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THE POLICY AND REGULATORY LEEWAY AVAILABLE TO THE MEMBER STATES UNDER THE TFEU ON THE FREE MOVEMENT OF CAPITAL

A LEGAL MAPPING EXERCISE

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Executive summary

The liberalisation of payments and capital movements in the Single Market under Article 63 TFEU offers benefits to the Member States which would not be available to them when acting on their own. These benefits are provided under what, in principle, is a balanced and sustainable policy framework in which the liberalisation agenda – executed first at secondary, later at the level of primary law – is supplemented by parallel, potentially competing policy considerations. These range from controlling large, volatile capital movements to ensuring that states are able to exercise their tax powers over incomes made in the integrated European capital market. In order to maintain this balanced and sustainable policy framework, the Member States are allowed (and in some instances obliged) in EU legislation and under the derogations available in the Treaties to develop and introduce policies and specific legal and administrative frameworks at the national level giving effect to these parallel policy considerations.

Attaining the benefits of free capital movements comes with substantive and procedural restrictions for the Member States. These restrictions on national policy making and regulation follow not only from the EU provisions governing the liberalisation of capital movements, but also from the legal benchmarks which have emerged from the scrutiny by the Court of Justice of restrictions introduced by the Member States. These legal benchmarks are of particular relevance as they determine how the Member States may contribute through domestic policy action to establishing and maintaining the balanced and sustainable policy framework of the free movement of capital. As opposed to other fundamental freedoms, most restrictions applicable to Member State conduct were determined in a political process resulting in legislative instruments – as laid down in the original Treaty provisions, and judicial involvement in promoting the liberalisation agenda – at least in the earlier decades – was more confined.

The restrictions imposed on the Member States correspond with the rules and principles of the overall Treaty framework. In particular, the Member States need to observe the equal treatment principle, they are unable to rely on derogations based on economic considerations which are incompatible with the idea of the Single Market, and they must meet the substantive and procedural requirements following from the proportionality principle. The jurisprudence of the EU Court of Justice relating to these restrictions provides a number of more detailed legal benchmarks and signposts for Member State policy makers which, in essence, demand that Member State policies meet standards of good governance and regulation. The most fundamental legal benchmark is the equal treatment principle which is enforced in different forms more or less consistently in the jurisprudence.

The law under Article 63 TFEU provides two major avenues for the Member States to depart from their core liberalisation obligations. On the one hand, when the Member States aim to pursue objectives which are *per se* incompatible with the EU Treaties, for instance, they are in a situation when only discriminatory measures will be able to satisfy a domestic economic policy need, they need to follow a centralised procedural avenue where an authorisation to introduce those measures may be obtained. This is available only in special circumstances (e.g., emergency protective measures) and authorisations are subject to a political override. On the other, in areas listed in the Treaties and recognised in the case law, which are compatible with the idea of a balanced and sustainable European capital market, the Member States are able to introduce restrictive measures autonomously provided that they meet the legal benchmarks developed in the jurisprudence of the Court of Justice. The autonomy of the Member States in these domains is also supported by the fact that the EU may not have competences – original or acquired – in these domains and that some of these areas may fall within the core of Member State sovereignty (e.g., direct taxation and tax enforcement powers).

The policy and regulatory leeway available to the Member State under Article 63 TFEU is different in connection with domestic fiscal policy (taxation) and regulatory measures representing a restriction on the free movement of capital. While regulatory measures, such as those governing the control rights of national governments in private enterprises, are treated with the usual legal rigour of the free movement provisions of the Treaties, fiscal measures introduced by the Member States – based mainly on considerations related to the fiscal sovereignty of the Member States and to the lack of EU competences – may be given a more favourable assessment. Claims submitted by the Member States concerning national tax autonomy and tax sovereignty will be taken into account and judicial scrutiny may only focus on national fiscal measures meeting the most fundamental legal benchmarks (e.g., the equal treatment principle).

This, however, does not mean that the fiscal policy considerations of the Member States will be given the green light in the process of justifying restrictions on the free movement of capital. Because they tend to violate the fundamental equal treatment principle – mainly, by subjecting taxpayers to differentiated tax treatment, they promote interests which cannot be accommodated under the Single Market (e.g., the loss of tax revenue as a result of free movement), or because they have been addressed in parallel EU and other international instruments, establishing that the given fiscal policy objective may be pursued legitimately by the Member State concerned has particular relevance and may prove to be near impossible. This has led to a massive body of jurisprudence dealing with the legitimacy of the general interest ground raised by the Member States. Following the

general principle that derogations must be interpreted restrictively, the Court of Justice demands, in general, clear and precise, adequately (and specifically) targeted measures from the Member States so that the link between the restriction and the objective pursued can be established.

The weight of the Treaty restrictions on Member State policy and regulatory opportunities depends primarily on the intensity of the application of the necessity and proportionality test. In the case of Member State fiscal measures, elements of the test are often considered in the context of examining the legitimacy of the objective pursued by the national measure and the unjustifiability of the restriction is established without engaging in the scrutiny of proportionality. The legal requirements arising from proportionality are most confining when less restrictive alternative measures are demanded from the Member States. This could involve obliging the Member States to consider procedural solutions instead of imposing substantive restrictions, or reregulating the authorisation regimes or changing them into notification or declaration systems. The existence of parallel EU or other arrangements addressing a particular issue (e.g., administrative cooperation in taxation matters) could have a decisive influence on the proportionality of the national measure. Proportionality also imposes rather demanding requirements of good governance and administration on the Member States requiring that national measures are adequately targeted, meet the obligations arising from legal certainty, or provide for adequately regulated administrative discretion subject to effective judicial remedies. Although it is not excluded at all, deference to national discretion (to national courts) in assessing the compatibility of national measures in light of the circumstances of the given case with EU law is rarely granted.

Introduction

The aim of the legal mapping exercise is to identify and analyse the legal boundaries of the leeway available to the Member States under EU law to develop and regulate national policies. It is carried out under the working premise that the law governing EU policies provides a framework for Member State policy and regulatory action which may implement, supplement or correct European policies. EU law may also provide legal boundaries for autonomous Member State policies developed and executed in national competences. This legal mapping report offers an accessible and comprehensive overview of the principles, detailed rules and practices governing and delimiting Member State conduct in a selected EU policy area. It looks both at the benefits offered by the common policy to the Member States and the possibilities available under the common policy framework for Member State governments to pursue policies and adopt regulations on their own. The report reveals considerable substantive and procedural limitations on Member State action. Member State governments interested in exploiting the room for manoeuvring under the EU legal framework must meet high standards of good governance and administration.

Acknowledgement: this report benefited greatly from the contribution of Dániel Deák and Vija Pakalkaite.

1 The policy framework of the free movement of capital

Restrictions and prohibitions

In Article 63 TFEU, the Member States imposed on themselves mutual legally enforceable restrictions delimiting their policy and regulatory choices in various matters, such as taxation, company law, property ownership, or market regulation. Article 63 TFEU, which lays down more concrete restrictions than the original provisions of the EEC Treaty,[1] has – just like the former Article 56 EC – direct effect[2] and its implementation at the Member State level does not depend on the adoption of secondary EU legislation.[3] The Treaty prohibitions are applied together with the general EU principles of non-discrimination and proportionality.

1.1 The expected benefits of the free movement of capital

The benefits of free capital movements

This Treaty-level direct abolishment of Member State controls on payments and capital movement and other restrictive national measures was undertaken with the benefits offered by free capital movements in an open and integrated European market in mind. Following the categorisation offered by what is known as the Washington Consensus,[4] the Member States aim to secure in a common policy framework for liberalised capital movements, at a general level, that the European economy and national economies grow and, at the level of the individual, that individual investors

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[1] The direct effect of original Article 67 EEC was rejected in Case 203/80 Casati [1981] ECR 2595. See, however, Joined Cases 286/82 and 26/83 Luisi and Carbone [1984] ECR 377 on the direct effect on ex Article 106 EEC on current payments and Case 308/86 Lambert [1988] ECR 4364 delimiting direct effect to allowing payments in the creditor's currency. Means of payment are not considered as goods in the meaning of the Treaty, Case 7/78 Thompson ECLI:EU:C:1978:209. Current payments were held to fall within the scope of other fundamental freedoms representing a precondition for exercising those freedoms, Case 95/81 Commission v Italy [1982] ECR 2187. The judgment in Luisi and Carbone, however, maintained the distinction between capital movements ('financial operation' (or 'physical transfer of assets', para. 13, Case C-358/93 Bordessa ECLI:EU:C:1995:54)) and current payments (a 'consideration').

[2] Paras. 41-47, Joined Cases C-163, C-165 and C-250/94 Sanz de Lera [1995] ECR I-4821. The direct effect of Article 1(1) of the 1988 Capital Directive postulating a complete liberalisation of capital movements as envisaged by the Treaties, and also of Article 4 of the 1988 Directive on Member State derogations when read in conjunction with its Article 1 were recognised in para. 33, Case C-358/93 Bordessa ECLI:EU:C:1995:54.

[3] Liberalisation – as intended by the Treaties – was achieved through secondary legislation (e.g., the First and Second Captial Directives and the 1988 Capital Directive), and the EEC Treaty provisions were denied direct effect, which led to a more than 20 year delay in achieving freedom of movement, which was eventually closed by the adoption of the general free movement principle in the 1988 Capital Directive, J. Usher, 'Monetary movements and the internal market', in N.N. Shuibhne (ed.), *Regulating the Internal Market* (Elgar, 2006), 181-209, at 181 and 186.

[4] For the 10 points gathered by Williamson, see J. Williamson, *Latin American Adjustment: How Much Has Happened?* (IEE, 1990), Chapter 2.

realise returns on their investments.[5] The Member States also associate the optimal allocation of financial resources in a larger market space and access to funds in foreign locations with the freedom of capital movements.[6]

The Spaak Report

The Spaak Report first identified the expected benefits of the free movement of capital for the Member States.[7] It spoke about free capital movements enlarging the sources for financing investments and enabling the exploitation of an enlarged economies of scale in resource allocation. It also mentioned that free capital flows will enable addressing payment imbalances and optimising production costs in terms of interest rates and the costs of financing. In the context of European market integration, the report emphasised that the free movement of capital is necessary for the operation of the other economic freedoms and also for enhancing cross-border corporate activities including corporate investment. As a condition for the success of the free movement of capital in the internal market, it mentioned that because of the linkage of capital movements with Member State fiscal, financial, monetary and social policies sufficient convergence must be achieved in these areas.

The Commission's policy

The benefits of the free movement of capital and payments have been made explicit by the EU policy-maker. According to the Commission, it will bring 'an optimal allocation of resources and the integration of open, competitive and efficient European financial markets and services' for the benefit of all, and it helps maintain '"responsible" macro-economic policy and can foster growth through finance and knowledge transfers'.[8] It also claimed that liberalisation is in the direct interests of individuals, economic operators and national governments, which are thus enabled to make payments and investment transactions under the best circumstances, own other companies or take part in their management, raise money where it is the cheapest, and borrow money under lower rates to finance investment and spending.[9]

The 1985 Commission White Paper[10] recognised that the integration of financial markets through guaranteeing the free movement of capital holds a

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[5] Economists have questioned the correlation between economic growth – the main promise of free capital movment – and abolishing capital controls, see, *inter alia*, D. Rodrik, 'Trading in illusions', 123 *Foreign Policy* (2001) 54-62.

[6] It is also a necessary legal prerequisite for the second stage of the European Monetary Union.

[7] Report of the Heads of Delegations to the Foreign Ministers at the Messina Conference, 21 April 1956

[8] http://ec.europa.eu/finance/capital/index_en.htm; http://ec.europa.eu/finance/capital/overview_en.htm#what; Commission Staff Working Document Capital Movement and Investments in the EU, SWD(2012) 6 final, 2, 'brings about cricual advantages to our economies and societies at large'; and Commission Staff Working on the free movement of capital in the EU, SWD(2013) 146 final, 1.

[9] http://ec.europa.eu/finance/capital/overview_en.htm#what; Staff Working Document (2012), 4.

