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Acts of Financial Distress in the EU: Is the EU to Blame?

Venetia Argyropoulou

ACTS OF FINANCIAL DISTRESS IN THE EU: IS THE EU TO BLAME?

Venetia Argyropoulou[†]

Abstract: This Article seeks to determine if there is a legal basis for European Union ("EU") Institutions to be held accountable for measures taken by an EU Member State in cases of financial distress. The Article begins by exploring the concept of sovereignty and then evaluates the limitations placed on state sovereignty by participation in the EU. Next, it explores the definitions of economic coercion and countermeasures and considers whether the actions taken by EU institutions in the context of the Cyprus banking haircut would satisfy either of these definitions. Lastly, this Article studies whether EU law can provide a basis for liability of EU institutions in case of acts adopted by such institutions to address a financial crisis in a manner that targets the rights of investors and, in particular, in the Cyprus Banking Haircut.

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I. INTRODUCTION

There is no question that, in cases of extreme financial crisis, investors' expectations and the value of their investments may be greatly affected by actions taken by the state. However, before investors can seek recourse there are several important elements to consider. Apart from the procedural and substantive legal hurdles an investor will face, investors must also determine the parties/persons against which investors' claims will be raised. Indeed, establishing the relevant party is of material importance; it determines competent courts, applicable law, and available property for enforcement. At first glance, the question of the suitable defendant appears easy to answer, as in most cases the negative measures were adopted by the States themselves.

However, this presumption of state responsibility was challenged in the 2013 Cyprus banking crisis that led to the haircut[1] of deposits in Cyprus's two largest banks. Indeed, Cyprus's president proclaimed that the decision for the haircuts actually was imposed by European Institutions.[2] This Article explores such allegations. Additionally, in the case of sovereign default within the European Union ("EU"), this Article attempts to answer

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[†] Lecturer, European University of Cyprus; PhD, Tilburg University.

[1] A haircut is the difference between prices at which someone can buy or sell a security.

[2] *See* President Nicos Anastasiades, Address to the People of Cyprus (Mar. 17, 2013) (stating that Eurogroup had given him two blackmail-style options, either disorderly bankruptcy or the depositors' bail in).

the question of whether the EU can be held accountable for investors' losses. In response to the above question, Part II of this Article explores the concept of sovereignty vis-à-vis a state's participation in international organizations, with a focus on the EU. In Part III, this Article studies the negative aspect of sovereignty, namely the principle of non-intervention, which protects a state from external interference by other sovereign states. In this context, this Article reviews the notion of economic coercion and examines whether it constitutes such prohibited intervention. In Part III, this Article explores whether the recent banking haircut in the eurozone, especially the Cyprus banking haircut, can be attributed to the EU and its institutions on the basis of economic coercion. Lastly, the Article explores whether the EU and its institutions can be held liable for the Cyprus banking haircut under EU Law.

II. THE NOTION OF SOVEREIGNTY

A. The History of the Concept of Sovereignty

To explore whether liability can be attributed to the EU for the Cyprus banking haircut and the EU can therefore serve as a defendant, the notion of sovereignty is of vital importance. The notion of sovereignty is controversial and has puzzled law scholars and political scientists almost since the inception of international law itself.[3] The concept of sovereignty first arose in Rome. However, the Roman understanding of sovereignty lacked a definite theory of how sovereignty is created.[4] The current concept of sovereignty arose much later, in the 16th and 17th centuries.

In the 16th century, in *Les Six Livres de République*, Jean Bodin recognized sovereignty as the absolute and perpetual power of a state to set binding laws, limited only by the laws of God and natural law.[5] Thomas Hobbes, a century later, indicated that the sovereignty of the state is an absolute power superior to all, having a right over all.[6] While both these theories conceptualize sovereignty as the absolute power of the state, they differ in how they treat powers outside of the state. Specifically, Jean Bodin's theory identified sovereignty as an unlimited power subject to

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[3] Helmut Steinberger, *Sovereignty*, ENCYCLOPEDIA OF PUBLIC INTERNATIONAL LAW, Vol. IV 501 (Rudolph Bernhardt 1st ed., 2000).

[4] C. H. McIlwain, *A Fragment on Sovereignty*, 48 POL. SCI. Q. 94, 96 (1933).

[5] Richard McKeon, Book Review, 74 ETHICS 74, 74–75 (1963) (reviewing JEAN BODIN, THE SIX BOOKS OF A COMMONWEALE (1576)).

[6] THOMAS HOBBES, THE CITIZEN Ch. 6 ¶¶ 12-15 (Bernard Gert ed., Thomas Hobbes trans., 1972) (1651).

neither external powers nor human laws.[7] On the other hand, Hobbes considered sovereignty an absolute power within the state's territory but failed to address the relationship of sovereignty to international law and international organizations.[8]

Most scholars[9] trace the modern concept of sovereignty to the end of the Thirty-Years' War and the Treaty of Westphalia.[10] The Treaty of Westphalia laid the ground for states to become "sovereign and independent" from the Holy Roman Empire.[11] These states were sovereign in the sense that they enjoyed "supreme authority" over internal affairs within their territory and independence in their external relations.[12] Such authority was secular, derived out of self-assertion and survival, rather than stemming from religious grounds.[13] The Treaty of Westphalia recognized states were equal regardless of their form of governance or their allegiance to the Catholic or Protestant Church.[14] As a consequence of these concepts of sovereignty and equality, the principle of non-intervention, or the idea that other states cannot interfere in a state's internal affairs, is now a well-established principle of international law.[15]

B. The Current Concept of Sovereignty

Since the Treaty of Westphalia, case law and scholarly research have extensively explored the principles of sovereignty and non-intervention.

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7 URMILA SHARMA & SUDESH KUMAR SHARMA, PRINCIPLES AND THEORY OF POLITICAL SCIENCE 145 (2000); *see also* William C. van Vleck, Book Review, 44 HARV. L. REV. 317, 317 (1930) (reviewing CHARLES GROVE HAINES, THE REVIVAL OF NATURAL LAW CONCEPTS (1930)) (stating that Bodin's philosophy "tended to discredit the old natural law ideas and to make the state the sole source of law").

8 *See* HOWARD WARRENDER, THE POLITICAL PHILOSOPHY OF HOBBES: HIS THEORY OF OBLIGATION 119 (1970) (analyzing what Hobbes considered international relations and the causes for the war among nations).

9 *See* ROBERT ROSWELL PALMER & JOEL COLTON, A HISTORY OF THE MODERN WORLD 148 (1992) (noting the elements of statehood can be traced before that time); *but see* K. J. Holsti, Book Review, 1 JAPANESE J. POL. SCI. 157–72 (2000) (reviewing STEPHEN D. KRASNER, SOVEREIGNTY: ORGANIZED HYPOCRISY (1999)).

10 G. John Ikenberry, Book Review, 80 FOREIGN AFF. 157 (2001) (reviewing DANIEL PHILPOTT, REVOLUTIONS IN SOVEREIGNTY: HOW IDEAS SHAPED MODERN INTERNATIONAL RELATIONS (2001)).

11 D. W. Greig, Book Review, 58 BRIT. Y.B. INT'L L. 366, 366–68 (1988) (reviewing ANTONIO CASSESE, INTERNATIONAL LAW IN A DIVIDED WORLD (1986)).

12 DJURA NINČIĆ, THE PROBLEM OF SOVEREIGNTY IN THE CHARTER AND IN THE PRACTICE OF THE UNITED NATIONS 5 (1970).

13 Helmut Steinberger, *Sovereignty*, ENCYCLOPEDIA OF PUBLIC INTERNATIONAL LAW, Vol. IV 501 (Rudolph Bernhardt, 1st ed. 2000).

14 BRIAN R. URLACHER, INTERNATIONAL RELATIONS AS NEGOTIATION 19 (2015).

15 Michael Wood, *Non-Intervention (Non-interference in domestic affairs)*, ENCYCLOPEDIA PRINCETONIENSIS, https://pesd.princeton.edu/?q=node/258 (last visited Nov. 27, 2017).

However, despite this analysis, both concepts continue to be fluid and puzzling. The first case to set out a widely-accepted definition of sovereignty was the *Island of Palmas Arbitral Award of 1928*. The award stipulated that "[s]overeignty in the relations between states signifies independence. Independence in regard to a portion of the globe is the right to exercise therein, to the exclusion of any other state, the functions of a state."[16] As the *Palmas* case indicates, independence is inherently linked with the element of territory in the sense that, for an entity to be independent, it should be able to freely dispose of its own territory without external interferences.[17]

This definition also directly linked sovereignty with the concept of statehood, although the two concepts are not identical. Indicatively, Article 1 of the Montevideo Convention on Rights and Duties of States of 1933, which echoes customary international law, defines a state as a person of international law which possesses: (a) a permanent population; (b) a defined territory; (c) government in the sense of dominion; and (d) capacity to enter into relations with other States."[18] Indeed, it is a principle of international law that sovereign states enjoy absolute dominion within their territory without external intervention.

C. *The Sovereignty of International Entities*

These definitions focus on states. However, they do not indicate whether international entities other than states may enjoy sovereignty in the sense described above. This question is of particular relevance in relation to international organizations, particularly the EU.

EU institutions possess unusual powers and traits, including, *inter alia*, citizenship, the lack of internal borders within member states, and the development of a supranational legal system of "EU law."[19] However, such powers and traits were awarded to the EU by the member states through international conventions rather than arising as inherent EU characteristics.

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[16] Island of Palmas Case (U.S. v Neth.), Hague Ct. Rep. II RIAA 829, 838 (Perm. Ct. Arb. 1928).

[17] Geert Van Calster, *International Law and Sovereignty in the Age of Globalization*, *in* INTERNATIONAL LAW AND INSTITUTIONS 106 (Aaron Schwabach & John Cockfield eds., 2009).

[18] Convention on Rights and Duties of States art. 1, Dec. 26, 1933, 165 U.N.T.S. 19.

[19] *See* Case 6/64, Costa v. E.N.E.L., 1964 E.C.R. 587 (" . . . the EEC Treaty has created its own legal system which . . . became an integral part of the legal systems of the Member States and which their courts are bound to apply.").

In particular, the Treaty of Rome,[20] the Treaty of Maastricht,[21] and the Treaty of Lisbon[22] created the EU institutions which enjoy these powers and thus played a large role in the creation of the EU.

Prior to these treaties, the powers listed above were exercised by the governments of each member state. Through these treaties, states agreed to award such powers to EU institutions. As with any other international treaty, the obligations assumed by the states through these treaties are mandatory on the basis of states' consent and the well-established international law principle "*pacta sunt servanda*."[23] In this sense, no member state can enjoy sovereignty in the sense described above—an absolute power free from external interventions—as, *inter alia*, member states have delegated their sovereignty to the EU and share that power in certain policy areas.

The EU has led scholars to question the previous definition of sovereignty and consider alternative theories of sovereignty that will adequately include the EU in their ambit. Bodin's unitary and indivisible nature of sovereignty does not allow for delegation of powers by a state to an external authority and therefore could not address the current situation with the EU.[24] In response, scholars have invoked other theories of sovereignty, such as pooled sovereignty.[25] Indeed, the EU is considered a prominent example of pooled sovereignty,[26] or "poly-centered sovereignty." In the model of pooled sovereignty, the powers are both disaggregated and reaggregated. They are disaggregated in the sense that the state does not enjoy exclusive authority over its policies,[27] while they are reaggregated in the sense that EU regulations and directives are adopted by the EU

[20] Treaty Establishing the European Economic Community, Mar. 25, 1957, 294 U.N.T.S. 3.

