ADVISORY OPINION OF THE COURT

10 December 1998*

(Council Directive 80/987/EEC – Incorrect implementation of a directive – Liability of an EFTA State)

In Case E-9/97

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 (Reykjavik City Court) for an Advisory Opinion in the case pending before it between

Erla María Sveinbjörnsdóttir

and

The Government of Iceland

on the interpretation of Article 6 of the EEA Agreement and Council Directive 80/987/EEC, as amended by Council Directive 87/164/EEC, and referred to in Point 24 of Annex XVIII to the EEA Agreement.

THE COURT,

composed of: Bjørn Haug (Judge-Rapporteur), President, Thór Vilhjálmsson and Carl Baudenbacher, 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, Erla María Sveinbjörnsdóttir, represented by Counsel Stefán Geir þórisson, Lögmenn Klapparstíg;

– the defendant, the Government of Iceland, represented by Counsel Árni Vilhjálmsson, Adelsteinsson & Partners, assisted by Martin Eyjólfsson, Legal Officer, Ministry for Foreign Affairs;

– the Government of Norway, represented by Jan Bugge-Mahrt, Assistant Director General, Royal Ministry of Foreign Affairs, acting as Agent;

– the Government of Sweden, represented by Erik Brattgård, Director, Ministry for Foreign Affairs, acting as Agent;

– the Government of the United Kingdom, represented by Dawn Cooper, Treasury Solicitor's Department, acting as Agent;

– the EFTA Surveillance Authority, represented by Håkan Berglin, Director, Legal & Executive Affairs Department, acting as Agent and assisted by Bjarnveig Eiriksdóttir and Anne-Lise H. Rolland, Officers of that Department;

– the Commission of the European Communities (hereinafter "EC Commission"), represented by Peter Jan Kuijper and Dimitrios Gouloussis, both Legal Advisers in its Legal Service, acting as Agents;

having regard to the Report for the Hearing,

after hearing the oral observations of the plaintiff, the defendant, the Government of Norway, the Government of Sweden, represented by Anders Kruse, Director General, Ministry for Foreign Affairs, the EFTA Surveillance Authority and the EC Commission at the hearing on 17 September 1998,

gives the following

Advisory Opinion

Facts and procedure

1 By an order dated 5 November and a request dated 12 November 1997, registered at the Court on 18 November 1997, Héraðsdómur Reykjavíkur (Reykjavik City Court) of Iceland made a request for an Advisory Opinion in a case pending before it between Erla María Sveinbjörnsdóttir, plaintiff, and the Government of Iceland, defendant.

2 Ms Sveinbjörnsdóttir, the plaintiff in the case before the national court, had been employed for a number of years at a machine workshop when she was dismissed from her position by a letter of 29 December 1994 with effect from 1 January 1995. The plaintiff was dismissed with six months' notice and was not required to work during the notice period. The plaintiff received her wages until 12 March 1995. On 22 March 1995, the machine workshop was declared insolvent.

3 Ms Sveinbjörnsdóttir filed claims against both the insolvency estate of the machine workshop and the Icelandic Wage Guarantee Fund, claiming payment of wages for the notice period, unpaid wage increases, vacancy pay from 1 May 1994 to the end of the notice period, *i.e.* until 30 June 1995, vacancy pay supplement and a December wage supplement, in total 743 844 Icelandic crowns. Both claims were subsequently rejected.

4 The claim against the insolvency estate was rejected on the grounds that the plaintiff was the sister of the holder of 40% of the shares in the machine workshop, so that her claim could not be given privileged status. Reference was made to Article 112 in conjunction with Article 3 of the Icelandic Insolvency Act (*Lög um gjaldþrotaskipti* – Act No. 21/1991) (hereinafter the "Insolvency Act"). Article 112 of the Insolvency Act provides that claims for unpaid wages, etc. are, as a general rule, privileged but makes an exception for claims by persons "close" to the insolvent entity. The expression "close" is defined in Article 3 of the Insolvency Act and comprises *inter alia* the relationship between a person and a company owned to a considerable extent by a another person to whom the first person is "related through direct descent or collateral relation".

