

The legal and regulative aspect of the free movement of capital towards the Capital Markets Union

I. Introduction

The free movement of capital – as it is traditionally seen as the fourth freedom, after goods, workers and persons, services and establishment – is a long-standing objective of the European Union, a fundamental freedom at the heart of the single market. Despite the progress that has been made, Europe's capital markets remain fragmented along national lines and European economies remain heavily reliant on the banking sector for their funding needs.² This makes them more vulnerable should bank lending tighten, as happened during the financial crisis. The European economy is as big as the American one, but Europe's equity markets are less than half the size, its debt markets less than a third. More integrated capital markets will lead to efficiency gains and support Europe's ability to fund growth. The establishment of the Capital Markets Union is important, because with a uniform regulation of cross-border investments and – above all, with – the creation of common rules for the covered bond market (€ 2.1 trillion estimated by the Commission) results in a tangible new dimension in the deepening of European integration, and would save EU borrowers an estimated € 1.5 to 1.9 billion annually. The European Fund and Asset Management Association (EFAMA) represents through its 28 member associations and 62 corporate members close to € 23 trillion in assets under management of which € 15.6 trillion managed by 60,174 investment funds at end 2017. Close to 32,000 of these funds were UCITS (Undertakings for Collective Investments in Transferable Securities) funds, with the remaining 28,300 funds composed of AIFs (Alternative Investment Funds).

The paper summarizes the development of the free movement of capital by describing the provisions of the primary law sources and listing the prominent directives and regulations. The major challenges of the capital liberalisation are demonstrated through the case law of the Court of Justice of the European Union, highlighting the different areas and judgments, legal principles. Finally, the situation of the Capital Market Union initiative and the Action plan are presented in details.

II. Historical preliminaries

At beginning of the creation of the European Economic Community, the Article 67 of the *Treaty of Rome* (25 March 1957) expressly declared, that during the transitional period and to the extent necessary to ensure the proper functioning of the common market, Member States shall progressively abolish between themselves all restrictions on the movement of capital belonging to persons resident in Member States and any discrimination based on the nationality or on the place of residence of the parties or on the place where such capital is invested. To foster these Article 71 contained, that the Member States are endeavour to avoid introducing within the Community any new exchange restrictions on the movement of capital

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² European Commission (2015): Action Plan on Building a Capital Markets Union COM(2015) 468 final

and current payments connected with such movements, and shall endeavour not to make existing rules more restrictive. It is interesting, that later the liberalisation of payments can be found in in Article 106: each Member State undertakes to authorise, in the currency of the Member State in which the creditor or the beneficiary resides, any payments connected with the movement of goods, services or capital, and any transfers of capital and earnings, to the extent that the movement of goods, services, capital and persons between the Member States has been liberalised pursuant to this Treaty. Therefore, while Article 67 has released autonomous capital-purpose movements, Article 106 has liberalized the payments related to the flow of other production factors, that is, ancillary natural payments. The legislation for the partial realization of the freedom of movement of capital is based on Article 69 of the Treaty of Rome, which authorized the Council to issue the necessary *directives*:

-EEC Council: First Directive for the implementation of Article 67 of the Treaty, OJ 43, 12.7.1960,

-Council Directive 72/156/EEC of 21 March 1972 on regulating international capital flows and neutralizing their undesirable effects on domestic liquidity, OJ L 91, 18.4.1972,

-Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty, OJ L 178, 8.7.1988.

It was also allowed for some countries to maintain temporary restrictions, but only for a specific period: Ireland, Portugal and Spain until 31 December 1992, and Greece until 30 June 1994. Protocol 32 to the Treaty on European Union (TEU) continues to allow Denmark to maintain existing legislation which restricts the acquisition of second homes by non-residents.

In the *Maastricht Treaty*, Article 63 TFEU prohibits all restrictions on the movement of capital and on payments between the Member States, and between the Member States and third countries. This terminates any limits on intra-EU buying or transferring currencies (transfers in euro are considered as domestic payments³), securities, company shares, stocks, bonds or financial assets, collective investment funds, credits, loans, sureties and guarantees, or government approval requirements for foreign investment.⁴ By contrast, the different types of taxes and or other charges with an equivalent effect on capital (e.g. corporate tax, capital gains tax – personal income tax, or financial transaction tax) are allowed, so long as they do not discriminate by nationality.

In cases where the Member States *restrict* the freedom of capital movement in an unjustified way, the usual infringement procedure set out in Article 258-260 TFEU applies. Some reasonable and rational exceptions and justified restrictions were built into the system, which related mostly to third countries. There was a so-called stand-still clause, because the provisions of Article 63 are without prejudice to the application to third countries of any restrictions which exist on 31 December 1993 under national or Union law adopted in respect of the movement of capital to or from third countries involving direct investment – including in real estate – establishment, the provision of financial services or the admission of securities to capital markets. In respect of restrictions existing under national law in Bulgaria, Estonia and Hungary, the relevant date shall be 31 December 1999. Furthermore, Article 65 reserves the right of Member States to take all requisite measures to prevent infringements of national law and regulations, in particular in the field of taxation and the prudential supervision of

³ This includes all member States of the EU, even those outside the eurozone providing the transactions are carried out in euro. Regulation (EC) No 2560/2001 of the European Parliament and of the Council of 19 December 2001 on cross-border payments in euro, OJ L 344, 28.12.2001

⁴ cf. 88/361/EEC for the implementation of Article 67 of the Treaty Annex I, including (i) investment in companies, (ii) real estate, (iii) securities, (iv) collective investment funds, (v) money market securities, (vi) bonds, (vii) service credit, (viii) loans, (ix) sureties and guarantees (x) insurance rights, (xi) inheritance and personal loans, (xii) physical financial assets (xiii) other capital movements.

financial institutions, or to lay down procedures for the declaration of capital movements for purposes of administrative or statistical information, or to take measures which are justified on grounds of public policy⁵ or public security. (The latter was invoked during the euro area crisis, when Cyprus (2013) and Greece (2015) were forced to introduce capital controls in order to prevent an uncontrollable outflow of capital.) The countries can even apply relevant provisions of their tax law which distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where their capital is invested. Articles 75 and 215 TFEU provide for the possibility of financial sanctions either to prevent and combat terrorism or based on decisions adopted within the framework of the common foreign and security policy.

