

# German Federal Constitutional Court enables Germany to ratify ESM Treaty

On 12 September 2012, the German Federal Constitutional Court (*Bundesverfassungsgericht*) rejected temporary injunctions to prevent the ratification of the Treaty on the European Stability Mechanism ("ESM"), the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (the "**Fiscal Compact**") and amendments to the Treaty on the Functioning of the European Union ("TFEU").

However, the Federal Constitutional Court has reinforced again the position of the German Federal Parliament (*Bundestag*) *vis-à-vis* the German Federal Government (*Bundesregierung*) in matters of European monetary and economic integration and set out limitations on the transfer of powers to the EU by the Federal Republic of Germany.

## The Federal Constitutional Court's position on constitutional implications of monetary and economic integration

The Federal Constitutional Court has never fully accepted the supremacy of European law. Rather, it has emphasised that the national parliaments of sovereign member states are still the primary sources of democratic legitimacy in respect of actions taken by any bodies of the EU. On this basis the Federal Constitutional Court is prepared to assess whether actions by EU institutions fall outside the scope of the competences conferred on them by the Treaties establishing the EU and to test the validity of their actions against the core standards of fundamental rights set out in the German Constitution.

In the course of the current European sovereign debt crisis, the Federal Constitutional Court has attempted through

various decisions to restrain a shift of competences from the Federal Parliament to the Federal Government. On the one hand, the Federal Constitutional Court is concerned with preventing the Federal Government from assuming obligations at an international level which undermine the Federal Parliament's right to exercise its power to decide on public revenue and public expenditure matters and, on the other, with preventing the Federal Parliament from relinquishing its own powers. The ruling issued by the Federal Constitutional Court on 12 September 2012 confirms once again this approach.

## Decision of 12 September 2012

On 29 June 2012, after the member states of the Eurozone agreed on (i) the implementation of the ESM, (ii) the amendments required to be made to the TFEU in order to establish the ESM, and (iii) the Fiscal Compact, the Federal Parliament passed the necessary legislation to implement these measures in Germany. Immediately, numerous constitutional complaints were filed. The plaintiffs also sought temporary injunctions from the Federal

Constitutional Court to prevent the President of the Federal Republic of Germany from signing the relevant statutes into law, since the Federal Constitutional Court wanted to avoid a situation whereby an obligation of Germany at international level was being created irrespective of whether or not the Federal Constitutional Court would ultimately hold the statutes unconstitutional and void.

Exceptionally, the President of the Federal Constitutional Court asked the President of the Federal Republic of Germany to wait for the Federal Constitutional Court's judgment before signing the new statutes into law. Also unusually, the Federal Constitutional Court decided to hold a public hearing prior to the delivery of its ruling on the temporary injunctions and announced a delay in its decision making in order to conduct an in-depth constitutional analysis.

On 12 September 2012, the Federal Constitutional Court released its much anticipated ruling on the temporary injunctions. Following an analysis of the pertinent legislation and of the accompanying laws which were subject to the challenge, the Federal Constitutional Court confirmed that these may be put on the statute book and that the relevant treaties can be ratified. However, it has also imposed an obligation on the Federal Republic to ensure:

1. that the amount of all payment obligations of the Federal Republic of Germany arising under the ESM Treaty is limited to its share in the authorised capital stock of the ESM (EUR 190,024,800,000) and that no provision of the ESM Treaty may be interpreted in a way that imposes higher payment obligations on the Federal Republic of Germany without the agreement of the German ESM representative; and
2. that the provisions of the ESM Treaty concerning the confidentiality of documents of the ESM and the professional secrecy of all persons working for the ESM must not prevent the comprehensive information obligations owed to the German Federal Parliament and to the German Federal Council (*Bundesrat*) from being met.

As in its former decisions on this topic, the Federal Constitutional Court confirmed that decisions on public revenue and public expenditure must remain in the hands of the Federal Parliament as a fundamental tenet of the Federal Republic of Germany to conduct itself democratically. This particularly applies in a system of intergovernmental decision making. Accordingly, the Federal Parliament is prohibited from participating in

mechanisms of considerable financial importance which may result in an incalculable financial burden with budgetary implications of significance without mandatory parliamentary approval. The Federal Parliament is also prohibited from establishing permanent mechanisms based on international treaties which enable other states to impact on any liabilities to be incurred by the Federal Republic of Germany, in particular, and most importantly, if they entail unpredictable consequences. Rather, the Federal Parliament must individually approve every large-scale federal support measure to be made at international or European Union level which would result in such expenditure being incurred. Sufficient parliamentary influence must also be retained over the manner in which the funds provided are dealt with.

