives that mere administrative practices, which by their nature are alterable at will by the authorities and are not given the appropriate publicity, cannot be regarded as constituting the proper fulfilment of an EEA/EFTA State's obligations under the EEA Agreement (see Case E-15/12 *Wahl,* cited above, paragraph 53).

73 Moreover, Article 3 EEA requires the EEA States to take all measures necessary, regardless of the form and method of implementation, to ensure that a directive which has been implemented and satisfies the conditions set out above prevails over conflicting national law and to guarantee the application and effectiveness of the directive. The Court has consistently held that it is inherent in the objectives of the EEA Agreement that national courts are bound to interpret national law in conformity with EEA law. Consequently, they must apply the methods of interpretation recognised by national law in order to achieve the result sought by the relevant EEA rule. The Court recalls that the EEA States may not apply rules which are liable to jeopardise the achievement of the objectives pursued by a directive and, therefore, deprive it of its effectiveness (see, Case E-15/12 *Wahl,* cited above, paragraph 54 and case law cited).

74 Finally, it must be added that it is inherent in the general objective of the EEA Agreement of establishing a dynamic and homogeneous market, in the ensuing emphasis on the judicial defence and enforcement of the rights of individuals, as well as in the principle of effectiveness, that, when interpreting national law, national courts will consider any relevant element of EEA law, whether implemented or not.

75 Decision 85/2010 of the EEA Joint Committee of 2 July 2010 entered into force on 1 January 2012, being the latest of the three alternative dates set by Article 3 of Decision 85/2010. The time limit for EEA/EFTA States to adopt the measures necessary to implement the Directive expired on the same date. Article 3 of Decision 85/2010 did not set a separate EEA time limit for the implementation of the Directive into national law.

76 The question of whether an EFTA State has failed to fulfil its obligations must be determined by reference to the situation in that State as it stood at the end of the period laid down in the reasoned opinion (see, *inter alia*, *ESA* v *Iceland*, cited above, paragraph 21, and case law cited).

77 As regards Article 1 paragraphs 15 to 18, 19(a), 21, 22(a), 23 to 28, 36, 37, and 39 to 42 of the Directive, it is undisputed that Iceland did not adopt and notify to ESA the measures necessary to implement those provisions before the expiry of the time limit given in the reasoned opinion.

78 It must therefore be held that by failing, within the time limit prescribed, to adopt and notify to ESA the measures necessary to implement Article 1 paragraphs 15 to 18, 19(a), 21, 22(a), 23 to 28, 36 to 37, and 39 to 42 of the Directive, Iceland has failed to fulfil its obligations pursuant to Article 4 of the Directive and Article 7 EEA.

Article 2(5) of the Directive

79 Article 2(5) of the Directive amends Directive 2006/49/EC by replacing the first subparagraph of Article 32(1) of the latter Directive.

80 Consequently, the EEA States are required to ensure, pursuant to Article 7(b) EEA, that their competent authorities shall establish procedures to prevent institutions from deliberately avoiding the additional capital requirements that they would otherwise incur, on exposures exceeding the limit laid down in Article 111(1) of Directive 2006/48/EC (i.e. an exposure to a client or group of connected clients the value of which exceed 25 % of its own funds) once those exposures have been maintained for more than 10 days, by means of temporarily transferring the exposures in question to another company, whether within the same group or not, and/or by undertaking artificial transactions to close out the exposure during the 10-day period and create a new exposure.

81 In essence, Iceland argues that there was no need for it to enact an anti-avoidance rule as proposed by ESA because its legislation was already in conformity with what is required by Article 2(5) of the Directive.

82 At this point, it should be recalled that in proceedings pursuant to Article 31 SCA for failure to fulfil obligations, it is incumbent upon ESA to prove the allegation that the obligation has not been fulfilled. It is ESA's responsibility to place before the Court the information needed to enable the Court to establish that the obligation has not been fulfilled, and in so doing ESA may not rely on any presumption (compare, to this effect, Case 96/81 *Commission* v *Netherlands*, [1982] ECR 1791, paragraph 6).

83 However, the EEA/EFTA States are required, pursuant to Article 3 EEA, to facilitate the achievement of ESA's tasks (compare, to this effect, Case C-494/01 *Commission* v *Ireland* [2005] ECR I-3331, paragraph 42). It follows in particular that, where ESA has adduced sufficient evidence of certain matters in the territory of the defendant EEA/EFTA State, it is incumbent on the latter to challenge in substance and in detail the information produced and the consequences flowing therefrom (compare, *Commission* v *Ireland*, cited above, paragraph 44).