Overview of exceptions stipulated in the Treaty

Specific exceptions of the Treaty		General exceptions of the Treaty
Free movement of capital - 63 TFEU	Third-country restrictions (grandfathered provisions) 64(1)TFEU	Restrictions on property ownership - 345 TFEU
	Tax differentiation 65(1)(a)TFEU	National security 346 TFEU
	Prudential measures 65(1)(b)TFEU	Defence 346 TFEU
	Public policy and public security 65(1)(b)TFEU	Financial sanctions 75 and 215 TFEU
Right of establishment 49-55 TFEU		General interest - CJEU jurisprudence

Source: Own compilation based on Treaty on the Functioning of the European Union and Kiefer Alonso Betina (2017): Legal basis for the free movement of capital

The legislation was continued by the following *major directives and regulations*:

- Regulation (EC) No 2560/2001 of the European Parliament and of the Council of 19 December 2001 on cross-border payments in euro, OJ L 344, 28.12.2001,
- Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC, OJ L 345, 31.12.2003
- Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market amending Directives 97/7/EC, 2002/65/EC, 2005/60/EC and 2006/48/EC and repealing Directive 97/5/EC, OJ L 319, 5.12.2007, so-called Payment Services Directive (PSD)
- Regulation (EC) No 924/2009 of the European Parliament and of the Council of 16 September 2009 on cross-border payments in the Community and repealing, OJ L 266, 9.10.2009,
- Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010, OJ L 174/1, 1.7.2011
- Regulation (EU) No 260/2012 of the European Parliament and of the Council of 14 March 2012 establishing technical and business requirements for credit transfers and direct debits in euro and amending Regulation (EC) No 924/2009, OJ L 94, 30.3.2012,

⁵ Article 144 TFEU Where a sudden crisis in the balance of payments occurs and a decision within the meaning of Article 143 (2) is not immediately taken, a Member State with a derogation may, as a precaution, take the necessary protective measures.

- Regulation (EU) No 345/2013 of the European Parliament and of the Council of 17 April 2013 on European venture capital funds. OJ L 115/1, 25.4.2013
- Regulation (EU) No 346/2013 of the European Parliament and of the Council of 17 April 2013 on European social entrepreneurship funds, OJ L 115/18, 25.4.2013
- Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market, amending Directives 2002/65/EC, 2009/110/EC and 2013/36/EU and Regulation (EU) No 1093/2010, and repealing Directive 2007/64/EC, OJ L 337, 23.12.2015.

III. Jurisdictions and the practice of the European Court

The Court of Justice of the European Union is charged with the task of interpreting the provisions related to the free movement of capital, and extensive case law exists in this area.⁶ The European Commission's Case Law Guide – Free Movement Of Capital is a practical orientation tool which explains the meaning and the scope of the rules on free movement of capital through the wording of the European Court of Justice.⁷ This compilation classifies the major and governing cases and judgments into seven categories:

- capital movements and payments definitions: general definition of capital movements and payments, examples of capital movements (direct investments, investments in real estate, operations in securities, operations to liquidate or assign assets built up, financial loans and credits, operation in units of collective investment undertakings, sureties and other guarantees, gifts and endowments, inheritances, taxation);
- territorial scope of article 63 TFEU: general principle, inter-state movements of capital, movement between EU member state and a third country;
- the direct effect of article 63 TFEU: vertical direct effect, cases with a private individual as a defendant;
- definition of restrictions: general definition of restrictions, restrictions according to their effects (directly, indirectly and non discriminatory measures);
- types of restrictive measures divided by sector: direct investments, investments in real estate, operations in securities and in units of collective investment undertakings, financial loans and credits, taxation, physical import and export of financial assets, inheritances;
- exceptions to the free movement of capital: article 64 TFEU (grandfather clause), article 65 TFEU (exception clause), case law justifications (emergency brake), proportionality, article 66 TFEU (restrictive measures against third countries justified by economic reasons), article 75 TFEU (freezing of funds to prevent and combat terrorism);
- relationship with other treaty articles: article 49 TFEU (freedom of establishment), article 56 TFEU (freedom to provide services), article 344 TFEU (exclusive jurisdiction clause), article 345 TFEU (principle of the neutrality of the treaties in relation to the rules in member states governing the system of property ownership), article 351 TFEU (obligation for member states to abolish all previous provisions incompatible with the treaties).

Although the Treaty does not define the terms “movements of capital”, the nomenclature in respect of movements of capital annexed to Directive 88/361/EEC,⁸ which

⁶ Király Miklós (2003): Az Európai Közösség kereskedelmi joga. KJK-KERSZÖV, p. 117.

⁷ European Commission (2016): Case Law Guide of the European Court of Justice on articles 63 et seq. TFEU – Free Movement Of Capital

⁸ Judgment of the Court of 4 June 2002. *Commission of the European Communities v French Republic*. Failure by a Member State to fulfil its obligations - Articles 52 of the EC Treaty (now, after amendment, Article 43 EC) and 73b of the EC Treaty (now Article 56 EC) - Rights attaching to the 'golden share held by the French Republic in Société Nationale Elf-Aquitaine. Case C-483/99. § 36.

list set out therein is not exhaustive.⁹ The physical transfer of assets falls not under Articles 30 and 59 but under Article 67 and the directive implementing that provision,¹⁰ and the physical export of means of payment cannot itself be regarded as a capital movement involving direct investment (including in real estate), establishment, the provision of financial services or the admission of securities to capital markets.¹¹ Means of payment are not to be considered as goods falling within the terms of Articles 30 to 37 of the treaty, these provisions do not, therefore, apply to silver alloy coins which are legal tender in a member state, gold coins such as Krugerrands which are produced in a non-member country but which circulate freely within a member state.¹² Current payments are transfers of foreign exchange which constitute the consideration within the context of an underlying transaction, whilst movements of capital are financial operations essentially concerned with the investment of the funds in question rather than remuneration for a service. The physical transfer of banknotes may not, therefore, be classified as a movement of the capital where the transfer in question corresponds to an obligation to pay arising from a transaction involving the movement of goods or services.¹³ Direct investment in the form of participation in an undertaking by means of a shareholding or the acquisition of securities on the capital market constitute capital movements.¹⁴