5 The claim against the Wage Guarantee Fund was rejected on the grounds that the plaintiff's claim had not been recognized as a privileged claim in the insolvency estate. Reference was also made to Article 5, first paragraph, and Article 6 of the Wage Guarantee Fund Act (*Lög um ábyrgðasjóð launa vegna gjaldþrota* – Act No. 53/1993) (hereinafter the "Wage Guarantee Fund Act"). Article 5, first paragraph of that Act provides that the guarantee covers claims for unpaid wages, etc. "which have been recognized as privileged claims under the Insolvency Act". Article 6 excludes from the scope of the Wage Guarantee Fund *inter alia* claims from persons who have held 5% or more of the share capital in an

insolvent joint-stock company, and claims from the spouse of such a person "and also his relatives in direct line of descent and the spouse of any relative in direct line of descent".

6 The plaintiff then brought an action for compensation against the Government of Iceland with a writ of summons served on the defendant on 12 March 1997. In the writ of summons the plaintiff submitted that the Government is liable for damages for not having adjusted its national legislation correctly to the EEA Agreement, *i.e.* for not having adapted national legislation (Article 5, first paragraph, and Article 6 of the Wage Guarantee Fund Act and Article 112, third paragraph, of the Insolvency Act, cf. Article 3 of that Act) correctly to the act referred to in point 24 of Annex XVIII to the EEA Agreement.

7 Considering that it was necessary to interpret provisions of the EEA Agreement in order for it to reach a decision and pursuant to Article 34 of the Surveillance and Court Agreement, Héraðsdómur Reykjavíkur submitted a request to the EFTA Court for an Advisory Opinion on the following questions:

> *1. Is the act referred to in point 24 of Annex XVIII to the EEA Agreement (Council Directive 80/987/EEC of 20 October 1980, as amended by Council Directive 87/164/EEC of 2 March 1987), in particular Article 1, paragraph 2, and Article 10 of the Directive, to be interpreted to mean that national legislation may provide that an employee may be precluded from receiving payment of a wage claim against an insolvency estate from the State's Wage Guarantee Fund on grounds of family relation to an owner of 40% of the shares in the insolvent company. The relevant relation in the case at hand is collateral, i.e. siblings?*
>
> *2. If the answer to question 1 is to the effect that such an employee may not be precluded from receiving payment of a wage claim, is the State liable vis-à-vis the employee for not having adapted national legislation when it became party to the EEA Agreement, so that the employee has a legal right to the payment of the wage claim?*

8 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.

Legal background

EEA law

9 Council Directive 80/987/EEC of 20 October 1980 on the approximation of the laws of the Member States relating to the protection of employees in the event of the insolvency of their employer, as amended by Council Directive 87/164/EEC (hereinafter the "Directive"), is referred to in Point 24 of Annex XVIII to the Agreement on the European Economic Area (hereinafter variously "EEA" and the "EEA Agreement").

10 Article 1 of the Directive reads:

> "1. This directive shall apply to employees' claims arising from contracts of employment or employment relationships and existing against employers who are in a state of insolvency within the meaning of Article 2(1).
>
> 2. Member States may, by way of exception, exclude claims by certain categories of employee from the scope of this directive, by virtue of the special nature of the employee's contract of employment or employment relationship or of the existence of other forms of guarantee offering the employee protection equivalent to that resulting from this directive.
>
> The categories of employee referred to in the first subparagraph are listed in the Annex.
>
> 3. This directive shall not apply to Greenland. This exception shall be re-examined in the event of any development in the job structures in that region."

11 For the purposes of the EEA Agreement, Point 24 of Annex XVIII to the EEA Agreement, provides for, *inter alia*, the following adaptation:

> "(a) The following shall be added to section I of the Annex:
>
> ...
>
> H. ICELAND
>
> 1. Those members of the Board of Directors of a bankrupt company after the company's financial situation became considerably adverse.
>
> 2. Those having held 5% or thereover of the capital of a bankrupt limited company.
>
> 3. The general manager of a liquidated company or those others who, on account of their work with the company, had had a survey of the company's finances in such a manner that it could not be concealed from them that a company's liquidation had been impending at the time the wages were being earned.

4. The spouse of a person in a situation specified in clauses 1 to 3 as well as his/her direct relative and direct relative's spouse."

12 Article 10 of the Directive reads:

"This directive shall not affect the option of Member States:

(a) to take the measures necessary to avoid abuses;

(b) to refuse or reduce the liability referred to in Article 3 or the guarantee obligation referred to in Article 7 if it appears that fulfilment of the obligation is unjustifiable because of the existence of special links between the employee and the employer and of common interests resulting in collusion between them."