[21] Treaty on European Union, Feb. 7,1992, 1755 U.N.T.S. 3.

[22] Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community, Dec. 13, 2007, 2702 U.N.T.S. 3.

[23] FABRIZIO CAPOGROSSO, SHARED SOVEREIGNTY AND DENATIONALISATION OF STATEHOOD IN THE EUROPEAN UNION 11 (2008).

[24] *See generally* STEPHEN D. KRASSNER, SOVEREIGNTY: ORGANIZED HYPOCRISY (1999).

[25] *See* NANNERL O KEOHANE, PHILOSOPHY AND THE STATE IN FRANCE 71 (1980) (stating "we see the principal point of sovereign majesty and absolute power to consist in giving laws to subjects in general, without their consent"); *see also* Robert Keohane, *Ironies of Sovereignty: The European Union and the United States*, 40 J. COMMON MKT. STUD. 743, 743–65 (2002).

[26] *Pooled sovereignty*, OXFORD INDEX , http://oxfordindex.oup.com/view/10.1093/oi/authority.20110803100336931 (last visited Nov. 30, 2017).

[27] Hadii M. Mamudu & Donley T. Studlar, *Multilevel Governance and Shared Sovereignty: European Union, Member States, and the FCTC*, 22 GOVERNANCE 73, 73–97 (2009).

institutions and apply uniformly to all member states.[28] In pooled sovereignty, states remain sovereign but contractually delegate their powers to an external institution. The external institution operates collectively, as it is comprised by all member states, and sets policies that may differ from each individual state's ideal standpoint in the interest of international cooperation and collective good.[29]

Some commentators suggest that pooled sovereignty is not an appropriate concept for the EU because this type of sovereignty is exercised by several actors and is therefore unable to address the current status of the EU, especially the Economic Monetary Union ("EMU").[30] On one hand, the transfer of sovereignty within the EU exceeds mere "pooling" in the area of monetary policy, as monetary authority is exercised almost exclusively at an EU level. On the other hand, in areas such as fiscal policy, power is mostly exercised by the states independently.[31] Some commentators argue that, in such a case, sovereignty is divided: certain competencies are prerogatives of the State, while others belong to the EU. [32]

Even this notion appears simplistic and falls short of addressing the shared competencies that belong both to the states and to the EU.[33] In response, scholars developed the theory of cooperative sovereignty. Here, sovereign states collaborate with other sovereign entities while applying the same rules and principles as in a pluralist constitutional order.[34] Instead of being applied in an hierarchical order, these rules work toward the same end, namely the fulfilment of their shared sovereign values, including a common market free from internal borders, common agriculture and fishery policies, and common minimum standards on human rights.[35] Scholars have criticized this as "unsound," because sovereignty in itself cannot be

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[28] Thomas W. Pogge, *Cosmopolitanism and Sovereignty*, 103 ETHICS 48, 48–75 (1992); *See also* Neil Walker, *Late Sovereignty in the European Union*, *in* SOVEREIGNTY IN TRANSITION 15 (Neil Walker ed., 2006).

[29] Nicolas Jabko, *Which Economic Governance for the European Union? Facing up to the Problem of Divided Sovereignty*, SWEDISH INST. FOR EUR. POL'Y STUD. 13 (2011), http://www.sieps.se/sites/default/files/2011_2_1.pdf.

[30] Samantha Besson, *Sovereignty in Conflict*, EUROPEAN INTEGRATION ONLINE PAPERS (2004), http://eiop.or.at/eiop/texte/2004-015a.htm.

[31] Jabko, *supra* note 29, at 13.

[32] *Id*.

[33] Enzo Cannizzaro, *Introduction* to THE EUROPEAN UNION AS AN ACTOR IN INTERNATIONAL RELATIONS xiv (Enzo Cannizzaro ed., 2002).

[34] NEIL MACCORMICK, QUESTIONING SOVEREIGNTY: LAW, STATE, AND NATION IN THE EUROPEAN COMMONWEALTH 203 (2002).

[35] *See id*.; Besson, *supra* note 30, at 14.

divided.[36] Dividing sovereignty would undermine the nature of sovereignty as an absolute power, as it is only competencies that can be limited.[37] Nonetheless, cooperative sovereignty supports the notion that competencies can be delegated, because delegation is nothing more than a demonstration and reaffirmation of sovereignty.[38]

While it is clear that the concept of sovereignty is unresolved, particularly in terms of the EU, a few conclusions can be drawn. Specifically, sovereignty allows a state, in such fields and policy areas where it has not delegated authority to other institutions, to regulate its internal affairs free from external interferences. The EU is a unique case. The EU enjoys *sui generis* powers similar to the sovereignty awarded by the member states through international conventions.

III. THE NEGATIVE ASPECT OF SOVEREIGNTY

A. The Non-Intervention Principle

As noted above, sovereignty entails absolute dominion over a state's territory, free from any external interference by other sovereign states. The definition of sovereignty thus implies that sovereign states have a negative obligation not to interfere in the internal affairs of other states, as all states are equal. The principle of non-intervention constitutes one of the fundamental norms of international law. In fact, many scholars, such as Antonio Cassese and Jianming Shen, argue that the principle of non-intervention has risen to the status of *jus cogens*.[39] The principle is embodied in the Charter of the United Nations. Although the Charter does not explicitly refer to non-intervention, it can be inferred from Articles 2(4) and 2(7).[40] It can also be inferred from the Friendly Relations Declaration.[41]

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[36] *See* Martin Loughlin, *Why Sovereignty?*, *in* SOVEREIGNTY AND THE LAW: DOMESTIC, EUROPEAN AND INTERNATIONAL PERSPECTIVES 46 (Richard Rawlings et al. eds., 2013).

[37] *Id.* at 47.

[38] *Id.*

[39] ANTONIO CASSESE, INTERNATIONAL LAW IN A DIVIDED WORLD 147 (1986) ("The importance of this principle [of nonintervention] for States leads one to believe that it has by now become part and parcel of jus cogens."); Jianming Shen, *The Non-Intervention Principle and Humanitarian Interventions under International Law*, 7 INT'L LEGAL THEORY 1, 5 (2001); *see also* 1 OPPENHEIM'S INTERNATIONAL LAW 428 (Robert Jennings & Arthur Watts eds., 9th ed. 2008) (stating that the principle "is a corollary of every state's right to sovereignty, territorial integrity and political independence").

[40] Philip Kunig, *Prohibition of Intervention*, MAX PLANCK ENCYCLOPEDIA OF PUBLIC INTERNATIONAL LAW (Apr. 2008), http://opil.ouplaw.com/view/10.1093/law:epil/9780199231690/law-9780199231690-e1434?prd=EPIL.

[41] G.A. Res. 2625 (XXV), at 121–24 (Oct. 24, 1970).

The principle of non-intervention is explicitly identified in the UN General Assembly Declaration on the Inadmissibility of Intervention and Interference in the Domestic Affairs of States.[42] Furthermore, Article 32 of the Charter of Economic Rights and Duties of States prohibits "the use of economic, political or any other type of measures to coerce another State in order to obtain from it the subordination of the exercise of its sovereign rights."[43] The principle was also recognized by the International Court of Justice ("ICJ") in its very first case, *Corfu Channel, United Kingdom v. Albania*.[44]

Finally, the principle was emphasized in the renowned judgment in *Nicaragua vs. United States*. There, the court determined that "the principle of non-intervention involves the right of every sovereign State to conduct its affairs without outside interference; though examples of trespass against this principle are not infrequent, the Court considers that it is part and parcel of customary international law."[45] The Court later states "the principle forbids all States or groups of States to intervene directly or indirectly in the internal or external affairs of other States" and that:

> [A] prohibited intervention must accordingly be one bearing on matters in which each State is permitted, by the principle of State sovereignty, to decide freely. One of these is the choice of a political, economic, social and cultural system, and the formulation of foreign policy. Intervention is wrongful when it uses methods of coercion in regard to such choices, which must remain free ones . . . the element of coercion . . . defines, and indeed forms the very essence of, prohibited intervention.[46]

According to Professor Antonios Tzanakopoulous, a scholar and author in this area, the Court in the *Nicaragua* case recognized that states enjoy an area of freedom where each respective state may act alone in the

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42 G.A. Res. 2131 (XX), at 11–12 (Dec. 21, 1965).

43 G.A. Res. 3281 (XXIX), at 50–55 (Dec. 12, 1974).

44 Corfu Channel (U.K. v. Alb.), Merits, 1949 I.C.J. Rep. 4, ¶ 121 (Apr. 9, 1949) (The Court proclaimed "the alleged right of intervention as the manifestation of a policy of force, such as has, in the past, given right to the most serious abuses and as such cannot, whatever be the present defects in international organization, find a place in international law.").

45 Case Concerning Military and Paramilitary Activities in and Against Nicaragua (Nicar. v. U.S.), Merits, 1986 I.C.J. Rep. 14, ¶ 202 (June 27).

46 *Id.* at ¶ 205.

manner it pleases stemming from that state's sovereignty.[47] That area includes fiscal, tax, and foreign policy and the free choice of political, economic, social, and cultural systems.[48] Within that area, as discussed above, no external intervention is permissible. However, that freedom may be circumscribed by obligations assumed by states through international treaties.

Despite the seemingly-established status of the principle of non-intervention, as will be demonstrated below, the actual content of the non-intervention principle is unclear.[49] Additionally, the principle has been set aside or abused several times by states with significant economic power through economic coercion.[50]

Contributing to the lack of clarity on the principle of non-intervention, case law is limited to few cases with very specific fact patterns. Indicatively, the ICJ has only examined three cases relating to the principle of non-intervention, namely the *Corfu Channel* case,[51] the case of *Nicaragua v. United States of America*,[52] and the case of *DRC v. Uganda*,[53] all of which had very specific facts that related to the use of military force.[54] Thus, in light of the limited caselaw, there is no consensus on what constitutes intervention, and therefore which intervention is not allowed under international law.[55] For the purposes of this study, this Article will focus only on the notion of "economic coercion," which constitutes a form of prohibited intervention.

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47 Antonios Tzanakopoulos, *The Right to be Free from Economic Coercion*, 4 CAMBRIDGE J. INT'L & COMP. L. 616, 618–19 (2015).

48 *Id.*

49 *See generally* Oliver J. Lissitzyn, Book Review, 76 HARV. L. REV. 668 (1963) (reviewing MYRES S. MCDOUGAL & FLORENTINO P. FELICIANO, LAW AND MINIMUM WORLD PUBLIC ORDER: THE LEGAL REGULATION OF INTERNATIONAL COERCION (1961)).

50 *See generally* T. Akinola Aguda, Book Review, 81 AM. J. INT'L L. 284 (1987) (reviewing DILEMMAS OF ECONOMIC COERCION: SANCTIONS IN WORLD POLITICS (Miroslav Nincic & Peter Wallensteen eds., 1983)).

51 *See generally* Corfu Channel, *supra* note 44 (referred to U.K.'s unauthorized entry into the territorial waters of Albania, so as to look for mines that would be brought as evidence before the I.C.J.).

52 *See generally* Case Concerning Military and Paramilitary Activities in and Against Nicaragua, *supra* note 45 (related to armed activities taken by U.S. military forces against the Nicaraguan Government).