Measures were taken by Member State which are liable to dissuade its residents from obtaining loans or making investments in other Member States constitute restrictions on movements of capital within the meaning of that provision.¹⁵ A provision of national law which makes a direct foreign investment subject to prior authorisation constitutes a restriction on the movement of capital within the meaning of Article 73b (1) of the Treaty.¹⁶ Accordingly, a procedure of prior authorisation, such as that under the TGVG 1996, which entails, by its very purpose, a restriction on the free movement of capital, can be regarded as compatible with Article 56 EC only on certain conditions.¹⁷ But in the same case, it was declared, that

⁹ Judgment of the Court of 16 March 1999. - *Manfred Trummer and Peter Mayer*. - Reference for a preliminary ruling: Oberster Gerichtshof - Austria. - Free movement of capital - National prohibition on the creation of a mortgage in a foreign currency - Interpretation of Article 73b of the EC Treaty. - Case C-222/97. § 21.

¹⁰ Judgment of the Court of 23 February 1995. - Criminal proceedings against *Aldo Bordessa and Vicente Mari Mellado and Concepción Barbero Maestre*. - References for a preliminary ruling: Audiencia Nacional - Spain. - Directive 88/361/EEC - Authorization for the transfer of money in the form of banknotes. - Joined cases C-358/93 and C-416/93. § 13.

¹¹ Judgment of the Court of 14 December 1995. Criminal proceedings against *Lucas Emilio Sanz de Lera, Raimundo Díaz Jiménez and Figen Kapanoglu*. References for a preliminary ruling: Juzgado Central de lo Penal de la Audiencia Nacional - Spain. Capital movements - Non-member countries - National authorization for the transfer of banknotes. Joined cases C-163/94, C-165/94 and C-250/94.

¹² Judgment of the Court of 23 November 1978. - *Regina v Ernest George Thompson, Brian Albert Johnson and Colin Alex Norman Woodiwiss*. - Reference for a preliminary ruling: Court of Appeal (England) - United Kingdom. - Means of payment and movements of capital. - Case 7/78. § 26-27.

¹³ Judgment of the Court of 31 January 1984. - *Graziana Luisi and Giuseppe Carbone v Ministero del Tesoro*. - References for a preliminary ruling: Tribunale civile e penale di Genova - Italy. - Invisible transactions - National control requirements. - Joined cases 286/82 and 26/83. § 21-22.

¹⁴ Judgment of the Court of 4 June 2002. *Commission of the European Communities v Portuguese Republic*. Failure by a Member State to fulfil its obligations - Articles 52 of the EC Treaty (now, after amendment, Article 43 EC) and 73b of the EC Treaty (now Article 56 EC) - System of administrative authorisation relating to privatised undertakings. Case C-367/98. § 38.

¹⁵ Judgment of the Court of 14 November 1995. - *Peter Svensson et Lena Gustavsson v Ministre du Logement et de l'Urbanisme*. - Reference for a preliminary ruling: Conseil d'Etat - Grand Duchy of Luxemburg. - Free movement of capital - Freedom to provide services - Interest rate subsidy on building loans - Loan by a credit institution not approved in the Member State granting the subsidy. - Case C-484/93. § 10.

¹⁶ Judgment of the Court of 14 March 2000. - *Association Eglise de scientologie de Paris and Scientology International Reserves Trust v The Prime Minister*. - Reference for a preliminary ruling: Conseil d'Etat - France. - Free movement of capital - Direct foreign investments - Prior authorisation - Public policy and public security. - Case C-54/99. § 14.

¹⁷ Judgment of the Court of 1 June 1999. *Klaus Konle v Republik Österreich*. Reference for a preliminary ruling:

Section 10(2) of the TGVG 1993, which exempts only Austrian nationals from having to obtain authorisation before acquiring a plot of land creates a discriminatory restriction against nationals of other Member States in respect of capital movements.

The golden shares (especially if they are owned by the state) is a crucial point in the free movement of capital. Paragraph 4(3) of the VW Law thus creates an instrument enabling the Federal and State authorities to procure for themselves a blocking minority (20 %) allowing them to oppose important resolutions. By limiting the possibility for other shareholders to participate in the company with a view to establishing or maintaining lasting and direct economic links with it which would make possible effective participation in the management of that company or in its control, this situation is liable to deter direct investors from the other Member States. It must, therefore, be held that the combination of Paragraphs 2(1) and 4(3) of the VW Law constitutes a restriction on the movement of capital within the meaning of Article 56(1) EC, and it is disproportionate for the government's stated aim of protecting workers or minority shareholders.¹⁸ Similarly, in so far as the national measures at issue entail restrictions on freedom of establishment, such restrictions are a direct on sequence of the obstacles to the free movement of capital, to which they are inextricably linked. Portugal infringed free movement of capital by retaining golden shares in Portugal Telecom that enabled disproportionate voting rights, by creating a deterrent effect on portfolio investments and reducing the attractiveness of an investment.¹⁹

IV. Capital Markets Union

Within the building on the Investment Plan for Europe, for a closer integration of capital markets,²⁰ on 30th September 2015, the Commission adopted the *Action Plan on Building a Capital Markets Union* (CMU) setting out a list of key measures to achieve a true single market for capital in Europe, which deepens the existing Banking Union,²¹ because this revolves around disintermediated, market-based forms of financing, which should represent an alternative to the traditionally predominant (in Europe) bank-based financing channel.²² The EU's political and economic context²³ call for strong and competitive capital markets to finance the EU economy.²⁴ The CMU project is a political signal to strengthen the Single

Landesgericht für Zivilrechtssachen Wien - Austria. Freedom of establishment - Free movement of capital - Articles 52 of the EC Treaty (now, after amendment, Article 43 EC) and 56 EC (ex Article 73b) - Authorisation procedure for the acquisition of immovable property - Article 70 of the Act concerning the conditions of accession of the Republic of Austria - Secondary residences - Liability for breach of Community law. Case C-302/97. § 39. and § 23.