National law

13 Article 5, first paragraph, of the Icelandic Wage Guarantee Fund Act reads:

"The obligations of the fund shall extend to the following claims against an employer's estate which have been recognized as privileged claims under the Insolvency Act:

a. a wage earner's claim for wages for his last three working months spent with the employer, including the part of wages retained by the employer under Section VIII of the Act No. 86 of 1988;

b. a wage earner's claim for vacation pay which was to have been paid during his last three working months spent with the employer;

c. a claim by a recognized pension fund for pension fund premiums in arrears which fell due in the last 18 months before the deadline, providing the conditions of Section III of this Act are met; this obligation shall, however, be subject to the minimum limit stated in Article 4 of the Act No. 55 of 1980;

d. compensation for lost wages for up to three months as a consequence of the cancellation or rescission of an employment agreement, providing that the claimant under this item demonstrates by means of a declaration from an employment agency that he sought other employment during the period for which compensation is claimed;

e. compensation to a wage earner which an employer is obliged to pay in respect of damage caused by a work-related accident, or to a person who has the right to compensation in respect of the death of a wage earner, providing that the claim for compensation enjoys privilege status in the employer's estate;

f. interest under Article 5 of the Interest Act, No. 25 of 1987, on claims under items a-e from the due date of their payment to the date on which the claims are paid by the guarantee fund;

g. insurance to cover the costs of liquidation paid by wage earners or pension funds. This shall also apply to unavoidable expenses incurred by the wage earner or other claimant under item e in connection with measures necessary to secure the payment of his claim, subject, however, to a maximum determined by the fund's management board."

14 Article 6, first paragraph, of the Wage Guarantee Fund Act reads:

"However, the following wage earners may not demand payment by the fund of claims under items a-d of Article 5, paragraph 1:

a. Those who sat on the board of an insolvent enterprise after its financial position began to deteriorate substantially. ...

b. Those who have held 5% or more of the share capital in an insolvent joint-stock company.

c. The director, managing director and others who, in view of their positions with the insolvent employer, ought to have had sufficient knowledge of the enterprise's financial position for it to be clear to them that insolvency was imminent during the period during which they worked for their wages.

d. The spouse of any person covered by items a-c, and also his relatives in direct line of descent and the spouse of any relative in direct line of descent. ..."

15 According to Article 112, first paragraph, of the Insolvency Act, claims for wages and related sums have, as a general rule, privileged status in the estate of an insolvent employer. Article 112, third paragraph, makes the following exception to this main rule:

"Persons close to the insolvent entity do not enjoy the rights stipulated in 1-3 of the first paragraph relating to their claims; nor do persons who have been on the Board of the insolvent entity or were engaged in managing the insolvent entity."

16 The term "close" used in that Article is defined in Article 3 of the Insolvency Act, which reads:

"In this Act, the term "close" refers to persons having any of the following relations:

1. Married couples and common-law couples,

2. Those related through direct descent or collateral relation, including relations through adoption or fostering,

3. Those related as in point 2 through marriage or common-law marriage,

4. A person and a company or institution owned to a considerable extent by that person or someone close to that person,

5. Two companies or institutions where one is owned to a considerable extent by the other or some person closely related to it,

6. Persons, companies or institutions related in ways comparable to those in points 1-5."

The first question

17 Article 1(1) of the Directive sets out as a main rule that all employees are entitled to coverage from a national wage guarantee fund in the case of their employer's insolvency. The Directive allows for two exceptions to this main rule, set out in Articles 1(2) and 10, respectively. By its first question, the national court seeks to determine the scope of both of these exceptions, by asking whether the Directive must be interpreted so as to permit a general rule in Icelandic legislation that excludes from the scope of the wage guarantee fund siblings of an owner of 40% of the shares in an insolvent employer company.

18 The Court notes that the claims of the plaintiff relate to a period of time from 1 May 1994 until 30 June 1995. The Court finds appropriate to point out that, under the Directive, the Contracting Parties are only required to ensure payment of employees' outstanding claims for a minimum period specified in Articles 3 and 4 of the Directive. It is up to the national authorities to determine the end date, within the options set out in Article 3(2), with such guarantee periods as determined by Article 4(2). The protection of employees under the Directive is a minimum level of protection, limited to the period following the national authorities' choice. However, according to Article 9, the Directive does not prevent the Contracting Parties from applying or introducing national rules which are more favourable to employees, including rules which extend the period for which payments are to be made under the guarantee. If a Contracting Party decides to extend the protection beyond what is required by the Directive, the State concerned is free to determine the scope of such extended protection, both with regard to the periods and persons covered. Since it is not for the Court to express itself on national law, the following discussion is only relevant with regard to the minimum period specified in Articles 3 and 4.