[10] Commission White Paper on completing the internal market, COM (1985) 310 final.

great potential for boosting 'the economic development of the Community by prompting the optimum allocation of European savings.' Other than this, it saw that the success of market integration in goods and services and the success of the free movement of persons necessitates abolishing restrictions on the 'corresponding capital movements' and building an effective financial dimension for the internal market.[11] It also accepted that the free movement of capital – in parallel, with the strengthening of the European monetary system – can secure maintaining monetary, especially price and exchange rate, stability in the internal market. The 2010 Monti Report repeated the well-rehearsed rationale that the free movement of capital is critical for the efficient allocation of resources – which is a key driver of growth and employment – and for the stability of the European economy.[12]

With regards to capital movements involving third countries, the Commission's position is equally optimistic. Inward foreign direct investment was seen as fostering economic growth in the EU 'due to the expansion of productive capacity, job creation, human capital enhancement innovation and technology diffusion and enterprise development,' all which 'contribute to the increase in income and wealth'.[13] It was also suggested to reinforce the 'social economy in a competitive market, by spreading responsible business conduct rules among companies and by channelling resources towards "impact investment" and social entrepreneurship.'[14] The benefits of outward foreign direct investment were identified as improving access for European firms to foreign markets, enabling them to fully exploit the opportunities offered by those markets, helping them to acquire resources or other assets, such as technology, having a positive impact on firm profitability, and as generating 'positive spill-overs from technology sourcing investments.'[15]

1.2 A balanced and sustainable policy framework

Avoiding negative consequences

Under Article 63 TFEU, a balanced and sustainable policy framework was created for the integrated European capital market. The central liberalisation agenda is counterbalanced – by means of introducing legal safety valves – with parallel objectives so as to prevent financial crises or to avoid the externalities associated with liberalised capital movements. The Member States also took particular care that their taxation powers are not severed

[11] See also Preamble of Directive 60/921/EEC (First Council Directive for the implementation of Article 67 of the Treaty), OJ L43 (1960), 921-932 and Preamble of Directive 63/21/EEC (Second Council Directive of 18 December 1962 adding to and amending the First Directive for the implementation of Article 67 of the Treaty), OJ L9 (1963), 62-74.
[12] *A new strategy for the single market*, (European Commission, 2010), 62.
[13] Staff Working Document (2013), 1.
[14] Ibid.
[15] Ibid.

unduly by their EU obligations. In its current form, the legal framework – at Treaty level and in secondary legislation – recognises policy, regulatory and certain economic[16] (e.g., macropurdential) considerations which balanced against the fundamental obligations laid down in Article 63 TFEU can be pursued by the Member States within the policy framework of the Treaties. Predominantly, Member State action restricting or interfering with cross-border capital movements and payments is allowed for the purpose of establishing and maintaining a balanced and sustainable integrated capital market in the EU where considerations and interests relevant for that market are given sufficient recognition even through Member State action. Member State measures may also be introduced to prevent individuals relying on the free movement of capital for illicit purposes (e.g., tax avoidance) jeopardising the policy balance established under Article 63 TFEU.

The role of national policy-making

The free movement of capital allows the Member States to realise policy opportunities both by complying with the restrictions imposed on them and by maintaining national policies and regulations within the legal framework allowed under the Treaties and in secondary legislation. Beyond the earlier mentioned promised benefits, the collective undertaking of mutual obligations under Article 63 TFEU by the Member States enables them to avoid the negative consequences of policy unilateralism including unilateral retaliatory action taken by other Member States and of what is called by the OECD as 'beggar-thy-neighbour' approaches[17] to controlling and restricting capital movements. In parallel, the Member States are entitled to shape the integrated European market through national policies and measures so that liberalised capital movements can be reconciled with their interests, such as the balanced allocation of taxation powers among the Member States, effective cross-border tax enforcement, the protection of public service markets, or the effective delivery of national social, cultural and other policies.

1.3 Legal and policy recognition of a balanced and sustainable policy framework

Gradual and balanced progress

Member State expectations that a balanced and sustainable integrated market for payments and capital movements will be created, where liberalisation is not absolute and the necessary controls may be introduced and where the Member States are able to maintain largely autonomous tax policies, are reflected in the relevant legal provisions and policy documents. This understanding of the free movement of capital is also reflected in the

[16] See also Article 3(2) of the First Capital Directive on the Member States introducing restrictions for the purpose of protecting national economic policy objectives.
[17] *Fifty Years of Promoting Orderly Capital Flows: OECD Code of LIberalisation of Capital Movements Brochure*, (OECD, 2015).

Member States being prepared to progress with this policy gradually over a longer time period and in their insistence that the legal arrangements must be accompanied by certain forms and mechanisms of legal and political flexibility capable of counterbalancing the central liberalisation agenda.

Parallel considerations

The constitutional frame provided by Articles 63 to 66 TFEU clearly reflects the idea of a balanced and sustainable integrated European capital market where its benefits are balanced against its risks and where the central rationale of free movement is accompanied by parallel regulatory, policy and economic considerations. The liberalisation obligations of Article 63 are supplemented by Article 65, the content of which is presented in the table below.

Article 65 TFEU allows the Member States to

- introduce differentiated tax treatment of taxpayers that are not in an objectively comparable situation;
- take all requisite measures to prevent infringements of national law and regulations, in particular in the field of taxation and the prudential supervision of 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 policy or public security.

Safeguard and protective measures

Further instruments pursuing this aim include Article 66 TFEU which enables the Council to introduce safeguard measures against movements of capital to or from third countries which cause, or threaten to cause, serious difficulties for the operation of the economic and monetary union, and EU secondary legislation examined in detail below which empowered the Member States to take protective measures for the protection of national economies. Even the First Capital Directive – now repealed – pursuing a robust liberalisation agenda accepted that its provisions do not restrict the Member States in verifying the nature and genuineness of transactions of transfers or to take all requisite measures to prevent infringements of their laws and regulations (Article 5(1))[18] and that the Member States – having consulted the Commission – may maintain or reintroduce foreign exchange restrictions on capital movements[19] in the case when capital movements

[18] In Case 157/85 Brugnoni ECLI:EU:C:1986:258, the Court of Justice held that 'such measures may include controls to verify compliance with the conditions which purchasers of foreign securities must observe pursuant to the protective measures authorised by the Commission under Article 108 of the Treaty' and that 'in particular, such controls may be designed to ensure that the purchaser comlies with the obligation to hold the securities for at least a year', para. 23. It also ruled that it is for the national court to determine whether the supervisory measures at issue are 'requisite' in the meaning of Article 5, para. 24.

[19] Which were operative on the date of the entry intro force of the First Directive.

'might form an obstacle to the achievement of the economic policy objectives of a Member State' (Article 3(2) and (3)).[20]

The cautious engagement of the Member States with free capital movements is also expressed in ex Article 73 EEC. This provision is no longer part of the Treaty regulation of the free movement of capital as the similarly worded Article 66 TFEU applies only in connection with third countries and not within the Single Market for capital. Phrased as Article 3 of the 1988 Capital Directive, ex Article 77 EEC enabled the introduction of protective measures upon the authorisation of the Commission in the case the functioning of Member State capital markets are disturbed by the free movement of capital. The Commission authorisation was subject to a political override by the Council which in a decision taken with qualified majority could revoke or amend the Commission's decision. The Member States were also entitled to take protective measures themselves, in case considerations of secrecy or urgency required autonomous Member State action, provided that their introduction was necessary. In such an event, the Member State had to inform the Commission, which could oblige the Member State concerned to modify or withdraw the measure.

Articles 143 and 144 TFEU

Similar opportunities were regulated in ex Article 108 EEC concerning the balance of payments which, however, must be distinguished both substantively and procedurally from the possibilities available under ex Article 77 EEC.[21] The original provisions applied to all Member States. Its current equivalent, Article 143 TFEU, applies only with regards to Member States 'with a derogation', which are Member States 'in respect of which the Council has not decided that they fulfil the necessary conditions for the adoption of the euro'.[22] The ability to introduce protective measures in case the Member State concerned 'is in difficulties or is seriously threatened with difficulties as regards its balance of payments' and 'where such difficulties are liable in particular to jeopardise the functioning of the internal market or the implementation of the common commercial policy' is subject to strict procedural and substantive conditions. Most importantly, they may only be introduced when, first, the action taken by the Member State concerned and the measures suggested by the Commission do not prove sufficient to overcome the difficulties and, second, when the mutual assistance instruments granted by the Council in place of the previously mentioned unsuccessful measures are insufficient or the mutual assistance is not

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[20] The Commission may recommend that the Member State abolish the maintained or reintroduced restrictions. The Commission is also empowered to investigate the economic policy difficulties faced by the Member State and recommend the adoption of measures in this regard to the Member States.

[21] Paras. 26-28, Case 157/85 Brugnoni holding that the different measures must be adopted under the respective procedural avenues and the procedures cannot be regarded as applicable cumulatively.

[22] Article 139 TFEU.

granted by the Council. The conditions and details of the protective measures are determined by the Commission and the Commission's authorisation is subject to the political override of the Council. Under Article 144 TFEU, Member States with a derogation, in case of a sudden crisis in the balance of payments and when mutual assistance instruments are not granted immediately, may take protective measures. These measures must be necessary and must be introduced as a form of precaution. They must also meet the requirement of proportionality in that they 'must cause the least possible disturbance in the functioning of the internal market and must not be wider in scope than is strictly necessary to remedy the sudden difficulties which have arisen.' The Commission and the other Member States must be informed of the introduction of such protective measures and the Council has the power to override the Member State decision by requiring it to amend, suspend or abolish the measures in question.

Anti-terrorism measures

A further area of balancing between liberalised capital movements and payments and competing considerations in the general interest is found under Title V of the TFEU on the Area of Freedom, Security and Justice. Article 75 TFEU provides that in order to achieve the Union's objectives in preventing and combatting terrorism and related activities a 'framework for administrative measures with regard to capital movements and payments' must be adopted. The administrative measures include the freezing of funds, financial assets, or economic gains belonging to, or owned or held by, natural or legal persons, groups or non-State entities. The implementation of the framework takes place in the adoption of measures by the Council.

Recognising risks and benefits

Beyond urging convergence in Member State policies linked to the free movement of capital, the Spaak Report made explicit in connection with the question of capital controls introduced by the Member States the necessity of a balanced policy framework capable of recognising both the benefits and risks of liberalised capital movements. The Report urged the understanding and addressing of the issues and dilemmas which may lead to restrictive and often prejudiced national responses to capital movements. It argued that capital controls should be allowed when they 'serve the utmost economic interest and they do not provoke enhanced imbalances.' It recognised that volatile capital movements capable of causing severe geographical imbalances represent a risk for monetary stability and claimed that broader common policy action is needed to ensure coherence between the parallel policy areas.[23] In order to establish a balanced and sustainable European capital market, it suggested coordinating and levelling national control mechanisms. In particular, it proposed that discrepancies in national

[23] The report saw the solution at European level in developing further the 'Common Market' with rules and mechanisms avalable to address these problems.

treatment – although not without regard to the economic circumstances – should be eliminated, divergences among national regulatory regimes – especially in the field of taxation – should be corrected by harmonisation, and that territorial inequalities following from capital investment favouring regions where the basic conditions of profitability are provided for should be addressed.

Graduality and flexibility

Because of the equal relevance of risks as well as benefits in liberalising capital movements, and because of the complexity of the parallel (economic, fiscal, monetary etc.) policy issues which need to be addressed so as to enable the effective operation of an integrated capital market in Europe, the Spaak Report introduced the ideas of graduality and flexibility which came to characterise the development of law and governance in this segment of market integration. The Report argued that the enforcement of rigid rules and automated procedures would be a mistaken approach and that there is no need for setting a fixed roadmap for realising the free movement of capital in the internal market. It maintained that a strict governance approach would require the development of multiple safety clauses and the strict enforcement of rules 'could paralyse the desired capital movements and encourage those that are not wanted.' It, therefore, argued for a flexible procedure for capital movement liberalisation in which only the fundamental conditions and general directions would be fixed.

Large and volatile capital movements

From the 1970s onwards, the secondary legislation adopted under the free movement of capital expressed the concerns of the Member States for the negative consequences of capital movements liberalisation. In particular, large and volatile capital movements were seen as capable of damaging national economies and of hindering the related common policies (e.g., the Economic and Monetary Union).[24] Although their impact depends on the size, structure and preparedness of national financial markets and economies, they can damage local economic development and growth, for instance, by affecting currency stability, generating crippling public and private debt when borrowing is in a foreign currency and the local currency depreciates, contributing to inflation, and by leading to unsustainable economic bubbles. The 1972 Capital Directive clearly indicated that in a liberalised European capital market the Member States should be afforded sufficient and immediately available instruments – supplementing those available for regulating domestic liquidity – to discourage exceptionally large capital movements and to neutralise their effects on the domestic monetary situation.[25] Its preamble claimed that exceptionally large capital movements

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[24] See also Council Resolution of 9 May 1971 on the monetary union, OJ C58 (1971), 1; Staff Working Document (2013), 2; Commission Staff Working on the free movement of capital in the EU, SWD(2014) 115 final, 1.

[25] Council Directive 72/156/EEC on regulating international capital flows and neutralizing their undesirable effects on domestic liquidity, OJ L91 (1972), 13-14.

can cause serious disturbances in the monetary situation and in economic trends in the Member States. It emphasised that ensuring 'smooth trading conditions' within the EU, the achievement of the Economic and Monetary Union and the 'smooth operation' of exchange markets in the Member States required 'concerted action' from the Member States.