¹⁸ Judgment of the Court (Grand Chamber) of 23 October 2007. *Commission of the European Communities v Federal Republic of Germany*. Failure of a Member State to fulfil obligations - Article 56 EC - Legislative provisions concerning the public limited company Volkswagen. Case C-112/05. § 50-59

¹⁹ Judgment of the Court (First Chamber) of 8 July 2010 - *European Commission v Portuguese Republic* (Failure of a Member State to fulfil obligations - Articles 56 EC and 43 EC - Free movement of capital - Portuguese State's 'golden' shares in Portugal Telecom SGPS SA - Restrictions on the acquisition of holdings and on the management of a privatised company - State measure) Case C-171/08. § 80

²⁰ Ruediger Veil, Philipp Koch (2012): Towards a Uniform European Capital Markets Law: Proposals of the Commission to Reform Market Abuse. in Bucerius Law School Working Paper No. 1/2012

²¹ Csaba László (2018): Tőkepiaci unió vagy szabadságharc? in *Közgazdasági Szemle*, LXV. évf., 2018. május

²² Vincenzo Bavoso (2017): Capital Markets, Debt Finance and the EU Capital Markets Union: A Law and Finance Critique. University of Manchester, p. 7.

²³ Lucia Quaglia, David Howarth, Moritz Liebe (2016): The Political Economy of European Capital Markets Union in *JCMS-Journal of Common Market Studies*, Vol. 54, No. S1, 2016, p. 185-203.

²⁴ European Commission (2017): on the Mid-Term Review of the Capital Markets Union Action Plan COM(2017) 292 final

Market as a project of all 28 Member States,²⁵ instead of just the Eurozone countries, and sent a strong signal to the UK to remain an active part of the EU, before Brexit.²⁶The goals are widely acceptable: boosting investments, growth and employment; reducing financial fragmentation between member states; and establishing more integrated, efficient and competitive financial markets.

²⁵ Danny Busch (2017): A capital markets union for a divided Europe. SSRN Electronic Journal

²⁶ Wolf-Georg Ringe (2015): Capital Markets Union for Europe - A Political Message to the UK. in Law and Financial Markets Review 9 (2015), p. 5 and Oxford Legal Studies Research Paper No. 26/2015

Actions and indicative timeline

Financing for innovation, start-ups and non-listed companies	
Promote innovative forms of corporate financing - Report on crowdfunding	Q1 2016
Support venture capital and equity financing - Proposal for pan-European venture capital fund-of-funds and multi-country funds	Q2 2016
Overcome information barriers to SME investment - Strengthen feedback given by banks declining SME credit applications	Q2 2016
Revise EuVECA and EuSEF legislation	Q3 2016
Develop a coordinated approach to loan origination by funds and assess the case for a future EU framework	Q4 2016
Study on tax incentives for venture capital and business angels	2017
Map out existing local or national support and advisory capacities across the EU to promote best practices	2017
Investigate how to develop or support pan-European information systems	2017
Making it easier for companies to enter and raise capital on public markets	
Strengthen access to public markets - Proposal to modernise the Prospectus Directive	Q4 2015
Support equity financing Address the debt-equity bias, as part of the legislative proposal on Common Consolidated Corporate Tax Base	Q4 2016
Review regulatory barriers to SME admission on public markets and SME Growth Markets	2017
Review EU corporate bond markets, focusing on how market liquidity can be improved	2017
Investing for long term, infrastructure and sustainable investment	
Review of the CRR for banks, making changes on infrastructure calibrations, if appropriate	Ongoing
Support infrastructure investment - Adjust Solvency II calibrations for insurers' investment in infrastructure and European Long Term Investment Funds	Q3 2015
Ensure consistency of EU financial services rulebook - Call for evidence on the cumulative impact of the financial reform	Q3 2015
Fostering retail and institutional investment	
Increase choice and competition for retail - Green Paper on retail financial services and insurance	Q4 2015
Consultation on the main barriers to the cross-border distribution of investment funds	Q2 2016
Support saving for retirement - Assessment of the case for a policy framework to establish European personal pensions	Q4 2016
Help retail investors to get a better deal - EU retail investment product markets assessment	2018
Expand opportunities for institutional investors and fund managers - Assessment of the prudential treatment of private equity and privately placed debt in Solvency II	2018
Leveraging banking capacity to support the wider economy	
Strengthen local financing networks - Explore the possibility for all Member States to authorise credit unions outside the EU's capital requirements rules for banks	Ongoing
Build EU securitisation markets - Proposal on simple, transparent and standardised (STS) securitisations and revision of the capital calibrations for banks	Q3 2015
Support bank financing of the wider economy - Consultation on an EU-wide framework for covered bonds and similar structures for SME loans	Q3 2015
Facilitating cross-border investing	
Strengthen supervisory convergence and capital market capacity building - Strategy on supervisory convergence to improve the functioning of the single market for capital	Ongoing
White Paper on ESAs' funding and governance	Q2 2016
Develop a strategy for providing technical assistance to Member States to support capital markets' capacity	Q3 2016
Remove national barriers to cross-border investment - Report on national barriers to the free movement of capital	Q4 2016

Foster convergence of insolvency proceedings - Legislative initiative on business insolvency, addressing the most important barriers to the free flow of capital	Q4 2016
Enhance capacity to preserve financial stability - Review of the EU macroprudential framework	2017
Improve market infrastructure for cross-border investing - Targeted action on securities ownership rules and third-party effects of assignment of claims	2017
Review progress in removing remaining Giovannini barriers	2017
Remove cross-border tax barriers - Best practice and code of conduct for relief-at-source from withholding taxes procedures	2017
Study on discriminatory tax obstacles to cross-border investment by pension funds and life insurers	2017