In its summary ruling, the Federal Constitutional Court has not considered Article 136 (3) of the TFEU, which enables member states of the Eurozone to establish and operate a stability mechanism if indispensable to safeguard the stability of the euro area.

The Federal Constitutional Court held that the ESM Treaty complies with the requirements set out under constitutional law with regard to the safeguarding of the overall budgetary responsibility of the Federal Parliament. But in relation to the ESM Treaty (as stated above), the Federal Constitutional Court requires the Federal Republic to ensure that within the framework of the ratification procedure under international law the provisions of the ESM Treaty may only be interpreted or applied in such a way that the liability of the Federal Republic cannot be increased beyond its share in the authorised capital stock of the ESM ("liability ceiling") by an expansive interpretation of certain provisions of the ESM Treaty. The particular provision in relation to which an expansive interpretation might be possible is the right of the ESM, in the case of a payment shortfall by an ESM member state, to make "revised increased" capital calls to all other ESM member states. In order to prevent such an expansive interpretation, the Federal Constitutional Court requires the Federal Government to ensure that it is only bound by the ESM Treaty in its entirety if no payment obligations beyond the liability ceiling can apply to it without the consent of the Federal Parliament. Whether the Federal Republic of Germany can comply with the Federal Constitutional Court's requirements by merely making a unilateral reservation in the European ratification process is not without doubt given the importance (for all member states) of whether or not the liability ceiling is an absolute one. Under the Vienna Convention on the Law of Treaties,

unilateral reservations are an adequate tool to evidence a state's views on the interpretation of an international treaty but are effective under certain preconditions only. It remains to be seen whether the Federal Republic chooses to increase legal certainty by seeking a joint declaration of the ESM member states clarifying the contents of the ESM Treaty in this respect.

The Federal Constitutional Court has imposed a second obligation on the Federal Government with respect to a further provision in the ESM Treaty which may be subject to a broader interpretation. The ESM Treaty does not include an exemption from professional secrecy obligations and confidentiality of documents with respect to the provision of information to the parliaments of member states. Therefore, Germany must ensure an interpretation of the ESM Treaty which guarantees such an exemption. The Federal Parliament and Federal Council must be able to receive such comprehensive information as is required to be able to develop an informed opinion on relevant matters.

In contrast, the Federal Constitutional Court has not considered a temporary suspension of voting rights of an ESM member state under the ESM Treaty as obviously incompatible with the required overall budgetary responsibility of the Federal Parliament. Under the ESM Treaty, all voting rights of an ESM member state are suspended if it fails to meet fully its obligations to make payment vis-à-vis the ESM. During such a period, the member state concerned (and, accordingly, the parliament which would ratify its decisions) would no longer be able to influence the decisions of the ESM which could in such a period, for example, be called on to decide whether to grant financial support to a member state and to agree on the relevant conditionality (but not to increase ESM member states' capital stock). However, in the Federal Constitutional Court's view this temporary suspension does not necessarily violate the overall budgetary responsibility of the Federal Parliament because it can, and must, procure that the German voting rights are not suspended by ensuring that at any time Germany will be in a position to pay in its shares in the authorised capital stock of the ESM.

On the economic front, the Federal Constitutional Court stated that it had to accept the evaluation of the German legislator that potential payment obligations in an amount of up to EUR 190,024,800,000 are justified given the risk of unforeseeable, serious consequences for the entire economic and social system if such financial assistance were needed and not provided. It has emphasised the broad discretion of the legislator, which also applies to the

assessment of the future soundness of the federal budget and the economic performance capacity of the Federal Republic of Germany.

The Federal Constitutional Court has not ruled on any measures taken by the European Central Bank ("ECB") as yet and in particular on its measures on the acquisition of Eurozone government bonds on the secondary market. Although it is not entirely clear whether the Federal Constitutional Court is competent to rule directly on the legality of measures conducted by the ECB and on the interpretation of the TFEU's scope in this respect, a petition was also filed which requested that the Federal Constitutional Court consider whether the ECB's measures are in compliance or not with the relevant German acts on the assent to the European Union Treaties. This will be reviewed in subsequent principal proceedings.

In its decision the Federal Constitutional Court has, however, outlined various considerations with respect to Art. 123 of the TFEU. This Article prohibits the ECB or a national central bank from providing credit facilities in favour of European Union institutions, bodies, offices or agencies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of member states. The same applies to the purchase of debt instruments by the ECB or national central banks directly from such entities.