53 *See generally* Case Concerning Armed Activities on the Territory of the Congo (Dem. Rep. Congo v. Uganda), Judgment, 2005 I.C.J. Rep. 168 (Dec. 19, 2005) (related to the presence and action of the military forces of Uganda on the borders of eastern Congo).

54 NATALINO RONZITTI, COERCIVE DIPLOMACY, SANCTIONS AND INTERNATIONAL LAW 6 (2016).

55 JOHN CHARVET & ELISA KACZYNSKA-NAY, THE LIBERAL PROJECT AND HUMAN RIGHTS 275 (2008); one exception is the use of force which is specifically prohibited under Art. 2.4 of the UN Charter. U.N. Charter art. 2, ¶ 4.

B. Economic Coercion

Defining economic coercion is not an easy task, as a large portion of the actions taken by states to optimize their economic self-interests leads to detrimental consequences for other states.[56] Economic coercion can include all methods traditionally used for economic compulsion.[57] In fact, since World War II, economic relations among states have been shaped by the practice of economic coercion.[58] Clearly not every action that falls into this category can be deemed illegal. Rather, only those practices that are unnecessarily or unreasonably destructive to the essential values of an innocent target state, or which might significantly endanger international peace, are prohibited.[59]

Professor Derreck Bowett suggested that the decisive element of whether various economic measures should be considered illegal coercion depends on if the action taken by the involved state can be attributed to an improper motive or intent.[60] Put simply, an act on its own cannot be coercive, but it may become illegal coercion upon proof of improper motive or purpose.[61] Since a state's *mens rea* is not easy to deduce, let alone prove, Professor Bowett indicated that "it will require a great deal of practice, of 'case-law', to give the concept of illegal economic coercion substance and definition."[62]

Another criterion that was suggested to determine whether economic measures could constitute illegal coercion is whether the state imposing the measures does so to obtain "advantages of any kind" while subordinating the sovereignty of the state upon which the coercion is inflicted.[63] Again, this criterion is vague, as economic measures cannot be deemed illegal on the sole basis that they convey advantages to the acting state while damaging the interests of another state, particularly given the competition existing between

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[56] *See* Lissitzyn, *supra* note 49.

[57] Comment, *The Use of Nonviolent Coercion: A Study in Legality under Article 2(4) of the Charter of the United Nations*, 122 U. PA. L. REV. 983, 991 (1974).

[58] *See* Aguda, *supra* note 50.

[59] Paul Stephen Dempsey, *Economic Aggression & Self-Defense in International Law: The Arab Oil Weapon and Alternative American Responses Thereto*, 9 CASE W. RES. J. INT'L L. 253, 261 (1977).

[60] Derek Bowett, *Economic Coercion and Reprisals by States*, 13 VA. J. INT'L L. 1, 5 (1977).

[61] Edwin Ifeanyichukwu Nwogugu, *Legal problem of foreign investments*, *in* 153 RECUEIL DES COURS: COLLECTED COURSES OF THE HAGUE ACADEMY OF INTERNATIONAL LAW, at 253 (1983).

[62] *See* Bowett, *supra* note 60, at 4.

[63] *See, e.g.*, G.A. Res. 3171 (XXVIII), at 52–53 (Dec. 17, 1973); Andre Beirlaen, *Economic Coercion and Justifying Circumstances*, 18 REV. B.D.I. 57, 67 (1984).

various economies.[64] According to Professor Tzanakopoulos, a decisive conclusion can be inferred from Article 52 of the Vienna Convention on the Law of Treaties, which refers to the case when a State is coerced to enter into an international treaty. In such a case, the treaty is nonetheless valid unless coercion was exercised by threat or use of force.[65]

"Force" refers to any military force or physical force, used or threatened. However, it is unclear whether economic or political force is included in the definition of "use of force." The definition of "force" becomes essential in such a case, as a literal interpretation of the word might lead to the conclusion that force is limited to armed force, while a broader, liberal interpretation of the term would include political and economic force. This matter troubled the states when negotiating the Vienna Convention,[66] but the choice of words of Article 52 demonstrates their unwillingness to clear up this matter.[67]

As might be expected, the scholars are divided on this topic. Some commentators support the view that political and economic pressure is not included in the notion of force.[68] Others argue that the term "force" should not be limited to military action, but should also include economic and political coercion that may endanger international peace, security, or justice.[69] This view is supported by the Separate Declaration on the Prohibition of Military, Political and Economic Coercion in the Conclusion of Treaties, which was separately adopted in 1969 by the delegates of the UN Conference on the Law of Treaties.[70] The declaration specifically

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[64] *See* Beirlaen, *supra* note 63, at 69.

[65] *See* Tzanakopoulos, *supra* note 47, at 621.

[66] In the first session of the International Conference held to formulate the Draft Articles on the Law of Treaties into an International Treaty in 1968, the meaning of coercion was deliberated in great detail. In this regard, Article 49 of the Draft Articles (current Article 51) was proposed to be amended by the 19th Amendment so that economic and political pressure would be included. This issue was discussed in the fiftieth meeting, held on May 3, 1968, but no consensus could be reached. *See* K.R. Vivek, *Coercion: Economic and Political Pressure*, 1 "UGDAM VIGYATI" - THE ORIGIN OF KNOWLEDGE 1, 2 (2015) (India).

[67] Robert E. Dalton, Book Review, 106 AM. J. INT'L L. 898, 898–903 (2012) (reviewing THE VIENNA CONVENTIONS ON THE LAW OF TREATIES: A COMMENTARY (Olivier Corten & Pierre Klein eds., 2011)).

[68] *See, e.g.*, LASSA FRANCIS & LAWRENCE OPPENHEIM, INTERNATIONAL LAW: A TREATISE. DISPUTES, WAR AND NEUTRALITY (Hersch Lauterpacht ed., 7th ed. 1952); C.H.M. Waldock, *The Regulation of the Use of Force by Individual States in International Law*, in 81 RECUEIL DES COURS: COLLECTED COURSES OF THE HAGUE ACADEMY OF INTERNATIONAL LAW 492 (1951).

[69] *See, e.g.*, JULIUS STONE, LEGAL CONTROLS OF INTERNATIONAL CONFLICT: A TREATISE ON THE DYNAMICS OF DISPUTES – AND WAR-LAW iv, 851 (1954).

[70] CATHERINE BRÖLMANN & YANNICK RADI, RESEARCH HANDBOOK ON THE THEORY AND PRACTICE OF INTERNATIONAL LAWMAKING 95 (2016).

condemns "the threat or use of pressure in any form whether military, political or economic by any State in order to coerce . . . ."[71]

In all cases, the equation of coercion with illegal intervention should be interpreted to mean that anything short of coercion, e.g. mere interference with a state's choices, is lawful, so long as the interfering state does not breach any of its own obligations under international law.[72] Thus, identifying the scope of what is considered coercion is necessary to determine whether recent haircuts in the eurozone, and especially the Cyprus banking haircut, can be attributed to the EU and its institutions on the basis of coercion.

IV. THE FACTS OF THE CYPRUS HAIRCUT

Cyprus is the third smallest country in the EU and is located in the northeastern Mediterranean Sea, to the south of Turkey. Although it joined the EU as a de facto divided island, the entire country is part of the EU territory.[73] Cyprus is a well-established financial and investment center due to its investor-friendly tax regime and, up to 2013, it had a strong financial and service sector.

In March 2013, Cyprus was shocked when the national government decided to close Cyprus' second largest bank, Cyprus Popular Bank ("CPB"), imposed a depositor bail-in on the deposits of Cyprus' largest bank, Bank of Cyprus ("BOC"), and imposed capital controls on all deposits in Cyprus banks. Other authors have explored reasons behind the financial and banking crisis in the Republic of Cyprus.[74] This Article explores whether the banking haircut was a product of coercion by the EU's institutions, especially the European Central Bank ("ECB") and the Council of the EU, as was contemplated by the President of Cyprus, Mr. Anastasiades.[75]

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[71] U.N. Conference on the Law of Treaties, *Reports of the Committee of the Whole*, art. 49, U.N. Doc. A/CONF.39/14 (1969).

[72] Tzanakopoulos, *supra* note 47, at 9

[73] *European Union Immigration: Cyprus*, EUROPEAN UNION IMMIGRATION, https://www.euimmigration.org/eu_cyprus.html (last visited Apr. 12, 2017).

[74] *See* G.I., *An interview with Athanasios Orphanides: What Happened in Cyprus?*, ECONOMIST (Mar. 28, 2013), https://www.economist.com/blogs/freeexchange/2013/03/interview-athanasios-orphanides.

[75] *See* Anastasiades, *supra* note 2 (stating that Eurogroup had given him two blackmail-style options: disorderly bankruptcy or the depositors' bail in).

The problems faced by the two major banks in Cyprus did not appear out of the blue. Indeed, there were several signs that the banks were in distress well before March 2013, but these were neglected. Indicatively, as part of a Capital Exercise conducted on October 26, 2011 by the European Banking Authority ("EBA") and the Central BOC, BOC identified a capital buffer of €1.472 billion and CPB identified a capital buffer of € 2.116 billion.[76] As a result, at the beginning of November 2011, the credit ratings agency, Moody's, downgraded three Cypriot banks. In particular, BOC was downgraded by one notch to Ba2 from Ba1, Hellenic Bank by one notch to Ba2 from Ba1, and Marfin Popular Bank Public Co. Ltd. by three notches to B2 from Ba2.[77] Not long after the downgrades, EBA issued its recommendation on the creation and supervisory oversight of temporary capital buffers to restore market confidence.[78] This recommendation required national supervisory authorities of participating EU member state banks to raise their Core Tier 1 Capital to nine percent after accounting for an additional buffer against stressed sovereign risk holdings by June 30, 2012.

Both BOC and CPB needed additional funding. Correspondingly, on March 2, 2012, CPB announced a capital-raising plan, but the Greek Sovereign Bonds Haircut through Private Sector Involvement ("PSI") had immediate and devastating implications for both banks. Indeed, the two banks had purchased large amounts of Greek Government Bonds and lost billions of euros through the Greek PSI.[79] In particular, BOC announced losses of one billion euros, while CPB announced losses of two and a half billion euros,[80] which further increased the needs for additional capital buffer. Cyprus could have requested support for its banks by the EU, but

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[76] *See* Fiona Mullen, *Greek Haircut: Cyprus Banks Announce EUR 3.6 Bln Buffer Need*, FIN. MIRROR (Oct. 26, 2011), http://www.financialmirror.com/news-details.php?nid=24841.

[77] *See Moody's Downgrades Three Cypriot Banks Following Cyprus Sovereign Downgrade; Banks On Review For Further Downgrade*, MOODY'S INV. SERV. (Nov. 8, 2011), https://www.moodys.com/research/Moodys-downgrades-three-Cypriot-banks-following-Cyprus-sovereign-downgrade-banks--PR_229745.

[78] *See EBA Recommendation on the Creation and Supervisory Oversight of Temporary Cap. Buffers to Restore Mkt. Confidence*, U.N. Doc. EBA/REC/2011/1, at 1 (Dec. 8, 2011).