Article 1(2) of the Directive and the adaptation in Point 24 of Annex XVIII to the EEA Agreement

19 As mentioned above, Article 1(2) of the Directive provides that Member States may, by way of exception, exclude claims by certain categories of employee from the scope of the Directive, by virtue of the special nature of the employee's contract of employment or employment relationship or of the existence of other forms of guarantee offering the employee protection equivalent to that resulting from the Directive.

20 It follows from the second subparagraph of Article 1(2) that the categories of employee referred to in the first subparagraph are listed in the Annex. For the purposes of the EEA Agreement, the Annex to the Directive has been adapted by virtue of Point 24 of Annex XVIII of the EEA Agreement, which sets out certain exceptions applicable with regard to Iceland.

21 One question that arises is whether a Contracting Party to the EEA Agreement may only rely on Article 1(2) in so far as an appropriate listing has been made in the Annex to the Directive. The *Government of Norway* argues that the listings in the Annex are not exhaustive and that a Contracting Party may exclude claims from certain categories of employee, provided that the conditions in the first subparagraph of Article 1(2) are fulfilled. By contrast, the *EFTA Surveillance Authority* and the *EC Commission* both submit that the listings in the Annex are exhaustive.

22 In the opinion of the *Court*, it follows both from the aim of the Directive, which is to provide a minimum level of protection for all employees, and from the exceptional nature of the possibility of exclusion allowed for by Article 1(2) of the Directive, that that provision cannot be interpreted broadly in the manner contended by the Government of Norway. It follows from the wording of the Directive that the Contracting Parties may only exercise the right to exclude certain categories of employee by virtue of Article 1(2) of the Directive in so far as the exceptions are listed in the Annex to the Directive. This interpretation is further supported by the fact that the Annex would be deprived of much of its purpose if the Contracting Parties were free to exclude categories of employee not listed there.

23 With this as a starting point, it becomes necessary to examine the scope of the exceptions with regard to Iceland which are actually listed in the Annex. Item H 2 in the Annex excludes from the scope of the Directive "[t]hose having held 5% or thereover of the capital of a bankrupt limited company". Item H 4 further excludes "[t]he spouse of a person in a situation specified in clauses 1 to 3 as well as his/her direct relative and direct relative's spouse". Thus, the question is whether the expression "direct relative" in H 4 can be interpreted so as to include the sister of a person referred to in item H 2.

24 The *plaintiff*, the *EFTA Surveillance Authority* and the *EC Commission* submit that the expression contained in the Icelandic listing must be interpreted as not comprising siblings. The *defendant* contends that siblings are indeed covered by

the listing. In both cases, arguments are related to the wording of the listing and the purpose of the entry made by Iceland.

25 As for the wording of the exceptions, the Court notes that the negotiations were conducted and the final text agreed in the English language. The chosen wording "direct relative" is not entirely precise but is, on a wide interpretation, capable of including siblings.

26 The Court further notes that in the subsequent translation of the agreed English wording into the other authentic language versions, there are variations in the precision and scope of the wording. The majority of the language versions use non-committal terms corresponding to "direct relatives" or "close relatives" which are capable of being interpreted as including siblings. Some language versions (the Icelandic, Finnish, French, German, Greek and Spanish) use more specific and restrictive terms to include only relatives in direct line of ascent or descent.

27 The translation into Greek may be an example of how such discrepancies in scope may arise. At the oral hearing, it was explained that the Greek version uses an expression comparable to "direct relative" which, however, in Greek legal terminology has the distinct meaning of "ascendants or descendants". In other words, by the intervention of Greek legal terminology, an accurate translation of the original English version is given a more specific and possibly narrower content than the Contracting Parties may actually have agreed.