Source: Own compilation based on European Commission (2015): Action Plan on Building a Capital Markets Union
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The CMU has a strong impact on competitiveness, according to the Commission calculations, if the integration of the EU venture capital markets were as deep as in the USA, more than € 90 billion of funds would have been available to finance companies between 2009 and 2014. Investment needs are also great – for example, it is estimated that for the EU's transition to a low carbon economy it will need EUR 200 billion of investment per year.²⁷ As a consequence of the CMU, the stronger capital markets will complement Europe's strong tradition of bank financing, and will.²⁸

-unlock more investment from the EU and the rest of the world: the CMU should help mobilise capital in Europe and channel it to all companies, including SMEs, and infrastructure projects that need it to expand and create jobs. It will provide households with better options to meet their retirement goals.

-connect financing more effectively to investment projects across the EU: the CMU is a classic single market project for the benefit of all 28 Member States. Those Member States with the smallest markets and high growth potential have a lot to gain from a better channelling of capital and investment into their projects. More developed market economies will benefit from greater cross-border investment and saving opportunities.

-make the financial system more stable: by opening up a wider range of funding sources and more long-term investment, reduce the vulnerability of EU citizens and companies to banking shocks such as those they were exposed to during the crisis.

-deepen the financial integration and increase competition: more cross-border risk-sharing, deeper and more liquid markets and diversified sources of funding should deepen financial integration, lower costs and increase European competitiveness.

Even the choice of “Union” for capital markets is a clear attempt to create parity of esteem with Economic and Monetary Union and Banking Union and thus to emphasise the importance of the subject and the European Commission's ambitions in this area. On a different scale to these two other ‘Unions’, the institutional content of CMU is smaller (with the possible exception of the strengthening of the powers of supervisory authorities). The other two Unions came into being first through the institutions and institutional mechanisms: EMU was founded on the creation of the European Central Bank (ECB) and the European system of central banks, whilst Banking Union was founded on the supervisory role granted to the ECB, on the Single Supervisory Mechanism (SSM), on resolution structures and on the planned European Deposit Insurance Scheme. The process is different for Capital Markets Union: the European Commission's initiatives will provide some, much needed, momentum, but it will be down to economic agents – savers, companies and the financial community – to transform this into a lasting trend.²⁹ Whereas Banking Union primarily concerns the euro area, CMU applies to all EU countries.³⁰

²⁷ European Commission (2015): Action Plan on Building a Capital Markets Union COM(2015) 468 final

²⁸ European Commission (2015): Action Plan on Building a Capital Markets Union COM(2015) 468 final

²⁹ Laurent Quignon (2018): The challenges of Capital Markets Union. BNP Paribas Eco Conjoncture January 2018

cf. The removal of the term “Community” and its replacement with the term “Union” in the Lisbon Treaty that came into effect on 1 December 2009 was about more than semantics. It recognised the establishment of the legal personality of the European Union and reflected the desire to increase political and economic integration.

³⁰ Christian de Boissieu (2017): The Banking Union Revisited - CMU and the Financing of the Real Economy in Raphaël Douady, Clément Goulet, Pierre-Charles Pradier (2017): Financial Regulation in the EU - From Resilience to Growth. Palgrave Macmillan. pp. 100-101



Source: European Commission (2018) Deepening Europe's Economic and Monetary Union. Commission Note ahead of the European Council and the Euro Summit of 28-29 June 2018.

The Action Plan sets out the measures that will be taken over the next years so that the building blocks of the CMU are in place by 2019. There is no single legislation that will deliver a Capital Markets Union. Instead, there will be a *range of steps* whose impact will cumulatively be significant. The Commission will take forward measures to remove the barriers which stand between investors' money and investment opportunities, and overcome the obstacles which prevent businesses from reaching investors.³¹

- financing for innovation, start-ups and non-listed companies (2016-2017)
- making it easier for companies to enter and raise capital on public markets (2015-2017)
- investing for long-term, infrastructure and sustainable investment (2015)
- fostering retail and institutional investment (2015-2018)
- strengthening banking capacity to support the wider economy and the capacity of EU capital markets- leveraging banking capacity to support the wider economy (2015)
- facilitating cross-border investing (2015-2017).

In 2015 two legislative proposals as immediate steps were introduced, one on establishing a framework high-quality and simple, transparent and standardised (so-called STS label) securitisation,³² and to set out revision of the new prudential calibrations for banks in the Capital Requirements Regulation (CRR), and another on allowing more funding to flow to infrastructure projects. Besides, an adjustment to the Solvency II legislation was prepared to make it easier for insurers to invest in infrastructure and European Long-Term Investment Funds (ELTIFs). Two consultations were also launched on how to build a pan-European covered bond (and similar structures for SME loan) framework and on venture capital to assess whether targeted changes to the regulations could boost the take-up of these investment funds. Even a call for evidence was started on the cumulative impact of financial services reforms, with the objective to ensure the consistency of EU financial services rulebook, and to assess the interactions between rules and the cumulative impact of the reforms adopted in the recent years. The purpose of the Green Paper on retail financial services and insurance is, to boost consumer choice and competition in cross-border retail financial services and insurance.