[79] *See* Panicos Demetriades, Governor, Cent. Bank of Cyprus, Cyprus Financial Crisis: The Framework for an Economic Recovery Within the Eurozone at ¶6 (Dec. 11, 2012) (transcript available at https://www.centralbank.cy/en/the-governor/previous-governors/previous-governor-s-speeches/panicos-o.-demetriades/11122012). The discussion was organised by the Hellenic American Bankers Association and the Cyprus-US Chamber of Commerce, where it stipulated that "The Greek PSI alone cost Cypriot banks nearly 25% of the country's GDP, because of excessive concentration of Greek debt in the balance sheets of the two largest Cypriot banks."

[80] George Psyllides, *2.5 Billion Euro Loss for Marfin*, LAWYERS IN CYPRUS (Mar. 1, 2012), http://www.lawyersincyprus.com/el/news-read/25-billion-euro-loss-for-marfin.

that would have required Cyprus to agree to a Memorandum of Understanding with the Troika, something that the Cyprus government was not prepared to do at the time due to the political cost that was at stake once agreeing to severe austerity measures. Instead, in an attempt to help salvage CPB, the Cypriot Parliament agreed on May 18, 2012 to underwrite the issue of €1.8 billion in capital for the bank's recapitalization, in case the latter was unable to raise funds from private sources. This underwriting raised state aid concerns, but it was approved by the European Commission on September 13, 2012 on the precondition that the Cyprus authorities would submit a plan no later than six months from the date of the European Commission's approval, to demonstrate how the bank would become viable with the assistance of the state.[81]

By the deadline of June 30, 2012, CPB had only raised €3 million, although the Cyprus government acquired bank shares which amounted to the equivalent of about €1.8 billion.[82] The state paid CPB by transferring a 12-month sovereign bond, which would be rolled over for a period of five years. By that time, all three major credit rating agencies had downgraded Cyprus' sovereign debt to junk status, thus eliminating the possibility that the ECB could accept Cypriot bonds as collateral for a loan.[83]

On June 25, 2012, Cyprus entered the European Stability Mechanism ("ESM") without specifying the amount of money it required, something that was necessary in order for a Memorandum of Understanding to be negotiated between Cyprus and the ESM. Unfortunately, a settlement was not reached until after the Eurogroup meeting on March 15, 2013. In the meantime, both major banks in Cyprus required Emergency Liquidity Assistance ("ELA") from the Central BOC. This was approved by both the Central BOC and by the ECB. The details of this provision were unknown at the time, as neither the ECB nor the National Central Banks ("NCBs"), including the Cyprus Central Bank, publish details on their collateral holdings that are part of the monetary policy operations of the Eurosystem.[84] As was later revealed, CPB had already resorted to ELA in September 27,

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[81] See European Commission Press Release IP/12/958, The Commission, Rescue Recapitalisation of Cyprus Popular Bank (Sep. 13, 2012).

[82] Press Release, Ministry of Finance, Recapitalisation of CPB Public Co. Ltd. and BOC Public Co. Ltd., (Sept. 2, 2012).

[83] James Wilson, Daniel Dombey & Peter Spiegel, *Cyprus Requests Eurozone Bailout*, FIN. TIMES, (June 25, 2012), https://www.ft.com/content/80320e0e-bed0-11e1-b24b-00144feabdc0.

[84] Willem Buiter, Jürgen Michels & Ebrahim Rahbari, *ELA: An Emperor without Clothes?* CITI INVESTMENT RESEARCH & ANALYSIS (2011), https://www.willembuiter.com/ela.pdf.

2011,[85] initially requesting 300 million euros. That amount grew to 1.8 billion on January 2012, 3.8 billion in May 2012, 4.2 billion by February 2013, and by the time CPB was led into resolution, the amount grew to a staggering 9.1 billion euros.[86]

The two banks received ELA from the Central BOC until March 21, 2013, with the consent of the Governing Council of the ECB. On March 21, 2013, the ECB's Governing Council announced that, in accordance with prior decisions, on March 25, 2013, it would cease to provide ELA to both Cypriot banks, due to "the lack of clear and binding policy decisions on behalf of the Cypriot side to implement a preliminarily agreed financial assistance programme."[87] However, it was already clear that CPB would become insolvent by the end of 2012, as it was in no position to service ELA past June 2012.[88]

This fact appears to have been known to the ECB. Indicatively, in response to a request for an opinion on the Cypriot government's plan for the recapitalization of CPB, the ECB stated that "the objectives pursued by the support measures may be better achieved through bank resolution tools."[89] Hence, the continued provisioning of ELA to CPB was questionable, as it is contrary to the ECB's rule that ELA is awarded only to solvent institutions.[90] In an attempt to defend its actions, the Central BOC argued that not assisting CPB would lead to bankruptcy, which would cause panic and threaten the entire banking system.[91]

In addition to the problems with the two major banks, Cyprus also had to address its own debt. By March 2013, the country was in need of an estimated 17 billion euros, which corresponded approximately to the size of

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85 Athanasios Orphanides, *What Happened in Cyprus? The Economic Consequences of the Last Communist Government in Europe* (Inst. for Monetary and Fin. Pol'y Working Paper Series, No. 79, 2014), https://www.econstor.eu/bitstream/10419/97787/1/IMFS_WP_79.pdf.

86 Gikas A. Hardouvelis, *Overcoming the Crisis in Cyprus*, EUROBANK (2014), http://www.hardouvelis.gr/FILES/PROFESSIONAL%20WORK/20January2014Q.pdf.

87 *Provision of Emergency Liquidity Assistance to the Two Largest Cypriot Banks*, CENT. BANK OF CYPRUS (June 17, 2013), https://www.centralbank.cy/en/announcements/17062013.

88 G.I., *supra* note 74, at 18

89 *Opinion of the European Central Bank* CON/2012/50, on the Recapitalization of the Cyprus Popular Bank (Jul. 2, 2012).

90 *Emergency Liquidity Assistance (ELA) and Monetary Policy*, EUR. CENT. BANK (2016), https://www.ecb.europa.eu/mopo/ela/html/index.en.html.

91 Sofronis Clerides, *The Collapse of the Cypriot Banking System: A Bird's Eye View*, 8 CYPRUS ECON. POL'Y REV. 3, 29 (2014).

the country's entire economy.[92] Thus, in March 2013, the newly appointed Cypriot government was faced with a difficult choice: accept the terms of the bailout programme offered by Troika "as is," or further delay the negotiations to achieve a better deal and face possible collapse of its banking system and economy. The initial deal negotiated by European finance ministers, the ECB, and the International Monetary Fund ("IMF"), provided for a one-time "haircut" of 6.75% for deposits of up to €100,000 and 9.99% for deposits above €100,000. This included all deposits (in current and fixed deposit accounts, interest bearing or not) and all banks (including branches of international banks) operating in Cyprus.[93] The measure was strongly criticized as a "disastrous precedent."[94] On March 18, 2013, the bill for said measure was debated in the Cyprus parliament and was rejected on March 19, 2013.[95]

On March 21, 2013, the Governing Council of the ECB decided to maintain the current level of ELA until March 25, 2013. After that, ELA could only be considered if an EU/IMF program was put in place that would ensure the solvency of the concerned banks. Thus, the deadline for the Cypriot government to reach a bailout program was March 25, 2013, after which "Pandora's Box" would open.

On March 22, 2013, the Cypriot Parliament focused on negotiations to find a way to reach a bailout deal before the 25th of March, but this deal required that Cyprus gather six billion euros to fund its share of the bailout.[96] During that period, the Cyprus banking system remained closed and capital controls were enforced in accordance with the terms of the bailout. In response to these developments, the Cypriot government enacted eight distinct laws aimed at emergency assistance for the economy and banks (the "Bank Resolution Framework"), including Law 17(I)/2013 for the

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[92] Michele Kambas & Deepa Babington, *After election win, Anastasiades faces Cyprus bailout quagmire*, REUTERS (Feb. 24, 2013), https://www.reuters.com/article/us-cyprus/after-election-win-anastasiades-faces-cyprus-bailout-quagmire-idUSBRE91N00220130224.

[93] *See* Charlemagne*, A better deal, but still painful*, ECONOMIST (Mar. 25, 2013), http://www.economist.com/blogs/charlemagne/2013/03/cyprus-bail-out.

[94] Tim Worstall, *The Cyprus Bank Bailout Could Be A Disastrous Precedent: They're Reneging On Government Deposit Insurance*, FORBES (Mar. 16, 2013) https://www.forbes.com/sites/timworstall/2013/03/16/the-cyprus-bank-bailout-could-be-a-disastrous-precedent-theyre-reneging-on-government-deposit-insurance/#629071215b6f.

[95] *See* Mitu Gulati & Lee Buchheit, *Walking Back From Cyprus,* VOX CEPR'S POLICY PORTAL (Mar. 20, 2013), http://voxeu.org/article/walking-back-cyprus.

[96] Graeme Wearden, *Cyprus crisis: MPs approve bank restructuring and solidarity fund—as it happened*, GUARDIAN (Mar. 22, 2013) https://www.theguardian.com/business/2013/mar/22/eurozone-crisis-cyprus-bailout-russia-vote.

Consolidation of the Banks. These provisions awarded the Central BOC extensive powers to enact a series of measures to assist in the consolidation or liquidation of financial institutions in Cyprus. The law further provided for the creation of a Consolidation Authority that would act as a "receiver manager" with extensive authority for the consolidation of the banks.

Finally, on March 25, 2013, a deal was reached. In fact, on the same day the Eurogroup had made a statement that an agreement had been reached with the Cypriot authorities on the key elements necessary for a future macroeconomic adjustment program. The Eurogroup said this agreement was supported by all euro area member states and by the Commission, the ECB, and the IMF. The statement contained an annex with the terms of the Agreement; including the following provisions[97]:

- It was agreed that Cyprus would receive 10 billion euro as financial assistance; such assistance would not be used to recapitalize either CPB or BOC. All other banks in Cyprus would be provided with unlimited funds as needed.
- Additionally, the Annex provided for certain measures to be taken immediately in relation to the two problematic banks:
    - CPB would be resolved immediately—with full contribution of equity shareholders, bond holders and uninsured depositors—based on the Bank Resolution Framework. CPB would be separated into a good bank and a bad bank; the good bank will be folded into BOC along with 9 billion of ELA, while the bad bank will be run down over time.
    - BOC would be recapitalized through a deposit/equity conversion of uninsured deposits with full contribution of equity shareholders and bond holders, so that a capital ratio of 9% would be secured by the end of the program.

On March 25, 2013, the Governor of the Central BOC placed both banks into resolution. On March 26, 2013 the Memorandum of Understanding was adopted by the ESM and the Republic of Cyprus, reiterating the terms of the Eurogroup's announcement. Shortly after, on

[97] *See Eurogroup Statement on Cyprus* (Mar. 25, 2013), http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ecofin/136487.pdf.

March 29, 2013, the Cyprus Central Bank published two decrees, Decrees No. 103 and 104, finalizing the agreement reached with the ESM.

V. THE CYPRUS HAIRCUT: COERCION OR JUST HARD POLITICS?

The Cyprus banking haircut was unprecedented. It is unclear, however, whether the bail-out terms were wilfully accepted by the Cypriot government or whether it was coerced and forced to accept same as a "take it or leave it plan" with the alternative being financial collapse of the country.