The 1988 Capital Directive was particularly detailed in enumerating the potential sources of risks of liberalised capital flows.[26] Its preamble mentioned bank liquidity problems, short-term capital movements which may 'seriously disrupt' the conduct of national monetary and exchange-rate policies, difficult balance-of-payment situations, high levels of external indebtedness, difficulties in the market for secondary residencies in some Member States, tax distortion, tax evasion and tax avoidance, serious disturbances in the monetary or financial situation of the Member States, serious stresses in exchange markets, the undermining of the European Economic and Monetary Union, and the jeopardising of the 'smooth operation of the internal market'. In Article 3, it recognised explicitly that short-term capital movements of exceptional magnitude impose severe strains on foreign-exchange markets and lead to serious disturbances in the conduct of national monetary and exchange rate policies, which will inevitably be reflected, in particular, in substantial variations in domestic liquidity. It, therefore, empowers the Member States to take protective measures – following the authorisation of the Commission or, in the case of urgency, without the prior authorisation by the Commission.

Risks recognised by the OECD

The necessity of approaching free capital movements with a balanced approach taking into account their benefits and risks has also been acknowledged in the policy documents of other international organisations and forums. The OECD, which provided a parallel framework for the Member States to create legally binding commitments as to the liberalisation of capital movements,[27] acknowledged long-term economic growth (and employment and development)[28] as the main benefit of the free movement of capital, which is achieved through an efficient allocation of savings and investment and through providing access to a greater pool of capital.[29] It also suggested that capital movements encourage 'competition and economic efficiency to the benefit of consumers' and provide 'financial

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[26] Council Directive 88/361/EEC for the implementation of Article 67 of the Treaty, OJ L178 (1988), 5-18.

[27] *OECD Code of Liberalisation of Capital Movements*, (OECD, 2013).

[28] On the potential areas of growth through foreign direct investment, see *OECD Foreign Direct Investment for Development* (OECD, 2002).

[29] *OECD International Capital Flows: Structural reforms and experience with the OECD Code of LIberalisation of Capital Movements*, (OECD, 2011), 1-2; *Forty Years' Experience with the OCED Code of Liberalisation of Capital Movements*, (OECD, 2002).

resources and technological innovation to companies'.[30] As risks associated with liberalised capital markets, it identified the vulnerability and reduced absorptive capacity of states and their economies to external shocks, exchange-rate appreciation, economic overheating, financial and asset-price cycles, and sudden stops or abrupt reversals in capital flow.[31] To indicate the complexity of the issues, the OECD maintained that the benefits and risk of liberalised capital movement are dependent upon the circumstances of individual countries (the 'state of development of its economy, infrastructure and financial markets') and emphasised that liberalisation must take into account competing needs, concerns and possibilities.[32]

Risks recognised by the G20

The 2011 Cannes G20 Coherent Conclusions[33] made it clear that the benefits of 'financial globalisation' must be secured in a manner which ensures that the risks of capital movements capable of undermining financial stability and sustainable growth at the national level are prevented and adequately managed. These risks mainly follow from volatile and large inward and outward capital flows. From this perspective, the assessment of capital flow management measures introduced by individual states needs to take particular care when distinguishing between unacceptable restrictions and legitimate macroprudential policies. In this regard, the Conclusions highlighted that it is especially problematic that these measures can be adopted in a package together with other measures (e.g. monetary policy, exchange rate, foreign reserve management or prudential measures) for the protection of national economies from shocks. Their legal assessment is further complicated by the fact that certain capital flows management measures are residency-based (the so-called capital controls measures) and others do not discriminate on the basis of residency. In the latter group, the measures concerned could differentiate capital transactions on the basis of the currency use, or manage capital movements in other ways (e.g. by taxing certain investments).

Similar to the OECD position, the Coherent Conclusions also emphasised that the assessment of capital flow management measures must take into account country-specific circumstances, for instance 'the size, depth, and level of development of the local financial sector, as well as the institutional and regulatory strength of a country'. Despite the relevance of local specificities, the Coherent Conclusions laid down some generally applicable benchmarks for the regulation of capital flow management measures. These

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[30] *OECD Codes of Liberalisation User's Guide*, (OECD, 2008).

[31] *OECD International Capital Flows*, (2011), p. 1-2; *Forty Years' Experience*, (2002). On other costs associated with direct foreign investment, see *OECD Foreign Direct Investment for Development*, (2002).

[32] *OECD Codes of Liberalisation User's Guide*, (2008).

[33] *G20 Coherent Conclusions for the Management of Capital Flows*, (G20 Cannes, 2011).

are transparency, their adequate communication to the public, their adequate targeting to respond to the specific risks identified, the regular review of measures, the possibility of their adaptation or reversal, and sufficient flexibility in their implementation to respond to the changing circumstances.

Risks recognised by the IMF

The 2012 IMF Institutional View[34] on capital movements considered the benefits and risks of liberalised capital movements in a similarly balanced manner. While the Institutional View recognised the substantial benefits of the free movement of capital, such as 'enhancing efficiency, promoting financial sector competitiveness, and facilitating greater productive investment and consumption smoothing', it also placed emphasis on its considerable risks – 'which can be magnified by gaps in countries' financial and institutional infrastructure' – such as those following from large-scale and rapid capital inflows and disruptive capital outflows. It maintained that the balance between the benefits and risks is not constant, and it can be managed – through 'well planned, timed and sequenced' measures – to ensure that capital flows produce the desired significant positive effects. The Institutional View also spoke about 'trade-offs between policy options for dealing with capital flows, harnessing the benefits of capital mobility, and addressing the implications of capital flow management for global economic and financial stability.'

Substantive and procedural constraints on addressing risks

For Member State governments, it may be problematic that despite the recognised risks of liberalised capital markets, the addressing of which may require swift government responses, and despite the necessity of assessing the impact of the free movement of capital on national economies in light of their particular characteristics, substantively and procedurally they are limited in their action by the common policy framework. According to settled case law, the Member States are prevented from relying on economic grounds when derogating from their obligations under Article 63 TFEU.[35] As will be shown below, the grounds for justifying national taxation arrangements interfering with the free movement of capital are so narrowly interpreted that it makes it nearly impossible for the Member States to derogate from their obligations. . Also, while in general the Member States are allowed to introduce measures pursuing legitimate objectives which compete with the liberalisation agenda of Article 63 TFEU on their own motion (mainly, under Article 65 TFEU), in the most controversial instances, when economic issues or questions of economic policy which seem to contradict the general policy framework are raised, they are tied to a centralised procedure allowing considerable discretion to the European level to assess the necessity of the national measure (Article 3 of the 1988

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[34] *IMF The Liberalization and Management of Capital Flows: an institutional view*, (IMF, 2012).

[35] Infra n.

Directive). Overall, the substantive and procedural limitations of the common policy put Member State policies and regulations aiming to counter the risks of free capital flows or intending to establish a balance within the common policy which reflects local fiscal and economic needs in a rather tight straightjacket.

1.4 EU measures to maintain a balanced and sustainable policy framework

Horizontal cooperation

With the achievement of liberalisation entrusted upon EU secondary legislation, establishing and maintaining a balanced and sustainable policy framework for free capital flows in the Single Market was not left solely to the competence of the Member States.[36] As discussed below, EU legislation enabled the Member States to equip themselves with instruments to address large and volatile capital movements and to introduce emergency measures in case capital movements represented a genuine risk to the national economy.[37] The freedom of payments and the free movement of capital may also affect the effective administration of national tax systems. For instance, they enable, in principle, tax avoidance by taxpayers by transferring incomes to low taxation Member States. In order to assist the Member States, the EU adopted a number of measures facilitating cross-border, horizontal administrative cooperation between the Member States. The availability of these EU measures, as discussed below, has an impact on the ability of the Member States to rely on certain derogations relating to the use of taxation powers by pre-empting the application of certain unilateral legislative and administrative restrictions on cross-border capital movements and payments.[38]

The Mutual Assistance Directive

The Mutual Assistance Directive (Directive 2011/16/EU, formerly Directive 77/799/EEC)[39] lays down obligations of administrative cooperation among the Member States 'with a view to exchanging information that is foreseeably relevant to the administration and enforcement' of national tax laws and it regulates 'rules and procedures under which the Member States are to cooperate on matters concerning coordination and evaluation' (Article 1). The directive includes provisions concerning the organisation and

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[36] See the 1988 Opinion of the Economic and Social Committee urging the adoption of further harmonisation measures in the related areas (e.g., financial services, stock markets, solvency, stability, or taxation) and the stabilization of exchange rates, OJ C175 (1988), 1.
[37] Infra n.
[38] Infra n.
[39] Council Directive 2011/16/EU on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC, OJ L64 (2011), 1-12; Council Directive 77/799/EEC concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation, OJ L336 (1977), 15-20. See also the mutual assistance provisions of Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision, OJ L235 (2003), 10-21.

operation of competent authorities in the Member States (Article 5) and it distinguishes between exchanges of information on request, mandatory automatic and spontaneous exchanges of information (Articles 5-10). As to further forms of administrative cooperation, the directive allows the officials of the requesting competent authority to be present in the administrative offices and to participate in the administrative enquiries of the requested authority (Article 11), multiple Member States to organise 'simultaneous controls' (Article 12), the competent authorities to request the competent authority of another Member States to notify the address of any instruments and decisions which emanate from the administrative authorities of the requesting Member State (Article 13), the competent authority providing information under Articles 5-9 to request feedback from the competent authority which receives the information (Article 14), and the competent authorities to share best practices and experience (Article 15). In Chapter IV, the directive regulates the conditions governing administrative cooperation among the Member States (e.g., official secrecy, the use of the information in other procedures and for other purposes, the limits of the obligation to exchange information, the obligations as to comply with a request for information, wider cooperation with third States, standard forms and computerised formats, 'practical arrangements', and the specific obligations of the Member States).

The mutual assistance obligations of the Member States are also regulated in connection with the recovery of claims which arise in another Member State relating to 'all taxes and duties of any kind levied by or on behalf of the Member State' or 'on behalf of the Union'.[40] The directive includes provisions concerning the organisation and operation of competent authorities in the Member States (Article 4) and it distinguishes between exchanges of information on request and without prior request (Articles 5-6). It allows the officials of the requesting competent authority to be present in the administrative offices and to participate in the administrative enquiries of the requested authority (Article 7). The directive also regulates mutual assistance in the notification of all relevant documents emanating from the requesting Member State (Articles 8-9) and the mutual assistance in the application of recovery and precautionary measures (Articles 10-20). In Chapter V, the directive regulates the general rules applicable to all types of assistance requests (e.g., standard forms and means of communication,

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[40] Directive 2010/24/EU concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures, OJ L84 (2010), 1-12. The obligations also relate to the recovery of refunds, interventions and other measures forming part of the system of total or partial financing of the European Agricultural Guarantee Fund (EAGF) and the European Agricultural Fund for Rural Development (EAFRD), including sums to be collected in connection with these actions, and levies and other duties provided for under the common organisation of the market for the sugar sector.

use of languages, official secrecy and disclosure of information and documents).

The UCITS Directive

The UCITS Directive[41] regulating the establishment of 'undertakings for the collective investment in transferable securities' (investment funds) contains mutual consultation obligations among Member State 'competent authorities' in the authorisation process (Article 8 and Article 20), an obligation of communicating information between the home Member State's 'competent authority' and the host Member State's 'competent authority' (Articles 17-18), an obligation of clarifying the communicated information and of providing information on the documents transmitted between the home Member State's 'competent authority' and the host Member State's 'competent authority' (Article 20), and an obligation of the host Member State's 'competent authority' to inform the home Member State's 'competent authority' of instances of non-compliance, of the necessity of imposing penalties and of withdrawal of authorisation (Article 21). Chapter XII governs the detailed obligations of Member State 'competent authorities' acting on their own or in cooperation with the 'competent authorities' of other Member States.

Directive 2003/48/EC

Directive 2003/48/EC[42] enables the Member States to subject foreign-sourced 'savings income in the form interest payments' to effective taxation (Article 1). This is achieved by imposing the obligation on the so-called 'paying agents' to report certain information concerning 'beneficial owners' to the 'competent authority' of their Member State of establishment (Article 8) and by obliging the 'competent authority' of the Member State of the paying agent to communicate automatically in certain periods this information to the 'competent authority' of the Member States of residence of the 'beneficial owner' (Article 9). From 1 January 2016, the obligation of 'paying agents', which is also modified together with the obligation of 'competent authorities', will be extended to 'other economic operators'[43] established or having their place of effective management in the Member State concerned (Article1).[44]

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[41] Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), OJ L302 (2009), p. 32-96 (formerly, Directive 85/611/EEC, OJ L365 (1985), p. 38-53).