28 In the case of differing authentic language versions, a preferred starting point for the interpretation will be to choose one that has the broadest basis in the various language versions. This would imply that the provision, to the largest possible extent, acquires the same content in all Member States. With respect to provisions applicable in all Member States, this is a preferable situation. However, in the present situation, it is not a question of a generally applicable provision but of an exception applicable to Iceland only, and of the certain freedom the Icelandic authorities had in choosing which exceptions it preferred to implement in national law. In such circumstances, it appears to be more appropriate to place greater weight on what the negotiators agreed to with respect to the Icelandic exceptions.

29 The Court notes that the Icelandic legislation has contained exceptions identical to those currently found in the Wage Guarantee Fund Act and the Insolvency Act since 1985. There is no indication that the Icelandic authorities intended to narrow the scope of the exceptions in national law in connection with the implementation of the EEA Agreement. It must therefore be presumed that the aim was to maintain the exceptions already established in Icelandic legislation. The Court further notes that such a scope of the Icelandic exceptions would lie within the latitude of choice available to the Contracting Parties.

30 However, it must be noted that the chosen English wording “direct relative” is not clear, and that the authentic Icelandic version (“ættingi í beinan legg”) has the clear and limited scope of ascendants and descendants, excluding siblings.

31 The Court further notes that, if the Icelandic listing is interpreted as not including siblings, this would mean that Iceland has made an entry in the Annex which is not sufficiently wide to cover the exceptions that were actually in force in its national legislation. Although this might seem unlikely, a possible explanation could be that it was overlooked at the time of the EEA negotiations that the Icelandic legislation actually contains two sets of exceptions – in the Wage Guarantee Fund Act and in the Insolvency Act. Item H in the Annex corresponds closely to Article 6, first paragraph, of the Wage Guarantee Act, and, when Iceland subsequently notified the implementation of the Directive to the EFTA Surveillance Authority, reference was only made to the Wage Guarantee Act and not to the Insolvency Act.

32 On the balance, the Court finds that the expression “direct relative” in item H 4 in Point 24 of Annex XVIII must be interpreted as referring only to relatives in direct line of ascent or descent. Consequently, siblings are not covered by the expression.

33 For the sake of good order, the Court points out that the Government of Iceland, in the proceedings before the Court, has also invoked the entry in item H 3 of point 24 of Annex XVIII as a basis for rejecting the plaintiff’s claim against the wage guarantee fund. Since the questions referred to the Court and the statements of facts only address the interpretation of the Directive with regard to the plaintiff’s status as sister of a main shareholder, the Court does not find it appropriate to express its view on the interpretation of item H 3.

Article 10 of the Directive

34 According to Article 10 of the Directive, the Directive does not affect the option of Member States to take the measures necessary to avoid abuses (Article 10(a)), or to refuse or reduce the liability otherwise provided for by the Directive if it appears that fulfilment of the obligation is unjustifiable because of the existence of special links between the employee and the employer and of common interests resulting in collusion between them (Article 10(b)). Both Article 10(a) and Article 10(b) have been invoked in the present case as a possible basis for the rule in Icelandic legislation that siblings of a major shareholder in an insolvent company are excluded from the coverage of the wage guarantee fund.

Article 10(a)

35 The Court has previously held that, having regard to the social objective of the Directive and taking into account the nature of the provision in Article 10(a) as an exception, the option to take measures to avoid abuses cannot be interpreted as generally permitting any kind of measure which may assist in preventing abuses of the system: see Case E-1/95 *Samuelsson* [1994-95] EFTA Court Report 145, paragraph 31 *et seq*. As with all provisions under which a State may adopt measures which derogate from the main principles of a Directive to the detriment of individual interests, Article 10(a) must be given a restrictive interpretation, and any measures undertaken on the basis thereof must be effective and proportionate. This is furthermore supported by the wording of Article 10(a), which provides that such measures are to be "necessary to avoid abuses". In such circumstances, the onus is on the State making the derogation to demonstrate that these conditions are fulfilled.

36 No convincing evidence has been presented to support the assertion that the aim of preventing abuses necessitates the general exclusion from the scope of the guarantee of employees who are related to a major shareholder in the insolvent employer company, irrespective of the circumstances in the individual cases. Nor has it been shown that this aim could not be achieved as efficiently through measures which would encroach to a lesser degree upon the rights granted by the Directive conferring social protection on employees.

37 Thus, Article 10(a) must be interpreted as not allowing the application, as a measure against abuse, of a provision of national law generally excluding a sibling of a major shareholder in the insolvent employer from compensation from the wage guarantee fund.