A. Coercion

Undoubtedly, Cyprus was "forced" to accept some difficult terms. However, does this mean that the banking haircut of the two major banks in Cyprus was a product of economic coercion? To analyze whether the facts of the Cyprus banking haircut satisfy the aforementioned criteria for economic coercion, this Article will focus on the decision of the Governing Council of the ECB of March 21, 2013. As a result of this decision, the provision of ELA to BOC and CPB was to be stopped on March 25, 2013 unless and until Cyprus agreed to a bailout program. To respond to this question, we must first examine the legal framework surrounding ECB's decision. This is the topic to which we now turn.

Primarily, the legal nature of ELA must be identified. ELA is a temporary measure to support solvent credit institutions that are facing temporary liquidity problems.[98] The provision of ELA is a competence enjoyed by each member state through their NCBs.[99] This discretion falls outside of the functions that generally arise from their membership in the European System of Central Banks ("ESCB") or Eurosystem.[100] ELA is therefore not a monetary policy instrument, nor is it an ESCB or Eurosystem function; it is awarded by the NCBs. Hence, to a large extent, the provision

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[98] EUROPEAN CENTRAL BANK, THE FINANCIAL RISK MANAGEMENT OF THE EUROSYSTEM'S MONETARY POLICY OPERATIONS 34 (2015), https://www.ecb.europa.eu/pub/pdf/other/financial_risk_management_of_eurosystem_monetary_policy_operations_201507.en.pdf.

[99] EUROPEAN YEARBOOK OF INTERNATIONAL ECONOMIC LAW 2014 (Christoph Herrmann, Markus Krajewski & Jörg Philipp Terhechte eds., 2013).

[100] *Opinion of the European Central Bank*, *supra* note 89, at 34.

of ELA facilities is a national matter governed by the national laws of the NCB's state of incorporation under the national NCB legal framework.[101]

As the NCBs are responsible for granting ELA, they enjoy wide discretion to decide the terms and conditions on which ELA is offered. In particular, Article 14.4 of the Statute of the ESCB and the ECB explicitly stipulates that NCBs may perform functions other than those specified in the Statute: "*Such functions shall be performed on the responsibility and liability of national central banks and shall not be regarded as being part of the functions of the ESCB*."[102]

That said, such discretion should not be exercised in contravention of other legal obligations of the states or the NCBs. In particular, the granting of ELA facility to a specific banking institution should not be contrary to rules on state aid. To this end, the European Commission has issued guidelines on how state aid rules apply in the case of ELA, recognizing four conditions which, if met, indicate there is no violation of the state aid rules. Those conditions are: a) an ELA should be awarded only to solvent, but illiquid, banking institutions,[103] and should be part of a larger "rescue package" but a limited and exceptional temporary case; b) the facility should be secured by adequate collateral; c) the Central Bank should impose a punitive interest rate to the beneficiary institution; and d) ELA should be provided at NCB's discretion and should not be supported on or by state's guarantees.[104]

Furthermore, although ELA is not provided within the ESCB framework, it should not interfere with the objectives and tasks of the ESCB. The provision of ELA should therefore be consistent with the "monetary financing prohibition" as defined under Article 123 of the Treaty of the Functioning of the European Union, which prohibits overdraft facilities or any other type of credit facility with an NCB in favor of the public sector. This prohibition includes any financing of the public sector's obligations

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[101] Buiter, Michels & Rahbari, *supra* note 84, at 2.

[102] Protocol (No 4) on the Statute of the European System of Central Banks and of the ECB art. 14.4, O.J. C 202, Oct. 26, 2012, https://www.ecb.europa.eu/ecb/legal/pdf/c_32620121026en_protocol_4.pdf

[103] *Emergency liquidity assistance (ELA) and monetary policy*, EUR. CENT. BANK, https://www.ecb.europa.eu/mopo/ela/html/index.en.html (last visited Apr. 11, 2017).

[104] FINANCIAL REGULATION: A TRANSATLANTIC PERSPECTIVE (Ester Faia, Andreas Hackenthal, Michael Haliassos & Katja Langenbucher eds., 2015).

vis-à-vis third parties.[105] The ECB has issued several opinions stressing the criteria that should be followed by NCB when providing ELA under Article 123. The criteria are: a) the credit provided by the NCB should be provided for as short a term as possible; b) there must be systemic stability aspects at stake; c) there must be no doubts as to the legal validity and enforceability of the state guarantee under applicable national law; and d) there must be no doubts as to the economic adequacy of the state guarantee, which should cover both principal and interest on the loans, fully preserving the NCB's financial independence.[106]

Lastly, Article 14.4 of the Statute of the ESCB and the ECB grants the Governing Council of the ECB the right to stop or restrict an ELA facility from operating. This can occur if the ECB considers that ELA is interfering with the objectives and tasks of the Eurosystem and at least two thirds of the votes cast oppose to further ELA. It is for these reasons that a NCB granting ELA must inform the ECB of all relevant details within two days.[107]

The Governing Council of ECB's March 21, 2013 decision to maintain the ELA level granted until March 25, 2013 was founded exactly on Article 14.4. As can be determined from the wording of Article 14.4, there are two conditions that should be met for the Governing Council to decide to terminate or otherwise restrict ELA. The first one is procedural and dictates that such a decision should be taken and ratified by at least two thirds of the votes. The second one is substantive and provides that the decision should be based on the premise that the continuation of ELA would impair some specific object and task of the Eurosystem. The second condition cannot be subject to review by any state (or other European institutions, for that matter) and is decided solely on the Governing Council's discretion. To the extent that the procedural condition of receiving at least two thirds of the votes was met, the decision of the Governing Council of March 21, 2013 can be considered justified. However, it is necessary to examine whether the exercise of such discretion constitutes coercion. This is the topic to which we now turn.

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[105] *See, e.g.*, European Central Bank, *Opinion of the European Central Bank*, CON/2012/4, at 6; *Opinion of the European Central Bank*, *supra* note 89, at 6.

[106] *See, e.g.*, European Central Bank, *Opinion of the European Central Bank*, CON/2008/42, at 4.11; *Opinion of the European Central Bank*, *supra* note 89, at 4.

[107] HAL S. SCOTT, CONNECTEDNESS AND CONTAGION: PROTECTING THE FINANCIAL SYSTEM FROM PANICS 116 (2016).

B. Theories of Coercion

As discussed above, the definition of economic coercion is not settled in international scholarship, is complicated, and requires examination of several factors. Nonetheless, this Article will examine whether the facts of the Cyprus banking haircut can satisfy the aforementioned criteria, which have been recognized by different scholars as ingredients of economic coercion.

The first criterion proposed by Professor Bowett requires an improper motive or intent on the part of the state performing the coercive act.[108] Such intent should be primarily for the purpose of damaging the economy of another state or as a means of coercing another state.[109] The question here, therefore, is whether the ECB acted with an improper motive for the purpose of damaging the Cypriot economy when it suddenly decided to stop the provision of ELA to Cyprus' second largest bank. As discussed above, the intent of a state or an EU institution is not easy to detect, let alone prove. It would require a thorough examination of the surrounding situations. In the case of the Cyprus banking haircut, the decision of the Governing Council of the ECB was made at a time when CPB had already been insolvent for several months, raising suspicions that the ECB decision might have been coercive. That said, at that period, the Cyprus government's six-month deadline to present a viability plan for CPB to the EU Commission had just expired. Furthermore, the ECB, as will be discussed below in detail, acted legally and in accordance with its policy when it decided to stop funding the insolvent CPB. Thus, although the timing of the decision, the very short notice given by ECB prior to the implementation of the decision, and the unprecedented terms of the bailout program certainly raise some questions regarding ECB's motives, these motives do not clearly indicate coercive intent. It is therefore very difficult to demonstrate persuasively that the ECB intended to damage the Cyprus economy. Furthermore, it is not demonstrably within ECB's interest to inflict this damage since it would ultimately hurt ECB's goals of price stability.

For ECB's decision to constitute coercion under the second criterion, ECB must have acted to obtain some benefit of any kind by subordinating Cypriot sovereignty. Any claim that ECB aimed to obtain specific benefits

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[108] Bowett, *supra* note 60, at 1–12.
[109] *Id.*

by exercising pressure on the Cypriot government is not supported by any official documentation. The decision was made in accordance with Article 14 of the ECBS Statute to safeguard Eurosystem's tasks and goals and to restore legality under ECB's statute. Furthermore, it cannot be claimed effectively that the ECB subordinated the sovereignty of the Cypriot state, as Cyprus has itself awarded such powers to the ECB.

The last criterion requires that the coercion be tantamount to force in the sense that it can endanger the coerced state's security, economy, and other structures. Certainly, the imminent collapse of the Cypriot Banking System was a credible threat to Cyprus' social security, safety, and economy, and could be directly linked with the ECB's decision. Even so, ECB was not responsible for the financial position of CPB and the latter's insolvency, nor for the dire state of the Cyprus economy, which was clearly attributed to the inadequate management of the Bank and to the Cypriot government.[110] Professor Tom Farer argues that non-concession of assistance or aid to another state falls short of coercion in every case, as a state is always free to decide whether to continue providing assistance on the basis of each state's own interests.[111] In this case, therefore, the ECB's decision to cease providing ELA to the Cypriot banks cannot be classified as coercive.

As such, it does not appear clear that the Cypriot government was coerced into agreeing to the bailout program. Even if that was the case, however, not all forms of coercion are illegal under international law, as indicated below.

1. Retorsion and Reprisals

Not all hostile and unfriendly competitive acts can be considered illegal coercion. Indeed, international law recognizes that a state is free to respond to an injurious act done by another state through a hostile, yet legal, act.[112] Such acts of retorsion are considered a state's means of self-help when it is subjected to an illegal act. Retorsions aim to compel the party acting illegally to rescind such an act.

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[110] *See* Gikas A. Hardouvelisa & Ioannis Gkionis*, Decade Long Economic Crisis: Cyprus versus Greece,* 10 CYPRUS ECON. POL'Y REV. 3, 13 (2016).

[111] Tom J. Farer, *Political and Economic Coercion in Contemporary International Law*, 79 AM. J. INT'L L. 405 (1985).

[112] JAN KLABBERS, INTERNATIONAL LAW 168 (2nd ed. 2013).

Overall, acts of retorsion are deemed legal, even in the absence of a previous injurious act, since states retain the right to be unfriendly to one another in pursuit of their interests.[113] However, some commentators have argued that if retorsion is in pursuit of a wrongful end, such as an act for the sole aim of causing harm to another state, it becomes illegal.[114] Once the act ceases to be legal, it no longer constitutes retorsion. Hence, retorsion falls short of coercion in the legal sense of the term. If a hostile act is of such degree so as to constitute coercion, it is considered a prohibited intervention under international law and no longer qualifies as retorsion.[115] Retorsion is distinguished from reprisals in that reprisals are in themselves illegal acts, which are justified under international law as a response to a previous violation of the law by the state at which the reprisal is directed.[116] Reprisals are allowed under international law, allowing states to respond to a prior illegal act as means of "self-help."

Self-help is a necessary remedy since international law does not provide an effective enforcement mechanism.[117] There is no "Court [or] central authority above the Sovereign States which could compel a delinquent State to give reparation."[118] The Naulilaa arbitration case provided the classic definition of the term reprisal and its elements, providing that:

> Reprisals are an act of self-help on the part of the injured states, responding after an unsatisfied demand to an act contrary to international law on the part of the offending State . . . . They would be illegal if a previous act contrary to international law had not furnished the reason for them. They aim to impose on the offending State reparation for the offense or the return to legality in avoidance of new offenses.[119]

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[113] ROBERT PIEDELIEVRE, PRECIS DE DROIT INTERNATIONAL PUBLIC, OU, DROIT DE GENS (1894).