[42] Directive 2003/48/EC on taxation of savings income in the form of interest payments, OJ L157 (2003), p. 38-48.

[43] Economic operator means a credit or financial institution, any other legal person, or natural person, which on a regular basis or occasionally makes or secures an interest payment within the meaning of Directive 2014/48/EU while acting in the exercise of its professional activity.

[44] Directive 2014/48/EU amending Directive 2003/48/EC on taxation of savings income in the form of interest payments, OJ L111 (2014), p. 50-78.

2 The limits of EU intervention in the capital market

Competences and scope

Member State governments must be aware that the obligations imposed on them under Article 63 TFEU have limitations. On the one hand, the Treaty obligations have no or limited application in areas outside of the competences of the European Union. On the other, the scope of the free movement of capital is confined by the availability of EU obligations in parallel policy areas. While this does not present the Member States with the same opportunities as the first limitation as their conduct falls under the scope of another Treaty prohibition, the fact remains that their policies and measures face a single and not multiple legal hurdles.

2.1 Competence matters

Fiscal autonomy

The European Union has not been endowed with powers of direct taxation. As a consequence, its interferences under the Treaty provisions with the substance of Member State tax regimes is influenced by the fact that these competences have remained with the Member States.[45] According to the EU Court of Justice, in absence of EU competences and EU unification or harmonisation measures on this matter, the Member States are free to exercise their powers of taxation.[46] This also follows from the model of transnational regulation selected by the Member States for the Union which favours the competition of national taxation regimes.[47] In other words, the Member States continue to enjoy autonomy in fiscal matters, which is also expressed in the grounds available to justify Member State interferences with the free movement of capital, such as the aim of effective fiscal supervision or the effective collection of taxes.[48]

No obligation of tax convergence

On this basis, despite the negative consequences of Member State diversity in tax regulation, under the free movement of capital the Member States are not obliged to adapt their own tax systems to the different systems of tax of the other Member States (adjust their tax rules on the basis of those of

[45] See infra n concerning the allocation of taxation powers among the Member States and regulating tax advantages on the basis of the principle of reciprocity as laid down in bilateral tax conventions between Member States.
[46] Para. 37, Joined Cases C-578/10 to C-580/10 van Putten ECLI:EU:C:2012:246; para. 31, Case C-157/10 Banco Bilbao ECLI:EU:C:2010:813; para. 18, Case C-489/13 Verest ECLI:EU:C2014:2210; para. 41, Case C-303/12 Imfeld ECLI:EU:C2013:822.
[47] VKI. See also infra n the jurisprudence allowing the preferential tax treatment of certain cross-border revenue streams in bilateral tax conventions.
[48] It could relate to practical matters, such as the Member States determining the evidence that must be provided by taxpayers and the formal and the material conditions which must be respected so as to enable the tax authorities to establish correctly the tax owed, para. 47, Case C-326/12 van Caster ECLI:EU:C:2014:2269. See, by analogy, para. 27, Case C-252/09 Meilicke EU:C:2011:438.

another Member State).[49] In other words, the Member States are not obliged to ensure taxation 'which removes any disparities arising from national tax rules'.[50]

No obligation to consider foreign tax rules

From another perspective, this means that disadvantages suffered from the parallel exercise of tax competences by different Member States – provided that the national measures in question are not discriminatory – are not incompatible with the Treaties and the Member States are able to regulate their tax laws without paying regard to the tax legislation of other Member States.[51] The Member States – when acting according to the equal treatment principle – are not required to enable tax payers to benefit from a tax advantage granted by another Member State in the exercise of its powers in tax matters.[52] Basically, the Member States do not have to assume responsibility (to take over the responsibility of the taxpayer) for decisions made by taxpayers to make investments abroad which – according to the circumstances – 'may be to the taxpayer's advantage or not'.[53]

The specific rules on Member State fiscal autonomy are presented in the table below.

Specifically, in the field of direct taxation, which falls within the competence of the Member States,[54]

- 'it is for each Member State to organise, in compliance with EU law, its system for taxing distributed profits and, in that context, to define the tax base and the tax rate'.[55]

Specifically, in the field of avoiding double taxation[56]

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[49] Para. 39, Case C-157/10 Banco Bilbao.
[50] Para. 80, Case C-322/11 K ECLI:EU:C:2013:76.
[51] Supra n and para. 38, Case C-157/10 Banco Bilbao. See, to that effect, paras. 19, 20 and 24, Case C-513/04 Kerckhaert [2006] ECR I-10967; paras 41, 42 and 47, Case C-194/06 Orange European Smallcap Fund [2008] ECR I-3747; para. 27, Case C-128/08 Damseaux [2009] ECR I-6823.
[52] Para. 39, Case C-157/10 Banco Bilbao, which could mean, for example, that when such access to foreign tax benefits are provided to residents they must also be offered to non-residents.
[53] Para. 80, Case C-322/11, K.
[54] Para. 16, Case C-80/94 Wielockx [1995] ECR I-2493; para. 38, Case C-190/12 Emerging Markets ECLI:EU:C: 2014:249; para. 36, Case C-387/11, Commission v Belgium ECLI:EU:C:2013:385; para. 14, Joined Cases C-338/11 to C-347/11 Santander Asset Management ECLI:EU:C:2012:286; para. 36, Case C-374/04 Test Claimants in Class IV of the ACT Group Litigation [2006] ECR I-11673.
[55] Para. 37, Case C-387/11, Commission v Belgium; para, 50, Case C-374/04 Test Claimants in Class IV of the ACT Group Litigation; para. 47, Case C-446/04 Test Claimants in the FII Group Litigation [2006] ECR I-11753; para. 30, Case C-194/06 Orange European Smallcap Fund; para. 25, Case C-128/08 Damseaux.
[56] The general attitude of the Court of Justice towards bilateral tax (double taxation) conventions is somewhat controversial. On the one hand, it acknowledges that the problems addressed under EU law arose primarily from the Member States starting to expand their tax jurisdiction in competition with each other in order to secure the base for national taxation. It

- 'in the absence of unifying or harmonising measures adopted by the European Union,[57] the Member States retain competence for determining the criteria for taxation on income and capital with a view to eliminating double taxation by means, inter alia, of international agreements. In that context, the Member States are free to determine the connecting factors for the allocation of fiscal jurisdiction in bilateral agreements for the avoidance of double taxation.'[58]
- 'Since European Union law, as it currently stands, does not lay down any general criteria for the attribution of areas of competence between the Member States in relation to the elimination of double taxation within the European Union each Member State remains free to organise its system for taxing distributed profits.'[59]
- 'It is for the Member States to take the measures necessary to prevent situations of double taxation by applying, in particular, the criteria followed in international tax practice.'[60]

Exemption v imputation method

At the level of technicalities, when the Member States decide to address the double taxation which they themselves have caused by extending their taxation competences to the territory of other states, they may, in principle, choose to implement the exemption method when the dividends are paid by a resident taxpayer and the imputation method when they are paid by a non-resident taxpayer.[61] The two methods will be equivalent provided that

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accepts this as the cause for the adoption of instruments to address the imposition of a series of charges or double taxation on incomes (infra n.). It is, therefore, reluctant to tolerate interferences with free movement introduced in this context (infra n.). In contrast, the new case law regarding the allocation of taxation powers among the Member States concerned, however, indicates a more welcoming attitude towards these international agreements (infra n).

[57] Apart from Convention 90/436/EEC on the elimination of double taxation in connection with the adjustment of profits of associated enterprises, OJ L225 (1990), p. 10-24, no unifying or harmonising measure for the elimination of double taxation had so far been adopted at EU level and neither did the Member States conclude any multilateral convention to that effect under ex Article 293 EC, para. 50, Case C-376/03 D ECLI:EU:C:2005:424.

[58] Para. 18, Case C-489/13 Verest; para. 41, Case C-303/12 Imfeld; para. 57, Case C-307/97 Saint-Gobain [1999] ECR I-6161; para. 93, Case C-385/00 de Groot [2002] ECR I-11819; para. 49, Case C-265/04 Bounaich [2006] ECR I-923, paragraph 49.

[59] Para. 40, Case C-35/11 Test Claimants in the FII Group Litigation ECLI:EU:C:2002:707; par. 22, Case C-513/04 Kerckhaert; para. 31, Case C-157/10 Banco Bilbao. See the same freedom to lay down, for the purpose of taxation of income of natural persons, methods of assessment of income from immovable property according to whether the property is situated in that Member State or in another Member State, para. 20, Case C-489/13 Verest. The Member States retain the power to define, by treaty or unilaterally, the criteria for allocating their powers of taxation, particularly with a view to eliminating double taxation, para. 31, Case C-157/10, Banco Bilbao.

[60] Para. 31, Case C-157/10, Banco Bilbao; para. 23, Case C-513/04 Kerckhaert.

[61] Para. 66, Case C-47/12 Kronos ECLI:EU:C:2014:2200; para. 39, Case C-35/11 Test Claimants in the FII Group Litigation; paras. 48 and 57, Case C-446/04 Test Claimants in the FII Group Litigation; para. 86, Joined Cases C-436/08 and C-437/08 Haribo [2011] ECR I-0305; para. 88, Case C-310/09 Accor [2011] ECR I-8115; para. 39, Order in Case C-201/05 Test Claimants in the CFC and Dividend Group Litigation [2008] ECR I-2875.

the tax rate applied to foreign-sourced dividends is not higher than the rate applied to nationally-sourced dividends and that the tax allowance (e.g., tax credit) is at least equal to the amount paid in the state where the taxpayer makes the distribution of dividends, up to the limit of the tax charged in the Member State of the taxpayer receiving the dividends.[62]

General obligation to observe EU law

However, as in other areas of EU law, the lack of EU competences to regulate taxation directly does not mean that the Member States would enjoy complete freedom from their EU obligations.[63] Even in these domains, they are required to observe the principle of equal treatment[64] and they must ensure compliance with EU law,[65] in particular, the free movement of capital.[66] Nevertheless, as will be discussed below, more recent jurisprudence dealing with the allocation of tax powers in bilateral double taxation conventions recognises that the rules on the allocation of Member State tax powers may contain a differentiated treatment of taxpayers without constituting unlawful discrimination and that the substantive tax rules of such treaties regulating tax advantages and disadvantages under the principle of reciprocity do not have to extended to the taxpayers of Member States that are not party to the convention.[67] This way the consistent enforcement of the equal treatment principle in the entire Single Market seems to have been undermined by the interest of the Member States to regulate – in the absence of EU measures of similar kind – cross-border taxation affairs in bilateral tax treaties.

Member State derogations

In relation to the clause that Member State derogations are accepted to the extent that there are no EU harmonisation measures providing for measures necessary to protect the interest raised,[68] the Court of Justice held that in absence of such EU harmonisation 'it is for the Member States to decide on the degree of protection which they wish to afford to such legitimate interest and on the way in which that protection is to be achieved.'[69] Again, these

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[62] Ibid. See, in detail, paras. 87-89, Case C-47/12 Kronos.

[63] See the distinction introduced in Case C-47/12 Kronos regarding the obligations of a Member State when opting to tax and when opting not to tax under a double taxation convention, infra n.

[64] Para. 40, Case C-35/11 Test Claimants in the FII Group Litigation; paras. 37-40, Case C-157/10, Banco Bilbao; paras. 21 and 26, Case C-279/93 Schumacker [1995] ECR I-0225; para. 16, Case C-80/94 Wielockx [1995] ECR I-2493; para. 36, Case C-107/94 Asscher [1996] ECR I-3089.

[65] And with the similar provisions of the EEA Agreement, para. 23, Case C-72/09 Rimbaud [2010] ECR I-10659.

[66] Para. 18, Case C-489/13 Verest; para. 41, Case C-303/12 Imfeld; para. 37, Joined Cases C-578/10 to C-580/10 van Putten; para 14, Joined Cases C-338/11 to C-347/11 Santander Asset Management; para. 39, Case C-35/11 Test Claimants in the FII Group Litigation; paras. 48 and 57, Case C-446/04 Test Claimants in the FII Group Litigation; para. 86, Joined Cases C-436/08 and C-437/08 Haribo; para. 88, Case C-310/09 Accor; para. 39, Order in Case C-201/05 Test Claimants in the CFC and Dividend Group Litigation.

[67] Infra n.

[68] Infra n.

[69] Para. 33, Case C-282/04 Commission v Netherlands ECLI:EU:C:2006:608.

powers must be exercised in compliance with EU law, especially, the principle of proportionality.[70]

2.2 Definition matters

Overlapping fundamental freedoms

For a national measure to fall under the scope of Article 63 TFEU, it needs to affect capital movements or the freedom of payments between the Member States (and between the Member States and a third State).[71] There may be considerable overlap with the other fundamental economic freedoms,[72] especially with the freedom of establishment under Article 49 TFEU in matters of taxation of incomes (dividends) gained from investment (in shares) abroad.[73] Establishing under the scope of which Treaty provision the national measure may fall has particular legal importance as in contrast with the freedom of establishment, or other fundamental freedoms, the geographical scope of the free movement of capital extends to transactions involving third States.[74] In case the national measure constitutes an interference with the free movement of capital, Member State governments

A wider geographical scope

[70] Ibid.