Article 10(b)

38 In the opinion of the *Court*, the arguments mentioned above in connection with Article 10(a) of the Directive are equally valid with regard to Article 10(b). The social objective of the Directive, together with the provision in Article 10(b) being in the nature of an exception, imply that Article 10(b) must be interpreted restrictively.

39 As argued particularly by the *Government of the United Kingdom*, Article 10(b) is a free-standing basis for derogation, separate from Article 1(2). The mere fact that an employee is in a position that could have given rise to an exclusion pursuant to Article 1(2) does not prevent the application of Article 10(b) if the conditions of the latter provision are fulfilled.

40 However, Article 10(b) sets out several cumulative criteria that must be fulfilled before a claim can be excluded by reason of that provision. One criterion is "the existence of special links between the employee and the employer", whilst

another is the existence of "common interests resulting in collusion" between the employer and the employee. A third criterion is that "it appears that fulfilment of the obligation is unjustifiable" because of the special links and the common interest resulting in collusion. As submitted by the *plaintiff*, the *EFTA Surveillance Authority* and the *EC Commission*, the fact that those criteria are cumulative makes it difficult to accept that Article 10(b) may provide a basis for a general rule excluding from the scope of the wage guarantee fund siblings of a major shareholder in the insolvent employer company. In any event, the State which makes such a derogation must carry the burden of justifying the measures taken.

41 In the present case, no convincing evidence has been presented to support the assertion that the aims reflected in Article 10(b) necessitate the general exclusion of employees on the basis of a general relationship to a major shareholder in the insolvent employer company, irrespective of the circumstances in the individual cases.

42 Consequently, Article 10(b) of the Directive must be interpreted as precluding the application of a provision of national law according to which siblings of a major shareholder in the insolvent employer company are generally not entitled to compensation from the wage guarantee fund.

The second question

43 By its second question, the national court raises the issue whether, through the EEA Agreement, the EFTA States have taken on an obligation to provide for compensation to individuals and economic operators who have suffered loss or damage as a result of a State's incorrect implementation of the Directive.

The existence of State liability as a matter of principle

44 The *Government of Iceland*, the *Government of Norway*, the *Government of Sweden* and the *EC Commission* submit, on the one hand, that the EEA Agreement does not impose an obligation on the EFTA States to make good loss and damages caused to individuals by failure to implement correctly in their national legislation provisions of EEA legislation. The arguments presented in support of this view vary to some extent, but may essentially be summarized as follows. Neither the EEA Agreement nor the Treaty Establishing the European Community (hereinafter the "EC Treaty") contains an express provision on State liability. Under Community law, the principle of State liability has been established through the case law of the Court of Justice of the European Communities (hereinafter the "ECJ"). However, since the case law is largely based on special characteristics of the Community legal order that are not found in the EEA Agreement, this case law is not transferable to the EEA Agreement

by virtue of Article 6 EEA. Relevant differences between the EEA Agreement and the EC Treaty include the absence in the EEA Agreement of important principles of Community law such as transfer of legislative powers, direct effect and primacy of Community legislation.

45 The *plaintiff* and the *EFTA Surveillance Authority* submit, on the other hand, that the obligations undertaken by the EFTA States under the EEA Agreement include an obligation to make good loss and damage caused to individuals by incorrect implementation of EEA legislation. Reference is essentially made to the case law of the ECJ establishing the principle of liability under Community law, the similarities between the EEA Agreement and the EC Treaty, the homogeneity objective of the EEA Agreement, the recognition of the important role that individuals will play through the exercise of their rights in judicial proceedings and the stated intention of ensuring equal treatment of individuals and economic operators. The EFTA Surveillance Authority adds that a principle of State liability does not presuppose any transfer of legislative powers contrary to the system of the EEA Agreement.

46 The Court notes, firstly, that there is no explicit provision in EEA law establishing a basis for State liability on account of incorrect adaptation of national legislation.

47 In the absence of an express provision in the EEA Agreement, the question arises whether such a State obligation is to be derived from the stated purposes and the legal structure of the EEA Agreement. The general aim of the EEA Agreement, as laid down in Article 1(1) EEA, is to promote a continuous and balanced strengthening of trade and economic relations between the Contracting Parties with equal conditions of competition and the respect of the same rules, with a view to creating a homogeneous European Economic Area.

