

Position of ESTA on the Advocate General's opinion of 29 September 2020 on legal tender.

(Joint cases C-422/19 and C-423/19)

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Summary

The status of legal tender of any currency implies a full backing by the emitting Central Bank, which nothing can undermine. Cash, as the only public money, is an IOU over the emitter. The current status of EU law is such that only the value of physical money, euro banknotes and coins, can be fully preserved at any time. Non-physical forms of euros cannot and as such cannot claim to be Central Bank money. No private money can therefore be legal tender.

A limitation of legal tender based on contractual agreement, the legal basis of which is not specified in the Opinion, is incompatible with the EU treaties in as much as it bears the promise of the elimination of cash, as it allows market forces to gradually, but irreversibly, phase out cash in the economy.

ESTA welcomes the opinion of the Advocate General in the joint cases C-422/19 and C-423/19. In relation to legal tender, ESTA also welcomes the recognition that monetary policy, of which the definition of legal tender is one of the precondition (Point 65), is an exclusive Union's competence. It derives therefore that restrictions by Member States on the use of cash can only be compatible with EU law provided they do not govern legal tender. This means that Member state's legislation cannot expand or restrict the notion of legal tender.

It is also a welcomed confirmation that legal tender is a primary law provision.

Legal tender for banknotes and coins ("cash") is defined in the recommendation 2010/191 of 22 March 2010 as "mandatory acceptance, at full value with the power to discharge from payment obligations." Cash as a payment could only be refused on the basis of "good faith".

Restrictions to legal tender

Point 125 of the Opinion states that cash is "the means of payment by default, it *must* be accepted unless otherwise agreed independently by the parties, or unless otherwise provided by regulation restricting its use as a means of payment for *public reasons*." (ESTA emphasis)

The Advocate General’s Opinion flags two types of admissible restrictions to legal tender.

The first concerns the restrictions justified under recital 19 of Council Regulation (EC) No 974/98 of 3 May 1998 on the introduction of the euro which states that “limitations on payments in notes and coins, established by Member States for public reasons, are not incompatible with the status of legal tender of euro banknotes and coins, provided that other lawful means for the settlement of monetary debts are available”.

The second relates to the contractual freedom of the parties, or in other words, “*private reasons*”. ESTA would submit that the two restrictions are not of equal level, although this does not appear clearly from the Opinion.

Restrictions related to public reasons

Public reasons tend to put the threshold of acceptability fairly high. Indeed, the public reasons put forward by Member States are all based on overarching public policy objectives limited, in essence, to just three: fight against terrorism, fight against (organised) crime and fight against tax evasion (and related money laundering). It has been acknowledged in the Commission’s impact assessment on restriction in payments in cash that cash restrictions would, in effect, have little efficiency on terrorism due to the very low levels of amounts spent by terrorists,¹ and the fact, as pointed out by a number of anti-terrorism experts, that payments in cash or otherwise by terrorists are legal in nature, but only become illegal by a “change of purpose”: renting a lorry is legal, but running it into a crowd is criminal. This further restricts the scope of public reasons.

Arguably, these public reasons also are of primary law relevance as they are commonly justified restrictions on the four Fundamental Freedoms in the original treaties.

It should also be pointed out that the two specific examples in the Opinion’s point 122 related to anti-money laundering and the Regulation on cash entering or leaving the EU (which also applies to individual Members States’ borders) are no restriction *stricto sensu* to legal tender as they do not impose *per se* any limitation to payments but reporting/declaration requirements to payments in or transport of cash in addition to due diligence obligations.

Restrictions related to contractual freedoms –what about legal certainty?

The legal basis of the restriction related to contractual freedom is not clearly established in the AG’s opinion. The Opinion refers to a number of provisions in EU law that confer legal tender status to cash,² and systematically add “unless the parties exercise their contractual freedom”. Nowhere does the Advocate general establish in the Opinion which specific EU legal basis would allow contractual freedom to restrict the (primary law) legal tender status of cash.

¹ Report from the Commission to the European Parliament and the Council on restrictions on payments in cash, COM(2018) 483 final.

² The concept of legal tender as regards euro banknotes, is laid down in the third sentence of Article 128(1) TFEU, the third sentence of the first paragraph of Article 16 of Protocol No 4 on the Statute of the ESCB and of the ECB, the second sentence of Article 10, of Regulation No 974/98

The contractual freedom is therefore of a different level, not least because the public reasons mentioned above do often restrict contractual freedom itself.

