REPORT FOR THE HEARING
delivered in Case 143/86 *

I — Facts and procedure

A — *Facts and the legal background to the dispute*

(a) *Facts*

1. Thomas Cuddy and Winifred Cuddy, the defendants in the main proceedings, are Irish nationals resident in Ireland. Between January 1982 and July 1984 they bought and sold certain securities on the London Stock Exchange through the partnership of stockbrokers Margetts and Addenbrooke, the plaintiffs in the main proceedings. The securities bought and sold by the stockbrokers for Thomas and Winifred Cuddy were all shares in Irish companies called Atlantic Resources Limited and Eglinton Oil and Gas Limited. The nominal capital of those two companies is expressed in Irish pounds and their shares are quoted on the Stock Exchange both in Dublin and in London. However, all dealings in the shares in London must be settled in sterling.

2. In July 1984 Thomas and Winifred Cuddy owed the stockbrokers Margetts and Addenbrooke UKL 5 080.30. That sum was due in respect of 30 000 shares in Eglinton Oil and Gas Limited which had been bought by the stockbrokers on the instructions of Mr and Mrs Cuddy and subsequently sold at a loss.

3. Margetts and Addenbrooke requested Thomas and Winifred Cuddy to pay the sum in question. They, however, refused to pay, and the stockbrokers instituted proceedings before the Circuit Court of the County of Cavan. By way of defence, Thomas and Winifred Cuddy pleaded that the purchase and sale of foreign currency securities on the London Stock Exchange by Irish residents, without the appropriate exchange control permission, was in violation of the exchange control regulations. They claimed that in those circumstances the agreement which they had made with Margetts and Addenbrooke was illegal and therefore unenforceable.

4. The plaintiffs then argued that Article 67 of the EEC Treaty and the Council Directive of 11 May 1960 prohibited the restrictions resulting from the Irish Exchange Control Regulations. They further claimed that if the Commission Decision of 3 December 1980 authorized Ireland to take protective measures under Article 108 of the Treaty, thus enabling it temporarily to impose restrictions on the acquisition by Irish residents of foreign securities on the stock exchange, that decision was invalid. In the alternative, they claimed that the decision did not concern the type of dealings involved in this case.

(b) *Legal background*

The Directive of 11 May 1960 was adopted by the Council on the basis of Article 67 of the Treaty, which provides as follows:

* Language of the Case: English.

'(1) During the transitional period and to the extent necessary to ensure the proper functioning of the common market, Member States shall progressively abolish between themselves all restrictions on the movement of capital belonging to persons resident in Member States and any discrimination based on the nationality or on the place of residence of the parties or on the place where such capital is invested.

(2) Current payments connected with the movement of capital between Member States shall be freed from all restrictions by the end of the first stage at the latest.'

The directive was subsequently amended by the Second Directive of 18 December 1962 (63/21/EEC, Official Journal, English Special Edition 1963-64, p. 5), which was itself amended by Directive 85/583/EEC of 20 December 1985 (Official Journal 1985, L 372, p. 39), the provisions of which do not apply to the present case.

The provision of the Directive of 11 May 1960 which is relevant to the present case is Article 2 (1), which provides that: 'Member States shall grant general permission for the conclusion or performance of transactions and for transfers between residents of Member States in respect of the capital movements set out in List B of Annex I to this Directive.'

List B, which was not amended by the directive of 18 December 1962, covers the following operations:

'Capital movements referred to in Article 2 of the directive'

Operations in securities:

(i) Acquisition by *non-residents of domestic securities* dealt in on a stock exchange (excluding units of unit trusts) and repatriation of the proceedings of liquidation thereof;

(ii) Acquisition by *residents of foreign securities* dealt in on a stock exchange and use of the proceeds of liquidation thereof:

excluding the acquisition of bonds issued on a foreign market and denominated in national currency;

excluding units of unit trusts.