Based on this provision, the Federal Constitutional Court considers that it is not possible for the ESM to become a counterparty to Eurosystem monetary policy operations. In addition, the Federal Constitutional Court has outlined that it considers the purchases of sovereign debt instruments by the ECB in the secondary market as a circumvention of the prohibition contained in Art 123 of the TFEU where the aim of these purchases is to provide refinancing possibilities for member states other than through the capital markets.

Given this decision, ratification of the ESM Treaty, the Fiscal Compact and the amendment to the TFEU can now be progressed from a German perspective. However, the Federal Constitutional Court has again made clear that each step taken to overcome the Eurozone crisis must be in compliance with the precept of democracy. The German Constitution does not allow the right to grant the European Union the ability to create further own competencies (*Kompetenz-Kompetenz*) nor to grant any "carte blanche" authorisations.

In particular with respect to further steps to be taken in the course of the ESM, the Federal Constitutional Court has

indicated that it will provide more guidance as to the limits of discretion that the German Government and German ESM representative will have to ensure that the Federal Parliament's power to decide on public revenue and public expenditure is not curtailed. The Federal Constitutional Court mentioned, *inter alia*, the allocation of decision-taking between the Federal Parliament and the parliamentary budget committee as well as the right of the German ESM representative to determine whether the Federal Republic can subscribe for shares at an amount higher than their nominal value.

## Further background and other recent decisions of the Federal Constitutional Court

On 4 February 2012, the European Council with the participation of the German Federal Government adopted the ESM and the Euro Plus Pact as part of a comprehensive package of measures to respond to the European sovereign debt crisis, preserve financial stability and strengthen the economic governance as well as competitiveness of the Eurozone and of the European Union.

The ESM is intended to assume the role of the European Financial Stability Facility ("**EFSF**") and the European Financial Stability Mechanism in providing financial assistance to member states of the Eurozone after June 2013. The member states participating in the Euro Plus Pact agreed to take all necessary measures to foster competitiveness and employment, contribute further to the sustainability of public finances and reinforce financial stability.

The political party *Bündnis 90/Die Grünen* (i.e. Germany's green party) filed an action with the Federal Constitutional Court claiming that the Federal Government had not provided the necessary information and documents "at the earliest possible point in time" as prescribed by the German Constitution in matters relating to the European Union.

On 19 June 2012, the Federal Constitutional Court decided in favour of the plaintiff, finding that the Federal Government had indeed infringed the Federal Parliament's information and participation rights.

The Federal Constitutional Court concluded that constitutional provisions providing for a higher level of

participation by the Federal Parliament at national level in European integration procedures are essential to counter-balance the far-reaching competences of the Federal Government at the European level. The receipt of information at the earliest possible point in time would enable the Federal Parliament to exert influence in the decision-making process of the Federal Government from an early stage rather than just be required to implement its decisions.

The value and amount (with regard to quality, quantity and timeliness) of the information to be made available to the Federal Parliament will depend on the complexity of the procedure, the level of legislative authority and on whether the procedure is similar to a formal resolution or agreement.

According to the Federal Constitutional Court, the requirement to provide information or documents "at the earliest possible point in time" means that the Federal Parliament has to receive the information from the Federal Government early enough to be able to become involved in the procedure and produce a statement, before the Federal Government gives binding declarations or enters into binding intergovernmental agreements.

This decision will not have any effect on the validity of the commitments made by the Federal Government on behalf of the Federal Republic with regard to the ESM or the Euro Plus Pact, but strengthens the Federal Parliament's role with regard to future Federal Government decisions in respect of EU proceedings.

On 28 February 2012, the Federal Constitutional Court held that the establishment of a special committee (*Sondergremium*) of nine members of the parliamentary budget committee elected by the Federal Parliament to decide on an extension of the competences of the EFSF as set out in section 3 para 3 of the German Stabilisation Mechanism Act (*Stabilisierungsmechanismusgesetz*) would infringe the rights of the Federal Parliament. As a result of this decision, the Stabilisation Mechanism Act adopted by the Federal Parliament on 27 April 2012 provided that in most cases the plenary session of the Federal Parliament will need to decide on Euro stabilisation measures. Only in exceptional cases where confidentiality is of the utmost importance, such as the purchase of Eurozone governmental bonds on the secondary market, a special voting committee, whose nine members have to be elected by the Federal Parliament, may decide whether to provide the requisite approval.

The Federal Constitutional Court's decision of 12 September 2012 as well as extracts from the decision in English (press release no. 67/2012 of 12 September 2012) are available at <http://www.bverfg.de>.

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