Second, contractual freedom is restricted and regulated in numerous ways, which includes for example, laws to protect competition, to protect consumers, to restrict or prohibit the sale of certain products, to label products, to prohibit unsubstantiated health or nutritional claims, to protect geographical indications, unfair contractual terms, misleading information etc. to list but a few. Some regulations affecting the contractual freedom are such that the law prohibits, even by mutual and informed consent, that consumers waive their rights, for example in the context of cooling off periods. In general, the EU law philosophy in consumer protection is that the two parties, the professional and the consumer, are not on equal footing and the latter deserves stronger protection than the former.

Therefore, the argument of contractual freedom in the case of legal tender needs to be considered carefully, as it is fundamentally unbalanced. It is clearly not, contrary to the *public reason* justification, of primary law relevance. Even considered as secondary law, it is subordinated to a very large array of rules of any kind which takes precedence over or restrict it. It is therefore pretty much down the line of the hierarchy of norms. Its ability to affect the interpretation of primary law should be considered cautiously.

For example, contractual freedom may justify that one retail shop in a street refuses cash and informs the consumer accordingly at the entrance of the shop: it is then an informed decision of the consumer to proceed in this retail. However, if all shops in the same high street or in a shopping mall refuse cash (as has been seen due to COVID fears of contamination by cash),³ then consumers are left with no choice. One could argue that this would also be against competition rules, if there is a tacit agreement by a majority of retailers not to accept cash as a way to reduce cash management costs. This would therefore no longer be the outcome of a mutual agreement. The difficulty then becomes how to define what is, or not, a contractual agreement in the context of legal tender.

Contractual freedom therefore should come, at best, as an exceptional derogation to legal tender. It would imply a clear consensus by both parties to a transaction to agree on a different means of payment than cash. *Fait accompli* such as “cash not accepted here” is not a mutual agreement, particularly in specialised shops for which there is no competitor at reasonable arm’s length.

Ultimately, the fundamental question is, however, if anyone is entitled to accept or refuse cash as a payment as they see fit, does this mean that cash is still legal tender? Legal tender should entail the *legal certainty* that cash will be accepted, except in very specific – good faith – circumstances.

³ Arguably, the severe restrictions of cash usage due to COVID are not a contractual agreement, as consumers are led to fear for their health, if not life, if they use cash for their payments. See for example the MasterCard position paper “COVID19 – Contactless and SCA transactions”, 15 April 2020, stating that “cash is extremely dangerous”.

Legal tender of non-cash forms of currency

The Opinion states that it cannot be excluded that non-cash forms of currency may also be legal tender.

The Advocate General’s Opinion starts with the recognition that technological innovation has become so rapid and disruptive that it could [and, one could argue, already has] revolutionise[d] the financial sector. Indeed, as is pointed out, the EU has embraced the digital era, including for payments and money, and will continue to do so as the 2021 Work Programme of the Commission is showing.

The speculative argument of the Advocate General’s opinion

Under point 89, the Opinion states that if the EU legislation has not provided a precise definition of the concept of legal tender, “it remains free to do so at any time”. It further states, under point 96, that this does “not exclude the possibility of the Union to assign the status of legal tender to other forms of currency that are not necessary physical”.

ESTA would be wary of such a reasoning that suggests, in essence, that legislation that has not been adopted might have been and thus produces some kind of legal effect: this approach could severely undermine the nature of the rule of law. As the Opinion points out, the EU has “regulated other forms of money and therefore favoured other (electronic forms) of currency”. It argues that since the EU might not have excluded that legal tender applies to non-physical forms of currency, they might be legal tender too. This risks opening a very large Pandora Box, considering all the legislation the EU *might have adopted*, but has not. By definition, this is the case of any legislation that has not yet been proposed: the list is infinite.

Borrowing the same speculative reasoning as in the Advocate General’s Opinion: “if it had wanted non-physical forms of currency to be legal tender, it would have done so”. Since it did not, one could argue, as the AG does in the context of cash, that “this is not an accident, considering the sensitivity of the issue”.⁴

The line of reasoning might become trickier at a time of crypto-currencies. The Commission is currently proposing regulating on stable coins (the MiCA Regulation) and one could argue that by regulating to protect consumers and investors, it is also *supporting* this form of money. Should that imply that crypto-currencies and stable coins regulated by the EU might have legal tender, if the EU has not explicitly ruled it out ?