[114] ANGELO LABELLA & BENEDETTO CONFORTI, AN INTRODUCTION TO INTERNATIONAL LAW 24 (2012).

[115] Antonios Tzanakopoulos, *Legal Mechanisms to Assess and Mitigate Adverse Human Rights Impact of Unilateral Sanctions Through Accountability* (2015) http://www.ohchr.org/Documents/Events/Seminars/CoercitiveMeasures/AntoniosTzanakopoulos.doc.

[116] KLABBERS, *supra* note 112, at 168.

[117] Andrew D. Mitchell, *Does One Illegality Merit Another? The Law of Belligerent Reprisals in International Law*, 170 MIL. L. REV. 155 (2001).

[118] FRANCIS & OPPENHEIM, *supra* note 68.

[119] Julia Pfeil, *Naulilaa Arbitration (Portugal v Germany)*, MAX PLANCK ENCYCLOPEDIA OF PUBLIC INTERNATIONAL LAW (March 2007) http://opil.ouplaw.com/view/10.1093/law:epil/9780199231690/law-9780199231690-e178?rskey=HJjp7b&result=1&prd=EPIL.

Reprisals can constitute a form of coercion. The Institut de Droit International defines reprisals as:

> [M]easures of coercion, derogating from the ordinary rules of the law of the people, determined and taken by a State, following the commission of illicit acts against it by another State, and having as their aim to impose on the second State, through pressure exerted by means of harm, a return to legality.[120]

Traditionally, reprisals included any illegal act, including measures of economic coercion as well as armed attacks.[121] The term, however, has been replaced by two concepts: belliquent, or self-defense, reprisals used in armed conflict, and countermeasures, or those reprisals of a non-forcible nature.[122] Economic coercion can be considered a type of countermeasure.

Countermeasures are an exception to the rule that coercion constitutes an illegal intervention in that they are not illegal per se, but can be justified, provided certain conditions are met.[123] This is recognized by the Draft Articles on Responsibility of States for Internationally Wrongful Acts, ("DASR"). Although DASR is not a multinational convention, it codifies customary law.[124] Indeed, Article 22 of the DASR provides that "[t]he wrongfulness of an act of a state not in conformity with an international obligation towards another state is precluded if and to the extent that the act constitutes a countermeasure," provided certain substantive and procedural conditions are met.[125] Such substantive and procedural conditions constitute the limits of countermeasures. If these conditions are not met, countermeasures are illegal as coercive acts. The same principle is reiterated on Article 22 of the Draft Articles on Responsibility of International Organisations ("DARIO"), which aim to clarify the circumstances under which an international organization is liable for breach of an international

[120] M. Nicolas Politis, *Régime de répresaillies en temps de paix,* INSTITUT DE DROIT INTERNATIONAL (1934), http://www.idi-iil.org/app/uploads/2017/06/1934_paris_03_fr.pdf.

[121] Colin Warbrick, Book Review, 35 INT'L & COMP. L. Q. 202, 202–03 (1986) (reviewing ELIZABETH ZOLLER, PEACETIME UNILATERAL REMEDIES: AN ANALYSIS OF COUNTER-MEASURES (1984)).

[122] ARNOLD PRONTO & MICHAEL WOOD, 4 THE INTERNATIONAL LAW COMMISSION 1999-2009: TREATIES, FINAL DRAFT ARTICLES AND OTHER MATERIALS 329 (2011).

[123] *See generally* MAKIO MIYAGAWA, DO ECONOMIC SANCTIONS WORK? (2016).

[124] SUSAN BREAU, THE RESPONSIBILITY TO PROTECT IN INTERNATIONAL LAW: AN EMERGING PARADIGM SHIFT 68–69 (2016).

[125] Int'l L. Comm'n, Draft Articles on Responsibility of States for Internationally Wrongful Acts on its Fifty-Third Session, U.N. Doc. A/56/10, at 75 (2001).

obligation and the consequences of such breach. It must be stipulated that DARIO does not enjoy the status of customary law, as is the case with DASR. In fact, DARIO has been met with skepticism by states, international organizations, and academics. Nonetheless, as argued by Professor Kristina Daugirdas, DARIO may become customary law.[126] Thus, these conditions provide a means for testing whether the Cyprus bank haircut was the result of coercive actions. We shall now examine the substantive and procedural conditions that constitute the limits of countermeasures.

2. Limits of Countermeasures

Initially, arbitral tribunals, such as in the Naulilaa arbitration, set out certain conditions that must be met for countermeasures to be legal.[127] The Naulilaa decision indicates that for countermeasures to be legal, (1) they must be executed only by a state through its institutions; (2) they must be proportionate; and (3) they must follow an illicit act where negotiations to restore legality have failed.[128]

These criteria were re-affirmed in the arbitration case *Air Service Agreement*, which referred exclusively to countermeasures.[129] This case examined the decision of the United States to ban certain French flights from landing in the United States following France's decision to prohibit Pan American passengers from disembarking in Paris. France's decision was due to an alleged breach of the 1946 bilateral agreement between France and the U.S., which provided for civil air flights between the two countries. The tribunal reaffirmed states' rights to resort to countermeasures but noted that such measures should 1) be relevant to a previous violation by the state receiving the countermeasures and 2) be proportionate in light of the previous violation. In relation to the third requirement, which was upheld in the *Naulilaa* case—namely that a countermeasure should constitute the last resort following failed negotiations—the Tribunal in the Service Agreement case reasoned that starting countermeasures during negotiations was not

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[126] Kristina Daugirdas, *Reputation and the Responsibility of International Organizations*, 25 EUR.J. INT'L L. 991–1018 (2014).

[127] *See* Pfeil, *supra* note 119.

[128] *See id.*; *see also* EDWARD K. KWAKWA, THE INTERNATIONAL LAW OF ARMED CONFLICT: PERSONAL AND MATERIAL FIELDS OF APPLICATION (1992).

[129] Air Services Agreement of 27 March 1946 (U.S. v. France), 18 R.I.A.A. 417–93 (1979).

prohibited. Similar recognition of the legitimacy of countermeasures was indicated in the *Gabcíkovo-Nagymaros Project*[130] and the *Cysne*[131] cases.

These conditions were codified in Article 22 of the DASR, which echoes customary law. Furthermore, Articles 49–51 of the DASR outline the limits of economic countermeasures. Such limits are separated in substantive and procedural limits; the procedural limits are set in Article 49, while Articles 50 and 51 set out the substantive limits. According to Article 49, countermeasures are permissible if taken by an injured state to induce the responsible state to cease its internationally wrongful conduct. This upholds the principle initially set out in the *GabčÌkovo-Nagymaros Project* case,[132] by virtue of which the existence of an internationally wrongful act is a prerequisite for the justification of a countermeasure.[133] This leads to the following conclusions:

- Primarily, countermeasures may only be taken against the violating state, and acts directed against third states would not be justified as countermeasures. That said, if countermeasures taken against the violating state also indirectly affect third states, this alone does not necessarily render a countermeasure illegal under Article 22 of the DASR.[134]
- Secondly, countermeasures can only be taken by an injured state, meaning that non-injured states may not affect countermeasures. That said, in case there is a serious violation of an obligation owed to the international community as a whole, any state may take countermeasures.[135]
- Lastly, countermeasures may be taken to induce a state to cease its internationally wrongful conduct. A countermeasure cannot be justified if it goes beyond the goal of economic inducement to economic coercion, forcing the other state to do something it is not obligated to do under international law.[136] This also means that countermeasures should cease as soon as their aim

[130] Gabčikovo-Nagymaros Project (Hung. v. Slovk.), Judgment, 1997 I.C.J. 92 (Sept. 25, 1997).

[131] The Cysne (Port. v. Ger.), 3 R.I.A.A. 1371, 1371–86 (Perm. Ct. Arb. 1933).

[132] Gabčikovo-Nagymaros Project *supra* note 130 at ¶ 83.

[133] International Law Commission, *Comments on the Draft Articles on Responsibility of States for Internationally Wrongful Acts* [hereinafter Draft Articles], on its Fifty-Sixth Session, U.N. GAOR, Supp. No. 10, U.N. Doc. A/56/10 (2001).

[134] *Id.*

[135] GIORGIO GAJA, THE PROTECTION OF THE GENERAL INTERESTS IN THE INTERNATIONAL COMMUNITY, *in* 364 RECUEIL DES COURS 131 (2014).

[136] Tzanakopoulos, *supra* note 47, at 10.

> of inducement is met, and shouldn't continue thereafter as they would no longer constitute a response to an illegal act.

The wrongfulness of an international act can only be judged retrospectively, so a state resorting to countermeasures due to alleged wrongful violations does so at its own peril.[137]

Apart from the procedural limits described above, Articles 50 and 51 of the DASR set various substantive conditions for counter measures to be justified. Article 50 provides that countermeasures should refrain from violating international obligations regarding the use of force, fundamental human rights, obligations of a humanitarian character prohibiting reprisals, and obligations under peremptory norms of general international law.

Lastly, Article 51 sets a substantive limit on the nature and extent of countermeasures, providing that countermeasures should respect the principle of proportionality. Proportionality requires that adoption of countermeasures does not lead to inequitable results. Hence, for countermeasures to be proportionate, they should assess both the amount of injury suffered and the nature of the rights in question and the seriousness of the breach.[138] The reference to "the rights in question" should be broadly interpreted so as to refer not only to the rights infringed but also to the rights of the violating state.[139] Considering this, punitive countermeasures will likely never be permitted under international law.[140]

In relation to the limits set to countermeasures taken by an international organization against a state, DARIO does not specifically regulate this issue, but Article 22 of DARIO refers to the "substantive and procedural conditions required by international law." As per the commentary of DARIO, Articles 49 to 54 of DASR should be applied respectively.[141]

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137 *See*, Air Service Agreement (U.S. v. Fr.), 18 R.I.A.A. 417, 433 (Perm. Ct. Arb. 1978).

138 Draft Articles, *supra* note 133, at 135.

139 *See* U.S. v. Fr., 1978 R. I. A. A. at 433.

140 Draft Articles, *supra* note 133, at 326.

141 International Law Commission, *Comments on the Draft Articles on the Responsibility of International Organizations*, on its Sixty-Third Session, U.N. Doc. A/66/10, at 82–83 (2011); *see also*, Mirka Möldner, *Responsibility of International Organisations, Introducing ILC's DARIO*, in 12 MAX PLANCK Y.B OF U.N. L. 281, 281–328 (2012).

The Article will now examine whether the Governing Council of ECB's March 21, 2013 decision, if deemed coercive, can be justified as a countermeasure or an act of retorsion. As we have already established the decision of March 21, 2013 was legal, it is an act of retorsion, which is permitted under international law even if it is punitive or hostile so long as it is proportionate.