In 2016 the Commission defined three main targets for longer-term actions: supporting access to finance, increasing investment and removing (particularly national and tax) barriers to cross-border investment. Within supporting access to finance, innovative forms of corporate financing, venture capital and equity financing were supported by the Proposal for pan-European venture capital fund-of-funds and multi-country funds, focusing on SMEs.³³

³¹ European Commission (2015): Action Plan on Building a Capital Markets Union COM(2015) 468 final

³² Vincenzo Bavoso (2016): High Quality Securitisation and EU Capital Markets Union – Is it Possible? Convivium, Forthcoming

³³ Pierre Schammo (2015): Capital Markets Union and Small and Medium-Sized Enterprises (SMEs): A Preliminary Assessment in F. Allen, E. Carletti and J. Gray (eds), The New Financial Architecture of the

The European Venture Capital Fund (EuVECA)³⁴ and the European social entrepreneurship funds (EuSEF)³⁵ legislation were revised. A coordinated approach to loan origination by funds and assess the case for a future EU framework, and a strategy for providing technical assistance to the Member States to support capital markets' capacity were developed. The topic of increasing investment increased the choice and competition for retail consumers; supported saving for retirement for a policy framework to establish European personal pensions; and expanded opportunities for asset managers. The goals of the removing barriers to cross-border investment theme focus on removing national and tax barriers to cross-border investment, improve market infrastructure for cross-border investing; fostering convergence of insolvency proceedings; strengthening supervisory convergence; enhancing capacity to preserve financial stability. In order to foster the convergence of insolvency proceedings, a legislative initiative has launched on business insolvency, addressing the most important barriers to the free flow of capital.

According to the schedule, in 2017 different expert analytical documents were prepared: a study on tax incentives for venture capital and business angels, a study on discriminatory tax obstacles to cross-border investment by pension funds and life insurers, an investigation how to develop or support Pan-European information systems, and a fourth one to map out existing local or national support and advisory capacities across the EU to promote best practices. A major threat to the development of European capital markets is the financial transactions tax (FTT) proposed by the European Commission in September 2011, which highlights an apparent ambivalence of the Commission toward capital markets.³⁶The regulatory barriers to SME admission on public markets and SME Growth Markets; the EU corporate bond markets (focusing on how market liquidity can be improved); the EU macroprudential framework, and the progress in removing the remaining so-called Giovannini barriers³⁷ were reviewed. For removing cross-border tax barriers, best practice and code of conduct for relief-at-source from withholding taxes procedures were identified. To improve market infrastructure for cross-border investing, an action was targeted on securities ownership rules and third-party effects of assignment of claims. In this year the Commission prepared the Mid-Term Review of the Capital Markets Union Action Plan.³⁸ Over the past 18 months, in accordance with the original timetable, the Commission has delivered more than half the measures (20 out of 33) announced in the CMU Action Plan. The 178 responses to the public consultation on the CMU Mid-term Review confirmed the more specific challenges that CMU has to address. The report highlighted social-financial problems: there is not enough investment by insurance companies and pension funds in risk capital, equity and infrastructure, and engagement by retail investors with capital markets remains low. EU households are amongst the highest savers in the world, but the bulk of these savings are held in bank accounts with short maturities. More investment into the capital market can help meet the challenges posed by population ageing and low interest rates. The Pan-European Personal Pension Product (PEPP)

Eurozone (European University Institute, RSCAS, Florence School of Banking and Finance

³⁴ Regulation (EU) No 345/2013 of the European Parliament and of the Council of 17 April 2013 on European venture capital funds. OJ L 115/1, 25.4.2013

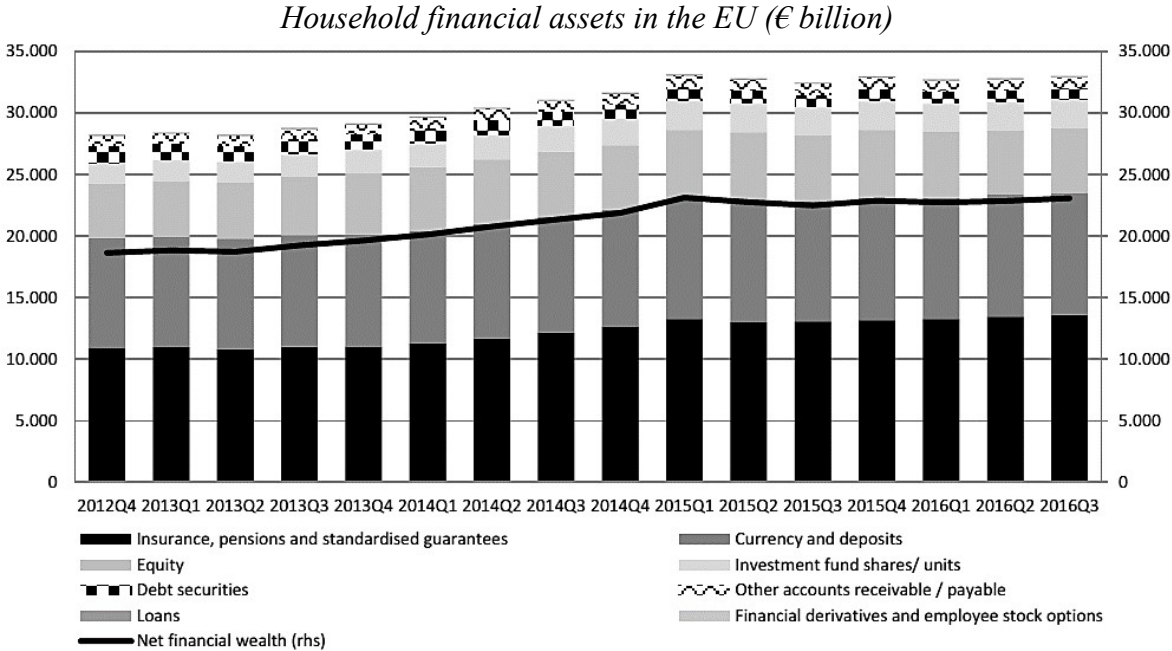
³⁵ Regulation (EU) No 346/2013 of the European Parliament and of the Council of 17 April 2013 on European social entrepreneurship funds, OJ L 115/18, 25.4.2013

³⁶ Franklin Allen and Luboš Pastor (2018): The Capital Markets Union: Key Challenges. in SSRN Electronic Journal January 2018. p. 19.