We fully agree with the Opinion that secondary law might help interpreting primary law, even in the form of recitals. However, it would probably be far-fetched to argue that secondary law *which has not yet been adopted* could also help in the interpretation of primary law, as seems to be the case in the Opinion.

⁴ Point 87.

Legal tender is, inter alia, about guarantee

The Opinion argues that all non-physical forms of currency also fulfil the three fundamental functions of cash: payment, storage of value and settlement of debt. ESTA would argue, however, that the Advocate General's opinion omits a few important points in its comparison of cash and non-cash relevant to legal tender. These omissions hide the fact that non-cash forms of currency would struggle to justify any legal tender status.

An area of financial regulation, not mentioned in the Opinion, is particularly relevant to illustrate this point: the rules on financial stability and deposits guaranty schemes which limit the guarantee to €100.000 per depositor for their aggregated accounts in each banking institution.⁵

This commonly called “*hair cut*” provision makes that cash and non-cash deposits are not equal. Take for example a depositor, Mr E, with one million euros on a bank account, and another person, Mrs C, with one million euros in cash in a vault. The authorities may decide that the conditions are met to implement the hair cut provision of the directive. Thus, the following day, Mr E is left with €100.000, i.e. a tenth of his initial deposit. Mrs C, in the contrary, still enjoys the comfortable cushion of her one million euros in cash in her vault.

Scriptural money has been wiped off up by 90% in this example. Cash has not. E-money could not fulfil its function of “storage of value”, whilst cash did.

Taking this into consideration, the Opinion shows a flaw in its reasoning. As the Opinion states, legal tender is, *inter alia*, about guarantee (point 96). The very fact that the guarantee of scriptural money may be only limited by EU law up to €100.000 is the very proof that it cannot be legal tender, if one million euro of e-money can become overnight just a tenth of its value.

Furthermore, the ability of any State's authority to prevent/restrict deposit holders, individually or collectively, to access or withdraw their money from their bank account (cf. Cyprus and Greece during the financial crisis), is also a fundamental obstacle for non-physical form of currency to claim legal tender: in such cases, the euros detained on an account would no longer be backed and guaranteed by the monetary authorities if they are blocked. In other words, it is not “Central Bank money”.

Also of relevance to the analysis, although overlooked in the Opinion, is that cash is the only form of money that makes it possible for anyone to withdraw deposits from a bank. Without cash, deposits can only be withdrawn from an account by spending it – which would then negate the function of storage of value – or by transferring it into another account, which again may not be the solution if the issue is that of mistrust in the banking sector.⁶ In relation to this, negative interest rates are also of relevance, if they are able to erode scriptural money deposits on an account, while not affecting cash reserves.

⁵ Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes

⁶ In a number of submissions to EU public consultation, ESTA has consistently argued that cash is critical to the stability of the banking system in so far as it gives reassurance to any depositor that they can withdraw their deposits from the bank at any time – although obviously not all at the same time.

In these three examples, cash fulfils a role, inherent to its status as legal tender, which no other forms of currency can. Cash in all these examples is guaranteed, whilst other forms of currency are not. The key issue is that cash is Central Bank money, backed by the monetary authorities. For the time being, only cash has this feature.

Incompatibility with the EU treaties of any legislation which would ban cash

Most importantly, the Advocate General's Opinion states that "it derives from §93-95 that legislation that could lead, in law or *in fact*, to the complete abolition of notes and coins, or which would render ineffective their legal tender must be regarded as incompatible to the Treaties" (Point 127 – we emphasise)

Indeed, cash is a volume driven industry and a critical mass of cash is necessary for the cash cycle to be sustainable. As Sweden has shown, the State had to adopt legislative measures to prevent cash from disappearing altogether, as the result of market forces operating in Sweden. The reasons are now well understood: they proceed through making cash less available to consumers and citizens, making deposits of cash more difficult for retail, through the drastic reduction of cash services in bank branches. And foremost, reducing the distribution of change money without which cash payments are impracticable. The consequence is that cash, despite being legal tender, is refused almost everywhere. Consumers have very little choice.