48 The scope of the EEA Agreement is laid down in Article 1(2) EEA, which states that, in order to attain those objectives, the association envisaged therein shall entail, in accordance with the provisions of the EEA Agreement, six elements specified in that Article: the free movement of goods, persons, services, and capital, the setting-up of a system ensuring that competition is not distorted, and closer co-operation in certain other fields.

49 As stated in Article 1(1) EEA, one of the main objectives of the Agreement is to create a homogeneous EEA. This homogeneity objective is also expressed in the fourth and fifteenth recitals of the Preamble to the EEA Agreement.

50 The fourth recital of the Preamble reads:

> "CONSIDERING the objective of establishing a dynamic and homogeneous European Economic Area, based on common rules and equal conditions of competition and providing for the adequate means of enforcement including at the judicial level, and achieved on the basis of equality and reciprocity and of an overall balance of benefits, rights and obligations for the Contracting Parties;"

51 The fifteenth recital of the Preamble reads:

> "WHEREAS, in full deference to the independence of the courts, the objective of the Contracting Parties is to arrive at, and maintain, a uniform interpretation and application of this Agreement and those provisions of Community legislation which are substantially reproduced in this Agreement and to arrive at an equal treatment of individuals and economic operators as regards the four freedoms and the conditions of competition;"

52 The achievement of the homogeneity objective rests, in particular, on two main foundations.

53 First, the material provisions of the EEA Agreement shall, within the agreed scope of co-operation, be largely identical to corresponding provisions of the EC Treaty and the Treaty Establishing the European Coal and Steel Community (hereinafter the "ECSC Treaty"). Such material provisions shall be made applicable in the EFTA States by means of incorporation into their respective national laws.

54 Secondly, the EEA Agreement establishes elaborate mechanisms with a view to ensuring homogeneous interpretation and application of the incorporated material provisions.

55 In accordance with Article 108 EEA, a separate EFTA Surveillance Authority is set up to constantly review the implementation and application of the material provisions in the EFTA States and to take action in case of a State's infringement of its implementation obligations under the Agreement. A court of justice (EFTA Court) is established to review the surveillance procedure and settle disputes between *inter alia* the EFTA States.

56 A uniform and homogenous interpretation and application of the material rules is further supported by various provisions, partly in the EEA Agreement itself and partly in the Surveillance and Court Agreement, agreed to by the EFTA States pursuant to Article 108 EEA. Thus, Article 6 EEA provides that provisions of the EEA Agreement which are in substance identical to corresponding provisions of the EC Treaty and the ECSC Treaty shall be interpreted in conformity with relevant rulings of the ECJ given prior to the signing of the EEA Agreement, whilst Article 3 of the Surveillance and Court Agreement requires that due

account be paid to relevant rulings of the ECJ subsequent to the signing of the EEA Agreement. According to Articles 105 and 106 EEA, an EEA Joint Committee shall keep under constant review the development of the case law of the ECJ and the EFTA Court, and there shall be established a system of exchange of information concerning judgments between the EFTA Court, the ECJ and the Court of First Instance. The EC Commission and the EFTA Surveillance Authority shall co-operate, exchange information and consult each other on surveillance policy issues and individual cases.

57 Another important objective of the EEA Agreement is to ensure individuals and economic operators equal treatment and equal conditions of competition, as well as adequate means of enforcement. Again, reference can be made to the fourth and fifteenth recitals of the Preamble (see paragraphs 50 and 51 above) and, in particular, to the eighth recital in the Preamble to the EEA Agreement, which states:

> "CONVINCED of the important role that individuals will play in the European Economic Area through the exercise of the rights conferred on them by this Agreement and through the judicial defence of these rights;"

58 The Court notes that the provisions of the EEA Agreement are, to a great extent, intended for the benefit of individuals and economic operators throughout the European Economic Area. Therefore, the proper functioning of the EEA Agreement is dependent on those individuals and economic operators being able to rely on the rights thus intended for their benefit.

59 The Court concludes from the foregoing considerations that the EEA Agreement is an international treaty *sui generis* which contains a distinct legal order of its own. The EEA Agreement does not establish a customs union but an enhanced free trade area, see the judgment in Case E-2/97 *Maglite* [1997] EFTA Court Report 127. The depth of integration of the EEA Agreement is less far-reaching than under the EC Treaty, but the scope and the objective of the EEA Agreement goes beyond what is usual for an agreement under public international law.