³⁷The Giovannini barriers identified by the Giovannini Group in 2001 and 2003 within two reports for the European Commission. The list of barriers has been sub-divided under three main headings: (i) national differences in technical requirements/market practice; (ii) national differences in tax procedures; (iii) to issues of legal certainty. See Giovannini Group Report (2001): Cross-border clearing and settlement arrangements in the European Union. and Giovannini Group Report (2003): EU clearing and settlement arrangements.

³⁸ European Commission (2017): on the Mid-Term Review of the Capital Markets Union Action Plan COM(2017) 292 final

will lay the foundations for a safer, more cost-efficient and transparent market in affordable and voluntary personal pension savings that can be managed on a Pan-European scale.



Source: European Commission (2017): Commission Staff Working Document - Economic Analysis Accompanying the document - on the Mid-Term Review of the Capital Markets Union Action Plan. European Commission, p. 73.

The CMU Mid-term review set out *nine new priority actions*:³⁹

- strengthen the powers of European Securities and Markets Authority to promote the effectiveness of consistent supervision across the EU and beyond;
- deliver a more proportionate regulatory environment for SME listing on public markets;
- review the prudential treatment of investment firms;
- assess the case for an EU licensing and passporting framework for FinTech activities;
- present measures to support secondary markets for non-performing loans (NPLs) and explore legislative initiatives to strengthen the ability of secured creditors to recover value from secured loans to corporates and entrepreneurs;
- ensure follow-up to the recommendations of the High-Level Expert Group on Sustainable Finance;
- facilitate the cross-border distribution and supervision of UCITS and alternative investment funds (AIFs);
- provide guidance on existing EU rules for the treatment of cross-border EU investments and an adequate framework for the amicable resolution of investment disputes;
- propose a comprehensive EU strategy to explore measures to support local and regional capital market development.

In 2018, one of the goals of the progress is, to help retail investors to get a better deal within an EU retail investment product markets assessment, and expand opportunities for institutional investors and fund managers. An assessment of the prudential treatment of private equity and privately placed debt in Solvency II is under construction. By May 2018, the Commission submitted 12 legislative proposals on this subject, which it intends to finalize in the course of 2019 by the Council and the European Parliament.

³⁹ European Commission (2017): Completing the Capital Markets Union: Building on the first round of achievements. European Commission - Press release, 8 June 2017.

Delivering on the Capital Markets Union

MEASURE	DESCRIPTION	European Commission	European Parliament	Council of the EU
Legislative proposal on business insolvency and restructuring	Legislative proposal on preventive restructuring and second chance for businesses	P/A	A	A
Commission proposal for a Pan-European Personal Pension Product (PEPP)	New rules to provide pension providers with the tools to offer a simple and innovative Pan-European Personal Pension Product	P/A	A	P/A
Commission proposal for a review of the European Supervisory Authorities	Reform of the EU's supervisory architecture for stronger and more integrated financial markets	P/A	A	A
More proportionate and effective rules for investment firms	A more targeted regime to reduce risks in investment firms' activities	P/A	A	A
Commission proposals implementing the Action Plan on sustainable finance	First legislative measures, including harmonised criteria to determine whether an economic activity is environmentally sustainable, to increase transparency and facilitate investment insustainability through new sustainable benchmarks	P/A	A	A
Commission Action plan on FinTech and a legislative proposal for framework on crowdfunding and peer-to-peer lending	EU strategy to promote financial innovation while protecting consumers and investors. New EU rules to boost and facilitate cross-border activity in the crowd funding sector	P/A	A	A
European covered bonds	New rules to promote covered bond markets as a source of funding for banks there by increasing lending to the economy	P/A	A	A
Facilitate cross-border distribution of investment funds	Legislative initiative for easier EU-wide distribution of investment funds	P/A	A	P/A
Clear rules on ownership of securities and claims	Measures to enhance legal certainty in cross-border transactions in claims and securities	P/A	A	A
Rules to give smaller businesses easier access to growth markets	New rules to give small and medium enterprises better access to financing through public markets	P/A	A	A
Targeted amendments to the European Market Infrastructure Regulation (EMIR)	Improving the functioning of the derivatives market ensuring a more robust supervision of central counterparties (CCPs)	P/A	A	A
Enabling framework for Sovereign Bond-Backed Securities	Help investors diversify their euro area sovereign portfolios and contribute to weakening the link between banks and their home countries, without involving any mutualisation of risks and losses among the Member States	P/A	A	A

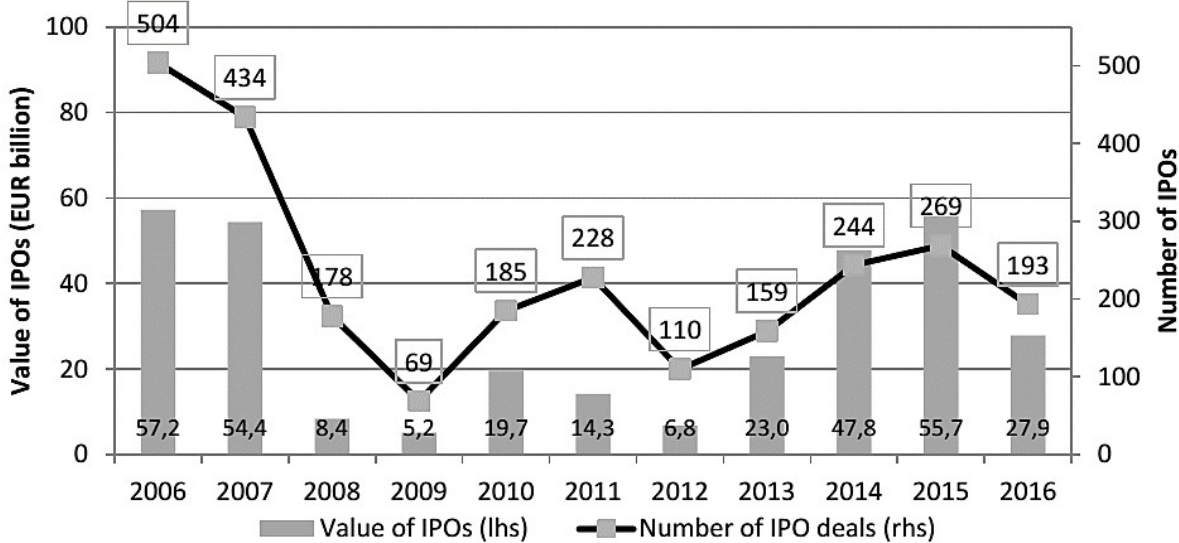
Source: European Commission (2018) Deepening Europe's Economic and Monetary Union. Commission Note ahead of the European Council and the Euro Summit of 28-29 June 2018.