This shows that the mere principle of cash being "legal tender subject to contractual agreements" is not enough to ensure that cash remains. Without further rules, cash is at risk, even if no law is adopted to abolish it. Some (powerful) market operators will always take benefit from the "contractual freedom" to impose their payment instrument over cash to consumers and merchants. ESTA would argue that a limitation of legal tender based on "contractual agreement" is *in fine* a provision that leads to the phase out of cash as it allows market operators to reduce its place an role to a level where it will become unsustainable, a general trend that can be observed particularly in some countries such as Sweden, the UK or the Netherlands.

For this reason, and according to the Advocate General's Opinion, a "contractual agreement" restriction to legal tender should be considered as contrary to EU law as it bears the promise of a cashless society. Its application is jeopardising the very existence of banknotes over time. This has to be appreciated over a longer term period as the consequence would only become apparent in the mid- to long-term.

The first necessary step to prevent this from happening is to confirm that legal tender means that cash cannot be refused as a payment unless on good faith principles.

Cash is trust: the Advocate General's missing element

The Opinion provides all the ingredients of what is legal tender in its points 78, 79 and 81:

- money is a *creation of the State* or, in the case of the euro, of the Economic and Monetary Union (point 78)
- From a historical point of view, the nature of money has evolved over time. Nowadays, modern economies, including the Economic and Monetary Union, are based on 'fiat money'. This is *money that is declared legal tender and issued by a central bank* (point 79)
- Historically, the most important form of money has been the physical form of cash (banknotes and coins), the *ultimate expression of the monetary sovereignty* of the State (point 81)

By opposition, e-money is private money. It is created and destroyed by commercial organisations.

However, one word is crucially missing from the entire AG's Opinion: *trust*. Money is about trust.⁷ It cannot work without the trust of the population. The miracle of the Währungsreform of 1948 in Germany with the introduction of the Deutsche Mark is the best illustration.

In the three paragraphs recalled above, the Opinion points out to the key conditions of what legal tender is: it is a *creation of the State, declared and issued by the Central Bank*, and as such is *Central Bank money*, and the *expression of the monetary sovereignty of the State*. Therefore it is backed by the Central bank, and fully guaranteed by it. Trust is entirely based on this. No *private* money can match these features.

Cash is the only form of public money guaranteed by the sovereign power of the State. All other forms of money are *private money*, guaranteed at best by prudential rules.

For the time being, only the physical form of money, banknotes and coins, can be legal tender, as this is the only one that the general public fully trusts. It is so because a banknote is emitted by the Central Bank and backed by it as an IOU over its emitter. Unless it has these features, no other form of currency can be legal tender.

Legal tender and the right to be paid in cash

ESTA also noted that the Advocate General's Opinion only refers to legal tender from the point of view of the *right to pay in cash*. It omits entirely the other side, namely the *right to be*

⁷ Trust is only mentioned in footnote 38 when explaining the concept of fiat currency: "*Fiat money has no intrinsic value – the paper used for banknotes is in principle worthless – yet it is still accepted in exchange for goods and services because people trust the central banks to keep the value of money stable over time. If central banks were to fail in this endeavour, fiat money would lose its general acceptability as a medium of exchange and its attractiveness as a store of value.*"

paid in cash. In ESTA's view, whilst it can be admitted that someone accepts to be paid in a form of currency which has not necessarily a status of legal tender, the very nature of legal tender calls for anyone being entitled to receive a payment only in a form of money, which is legal tender and, as such, guaranteed by the Central Bank, within the limits possibly set by Member States in relation to public reasons. This aspect is absent from the Advocate general's opinion, but is a very important one when looking at legal tender.

Conclusions

It derives from ESTA's analysis that it is critical that the Advocate General broad interpretation is not upheld in the ruling to come. A subjective right to pay in cash means nothing more than a subjective definition of legal tender, if it is up to anyone to decide upon its enforceability.

For the reasons mentioned in this note, e-money cannot fulfil all the functions that are deemed to a form of currency with legal tender. E-money and scriptural forms of money therefore cannot be granted legal tender status.

Only public reasons, provided they are justified, proportionate and effective in relation to their purported objectives, can justify restriction to legal tender. Market forces are currently using the "contractual freedom" to eliminate cash altogether, in a slow, but seemingly irreversible process if nothing is done. This can only be appreciated in a long run.

"Contractual agreements" restrictions, which has no clear legal basis in EU law, leaving to anyone the decision to grant or deny legal tender to cash, should not be accepted: this is precisely the main threat to cash. A "contractual agreement" restriction to legal tender should be considered as contrary to EU law as it bears intrinsically the promise of a cashless society.