84 Iceland has not demonstrated that the provisions of Article 30 (1), (2) and (4) of Act No 161/2002, whether read individually or collectively, are such as to prevent institutions from deliberately avoiding the additional capital requirements that they would otherwise incur on exposures in excess of 25% of their own funds if those exposures have been maintained for more than 10 days in a manner compliant with the requirements of Article 2(5) of the Directive. There is no element which addresses the matter of prevention as laid down by the Directive.

85 In light of paragraphs 66 to 74 and 76 above, it must thus be held that, by failing, within the time limit prescribed, to adopt and notify to ESA the measures necessary to implement Article 2(5) of the Directive, Iceland has failed to fulfil its obligations pursuant to Article 4 of the Directive and Article 7 EEA.

Article 2(6) of the Directive

86 Iceland has submitted in its defence on this point that it concluded after further study into the term "investment firm" that the Icelandic legal order was already compatible with Article 2(6) of the Directive on the basis that "verðbréfafyrirtæki" and other similar companies with limited authorisation are compatible with that term.

87 Iceland in its rejoinder has contended that "investment firms" are defined in Article 3(1)(b) of Directive 2006/49/EC by reference to the institutions defined in Article 4(1)(1) of Directive 2004/39/EC. Iceland has further referred to the definition of "investment services and activities" in Article 4(1)(2) of Directive 2004/39/EC which further refers to Annex I, Sections A and C of that Directive.

88 Iceland has submitted that Directive 2004/39/EC was implemented into the Icelandic legal order by Act No 108/2007 on securities transactions, which required, *inter alia*, that investment activities be subject to operating licences. The implementation of Directive 2004/39/EC therefore led to changes to Act No 161/2002.

89 Iceland has concluded that pursuant to Article 4(1)(5) of Act No 161/2002, operating licences are awarded to "verðbréfafyrirtæki" on the basis of Article 3(1)(6) of Act No 161/2002. Therefore "verðbréfafyrirtæki", it asserts, is compatible with the term "investment firms" within the meaning of Article 4(1)(1) of Directive 2004/39/EC and, accordingly, also Article 2(6) of the Directive.

90 The meaning of "investment firms" is defined by Article 3(1)(b) of Directive 2006/49/EC read in conjunction with Article 3(1)(p) of Directive 2006/49/EC and Article 4(1)(1) of Directive 2004/39/EC as set out in paragraphs 3 to 5 above.

91 The term "investment services and activities" is defined in Article 4(1)(2) of Directive 2004/39/EC and is mentioned in the first paragraph of Article 4(1)(1) of Directive 2004/39/EC. However its meaning is not synonymous with the term "investment firm".

92 Consequently, Iceland has failed to demonstrate that "verðbréfafyrirtæki" encompasses the meaning of the term "investment firm". It must thus be held that by failing, within the time limit prescribed, to adopt and notify to ESA the measures necessary to implement Article 2(6) of the Directive, Iceland has failed to fulfil its obligations pursuant to Article 4 of the Directive and Article 7 EEA.

VII Costs

93 Under Article 66(2) RoP, the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings. Since the EFTA Surveillance Authority has requested that Iceland be ordered to pay the costs, and the latter has been unsuccessful, and none of the exceptions in Article 66(3) apply, Iceland must therefore be ordered to pay the costs.

On those grounds,

THE COURT

hereby:

1. **Declares that by failing to implement correctly Article 1 paragraphs 15 to 18, 19(a), 21, 22(a), 23 to 28, 36, 37, 39 to 42 and Article 2 paragraphs 5 and 6 of the Act referred to at points 14, 16e and 31 of Annex IX to the Agreement on the European Economic Area (Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements and crisis management), as adapted to the EEA Agreement by way of Protocol 1 thereto, within the time prescribed, and by failing to inform the Authority of the text of such measures, Iceland has failed to fulfil its obligations under the Act and under Article 7 of the EEA Agreement.**

2. **Orders Iceland to bear the costs of the proceedings.**

Carl Baudenbacher Per Christiansen Páll Hreinsson

Delivered in open court in Luxembourg on 11 February 2014.

Gunnar Selvik
Registrar

Carl Baudenbacher
President