[71] The mere transfer of residence does not constitute capital movements and national tax measures disencouraging the transfer of residence – especially, with the purpose of avoiding the evasion of inheritance tax – does not constitute a restriction of the free movement of capital, paras. 48-50, Case C-513/03 van Hilten ECLI:EU:C:2006:131.

[72] See the case law supra n distinguishing between capital movements, the free movement of goods and current payments. The overlap between capital movements and the free movement of financial services follows directly from ex Article 61(2) TEC holding that the liberalisation of banking and insurance services connected with movements of capital shall be effected in step with the progressive liberalisation of movements of capital. See, in this regard, paras. 22-34, Case C-452/04 Fidium Finanz ECLI:EU:C: 2006:631, arguing, first, that there is no order of priority among the fundamental freedoms following from the Treaty definition of services in Article 57 TFEU, and, second, in case of an overlap between the free movement of capital and the free movement of (financial) services the Court of Justice will consider 'to what extent the exercise of thise fundametal liberties is affected and whether, in the circumstances of the main proceedings, one of those prevails over the other.' The Court will apply only one of the two freedoms 'if it appears, in the circumstances of the case, that one of them is entirely secondary in relation to the other and may be considered together with it.'

[73] Para. 89, Case C-35/11 Test Claimants in the FII Group Litigation; para 33, Joined Cases C-436/08 and C-437/08 Haribo; para. 33, Case C-310/09 Accor.

[74] Paras. 96-97, Case C-35/11 Test Claimants in the FII Group Litigation. Potentially, the Treaty provisions on capital movements could open up other fundamental freedoms, as a result of their overlap, to third State economic operators, Usher (2006), 182. See, however, paras. 47-49, Case C-454/04 Fidium Finanz where the inapplicability of Article 56 TFEU for the third country economic operator concerned to contest national legislation was not mitigated by the possibility of relying on Article 63 TFEU as the restriction on capital movements was 'merely an unavoidable consequence of the restriction on the free movement of services.' See also, in relation to the freedom of establishment, paras. 26-27, Order in Case C-492/04 Lasertec ECLI:EU:C:2007:273. This overlap is also relevant from the perspective of the express premission in the Treaty to maintain pre-1994 restrictions on capital movements to and from third States. Furthermore, it is not entirely clear how – in case of an overlap between the different fundamental freedoms – the tax differentiation permitted for the Member States under Article 65(1)(a) TFEU can be reconciled with the rules governing the freedom of establishment and the liberalisation of financial services under the free movement of services, Usher (2006), 200.

are prevented from introducing a differentiated treatment of third country nationals or third country transactions. Also, under Article 64(1) TFEU measures on the provision of financial services involving third States are freed from the oblig0ations of Article 63 TFEU.[75] In order to avoid the abuse of the different scopes of the different fundamental freedoms, the jurisprudence insists that the scope of Treaty freedoms cannot be interpreted in a way so that the applicability of a certain freedom enables individuals to benefit from another freedom, the scope of which does not extend to them.[76]

Different legal thresholds

A further relevance for distinguishing between the different fundamental freedoms is that the legal thresholds for invoking them to challenge national measures can vary (e.g., decisive (definitive) influence of shareholder to invoke the freedom of establishment and the free movement of capital being available irrespective of the size of the shareholding).[77] This means that Member State governments face different limitations when they regulate, for instance, the taxation of interests paid out after loans or of dividends distributed to shareholders.

Cross-border relevance

In order for Article 63 TFEU to be applicable, by definition, the transaction cannot have its 'constituent elements' confined to a single Member State.[78] This is generally satisfied when the persons concerned reside in different Member States, or the income is gained in a Member State different from the Member State exercising its powers of taxation.[79] In the context of purchasing immovable property situated in a Member State and transferring its ownership, the Court of Justice ruled that the directly effective liberalisation obligations laid down in Article 1(1) of the 1988 Capital Directive 'are not subject to the existence of other cross-border elements' and that 'the mere fact that the result of a national provision is to restrict

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[75] See paras. 21 and 27, Case C-560/13 Wagner-Raith ECLI:EU:C:2015:347. There needs to be a sufficiently close link between the movement of capital and the provision of financial services for Article 64(1) TFEU to apply, para. 44, ibid. Article 64(2) TFEU cannot be interpreted as providing a list of capital movements which fall outside the scope of Article 63 TFEU, para. 34, Case C-101/05 A [2007] ECR I-11531.

[76] Para. 100, Case C-35/11 Test Claimants in the FII Group Litigation.

[77] Para. 22, Case C-251/98 Baars [2000] ECR I-2787; para. 31, Case C-196/04 Cadbury Schweppes [2006] ECR I-7995; para. 27, Case C-524/04 Test Claimants in the Thin Cap Group Litigation [2007] ECR I-2107; paras. 66-68, Case C-436/00 X and Y ECLI:EU:C:2002:704; para. 18, Case C-282/12 Itelcar ECLI:EU:C:2013:629; para, 30, Case C-168/11 Beker ECLI:EU:C:2013:117.

[78] Para. 19, Case C-132/10 Olivier Halley [2011] ECR I-8353; para. 39, Case C-11/07 Eckelkamp and Others [2008] ECR I-6845; para. 24, Joined Cases C-515/99, C-519/99 to C-524/99 and C-526/99 to C-540/99 Reisch [2002] ECR I-2157; para. 20, Case C-510/08 Mattner ECLI:EU:C:2010:216.

[79] See para. 16, Case C-478/98 Commission v Belgium ECLI:EU:C:2000:497 stating that although the national measure is addressed to the residents of the Member State concerned, it cannot be regarded as a purely internal measure as the transactions affected (the Eurobonds kartet) have an obvious cross-border element. See also para. 69, Case C-436/00 X and Y.

movements of capital by an investor who is a national of a Member State on the basis of his place of residence' is sufficient for those obligations to apply.[80] It held that neither the fact that the person concerned had changed residence to another Member State nor the fact that his capital may have been distributed over two Member States is relevant as regards the application of Article 1(1).[81] The Court of Justice also added that 'it is not relevant that the tax measure at issue in the main proceedings was adopted by the Member State of origin of the person concerned.'[82]

Taxation and third State capital movements

The definitional distinction between intra-Union capital movements and EU-third State capital movements has crucial legal relevance. Beyond the differentiated treatment of these capital movements at the Treaty level, the Court of Justice, having recognised that movements of capital to or from third countries takes place in a different legal context from that which occurs within the Union, held that from a taxation perspective intra-Union and EU-third State capital movements are not in a comparable situation and the Member States may be able to demonstrate 'that a restriction on the movement of capital to or from third countries is justified for a particular reason in circumstances where that reason would not constitute a valid justification for a restriction on capital movements between Member States.'[83]

The purpose of the measure and the facts of the case

As a general rule, in defining whether the national measure falls under the scope of Article 63 TFEU its purpose will be taken into consideration.[84] This could entail distinguishing between situations where shareholdings are considered from the perspective of them enabling the holder to exert an influence over a company's decisions and determine its activities, which falls under the freedom of establishment, and where they are regulated as an investment tool with no intention of the shareholder to influence the management and control of the undertaking, which is covered by the free movement of capital.[85] Curiously, the legal definition of capital movements

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[80] Para. 59, Case C-364/01 Barbier ECLI:EU:C:2003:665.
[81] Para. 60, ibid.
[82] Para. 61, ibid, and para. 24, Case 115/78 Knoors [1979] ECR 0399; para. 13, Case C-61/89 Bouchoucha [1990] ECR I-3551; para. 15, Case C-19/92Kraus [1993] ECR I-1663; paras. 8 and 9, Case C-419/92 Scholz [1994] ECR I-0505; para. 32, Case C-107/94 Asscher[1996] ECR I-3089.
[83] Paras. 36-37, Case C-101/05 A and paras. 170-171, Case C-446/04 Test Claimants in the FII Group Litigation.
[84] See para. 22, Case C-157/05 Holböck [2007] ECR I-4051; para. 36, Case C-182/08 Glaxo Wellcome [2009] ECR I-8591; paras. 33-34, Joined Cases C-436/08 and C-437/08 Haribo; para. 17, Case C-132/10 Olivier Halley; paras. 31-33, Case C1196/04 Cadbury Schweppes; paras. 37-38, Case C-374/04 Test Claimants in Class IV of the ACT Group Litigation; paras. 26-34, Case C-524/04 Test Claimants in the Thin Cap Group Litigation; para. 31, Case C-310/09 Accor.
[85] Para. 35, Joined Cases C-436/08 and C-437/08 Haribo; para. 34, Case C-387/11 Commission v Belgium; para. 32, Case C-310/09 Accor; paras. 91-92, Case C-35/11 Test Claimants in the FII Group Litigation. See the detailed examination in paras. 20-24, Case C-282/12 Itelcar on the tax treatment of interest on overall debts regarded as excessive that

includes – as a matter of definition – both direct and portfolio investments in the concept of capital movements.[86] In the circumstance that this distinction cannot be made on the basis of the purpose of the national measure concerned (e.g., a tax on dividends received from shareholdings), the facts of the legal dispute will be decisive.[87] In this regard, the fact whether the shares held to confer the possibility of exercising definite influence over the decisions of the companies concerned and determining their activities could be of relevance.[88]

The role of the nomenclature

In interpreting the scope of Article 63 TFEU, the nomenclature provided in the 1988 Capital Directive will be relied upon as an indicative, but not an exhaustive list of the transactions covered.[89] Based on this broad interpretative approach, transactions, such as the lending of a vehicle free of charge,[90] gifts,[91] inheritances, (transfer of assets left by a deceased person),[92] financial guarantees linked to the performance of services,[93] financial loans, mortgages and credits,[94] acquisition, usage and disposal of immovable property,[95] 'direct' investments, 'namely investments in the form of participation in an undertaking through the holding of shares which confers the possibility of effectively participating in its management and control', and 'portfolio' investments, 'namely investments in the form of the acquisition of shares on the capital market solely with the intention of making a financial investment without any intention to influence the management and control of the undertaking',[96] will be considered as capital movements.

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are entered into by a resident company with a company of a non-member country, with which it has special relations, finding that the tax measure was applicable irrespective of the size or the relevance of the shareholding.

[86] Infra n.

[87] Para. 94, Case C-35/11 Test Claimants in the FII Group Litigation.

[88] Para. 99, Case C-35/11 Test Claimants in the FII Group Litigation; para. 29. Case C-168/11 Beker; para. 40, Case C-47/12 Kronos.

[89] Para. 20, Case C-322/11 K; paras. 20 and 21, Case C-222/97 Trummer and Mayer [1999] ECR I-1661; para. 37, Case C-483/99 Commission v France [2002] ECR I-4781; para. 38, Case C-503/99 Commission v Belgium [2002] ECR I-4809; para. 22, Case C-386/04 Stauffer [2006] ECR I-8203.

[90] Paras. 27-36, Joined Cases C-578/10 to C-580/10 van Putten.

[91] Para. 24, Case C-318/07 Persche [2009] ECR I-359.

[92] Para. 19, Case C-132/10 Olivier Halley; para. 20, Case C-181/12 Welte ECLI:EU:C:2013:662; para. 58, Case C-364/01 Barbier; paras. 40-42, Case C-513/03 van Hilten; para. 39, Case C-11/07 Eckelkamp; para. 30, Case C-43/07 Arens-Sikken [2008] ECR I-6887.

[93] Para. 36, Case C-279/00 Commission v Italy [2002] ECR I-4641.

[94] Para. 14, Case C-282/12 Itelcar; para. 18, Case C-22/97 Trummer and Mayer; para. 18, Case C-464/98 Stefan ECLI:EU:C:2001:9; para. 10, Case C-484/93 Svensson ECLI:EU:C:1995:379.

[95] Paras. 28-29, Case C-515/99 Reisch.

[96] Para. 40, Joined Cases C-105/12 to C-107/12 Essent ECLI:EU:C:2013:677; para. 37, Case C-483/99 Commission v France; para. 38, Case C-503/99 Commission v Belgium;

para. 19, Case C-282/04 Commission v Netherlands; para. 49, Case C-171/08 Commission v Portugal ECLI:EU:C:2010:412.