P/A: presented/agreed; A: agreement possible by May 2019 if there is strong political commitment from all EU institutions

The Commission on 24 May 2018 proposed new rules to give small and medium enterprises (SMEs) better access to financing through public markets, which initiative can help EU companies to tap market-based funding more easily and cheaply so that they can

expand. Most actions are intended to boost non-bank financing (market or fund financing) tailored in particular to SMEs and intermediate-sized firms, such as alternative investment funds (private equity, hedge funds, money markets funds, real estate funds, crowdfunding, etc.) regulated in the EU under the AIFM directive.⁴⁰ Today out of the 20 million SMEs in Europe, only 3,000 are listed on stock exchanges.⁴¹ Beside markets and banks, it is useful to make more explicit the role of funds. Main proposed changes to SME listings rules: avoid excessive administrative burden for SMEs; allow issuers with at least three years of listing on SME Growth Markets to produce a lighter prospectus⁴² when transferring to a regulated market; make it easier for trading venues specialised in bond issuance to register as SME Growth Markets, by setting a new definition of debt-only issuers;⁴³ and create a common set of rules on liquidity contracts for SME Growth Markets.

European Initial Public Offering (IPO) activity



Source: European Commission (2017): Commission Staff Working Document - Economic Analysis Accompanying the document - on the Mid-Term Review of the Capital Markets Union Action Plan. European Commission, p. 39.

Of course, the simplifications are welcome, but how and who will put the STS label on some securitization vehicles: ESMA or national financial regulators or independent rating agencies. The financial crises raised the attention to this problem earlier, and even the investor-protection needs to handle this. Additionally, common legislation and harmonisation are needed regarding crowdfunding practices, corporate law (e.g. bankruptcy rules) and corporate taxation.⁴⁴The Action Plan set out a programme of actions which aim to establish

⁴⁰ Christian de Boissieu (2017): The Banking Union Revisited - CMU and the Financing of the Real Economy in Raphaël Douady, Clément Goulet, Pierre-Charles Pradier (2017): Financial Regulation in the EU - From Resilience to Growth. Palgrave Macmillan. pp. 100-101

For legal background see Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010, OJ L 174/1, 1.7.2011

⁴¹ Valdis Dombrovskis (2018): Capital Markets Union: Making it easier for smaller businesses to get financing through capital markets. European Commission - Press release, 24 May 2018.

⁴² A prospectus is a legal document with information an investor needs to have before making a decision whether to invest in the company.

⁴³ Those would be companies that issue less than € 50 million of bonds over a 12-months period.

⁴⁴ For details, see Christoph Kaserer (2008): Restricting Interest Deductions in Corporate Tax Systems: Its Impact on Investment Decisions and Capital Markets. European Private Equity and Venture Capital Association Special Paper

the building blocks of an integrated capital market in the European Union by 2019, and will follow key principles: connecting financing to the real economy by developing non-bank funding sources; creating more opportunities for investors; fostering a stronger and more resilient financial system; deepening financial integration and increasing competition.⁴⁵

V. Conclusion

After more than six decades of the signing of the Treaty of Rome, the European capital markets remained fragmented along national lines and European economies remain heavily reliant on the banking sector for their funding needs. The proliferative case law and sometimes controversial jurisdictions of the Court of Justice of the European Union still reveal the deficiency and the need for uniform regulation. Today the Capital Markets Union is not a reality, but even not a persistent, foggy goal or an unattainable dream. It is an ambitious, concrete, operational economy regulation solution that will open a new dimension in the development of European (financial) integration in the foreseeable future. But there is still today a big gap between the very ambitious goals of CMU and the lack of a concrete and credible roadmap for such a project, the timetable is still too vague and not binding enough.⁴⁶ Currently, there are both technical and conceptual differences in this area between the Member States. In this particular case, the risk sharing and mitigation are envisaged in a different order, by other techniques and by the different rates of national / international burden-sharing. And the details are not clear yet. These aspects have hindered the establishment of the Banking Union for a decade and a half, it can be forecasted, that the swift and comprehensive solution advocated by the Commission will not happen soon. Common legislation and harmonisation are needed regarding securitisation, integrated covered bond market, STS labelling, the involvement of retail investments, savings for retirement, prospectus, crowdfunding practices, corporate law (e.g. bankruptcy rules) and corporate taxation. These topics cover a fairly wide spectrum, so it can be fearful that the long-term goals will drop out of focus. The Commission cannot build CMU alone. Its success will depend on the level of political commitment from the Member States, the European Parliament and market participants. Therefore, the catching up is important for the non-euro zone states, since they could have experienced the disadvantages of the backlog in the case of the Bank Union, where the European Central Bank granted unlimited liquidity with favourable conditions for the eurozone member banks after the financial crisis. Later even similar situation may occur on capital markets, and on the other hand, a boosting development can start. Whoever stays out, misses out.

⁴⁵ cf. European Commission (2017): Completing the Capital Markets Union: Building on the first round of achievements. European Commission - Press release, 8 June 2017. and European Commission (2015): Questions and Answers on the Action Plan on building a Capital Markets Union. European Commission - Fact Sheet, 30 September 2015

⁴⁶ Christian de Boissieu (2017): The Banking Union Revisited - CMU and the Financing of the Real Economy in Raphaël Douady, Clément Goulet, Pierre-Charles Pradier (2017): Financial Regulation in the EU - From Resilience to Growth. Palgrave Macmillan. pp. 100-101

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