Physical movements of the securities mentioned above.

The use of the proceeds of liquidation of assets abroad belonging to residents must be permitted at least within the limits of the obligations as regards liberalization accepted by Member States.'

In so far as it was admitted that those provisions covered the dealings by Mr and Mrs Cuddy on the London Stock Exchange, the plaintiffs in the main proceedings questioned the validity of the Decision of 3 December 1980 (C(80) 1817, unpublished), by which the Commission authorized Ireland to take certain protective measures under Article 108 of the Treaty. By Article 1 of that decision, which replaced a previous Decision of 22 December 1977 (78/153/EEC, Official Journal 1978, L 45,

p. 29) and which was itself later replaced by the Decision of 19 December 1984 (85/15/EEC, Official Journal 1985, L 8, p. 32), Ireland was authorized in the following terms to apply certain restrictions to the purchase by residents of foreign securities:

'1. By way of derogation from the Council Directives of 11 May 1960 and 18 December 1962, but without any other derogations to these directives being implied, Ireland is authorized on a temporary basis to continue applying protective measures restricting the purchase by residents of foreign securities dealt in on a stock exchange, except those securities mentioned at Article 2.

2. However, Ireland may not apply any restrictions on the purchase by a resident of foreign securities when this purchase is financed from the proceeds of the sale of other foreign securities held by him.'

B — Under those circumstances the Circuit Court decided by order of 11 November 1985 to refer to the Court for a preliminary ruling under Article 177 of the EEC Treaty the following four questions:

'(1) Does Article 2 (1) of the Council Directive of 11 May 1960 confer on individuals rights which are enforceable by them in the national courts of a Member State?

(2) If so, is the said Article 2 (1) of the said directive to be interpreted as giving individuals residing in one Member State the right to buy securities on a stock exchange in another Member State?

(3) Is the decision of the Commission of 3 December 1980 authorizing Ireland to continue to apply certain protective measures pursuant to Article 108 (3) of the EEC Treaty a valid decision?

(4) If the said decision is a valid decision, does it entitle Ireland to impose restrictions on its residents in regard to dealings in shares in companies registered in and having their principal place of business in Ireland on the stock exchange of another Member State?'

II — Summary of the written observations submitted to the Court

A — *The question whether Article 2 (1) of the Council Directive of 11 May 1960 for the implementation of Article 67 of the EEC Treaty has direct effect*

Article 2 (1) of this directive provides as follows: 'Member States shall grant general permission for the conclusion or performance of transactions and for transfers between residents of Member States in respect of the capital movements set out in List B of Annex I to this directive.'

List B, to which Article 2 of the directive refers, covers the following operations in securities:

(i) Acquisition by non-residents of domestic securities dealt in on a stock exchange (excluding units of unit trusts) and repatriation of the proceeds of liquidation thereof;

(ii) Acquisition by residents of foreign securities dealt in on a stock exchange and use of the proceeds of liquidation thereof (excluding the acquisition of bonds issued on the foreign market and denominated in national currency and excluding units of unit trusts).

List B was amended by Council Directive 85/583/EEC of 20 December 1985 (Official Journal 1985, L 372, p. 39), but that version does not apply to the facts in this case.

1. The plaintiffs in the main proceedings refer to the judgments of the Court in which it has held that although under Article 189 of the Treaty directives are addressed to Member States, they may, however, have direct effects which may be relied upon by individuals.

They consider that the Directive of 11 May 1960 is sufficiently precise and unconditional to give rise to such direct effects in the relations between Member States and individuals. They also consider that Article 67 of the Treaty on the abolition of restrictions on the movement of capital itself has direct effect. That being so, they consider that they are entitled to plead that the Irish Exchange Control Regulations are incompatible with the Directive of 11 May 1960.