3 The restrictions on national polices and regulation

Delimiting choices and freezing action

In order to secure the opportunities offered to national economies and individuals by free capital movements in the Union, the Member States have imposed on themselves legal restrictions delimiting their choices in policy-making and regulation. They also have an impact of freezing Member State efforts to introduce changes to existing policies and regulation. Without these restrictions, the rationale of the free movement of capital would be jeopardised and the Member States – through unilateral action – would damage not only the EU policy developed in their interest, but also the interests of the other Member States. The concrete limitations on the Member States are indicated both in EU legislation and the jurisprudence of the EU Court of Justice. The restrictions are different in the cases of taxation and 'regulatory' fields which are the two main areas of national law and policy affected.

3.1 The equal treatment principle

The most fundamental benchmark

Beyond the concrete prohibitions in the Treaties and in secondary legislation, which also prohibit discrimination, in the context of the free movement of capital the Member States have to observe the general equal treatment principle in EU law. The obligation of equal treatment within the EU irrespective of nationality, origin or residence is not only fundamental for realising the market integration agenda of the Treaties, but it also expresses that equal compliance is expected from the Member States – which are of equal status in the Union – with their mutually binding obligations. The principle is applied to determine whether an actual difference of treatment took place either as embedded under Article 63 TFEU,[97] or as an independent, general source of legal constraint on the Member States.[98] In both instances, the legal test entails examining whether (a) the persons affected are in an objectively comparable situation,[99] (b) they have been subjected to equal or unequal treatment,[100] (c) their differentiated treatment

[97] Mainly in the objective comparability element of the test, see paras. 42-44, Joined Cases C-578/10 to C-580/10 van Putten. As a general principle under Article 63 TFEU, see para. 65, Case C-47/12 Kronos.
[98] Paras. 42-43, Joined Cases C-578/10 to C-580/10, van Putten. See its application in Case 22/80 Boussac ECLI:EU:C:1980:251 in the context of a simplified procedure for debt recovery not being available for debt expressed in a foreign currency, and in Case 308/86 Lambert concerning restrictions on payments and exchanges in foreign currency affecting exporters.
[99] It seems as an important qualification in this regard that the position of a taxable person is not necessarily altered merely by the fact that he receives foreign-sourced income which could have been subject to taxation in another State, para. 42, Case C-157/10 Banco Bilbao.
[100] The application of different rules to comparable situations or the application of the same rule to different situations, para. 41, Case C-157/10 Banco Bilbao.

was justified by an overriding reason in the general interest, and (d) the measure in question meets the proportionality requirement.[101] In preliminary ruling cases, this issue may be deferred to the national court to determine.[102] Paragraph 3 of Article 65 TFEU holds that the derogations permitted therein must not 'constitute a means of arbitrary discrimination or a disguised restriction' on free movement under Article 63 TFEU.

Sufficient connection

In the case law, the equal treatment principle has led to the introduction of the legal concept of the transaction or situation having a sufficient connection with the Member State concerned. In the context of imposing registration tax on motor vehicles registered in another Member State, a legal distinction was made between vehicles which have a weaker connection with the Member State concerned (not used there on a permanent basis) and vehicles that are intended to be used in that Member State on a permanent basis or are, in fact, used in that way. In the first case, the Member States are required to produce an adequate justification for the tax imposed by being able to identify an overriding reason in the general interest and establish its proportionality.[103] In the second case, the Member States are entitled to impose such a tax as domestic and foreign registered vehicles are in an objectively comparable situation and are treated in a similar manner.[104]

The problem of cross-border taxation

In the domain of double taxation agreements,[105] where the Member States as indicated earlier enjoy considerable autonomy, and, generally, in the instance when the Member States exercise their tax competences in parallel, the equal treatment principle serves as an ultimate legal benchmark of Member State conduct.[106] As a general principle, the Member States must afford equal tax treatment of income (dividends) irrespective of the residence of the person distributing and the person receiving the income because the situation of persons receiving foreign-sourced income and those receiving nationally-sourced incomes are comparable 'in so far as, in each case, the profits made are, in principle, liable to be subject to a series of charges to tax.'[107] This obligation 'implies that the national system must

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[101] Paras. 42-44, Joined Cases C-578/10 to C-580/10 van Putten.
[102] Para. 49, ibid, and para. 45, Case C-157/10 Banco Bilbao.
[103] Paras. 47 and 53, Joined Cases C-578/10 to C-580/10 van Putten.
[104] Paras. 45-46, 48, Joined Cases C-578/10 to C-580/10 van Putten.
[105] Or when the Member States have a system for preventing or mtigiating a series of charges to tax incomes.
[106] Supra n. Para. 68, Case C-47/12 Kronos; para. 40, Case C-35/11 Test Claimants in the FII Group Litigation; para. 29, Case C-262/09 Meilicke; paras. 27-49, Case C-315/02 Lenz [2004] ECR I-7063; paras. 29-55, Case C-319/02 Manninen [2004] ECR I-7477; para. 55, Case C-374/04 Test Claimants in Class IV of the ACT Group Litigation.
[107] Paras. 37-38, Case C-35/11 Test Claimants in the FII Group Litigation; paras. 62, 72, Case C-446/04 Test Claimants in the FII Group Litigation; paras. 59-60, Joined Cases C-436/08 and C-437/08 Haribo; para. 65, Case C-47/12 Kronos.

be transposed, to the fullest extent possible, to cross-border situations.'[108] In the special circumstance when taxpayers aim to liberate themselves from disadvantages suffered from the parallel exercise of tax competences by different Member States, the Member States could be required to afford equal treatment not only in the taxation of foreign-sourced income, but also in determining the possibility of tax deductions and the assessment of tax allowances, such as tax exemptions or tax credits.[109]

Objective differences

As will be discussed later, the equal treatment principle does not impose an absolute requirement on the Member States as differentiated tax treatment can be introduced and maintained in case there is an objective difference in the situation of different taxpayers.[110] Such is the case when the Member States exercising their competences so as to avoid the double economic taxation of incomes waive their powers of taxation (e.g., elects not to tax them or take them into account under tax law in a different way).[111] The possibility of differentiated tax treatment is also supported by the argument that under Article 63 TFEU, the Member States cannot be required to 'go beyond cancelling of national income tax payable by a shareholder in respect of foreign-sourced dividends received and to reimburse a sum whose origin is in the tax system of another Member State' provided that 'the first Member State is not to see its fiscal autonomy limited by the exercise of the fiscal power of the other Member State.'[112] Furthermore, the Member State of residence cannot be required to offset a fiscal disadvantage arising where a series of charges to tax is imposed entirely by the Member State in which the company distributing those dividends is established' provided that the dividends received are neither taxed nor taken into account in a different way by the first Member State as regards investment enterprises established in that State.'[113] Fundamentally, Member States waiving their taxation powers in a double taxation convention cannot be obliged to 'offset the tax burden resulting from the exercise of the tax powers of another Member State' (or of a third State).[114]

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[108] Para. 31, Case C-262/09 Meilicke, 'Accordingly, in situations for which it is not possible to take account of indirect prior charges' tax at the national level, which it is for the national court to determine, such account is not to be taken of dividends paid to residents by non-resident companies.'

[109] Paras. 43-44, Case C-157/10 Banco Bilbao.

[110] Article 65(1)(a) TFEU.

[111] Paras. 81-82, Case C-47/12 Kronos.

[112] Para. 83, ibid. See also, para. 33, Case C-262/09 Meilicke; para. 47, Case C-446/04 Test Claimants in the FII Group Litigation; para. 30, Case C-194/06 Orange European Smallcap Fund; pata. 25, Case C-128/08 Damseaux.

[113] Para. 84, Case C-47/12 Kronos

[114] Para. 85, Case C-47/12 Kronos. The obligations of such a State differ 'as regards treatment of the taxation carried out by another Member State' from when it decides to tax both domestically- and foreign-sourced incomes and under a double taxation convention has

3.2 Article 63 TFEU and the legal test

A broad legal test

The broad legal test developed under Article 63 TFEU confines Member State action and freezes Member State attempts at amending existing policies to a considerable extent. In its different formulas, it holds that Member State measures which are 'liable to dissuade' or 'liable to deter' capital movements and payments, or which constitute a 'restriction', an 'impediment' or an 'obstacle' to the free movement of capital and payments are prohibited.[115] In the context of cross-border investment, it states that restrictions on the movement of capital include measures 'that are such as to discourage non-residents from making investments in a Member State or to discourage that Member State's residents from doing so in other States.'[116] In the same context, the test could also read as prohibiting national measures which are liable to prevent or limit such cross-border transactions.[117] Specifically, it has been held that quantitative or qualitative restrictions on investments made in other Member States have a restrictive effect on the free movement of capital as in relation to companies established in other Member States such a provision constitutes an obstacle to the raising of capital through the acquisition of shares.[118]

Lack of distinctions

Despite its different formulations, the legal test – on its own – is unable to provide clearly defined boundaries between legitimate and illegitimate Member State conduct. It is too general to indicate to Member State governments within what legal confines they should develop policies and regulations which may fall under the scope of Article 63 TFEU. It was raised that the legal test does not distinguish appropriately between discriminatory and non-discriminatory measures and between measures which impose

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to take into account the tax burden resulting from the exercise of the tax powers of the other Member State, para. 86.

[115] Para. 10, Case C-484/93 Svensson; para 26, case C-222/97 Trummer and Mayer; para. 41, Joined Cases C-105/12 to C-107/12 Essent. The prohibition goes beyond the mere elimination of unequal treatment on grounds of nationality and covers siutations which render the free movement of capital illusory (e.g., dissuading investors and impeding transactions), paras. 44-45, Case C-367/98 Commission v Portugal [2002] ECR I-4731 and paras. 40-41, Case C-483/99 Commission v France.

[116] See, inter alia, para. 28, Case C-342/10 Commission v Finland EU:C:2012:688; para. 15, Joined Cases C-338/11 to C-347/11 Santander Asset Management; para. 43, Case C-375/12 Bouanich EU:C:2014:138; para. 24, Case C-370/05 Festersen [2007] ECR I-1129; para. 40, Case C-101/05 A; para. 50, Joined Cases C-436/08 and C-437/08 Haribo; para 21, Case C-489/13 Verest; para. 44, Joined Cases C-197/11 and C-203/11 Libert EU:C:2013:288.

[117] Para, 23 Case C-322/11 K; para. 41, Joined Cases C-105/12 to C-107/12 Essent; paras. 45-46, Case C-367/98 Commission v Portugal; para. 40, Case C-483/99 Commission v France; paras. 61-62, Case C- 463/00 Commission v Spain [2003] ECR I-4581; paras. 47 and 49, Case C-98/01 Commission v UK [2003] ECR I-4641; patas. 30 and 31, Case C-174/04 Commission v Italy [2005] ECR I-4933.

[118] Para. 42, Joined Cases C-105/12 to C-107/12 Essent.

direct or indirect discrimination.[119] It was also claimed that it has failed to delimit its potential scope for application and nearly all measures affecting corporate activity, property ownership or taxation could be covered by the free movement of capital, without there being a visible *de minimis* or similar rule.[120] Finally, it was observed that the legal test contains no distinction – and it may not even be able to introduce such a distinction – between different classes of regulatory instruments on the basis of their practical impact on free movement, such as that between product rules and marketing rules under the free movement of goods, and there is no discussion – and arguably there is no need for a discussion[121] – concerning the application of an 'access to the market' test as under other fundamental freedoms.[122] This latter statement is somewhat contradicted by the Court of Justice examining in *Commission v Spain (administrative approval)* – instead of rejecting explicitly the application of the test – whether the measure in question had 'comparable effects' to those of the rules covered by the market access approach of *Keck and Mithouard*.[123] The use of the general formula on what measures are caught by Article 63 TFEU could, nevertheless, indicate that the distinction between national measures under the free movement of goods has no applicability.[124]

The test for prior authorisation schemes

The jurisprudence of the EU Court of Justice, however, offers a number of general and more specific signposts for Member State governments. It is well-established[125] that as opposed to prior declarations obligations of prior