60 The Court finds that the homogeneity objective and the objective of establishing the right of individuals and economic operators to equal treatment and equal opportunities are so strongly expressed in the EEA Agreement that the EFTA States must be obliged to provide for compensation for loss and damage caused to an individual by incorrect implementation of a directive.

61 A further basis for the obligation of the Contracting Parties to provide for compensation is to be found in Article 3 EEA, under which the Contracting Parties are required to take all appropriate measures, whether general or particular, to ensure fulfilment of their obligations under the Agreement, see the judgment of 30 April 1998 in Case E-7/97 *EFTA Surveillance Authority* v *Norway*, not yet reported. With regard to the implementation of directives integrated into the EEA Agreement, this means that the Contracting Parties have

a duty to make good loss or damage resulting from incorrect implementation of those directives.

62 It follows from all the forgoing that it is a principle of the EEA Agreement that the Contracting Parties are obliged to provide for compensation for loss and damage cause to individuals by breaches of the obligations under the EEA Agreement for which the EFTA States can be held responsible.

63 It follows from Article 7 EEA and Protocol 35 to the EEA Agreement that the EEA Agreement does not entail a transfer of legislative powers. However, the principle of State liability must be seen as an integral part of the EEA Agreement as such. Therefore, it is natural to interpret national legislation implementing the main part of the Agreement as also comprising the principle of State liability.

The conditions for State liability

64 Although the establishment of State liability is thus required by the EEA Agreement, the conditions under which such liability gives rise to a right to compensation must depend on the nature of the breach of the obligations thereunder which has caused the loss or damage.

65 In the event of incorrect implementation of a directive in national law contrary to Article 7 EEA, the effectiveness of that rule requires that there should be a right to reparation provided that three conditions are fulfilled.

66 First, the directive in question must be intended to confer rights on individuals, the content of which can be identified on the basis of the provisions of the Directive. Secondly, the breach on the part of the State concerned must be sufficiently serious. Thirdly, there must be a causal link between the breach of the State's obligation and the loss and damage suffered by the injured parties.

67 With regard to the present case, the Court notes that the purpose of Council Directive 80/987/EEC, as amended, is to grant to employees a right to a guarantee of payment of their unpaid wage claims. For similar reasons as in the case law of the ECJ, the scope and content of that right can be identified on the basis of the provisions of the Directive, see for comparison the judgment in Joined Cases C-6/90 and C-9/90 *Francovich and Others* [1991] ECR I-5357, paragraphs 10 *et seq*. Thus, it appears that the first condition is fulfilled.

68 As to the second condition, the decisive test for finding that a breach of an obligation under the EEA Agreement is sufficiently serious must be whether the Contracting Party concerned has manifestly and gravely disregarded the limits on its discretion.

69 The factors which the competent court may take into consideration include the clarity and precision of the rule breached, the measure of discretion left by that rule to the national authorities, whether the infringement and the damage caused was intentional or involuntary, whether any error of law was excusable or inexcusable, the fact that the position taken by an EEA or Community institution may have contributed towards the omission, and the adoption or retention of national measures or practices contrary to the EEA Agreement.

Costs

70 The costs incurred by the Government of Norway, the Government of Sweden, the Government of the United Kingdom, the EFTA Surveillance Authority and the EC Commission, 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,

THE COURT,

in answer to the questions referred to it by Héraðsdómur Reykjavíkur by an order dated 5 November and a request dated 12 November 1997, hereby gives the following Advisory Opinion:

1 The Act referred to in Point 24 of Annex XVIII to the Agreement on the European Economic Area (Council Directive 80/987/EEC of 20 October 1980 on the approximation of the laws of the Member States relating to the protection of employees in the event of insolvency of their employer) must be interpreted as precluding Iceland from maintaining a provision of national law, according to which, in the case of a sibling relationship between an employee and an owner of 40 per cent of the shares of the employer company, the employee is excluded from the guarantee provided for in Article 3 of the Act on the basis of that family relationship.

2 The Contracting Parties to the EEA Agreement are obliged to provide for compensation for loss and damage caused to an individual by incorrect implementation of a directive incorporated into the EEA Agreement.

Bjørn Haug Thór Vilhjálmsson Carl Baudenbacher

Delivered in open court in Luxembourg on 10 December 1998.

Gunnar Selvik
Registrar

Bjørn Haug
President