2. The Commission and the defendants in the main proceedings take the view that Article 2 (1) of the Directive of 11 May 1960 does not have direct effect. The Commission states that individuals may rely directly upon a directive only if the State to which it is addressed has failed to adopt the measures needed to comply with the directive within the prescribed period or if it has adopted measures for that purpose which do not comply with the directive.

According to the Commission, the Irish Government has correctly implemented the Directive of 11 May 1960.

The defendants in the main proceedings add that a directive must be distinguished from a regulation and that both Article 67 of the Treaty and the Directive of 11 May 1960 cannot be considered to have direct effects since they are conditional.

B — *The question whether the Directive of 11 May 1960 applies to the dealings in question*

1. The plaintiffs in the main proceedings take the view — shared by the defendants in the main proceedings, though on very different grounds — that the dealings which gave rise to the dispute are covered by List B of Annex I to the Directive of 11 May 1960. The plaintiffs in the main proceedings point out that List B covers 'acquisition by residents of foreign securities dealt in on a stock exchange'. In their view it follows that the Member States must grant general permission for such transactions in accordance with Article 2 (1) of the directive.

The plaintiffs in the main proceedings consider that, since free movement of capital is one of the fundamental freedoms of the European Community, the Member States must adopt the measures necessary to implement the directive and must not adopt any measure which might interfere with its implementation.

According to the plaintiffs in the main proceedings, in its Decision of 3 December 1980 adopted on the basis of Article 108 of the EEC Treaty, the Commission wrongly authorized Ireland to derogate from the liberalization of capital movements, as provided for in List B to Annex I of the Directive of 11 May 1960.

The defendants in the main proceedings consider that the transactions which gave rise to the dispute are covered by List B of Annex I to the Directive of 11 May 1960, since they do give rise to transfers of capital. However, they observe that in allowing the Irish Government to adopt measures restricting the liberalization of capital movements the Commission acted lawfully.

2. The Commission and Ireland take a radically different view. The Commission considers that the transactions which gave rise to the dispute are outside the scope of the Directive of 11 May 1960.

The same applies to Ireland, which considers that neither the Directive of 11 May 1960 nor the Commission Decision of 3 December 1980 authorizing derogation from the directive are applicable to the facts found or agreed before the domestic court. As has been seen, List B of Annex I to the Directive of 11 May 1960 covers two categories of operations in securities: 'acquisition by non-residents of domestic securities dealt in on a stock exchange' and 'acquisition by residents of foreign securities dealt in on a stock exchange'.

According to the directive, the terms 'residents' and 'non-residents' are defined in accordance with the provisions of national legislation. 'Domestic or foreign securities' are defined as 'securities according to the country in which the issuer has his principal place of business'.

Ireland points out that the transactions which gave rise to the dispute pending before the Circuit Court concern the purchase by residents of Ireland of shares in Irish companies quoted in Irish pounds on the London Stock Exchange. The case therefore concerns the acquisition by residents of Ireland of domestic securities, which is outside the scope of List B of Annex I to the Directive of 11 May 1960.

Ireland contends that 'there is no reference in the said directive to the acquisition by residents of Member States of domestic securities and no obligations are imposed upon Member States in relation to such transactions'.

C — *The question whether the Commission Decision of 3 December 1980 is unlawful*

By Decision 78/153/EEC of 22 December 1977 adopted on the basis of Article 108 of the Treaty, the Commission authorized the Irish Government to take certain protective measures. Under Article 1 of that decision, Ireland was authorized on a temporary basis to maintain the restrictions on the acquisition by residents of foreign securities dealt in on a stock exchange and on the use of the proceeds of liquidation thereof.

Those measures were provided for in virtually the same terms by a Commission Decision of 3 December 1980 (unpublished), which was itself subsequently replaced by Decision 85/15/EEC of 19 December 1984.