In this analysis, coercion would only need to be examined if ECB's decision was illegal; however, as analyzed above, we cannot classify ECB's decision as illegal under any of the coercion criteria, given that ECB acted within its scope of powers and rightfully exercised its discretion. Even if ECB's decision was deemed illegal, ECB could raise the defense of countermeasures given that all the respective conditions are met; namely, Cyprus may have been in breach of an obligation due to the EU under the Stability and Growth Pact, which is a pre-condition for EU Membership. The Stability and Growth Pact requires that all member states' government debt/GDP ratio is not over the 60%. Cyprus' government debt to GDP ratio was well above the relevant threshold in 2010, 2011, and 2012, and reached 102% in 2013. It can be argued further that ECB's decision of March 21, 2013 that "ELA would be continued if and only if a programme was in place that would ensure the solvency of the banks concerned,"[142] was made as a direct consequence of that breach. Indeed, ELA could not continue to be given to an insolvent bank. This would be a credit facility aimed to defer government-funded recapitalization, in breach of Article 123 of the Treaty of the Functioning of the European Union ("TFEU"), which prohibits the financing of public budgets in member states through the ECB and the NCB.[143]

To conclude, establishing liability for European institutions on the grounds of economic coercion, illegal retorsion or non-proportional countermeasure appears to be a very difficult task for Cyprus. Investors would be barred from even bringing such claims, as DARIO is not binding at its present state, but also can only be invoked by states and international organizations and not by individuals. This analysis indicates that it is a

[142] Jörg Asmussen, *Exchange of Views with the Economic and Monetary Affairs Committee of the European Parliament on Financial Assistance to Cyprus*, European Central Bank (May 8, 2013), https://www.ecb.europa.eu/press/key/date/2013/html/sp130508.en.html.

[143] *See* Willem Buiter & Ebrahim Rahbari, *The European Central Bank as Lender of Last Resort for Sovereigns in the Eurozone*, 50 J. COMMON MKT. STUD., 6, 6–35 (2012); *see also* Letter from Mario Draghi to Matt Carthy (Feb. 17, 2015), European Central Bank, https://www.ecb.europa.eu/pub/pdf/other/150218letter_carthy.en.pdf.

difficult task for investors to render European institutions liable or co-liable for such losses.

C. *Basing Liability on Other Grounds*

Due to these difficulties, it is worth exploring whether investors can base their claim against European institutions for losses associated with financial distress measures on other grounds, especially on the TFEU. To this end, this Article will examine available remedies under the TFEU.

1. Article 263 of the TFEU: Annulment of Illegal Actions

Article 263 of the TFEU contains a provision allowing judicial review of the acts of EU institutions. In particular, it allows, *inter alia*, individuals to bring actions in the Court of Justice of the European Union ("CJEU") against EU institutions that have acted illegally.[144] However, before individuals can demonstrate that the EU institution's act is illegal, they must first demonstrate they have fulfilled the *locus standi* preconditions set out in the relevant article. It is worth mentioning that before the Treaty of Lisbon, Article 263 had been scarcely used as a means of enforcing individual rights due to the onerous requirements that individual applicants must meet, namely that the act was a matter of "direct and individual concern" to them.[145] Indeed, in the leading *Plaumann* case, the Court held that an applicant would be successful in showing that he had direct and individual concern by a decision, only "if that decision affects them by reason of certain attributes which are peculiar to them or by reason of circumstances in which they are differentiated from all other persons and by virtue of these factors distinguishes them individually just as in the case of the person addressed."[146]

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[144] Consolidated Version of the Treaty on the Functioning of the European Union art. 263, Oct. 26, 2012, 2012 O.J. (C 326) 47 (hereinafter TFEU) (distinguishing between the so called privileged applicants, which consists of states and EU institututions, which are granted unlimited locus standi, and non-privileged applicants, including individual applicants, who are a given restricted locus standi).

[145] Vaughne Miller, *Taking a complaint to the Court of Justice of the European Union*, Standard Note SN05397, 6 (2010).

[146] Case 25/62, Plaumann & Co. v. Comm'n, 1963 E.C.R. 95. For an extensive presentation and analysis of former caselaw, see Anthony Arnull, *Private Applicants and the Action for Annulment Under Article 173 Of the EC Treaty*, 32 COMMON MKT. L. REV. 7 (1995).

Following the Treaty of Lisbon, the conditions for the admissibility of actions brought by individuals have been eased, depending on the act challenged, so that individual applicants can now challenge:

- An act addressed to them;
- An act addressed to another person, which was of direct and individual concern to them; or
- A regulatory act which was of direct concern to him and did not entail implementing measures.[147]

In relation to what constitutes a regulatory act, Professor De Witte argues that it is tantamount to non-legislative acts, that is, "acts not adopted in accordance with the ordinary or special legislative procedure."[148] Such acts, according to Girón Larrucea, need not directly affect an addressee, "except for the sole reason that they are one of the participants in a certain area of activity for the general regulation of which the act was adopted."[149]

Decisions of EU Institutions made in the framework of sovereign default, which constitutes exceptional circumstances, are likely to be regulatory acts, although this is not always the case. This issue was examined by the General Court when distressed depositors from the Cyprus Bank that had sustained haircuts in their bank deposits resorted to the court requesting the cancellation of the sale of operation in CPB in cases T-327/13 through T-331/13.[150] The applicants in all five cases turned against the European Commission and the ECB, as, according to the applicants, the decision of the Eurogroup of March 25, 2013 should be attributed to them. In their view, the decrees issued by the Cyprus Central Bank were simply putting Eurogroup's statement into effect. Their main argument was that the Eurogroup's decision of the 25th of March, which was materialized through the Banking Resolution Framework (Decree No. 103 and 104 of the Governor of Cyprus Central Bank as the representative and/or agent of the European System of Central Banks), was in excess of Eurogroup's power

[147] Richard Lang, *Quite a Challenge: Article 263(4) TFEU and the Case of the Mystery Measures*, SSRN ELECTRONIC J. 2 (2011).

[148] Floris De Witte, *The European Judiciary After Lisbon*, 15 J. EUR. & COMP. L. 43, 47 (2008).

[149] JA GIRÓN LARRUCEA, EL SISTEMA JURÍDICO DE LA UNIÓN EUROPEA: LA REFORMA REALIZADA EN EL TRATADO DE LISBOA 267, (Tirant lo Blanch, Valencia 2008); *but see* De Witte, *supra* note 148, at 47.

[150] Case T-327/13 Mallis and Mallis v Commission and ECB, Case T-328/13 Tameio Pronoias Prosopikou Trapezis Kyprou v Commission and ECB, Case T-329/13 Chatzithoma v Commission and ECB, Case T-330/13 Chatziioannou v Commission and ECB, and Case T-331/13 Nikolaou v Commission and ECB.

and authorities and thus intervening on Cyprus' sovereignty. The General Court initially examined whether the Eurogroup statement could, in fact, be attributed to the ECB or the European Commission, as otherwise the application would be inadmissible.[151] The General Court concluded that the Eurogroup is an informal discussion forum at ministerial level between representatives of the member states whose currency is the euro, without any legislative decision-making competences.[152] The General Court noted that, despite ECB's participation in its meetings, its actions could not be attributed to the ECB or the European Commission.[153] The General Court further considered if the statement could be attributed to the ESM, rather than to the Eurogroup. The applicants claimed that, in such case, the act would be attributable to the ECB. The General Court ruled, however, that, even in such case, this fact would still not allow the inference that the Commission or the ECB instigated the adoption of that statement.[154] As such, it ruled that an annulment was not possible under Article 263 of the TFEU and that the application was inadmissible. The case would be different if the statement was issued by the Council under its ECOFIN configuration, as in such a case, the Decrees 103 and 104 would in fact be implementing EU law.[155]

The decision of the General Court was appealed (Joined Cases C-105/15 P to C-109/15 P), but the CJEU upheld the dismissal. The CJEU reiterated that the Eurogroup's statement could not be regarded as a joint decision of the Commission and the ECB. Under the ESM framework, these bodies did not have the power to make decisions of their own under the ESM Treaty and the mere participation of the EU Commission and the ECB in the meetings of the Eurogroup was not sufficient to alter the nature of Eurogroup's statements and render such statements the expression of a decision-making power of the ECB and the EU Commission. Finally, the CJEU noted that, as Cyprus adopted the legal framework for the banks' restructuring, this cannot be regarded as having been imposed by an alleged

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151 Case T-327/13 Mallis and Mallis v Commission and ECB, at 30-34.

152 *Id.* at 53.

153 *Id.* at 42.

154 *Id.* at 43.

155 *See* Anastasios A. Antoniou, *Original Sin: the EU tampering with the right to property in Cyprus is an unprecedented departure from EU norms and shared constitutional rights*, EUTOPIA LAW (Mar. 19, 2013) https://eutopialaw.com/2013/03/19/original-sin-the-eu-tampering-with-the-right-to-property-in-cyprus-is-an-unprecedented-departure-from-eu-norms-and-shared-constitutional-rights/.

decision jointly taken by the EU Commission and the ECB expressed in the Eurogroup statement.

Therefore, only in cases where investors can prove an act was addressed to them, was a direct and individual concern to them, or was a regulatory act can investors challenge the legality of an act taken by an EU Institution within the framework of sovereign default to the extent, of course, that such an act directly affects the interests of such investors. However, for investors to succeed, they must further demonstrate that such act actually contradicts EU Law, something that seems difficult to do given the wide discretion that is enjoyed by EU institutions in this field.

2. Article 265 of the TFEU: Complaint for Failure to Act

Article 265 of the TFEU provides that, in cases where a European Institution has an affirmative duty—and not just discretionary power—to act but failed to do so, such inaction can be deemed an infringement of the TFEU and, as such, an illegal omission.[156] This article applies specifically in cases of inaction by European institutions when there was a legal obligation to act, and thus, "inaction" means non-adoption of a legal act.[157] To this end, Article 265 does not apply to negative acts.

If the European Court rules that there was in fact an infringement of EU law due to inaction, it will order the respective institutions to take all necessary actions to remedy the omission.[158] Article 265 differentiates between privileged and non-privileged investors, with the former comprised of member states and institutions of the EU and the latter private parties who have a limited right of *locus standi*[159] in that they must have a personal interest in taking action in order to bring proceedings before the Court of Justice.[160] In particular, the Court has stressed on several occasions that applications by individuals should be limited to decisions addressed to individuals.[161]

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156 NIGEL FOSTER, FOSTER ON EU LAW 220 (5th ed. 2015).

157 *See* Case 125/78, GEMA v. Eur. Comm., 1979, E.C.R. 3178–79.

158 ELSPETH BERRY, MATTHEW J HOMEWOOD & BARBARA BOGUSZ, COMPLETE EU LAW 259 (2015).

159 For definition, see FOSTER, *supra* note 156, at 221.

160 *See* TFEU art. 265, which provides "[a]ny natural or legal person may, under the conditions laid down in the preceding paragraphs, complain to the Court that an institution, body, office or agency of the Union has failed to address to that person any act other than a recommendation or an opinion."

161 *See, e.g.*, Case 15/70, Amedeo Chevalley v. Comm'n of Eur. Communities.

An action based on Article 265 can be brought only against an EU institution (the European Parliament, the European Council, the Council, the Commission, or the ECB).[162] This course of action might be used by investors where an EU institution failed to take action it was legally required to take to avert or minimize investors' losses due to sovereign default. The crucial element for investors is to demonstrate that the EU institution has unlawfully failed to act when such action was required by EU law. In such a case, investors could resort to the CJEU, provided they had followed the procedural conditions provided for in Article 265, including the preliminary procedure.[163]

To explore whether investors can resort to this alternative, this Article will once again explore the case of CPB. In the case of CPB, it is striking that, although CPB was insolvent and this was known to ECB, the Cyprus Central Bank continued to provide ELA to it nonetheless. This continued funding was contrary to Article 123 of the TFEU and ECB's policy. Even so, however, it must be remembered that ECB did not have a duty to intervene and stop ELA before the situation devolved so dramatically. Indeed, the provision of ELA is a national matter, while NCBs and respective national authorities maintain ultimate responsibly for prudential supervision of eurozone banks.[164] Indeed, in accordance with TFEU, ECB had no duty to maintain financial stability;[165] rather, ECB's authority is limited to "contribut[ing] to the smooth conduct of policies pursued by the competent authorities."[166] To this end, ECB had no duty to stop the Cyprus NBC from granting ELA to CPB and in fact the Governing Council's March 21, 2013 decision was a negative action that does not justify the use of TFEU Article 265.