[119] S. Peers, 'Free movment of capital: leaning lessons or slipping on spilt milk?', in C. Barnard and J.Scott (eds.), *The Law of the Single European Market* (Hart, 2002), 333-351, at 341-345.
[120] Ibid.
[121] It is the movement of capital which is considered, and not the uses to which it is put. See, however, T. Horsley, 'The concept of an obstacle to intra-EU capital movement in EU law', in N.N. Shuibhne and L.W. Gromley (eds.), *From Single Market to Economic Union* (OUP, 2012), 155-174, at 168-170, supporting a delimitation of the broad judicial interpretation of the prohibition using *Keck* or a similar solution.
[122] Peers (2002), 341-345. See also Horsley (2012), 170-173.
[123] Paras. 59-60, Case C-463/00 Commission v Spain and paras. 45-46, Case C-98/01 Commission v UK.
[124] Para. 61, Case C-463/00 Commission v Spain and para. 47, Case C-98/01 Commission v UK. In the former judgment, the Court of Justice added, however, to its conclusion that the measures areliable to deter cross-border investment in that they 'consequently, affect access to the market' (para. 61).
[125] Paras. 24-25, Case C-358/93 Bordessa; paras. 25-28, Joined Cases C-163, C-165 and C-250/94 Sanz de Lera; para. 15, Case C-54/99 Église de Scientologie ECLI:EU:C:2000:124. Contrast with the case law on prior authorisation in relation to immovable property, or in the context of public policy and public security risks, para. 39, Case C-302/97 Konle ECLI:EU:C:1999:271; paras 14, 19-20, Case C-54/99 Église de Scientologie. Prior authorisation schemes can be particularly restrictive when they have a suspensory effect on the transaction concerned. See para. 15, Case C-54/99 Église de Scientologie discussing that the restrictive nature of the prior authorisation process was not affected by the fact that the authorisation was deemed to have been obtained one month after receipt of the request where the competent authority did not declare a deferment of the

authorisation for direct foreign investments (currency movements), which would subject such transactions to administrative discretion,[126] are generally unacceptable,[127] even when the transaction in question may in fact take place without obtaining the authorisation. Conversely, when their application is necessary to address a genuine and sufficiently serious threat to public policy and public security and they are needed to prevent, 'at the outset', transactions which would adversely affect those interests,[128] a system of prior authorisations could be more adequate than a system of prior declarations.[129] For this, the system of prior authorisations must be adequately targeted and must regulate the specific circumstances in which a prior authorisation is required as otherwise individuals are not enabled to assess the extent of their rights and obligations under the Treaties and the principle of legal certainty may be breached.[130] With this, not only the requirements of good regulation and good administration, which are linked to the principle of legal certainty, will be met, but abusive, overly expansive uses of the public policy and public security grounds can also be avoided.[131]

The test for prior authorisation schemes for the acquisition of immovable property

As to prior notification, prior authorisation or prior declaration schemes applicable to the acquisition of immovable property, the jurisprudence laid down similar legal benchmarks. While they are considered by their purpose to restrict the free movement of capital, they can be permitted if they are applied without discrimination in pursuance of a public interest and they are proportionate in the sense that the same result cannot be achieved by less restrictive measures.[132] It seems that objectives which are relevant for the acquisition, use and disposal of immovable property, such as those of local and regional planning, population and economic policy, and which approach these from a broader perspective, such as those of environmental policy,

transaction in question within the same period, and by the fact that failure to comply with the obligation to request prior authorisation attracted no penalties.

[126] The discretion available to national authorities will be regarded as adequately regulated when it is based on objective, non-discriminatory criteria which are known in advance to the undertakings concerned, and all persons affected by a restrictive measure of that type must have a legal remedy available to them, para. 50, Case C-367/98 Commission v Portugal; para. 46, Case C-483/99 Commission v France, para. 69, Case C-463/00 Commission v Spain

[127] They were not, 'in the circumstances particular to those cases, necessary', para. 19, Case C-54/99 Église de Scientologie. They may be acceptable 'when they are proportionate to the aim pursued, inasmuch as the same objective could not be attained by less restrictive measures, in particular a system of declarations ex post facto', para. 50, Case C-367/98 Commission v Portugal.

[128] Because it is difficult to identify and block capital once it has entered a Member State, para. 20, Case C-54/99 Église de Scientologie.

[129] Paras. 19-20, ibid.

[130] Paras. 21-22, ibid.

[131] For instance, its usage to promote an otherwise illegitmate (e.g., economic) interest or its application in unrelated circumstances.

[132] Paras. 32-33, Case 515/99 Reisch; para. 39, Case C-302/97 Konle and para. 42, Case C-213/04 Burtscher ECLI:EU:C:2005:731. See also paras. 44-52, Case C-300/01 Salzmann ECLI:EU:C:2003:283.

are likely to be accepted.[133] The non-discrimination requirement can be satisfied when acquirers of title that are local and that reside in other Member States are treated equally under the law.[134] In *Salzmann*, the Court of Justice argued that the discretionary power available to the public authority concerned – through the acquirer of title being required to produce proof of the future use of the land he is acquiring – cannot exclude the discriminatory application of the prior authorisation system.[135] Concerning the proportionality requirement, as opposed to prior authorisation schemes a system of prior declaration, coupled with appropriate legal instruments (e.g., supervision of compliance by public authority or the possibility of penalties for land use departing from the agreed declaration), seems acceptable under EU law provided that it is able to achieve the desired aim.[136] The results of a prior authorisation system may also be achieved effectively by a less restrictive but effective prior notification scheme.[137] A prior authorisation system could be especially restrictive when it is coupled with strong supervision powers available to public authorities, criminal sanctions and with a specific action for annulment which may be brought when the project fails to comply with the conditions of the initial declaration, and when it can be initiated alone by the public authority on the basis of mere presumptions.[138] When the grating of prior authorisations is made subject to requirements on which national law 'does not impose any substantive restriction, and require the acquirer of title to provide security up to the value of property', the prior authorisation system will most likely be declared as excessively restrictive.[139]

Penalties in prior authorisation schemes

Concerning the imposition of penalties, in a case dealing with a prior declaration scheme the Court of Justice concluded that such penalties must be regarded as disproportionate when they are imposed automatically, following the passing of the time-limit provided, without taking into account

[133] Para. 34, Case C-515/99 Reisch; para 40. Case C-302/97 Konle and para. 46, Case C-213/04 Burtscher. The aim of national authorities to ensure the application of planning rules in compliance with the requirement of legal certainty of transactions is another acceptable objective, para. 46, Case C-213/04 Burtscher. The specific objectives of preserving agricultural communities and viable farms, the sympathetic management of green spaces and the countryside, encouraging a reasonable use of the available land by resisting pressure on land, and preventing natural disasters may also be accepted, paras. 37 and 39, Case C-452/01 Ospelt ECLI:EU:C:2003:493 referring to para. 10, Case 182/83 Fearon [1984] ECR 3677.

[134] Para. 34, Case C-515/99 Reisch and para. 48, Case C-213/04 Burtscher. The requirement to state the nationality of the person concerned in the administrative process and his intended use of the property is not such as to give rise to discrimination, para. 50, ibid..

[135] Paras. 46-47, Case C-300/01 Salzmann.

[136] Para. 35, Case C-515/99 Reisch; paras 44-48, Case C-302/97 Konle; para. 52, Case C-213/04 Burtscher and paras. 49-50, Case C-300/01 Salzmann.

[137] Para. 37, Case C-515/99 Reisch.

[138] Para. 38, ibid.

[139] Ibid.

the reasons and potential justifications for its being late,[140] and they – for no reason deriving from the infringement of the applicable substantive rules – radically call into question an agreement expressing the intentions of the parties and, therefore, violate legal certainty, which is particularly important in relation to property acquisitions.[141] These deficits are not compensated by the generous calculation of the time-limits by the national authorities.[142] As to less restrictive alternative solutions, the Court of Justice suggested on the basis of earlier case law that an action for annulment of a contract of sale could constitute a proportionate penalty and that under certain circumstances depending on the public interest objective pursued a prior authorisation system could be more appropriate.[143] The Court of Justice also mentioned that in the case of less wide-ranging measures, such as fines, the applicant is given an opportunity to explain his delay, or the authority is allowed, under certain conditions, to accept a late application or to uphold the validity of the agreement.[144]

The test for prior authorisation schemes for the acquisition of agricultural land

In contrast, a more deferential approach is followed in relation to prior authorisation/notification/declaration systems for agricultural land. This is based on the Court of Justice realising that without the prior involvement of national authorities the objectives of national policy relating to agricultural land can be 'irretrievably impaired' and that subsequent involvement by national authorities will not provide the same guarantee.[145] In particular, it cannot be ensured that agricultural land will be used for its intended agricultural purposes or will not be subjected to a use 'which might be incompatible with their long-term agricultural use.'[146] Also, subsequent legal actions aiming to address irregularities in land use 'would lead to delays inconsistent with the requirements of continuity of use and sound land management', and legal certainty, would thus be undermined.[147] This, however, does not mean that a review of proportionality would not be carried out.[148] In particular, despite the fact that the system as a whole applies specific and objective conditions, it cannot include restrictive conditions which are 'not in every case necessary with regard to the objectives which it pursues.'[149] This is especially the case when less

[140] It also prevents the authority from examining whether, on the merits, the proposed acquisition complies with the applicable rules, para. 59, Case C-213/04 Burtscher.
[141] Paras. 54-56, ibid.
[142] Para. 56, ibid.
[143] Paras. 57-58, ibid.
[144] Para. 60, ibid.
[145] Paras. 43-45, Case C-452/01 Ospelt.
[146] Para. 43, ibid.
[147] Para. 44, ibid.
[148] Para. 46, ibid.
[149] Paras. 48-51, ibid (the condition that the applicant must himself farm the land, which prevents collective schemes helping farmers without sufficient resources to lease land to acquire agricultural land).

restrictive conditions can achieve the same results (i.e., that land will be kept in agricultural use) without contradicting the overall objectives of the regime.[150]

National procedural rules

It has also been accepted that the procedural rules governing activities linked to capital movements and payments may be immune from Treaty prohibitions, although the parameters of this possibility were not specified in detail.[151] Further examples of potentially unlawful Member State conduct are discussed under point 5.4.

Unacceptable Member State claims

The Court of Justice will not accept claims from the Member States that they have committed themselves, 'as a matter of policy', not to apply the provisions found in breach of Article 63 TFEU and the powers derived from them, and that following the principles of direct effect and primacy those provisions of national law will be interpreted in compliance with EU law.[152] Similarly, the Member States cannot plead that the national measures under scrutiny explicitly state that they must be applied consistently with EU law: it will not be regarded as an appropriate justification and it will not be accepted as ensuring 'with any certainty that when the system at issue is actually applied, its application will always be consistent with the requirements of Community law.'[153] Temporal limitations in national law as to the operation of a regime found in breach of EU law are also irrelevant.[154] It follows from consistent case law that the incompatibility of the said provisions 'can be definitively eliminated only by means of binding domestic provisions having the same legal force as those which require to be amended.'[155] The jurisprudence has also established that 'mere administrative practices, which by their nature are alterable at will by the authorities and are not given appropriate publicity,' will not be accepted as adequate means of compliance with Treaty obligations, 'since they maintain, for the persons concerned, a state of uncertainty as regards the extent of their rights as guaranteed by the Treaty.'[156] It was also raised that an EU national 'cannot be deprived of the right to rely on the provisions of the Treaty on the ground that he is profiting from tax advantages which are legally provided by the rules in force' in the Member State concerned.[157]

3.3 The restrictions laid down in the Capital Directives

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[150] Para. 52, ibid (an obligation on legal person acquirers to lease land on long-term contracts or right of first refusals of tenants farming the land).
[151] The procedural rules which govern an action by a creditor seeking payment of a sum of money from a recalcitrant debtor are not covered by Article 63 TFEU, para. 17, Case C-412/97 ED ECLI:EU:C:1999:324.
[152] Para. 40, Case C-367/98 Commission v Portugal.
[153] Paras. 63-64, Case C-463/00 Commission v Spain.
[154] Para. 81, Case C-463/00 Commission v Spain.
[155] Para. 41, Case C-367/98 Commission v Portugal.
[156] Ibid.
[157] Para. 71, Case C-364/01 Barbier.

The First Capital Directive,[158] which followed a deliberate agenda of ensuring the 'greatest possible freedom of movement of capital' and of 'the widest and most speedy liberalisation' of capital movements,[159] introduced obligations – which were of different intensity and legal coerciveness depending on the sensitivity of the issue – on the Member States as follows.

The First Capital Directive

Granting foreign exchange authorisations for List A

to grant foreign exchange authorisations for List A (personal capital movements) transactions and transfers of capital between the Member States (Article 1(1));

- under this heading, to enable transfers of capital on the basis of 'the exchange rate ruling for payments relating to current transactions', or in foreign exchange markets without official restrictions on the fluctuations of exchange rates on the basis of exchange rates which do not 'show any appreciable and lasting differences from those ruling for payments relating to current transactions' (Article 1(2)).[160]

Granting general permissions

to grant general permissions for transactions and transfers of capital between the Member States (Article 2(1));

- under this heading, the Member States endeavour – in foreign exchange markets without official restrictions on the fluctuations of exchange rates – to ensure that exchange rates do not 'show any appreciable and lasting differences from those ruling for payments relating to current transactions' (Article 2(2));[161]

- Member State obligations to grant general permissions could be confined – temporarily – as regards the acquisition of foreign securities to financial institutions and to undertakings 'which acquire securities of foreign companies established for a like purpose', in the special case where the transfers are made either on the same foreign exchange market as payments relating to current transactions, or on a market on which

[158] Directive 60/921/EEC. No longer in force. It divided capital movments into four groups with different degrees of liberalization obligations (Lists A-D). This was amended by Directive 86/566/EEC OJ L332 (1986), 22-28, which created new groups by merging and relocating elements of the previous lists (Lists A-C). The 1988 Capital Directive introduced a new approach by introducing a general principle of free movement of capital (Article 1(1)) and replaced the lists distinguishing between the different treatment of different capital movements by a non-exhaustive nomenclature of capital movements intended to help the application of the general principle.