1. The plaintiffs and the defendants in the main proceedings consider that Decision 78/153/EEC is not valid. The plaintiffs advocate a strict interpretation of Article 108 of the Treaty. Article 108 provides that where a Member State is in difficulties or is seriously threatened with difficulties as regards its balance of payments, the Commission shall immediately investigate the position of the State in question and the action which, making use of all the means at its disposal, that State has taken or may take in accordance with the provisions of Article 104.

If the measures adopted are not sufficient, the Commission must, after consulting the Monetary Committee, recommend to the Council the granting of mutual assistance and appropriate methods therefor. The Council, acting by a qualified majority, may then grant such mutual assistance.

Article 108 (3) provides that 'if the mutual assistance recommended by the Commission is not granted by the Council or if the mutual assistance granted and the measures taken are insufficient, the Commission shall authorize the State which is in difficulties to take protective measures, the conditions and details of which the Commission shall determine'.

The plaintiffs in the main proceedings submit that that procedure was not complied with in so far as the Commission adopted decisions authorizing Ireland to take protective measures without ever requesting the Council for the mutual aid provided for in Article 108 (2). They therefore consider that the Commission exceeded its powers.

By contrast, the defendants in the main proceedings consider that the Commission's request to the Council for mutual assistance is not an obligatory stage in the introduction of protective measures. They add that the protective measures were in this case justified in view of the situation in Ireland.

2. The Commission claims firstly that the contested decision is lawful. It considers that it is unnecessary to request mutual assistance as provided for in Article 108 of the Treaty before protective measures are introduced where such assistance would not appear to be appropriate in view of the circumstances. However, the fundamental contention of the Commission and Ireland is that the reference to protective measures and in particular to the Commission Decision of 3 December 1980 is not relevant to the solution of the dispute.

That decision authorized Ireland to derogate from the provisions of the Directive of 11 May 1960. As has been explained above, however, the Commission and Ireland take the view that the transactions which gave rise to the dispute pending before the Circuit Court are outside the scope of List B of Annex I to the Directive of 11 May 1960.

D — *The question concerning the legality of the Irish Exchange Control Regulations*

Ireland maintains that, since operations such as those at issue were not covered by the Directive of 11 May 1960, it was entirely free to decide on any restrictions which it considered appropriate. It explains that under the Exchange Control Act of 1954 a person may not make or commit himself to make any payment to a person resident outside the scheduled territories except with the permission of the Minister for Finance. The Act provides that the Minister is entitled to delegate functions under the Act,

and he has done so in favour of the Central Bank of Ireland. Pursuant to that authority, the Central Bank of Ireland has published notices setting out general permissions for certain transactions.

The Central Bank has in particular issued Exchange Control Notice No. EX 5, from which it is clear that securities such as those concerned in the proceedings before the national court must be regarded as Irish quoted securities. The Irish Government then contends that there is nothing illegal about a deal being arranged in Irish quoted securities on the London Stock Exchange on behalf of Irish residents. However, under Notice No EX 5, the arrangement must be made through an approved agent, as defined in paragraph 11 of the said notice.

Ireland also explains that the requirement that such transactions are channelled through approved agents is designed to ensure that funds transferred to London for the purposes of giving effect to transactions effected on the London Stock Exchange are invested in Irish quoted securities rather than in foreign currency securities.

The restriction was therefore imposed in order to prevent the unauthorized purchase of foreign securities. The Commission Decision of 3 December 1980, however, expressly permitted the Irish Government to prevent the purchase of foreign securities by Irish residents.

III — The replies of the parties to the questions put to them by the Court

A — *Questions put to the Commission*

(a) In its observations the Commission maintains that the transactions carried out by Thomas and Winifred Cuddy which are the subject-matter of the main proceedings do not fall within the categories of operations which were liberalized by the Directive of 11 May 1960 as amended by the Directive of 18 December 1962. Yet it is stated in the explanatory memorandum to the proposal for a directive presented to the Council in June 1986 with a view to extending the liberalization of capital movements that the 1960 directive, as amended, applies explicitly only to operations by a resident of a Member State to acquire foreign securities and that, consequently, it 'does not formally cover the acquisition by a resident of domestic securities issued on a foreign market', which is a less categoric statement.