It is therefore difficult to imagine that in matters of extreme financial distress, where national states still enjoy exclusive sovereignty to decide, there will be situations where EU institutions have a duty to act to prevent a decision or situation personally affecting investors.

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[162] TFEU art. 265.

[163] *See generally* Inga Daukšienė & Arvydas Budnikas, *Has the Action for Failure to Act in the European Union Lost its Purpose?* 7 BALTIC J. OF L. & POL. 209 (2014).

[164] Daniel Wilsher, *Ready to Do Whatever it Takes? The Legal Mandate of the European Central Bank and the Economic Crisis*, 15 CAMBRIDGE Y.B. OF EUR. LEGAL STUD. 503, 503–36 (2013).

[165] Soko Tankaa, *Comment Paper to Chapters "The European Central Bank and Implications of the Sovereign Debt Crisis," in* EUROPE'S FINANCIAL MATURITY AND ASIA'S FINANCIAL MIGHT 62 (Sahoko Kaji & Eiji Ogawa eds., 2013).

[166] TFEU art. 127(5).

3. Non-Contractual Liability of EU Institutions

Finally, it is worth examining the non-contractual liability of EU institutions, which can be found in Article 340 of the TFEU. The article provides that the EU shall make good on damage caused by its institutions. The definition of attributable acts includes wrongful omissions.[167] In the case C-352/98 Bergaderm, the CJEU set out a set of conditions that must be met for establishing the existence of liability under Article 340 of the TFEU.[168] These are:

- The rule of law which has been breached must be one which is intended to confer rights on individuals. Here, later case law has adopted a more liberal approach.[169] In particular, the *Kampffmeyer* case[170] established that it suffices to show that the rule infringed was intended generally for the protection of individuals, and not necessary that the applicant was "directly and individually concerned" as required in Article 263 of the TFEU. Indicatively, in the more recent case, *Camos Grau v. Commission*, the requirement of impartiality into the conduct of Commission employees was found to aim not only to the respect of the public interest, but also to confer a right to individuals to see that the corresponding guarantees are complied with; [171]
- The breach must be sufficiently serious to merit an award of damages;[172] and,
- There must be a direct causal link between the infringement of the rule and the damage suffered by the claimant.[173]

All three conditions governing the EU's liability must jointly be satisfied. If one of them is not fulfilled, the application is dismissed in its entirety without the necessity for the Union courts to examine the remaining conditions for such liability. The Case T-79/13 *Accorinti v. ECB* is

[167] *See* Case C-40/71 Richez-Parise v. Comm'n of Eur. Communities, 1972 E.C.R. 73.

[168] *See* Case C-352/98 Bergaderm and Groupil v. Comm'n of Eur. Communities, 2000 E.C.R. 1–5291.

[169] *See* Case C-13-24/66 Kampffmeyer and others v. Comm'n of Eur. Communities, 1967 E.C.R. 245.

[170] *Id.*

[171] *See generally* Case T-309/03 Manel Camos Grau v. Comm'n of the European Community.

[172] *See generally* Case T-241/09 Court of Auditors of the European Union.

[173] *Id.*

indicative of this matter.[174] The case revolved around the Greek Sovereign Bonds Haircut through Private Sector Involvement (PSI). It was filed by Allessandro Accortini along with over 200 plaintiffs from Italy, all holders of Greek Sovereign bonds.

Plaintiffs claimed that, by virtue of the Exchange Agreement of February 15, 2012 and the ECB's Decision 2012/153/EU, which provided that Greek bonds had to be guaranteed by the Greek government in favor of the ECB and the NBCs in order to be eligible for Eurosystem operations, ECB and the NBCs received preferential treatment over all other holders of Greek Sovereign bonds.[175] Plaintiffs claimed the above constituted a breach of the principle of equal treatment amongst private creditors, while the fact that the ECB was buying Greek sovereign bonds while issuing calming statements for private investors was infringing their legitimate expectations and the principle of legal certainty. For these they claimed damages of more than 12.5 million euros in accordance with Article 268 and 340 of the TFEU.

As noted above, Article 340 of the TFEU provides the cumulative conditions that must be satisfied for the European Union to be liable under non-contractual liability. In particular, these are: a) that the institution must act unlawfully, b) actual damage must have been suffered and c) lastly, there must be a causal link between the unlawful and the damage pleaded.[176] The General Court in the *Accorinti* case concluded that the first condition of Article 340, namely the existence of an unlawful conduct, was not fulfilled, as the ECB acted within the discretion awarded to it by Articles 127 and 282 of the TFEU and therefore acted in compliance with EU law. The General Court concluded that bond holders' losses could not be attributed to the ECB, as economic risks are inherent in the commercial activities carried out in the financial sector. To this end, private investors could not rely on the principle of the protection of legitimate expectations or on the principle of legal certainty.

Furthermore, the General Court found that ECB's statements were generic and bondholders, as diligent and well-informed investors, should have had knowledge of the highly unstable economic circumstances surrounding the Greek sovereign bonds. The Court further concluded that in all cases, the decision of the Greek sovereign debt restructuring was made by

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174 *See generally* Case T-224/12 European Central Bank v. Accorinti and Others.

175 Decision of the European Central Bank 2012/153/EU (March 5, 2012).

176 *See* Case T-309/10 Christoph Klein v European Comm'n, 2014 E.C.R. ¶¶ 56–59.

the Greek government, which enjoyed exclusive competence on this matter and could not be attributed to the ECB. Lastly, the General Court rejected the argument that the general principle of equal treatment could apply between private investors and the ECB as some were not in a comparable situation, given the different motives that had driven them, namely public interest in the case of ECB and the pursuit of private profit in the case of private investors. Greece, and not the ECB, was only bound under *pari passu* clauses in the Greek sovereign bonds to ensure equal treatment of investors by ensuring that bonds were treated on "the same level footing without preference or priority among themselves . . . ."[177] The General Court dismissed the application on the above grounds.

The same result was also reached in the case *Nausicaa Anadyomène SAS and Banque d'escompte v. ECB*,[178] which was based on the same set of facts. The General Court found that the ECB had not infringed the legitimate expectations of the private holders of Greek bonds, the principle of legal certainty, or the principle of equal treatment of private creditors. The Court said that, in a field such as that of monetary policy, which is subject to constant changes, commercial banks may not rely upon the principle of the protection of legitimate expectations or upon the principle of legal certainty.[179] Hence, as the ECB had not actively encouraged investors to acquire or retain Greek debt instruments through its acts or statements, the General Court held that the ECB is not bound to compensate the loss sustained by commercial banks holding Greek debt instruments by the restructuring of Greek debt.[180]

The CJEU also examined the partial annulment of the Memorandum of Understanding of April 26, 2013 entered between Cyprus and the ESM in the Ledra Advertising Limited Joined Cases T 289-/13 to T-291/13. In those cases, applicants were depositors that claimed specific provisions of the Memorandum were in breach of human rights considerations, referring to the European Convention of Human Rights and the EU Charter of Human Rights.[181] Initially, the General Court did not examine the merits of the

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177 FRANCIS BEAUFORT PALMER, COMPANY PRECEDENTS 109–110 (8th ed. 1900).

178 Case T-749/15 Nausicaa Anadyomène SAS and Banque d'escompte v. European Central Bank,.

179 General Court of the European Union Press Release No. 5/17, The ECB is not bound to make good the loss allegedly sustained in 2012 by commercial banks holding Greek debt instruments in connection with the restructuring of Greek debt (Jan. 24, 2017).

180 *Id.*

181 *See generally* Case T-289/13 Ledra Advertising Ltd. v. European Comm'n and European Central Bank.

cases, but ruled the claims inadmissible. Although the EU Commission signed the Memorandum, it had done so on behalf of the ESM and so, as with the activities pursued by the Commission and the ECB in the context of the ESM, only the ESM is committed. As such, as "neither the ESM nor the Republic of Cyprus is among the institutions, bodies, offices or agencies of the European Union, the General Court has no jurisdiction to examine the legality of acts which they have adopted together."[182] The cases were appealed in the CJEU and, on September 20, 2016, the CJEU set aside the previous judgement and proceeded to examine the case on its merits.[183] On the grounds of admissibility, the CJEU held that, as the EU Commission acts as the guardian of the EU treaties, it must therefore refrain from signing a Memorandum of Understanding whose consistency with EU law is questionable, as would be the case in the event of breach of the EU Charter of Fundamental Rights.[184] On the merits, the CJEU held that, considering the imminent risk of financial losses that would have been sustained by depositors if the banking system had collapsed, the measures did not constitute a disproportionate and intolerable interference with the appellants' right to property and therefore there was no breach of the Charter.[185] Hence, the CJEU found that the EU Commission was not in breach and thus the conditions of Article 340 were not met.[186]

The above case demonstrates the large discretion enjoyed by EU institutions and the difficulties to attach liability to them for actions related to measures taken in case of sovereign default, especially when such institutions have acted lawfully within their wide discretionary powers.

VI. CONCLUSION

In cases of sovereign default, investors often sustain significant losses and are left looking for remedies. Recognizing the responsible actors is of paramount importance as it dictates the available remedies for investors. In particular, when an action can be attributed to multiple actors, investors may have additional legal recourse. Additionally, the party responsible may

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182 *Id.* at ¶ 58.

183 Joined cases C-8/15P to C-10/15P Ledra Advertising Ltd v. Comm'n and European Central Bank, 2016 E.C.R. at ¶ 78.

184 Case T-289/13 Ledra Advertising Ltd. v. European Comm'n and European Central Bank 2014 E.C.R. ¶ 58.

185 *Id.*

186 *Id.*

impact competent Courts, applicable law, and available property for enforcement.

In the recent case of the Cyprus banking haircut, investors were told by the Cypriot President that the measures leading to the haircut were attributable to the EU and its institutions. To this end, several investors brought claims against Eurogroup and the ECB.

This Article examined whether, in fact, liability could be attributed to the EU for the acts of a member state. As demonstrated above, there are several bases upon which investors can claim compensation from EU institutions in the framework of sovereign default within the EU. However, none of these conditions are easy to identify or fulfill.

Primarily, investors can examine whether sovereign actions can be attributed to EU institutions through coercion. As noted above, this is difficult to prove, since economic coercion is not as clear as military coercion and its definition is vague and subject to interpretation on a case-by-case basis. Even if coercion is found, investors might still be unable to succeed if the coercion was a countermeasure that could justify an otherwise illegal act. In this respect, TFEU might offer some other alternatives. However, case law seems too restrictive of such claims, which must be examined on a case-by-case basis. Thus, investors are unlikely to succeed in their claims against EU institutions in the case of sovereign default, as the concept of sovereignty imposes several obstacles on investors seeking remedies against EU institutions in case of sovereign default.