Accordingly, the Court asked the Commission the following questions:

(1) What were the reasons for not liberalizing transactions carried out by residents with regard to domestic securities issued on a foreign stock exchange when all the restrictions on similar transactions by non-residents were abolished?

(2) What factors lead the Commission to consider that henceforward such transactions could be liberalized in common with the other transactions falling within List B?

The Commission's reply

As it has explained in its observations, the Commission considers that the facts of this case concern transactions which are outside the scope of the directives adopted in 1960 and 1962 for the implementation of Article 67 of the Treaty.

According to the Commission, this case concerns an acquisition by a resident of national securities on a foreign stock exchange. Domestic and foreign securities are defined in the Explanatory Notes to the directive as 'securities according to the country in which the issuer has his principal place of business'. Thus the shares in question in the present case are clearly national securities. At that time, it was only the acquisition of foreign securities that was liberalized, subject to certain exceptions.

In the first place, the Commission observes that the liberalization of movements of capital provided for by Article 67 (1) of the Treaty must be carried out in accordance with Article 69, on the basis that such liberalization is necessary to ensure the proper functioning of the common market, as was held by the Court in Case 203/80 *Cassati* [1981] ECR 2595.

As regards the first question, concerning the reasons for which domestic securities purchased by residents on a foreign stock exchange were not liberalized under the directives adopted in 1960 and 1962, the Commission states that the principal reason for the maintenance of this restriction was the necessity, felt at the time, to ensure that the floating of a loan abroad would result in a net capital inflow and not simply result in a re-routing of national savings through the financial market of another country. It was necessary to guard against that risk in so far as a loan floated abroad, particularly by the State, very often carries conditions which are superior to those being offered on the domestic market.

If such loans floated abroad could be freely bought by residents at home, the internal cost of public debt could be increased or the desired effect of obtaining a net capital inflow defeated. When the Commission made its proposals for a new directive, it had come to the conclusion that, in the context of the completion of the common market and more particularly the creation of a unified financial structure, and having regard to the present economic circumstances, the maintenance of restrictions of this kind was no longer justified.

(b) The Court noted that the acquisition of 'bonds issued on a foreign market and denominated in national currency' was excluded from List B of Annex I to the Directive of 11 May 1960, as amended. It requested the Commission to explain its reasons for excluding such transactions when, by contrast, it appeared from the wording of the directive that residents could carry out transactions in securities, other than bonds, issued on a foreign market, even if those securities were denominated in national currency.

The Commission's reply

The Commission states that these restrictions were maintained owing to the need to enable States to regulate their own financial markets. Transactions of this kind concerned with bonds might have resulted in the uncontrolled development of parallel markets in the national currency in financial centres outside their control.

Although it was not thought necessary to exclude the acquisition of foreign shares in a foreign market even when these were denominated in national currency, this was because it was rare for a foreign company with its principal place of business in another country to issue shares denominated in a currency other than its own.

B — *Questions to Thomas Cuddy and Winifred Cuddy*

Thomas Cuddy and Winifred Cuddy carried out transactions in securities of Irish

companies on the London Stock Exchange. The Court asked them whether there was an objective reason for doing so, in view, for example, of differences in stock exchange rules. If there was any such reason, the Court requested them to state what it was.

The reply of Thomas Cuddy and Winifred Cuddy

Thomas Cuddy and Winifred Cuddy state that they had never dealt in shares until they were canvassed by an agent of the United Kingdom stockbrokers in question, who offered to act for them in the purchase of shares. Under those conditions Mr Cuddy agreed to the purchase in his name of a very small number of shares. But he knew nothing of the rules of the Stock Exchange or of the Exchange Control Regulations governing share transactions.

Y. Galmot
Judge-Rapporteur