[159] These formulas gave the opportunity for the Court of Justice to engage in an expansive interpretation of the relevant legal provisions, see infra.

[160] Exchange rate trends were to be monitored by the Monetary Committee, and in case any prohibited differences between the two rates mentioned would emerge, the Commission was obliged to initiate an infringement procedure (under ex Artcile 169 EEC (now Article 258 TFEU)) against the Member State concerned.

[161] The Commission were to make recommendations – after consulting the Monetary Committee – in this connection to the Member States.

exchange rate fluctuations are kept within limits applicable to such market (Article 2(3)).[162]

Granting foreign exchange authorisations for List B

to grant foreign exchange authorisations for List B (securities investments) transactions and transfers of capital between the Member States (Article 3(1));[163]

- under this heading, the Member States may maintain or reintroduce foreign exchange restrictions on capital movements[164] in the case when capital movements 'might form an obstacle to the achievement of the economic policy objectives of a Member State' (Article 3(2));
- this is not an automatic derogation, as the Member State concerned must consult the Commission – which may recommend the restrictions are abolished (Article 3(3)), and the Commission is entitled to examine whether measures for coordinating the economic policies of the Member States are available to address these difficulties and the Commission –after consulting the Monetary Committee – shall recommend their adoption by the Member States (Article 3(2)).

Other requirements

- To simplify – as far as possible – the authorisation and control formalities applicable of transactions and transfers of capital (Article 5(2)).[165]
- The Member States endeavour not to introduce any new exchange restrictions that were liberalised at date of entry into force of the Directive or to make existing provisions more restrictive (Article 6).
- Monitoring by the Monetary Committee – at least once annually – of Member State restrictions and reporting to the Commission which restrictions could be abolished (Article 4).
- The Member States are to notify the Commission (national provisions governing capital movements, the implementing provisions, and the procedural provisions for adopting the implementing provisions (Article 7).

The Second Capital Directive

The Second Capital Directive,[166] which followed the agenda of consolidating the liberalisation of capital movements and of contributing through the

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[162] The Commission were to make recommendations – after consulting the Monetary Committee – in this connection to the Member States.
[163] See Case 157/85 Brugnoni concerning the compulsory deposit of foreign securities at an approved bank as prescribed by Italian law, where the Court of Justice held that this provision also extends to the elimintation of administrative obstacles 'which, although not taking the form of exchange authorisations or affecting the acquisition of foreign securities, nonetheless constitute a hindrance to the widest liberalisation of capital movements, which (…) is necessary for the attainment of the objectives of the Community.'
[164] Which were operative on the date of the entry intro force of the First Capital Directive.
[165] Consult one another on this matter, where necessary.

abolition of capital movements closely connected to the free movement of goods, persons and services to the 'satisfactory establishment and functioning of a common market in these fields', pushed forward capital movement liberalisation mainly by **repealing** the possibility available to the Member States to temporarily confine under Article 2(3) of the First Directive the scope of its Article 2(1) on granting general permissions on capital movements, transactions and transfers (Article 1). The Second Directive also modified the nomenclature adopted for capital movements in the First Directive.

The 1972 Capital Directive

The 1972 Capital Directive,[167] aiming to counterbalance the liberalisation agenda and the obligations imposed on the Member States, focused on the ability of Member State to address large and volatile capital movements capable of damaging national economies.

The 1988 Capital Directive

The 1988 Capital Directive, which repealed the First Directive and the 1972 Capital Directive, in order for the Single Market for capital movements and payments to be completed, simplified Member State obligations and made them more robust. It includes obligations as follows.

Abolishment of restrictions on capital movements

The abolishment of restrictions on capital movements between the Member States (Article 1(1));

- under this heading, transfers of capital must be made on the same exchange rate conditions as those governing payments relating to current transactions (Article 1(2)).

Notification of the Commission

The Member States are to notify the Commission (measures regulating bank liquidity which have a specific impact on capital transactions carried out by credit institutions with non-residents)(Article 2).

Observing proportionality when regulating bank liquidity

To observe the proportionality requirement in case of national measures regulating bank liquidity (which have a specific impact on capital transactions carried out by credit institutions with non-residents) to be confined to what is necessary for the purposes of domestic monetary regulation (Article 2).

Third country capital movements

As to third country capital movements, the Member State to endeavour to attain the same degree of liberalisation as that applicable within the Union (Article 7(1));

- this must not prejudice the application of domestic or EU rules,

[166] Directive 72/156/EEC. No longer in force.
[167] Directive 88/361/EEC. No longer in force.

'particularly any reciprocal conditions, concerning operations involving establishment, the provisions of financial services and the admission of securities to capital markets'.

Monitoring

Monitoring by the Monetary Committee – at least once annually – of free movement of capital (especially, the domestic regulation of credit and financial and monetary markets which could have a specific impact on international capital movements and on all other aspects of this Directive) and reporting to the Commission on the outcome (Article 8).

3.4 Restrictions on regulatory measures and on measures of fiscal policy (taxation)

Different legal treatment of different types of national measures

As a matter of the application of the legal test, the law has evolved to distinguish between regulatory measures and measures of fiscal policy.[168] While regulatory measures, such as those governing the control rights of national governments in private enterprises, are treated with the usual legal rigour of the free movement provisions of the Treaties, fiscal measures – based mainly on considerations related to the fiscal sovereignty of the Member States as recognised in the jurisprudence[169] – are given a more favourable assessment.[170] Claims submitted by the Member States concerning tax autonomy and tax sovereignty are unlikely to be ignored and the case law openly departs from the standard requirements set against national regulatory instruments. Double regulatory burdens on individuals in matters of taxation are not considered as harmful to free movement, the principle of mutual recognition is recognised only with regards tax advantages offered and not in connection with taxes imposed by the Member States, the discriminatory impact of double taxation in cross-border situations is generally overlooked, and there is no reflection on the necessity of judicially engineered legal solutions in the absence of legislative instruments adopted at the European level.[171] There are, however, instances when national regulatory measures – mainly because of the policy area affected and the manner in which their content is regulated – are given broad judicial reference by the EU Court of Justice.[172]

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[168] J. Snell, 'Free movement of capital: Evolution as a non-linear process', in P. Craig and G. de Búrca (eds), *The Evolution of EU Law* (OUP, 2011), 547-574, at 555-563.
[169] Infra competence, especially, with regards double taxation.
[170] Contrast, for example, Case C-222/97 Trummer and Mayer and Case C-513/04 Kerckhaert.
[171] Snell (2011), 559-562. Infra competence
[172] See infra the analysis on Essent, and infra on Libert and VVO (prohibition on resident media companies investing in a media company established in another Member State and on providing that company with a bank guarantee, or on drawing up a business plan and

The following list of regulatory and taxation measures examined under the scope of Article 63 TFEU indicates what types of provisions and what kinds of regulatory mistakes may need to be avoided by the Member States.

3.4.1 Regulatory measures

These are examples of Member State regulatory measures which may be prohibited under Article 63 TFEU.

A 'sufficient connection' requirement – subject to being examined in a prior authorisation procedure – applicable to persons aiming to purchase or lease real estate in a particular community.[173]

Imposing particular 'social obligations' on economic operators in a prior authorisation procedure when planning permissions are granted.[174]

The prohibition of the privatisation of shares held in the national energy distribution system operator.[175]

Prohibiting the acquisition by foreign investors of more than a certain number of shares of certain local undertakings and requiring the prior authorisation of the State for the acquisition of a holding in certain local undertakings in excess of a specified level.[176]

Automatic suspension under law of voting rights attached to holdings exceeding 2% of the capital of undertakings operating in the electricity and gas sectors, where such holdings are acquired by public undertakings that are not quoted on regulated financial markets and hold a dominant position.[177]

'Golden shares' (e.g., holding of shares or voting rights over certain limits to be authorised by the Member State, or a decision to transfer or use as security of capital may be opposed by the Member State),[178]

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giving legal advice to a media company to be set up in another Member State, where those activities are directed towards the establishment of a commercial television station and national law aims to maintain a non-commercial audio-visual sector).

[173] Paras. 21-22, Case C-567/07 Woningstichting Sint Servatius [2009] ECR I-9021; paras. 44-45, Joined Cases C-197/11 and C-203/11 Libert ECLI:EU:C:2013:288.

[174] Paras. 21-22, Case C-567/07 Woningstichting Sint Servatius; paras. 64-66, Joined Cases C-197/11 and C-203/11 Libert.

[175] Paras, 38-47, Joined Cases C-105/12 to C-107/12 Essent permitting the transfer of shares only to public authorities or to legal persons owned, directly or indirectly, by those authorities, and prohibiting certain intra-group investments within a group consisting of undertakings established in another Member State and the national operator concerned.

[176] Para. 40, Case C-367/98 Commission v Portugal; para. 57, Case C-463/00 Commission v Spain; para. 49, Case C-98/01 Commission v UK.

[177] Paras. 29-30, Case C-174/04 Commission v Italy, the fact that the measure is restricted to public undertakings is irrelevant as private and public undertakings are not distinguished under the free movement of capital.

[178] Para. 42, Case C-483/99 Commission v France; para. 21, Case C-282/04 Commission v Netherlands. The restrictive effects of 'golden shares' are neither too uncertain nor too indirect because it cannot be excluded that the Member State concerned takes decisions

- ‘golden shares’ deter direct investments because important management decisions concerning company activities and their structures (e.g., mergers, demergers and dissolutions) depend on prior approval by the Member State concerned, they limit the influence of other shareholders in the companies affected, they can only be withdrawn with the consent of the Member State concerned,[179]

- ‘golden shares’ deter portfolio investments because a possible refusal by the Member State concerned to approve an important company decision would be capable of depressing the (stock market) value of shares and reduce their attractiveness.[180]

Requiring to follow an authorisation procedure, instead of a ‘straightforward notification procedure’,[181] for investing in authorised severance funds and being exposed to the payment of interest (a financial penalty) when that condition is not fulfilled.[182]

Residency requirement for the acquisition of agricultural land which may be waived only following the authorisation of the responsible minister.[183]

Requiring that a bank must be established in the Member State concerned in order for recipients of loans to obtain a subsidy from the State out of public funds.[184]

Requiring to establish a guarantee with a credit institution having its registered office or a branch office in the Member State concerned in order to obtain a licence to provide a service in that Member State.[185]

Requiring that a mortgage securing a debt is registered in the national currency and refusing to register such a mortgage if in a currency of another State.[186]

Imposing a duty on loans contracted – in the hope of avoiding taxation – in another Member State.[187]

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which violate the interests of the company concerned and there is a real risk of company decisions pursuing its economic interests are blocked by the State, paras. 29-30, ibid.

[179] Paras. 24-26, Case C-282/04 Commission v Netherlands.

[180] Paras. 27-28, ibid.

[181] Determining whether the procedure is an authorisation or a notification procedure is assessed under EU law on the basis of the facts of the case, para. 24, Case C-39/11 VBV ECLI:EU:C:2012:327. The relevant circumstances include: the power of the authority to examine whether the substantive conditions laid down in legislation have been met and the substantive legislative conditions applicable in the case, such as, the administrative and financial charges or the requirement of national establishment.

[182] Paras. 21-26, Case C-39/11 VBV.

[183] Para. 25, Case C-370/05 Festersen.

[184] Para. 10 Case C-484/93 Svensson.

[185] Paras. 37-38, Case C-279/00 Commission v Italy.

[186] Para. 26, Case C-222/97 Trummer and Mayer and para. 18, Case C-464/98 Stefan as it discourages denominating a debt in a foreign currency and there are clear transaction costs with the conversion of the debt into the national currency.

[187] Para. 19, Case C-439/97 Sandoz ECLI:EU:C:1999:499. See also the discriminatory imposition of a duty on loans contracted abroad, in paras. 29-31, ibid.

Prohibiting the acquisition by residents of securities of a loan on the European (Eurobond) market.[188]

Prior authorisation, notification or declaration of direct foreign investment.[189]

3.4.2 Fiscal measures

These are examples of Member State fiscal measures which may be prohibited under Article 63 TFEU (mainly concerning differentiated tax treatment).

Differentiated tax treatment of incomes from immovable property situated in another Member State.[190]

Differentiated tax treatment by not allowing in the determination of taxable profits the deduction of interests relating to the excessive part of debt owed by a company to another company, with which it has 'special relations'.[191]

Differentiated tax treatment by making tax credit available only to taxpayers insured in the national social security system.[192]

Differentiated or disadvantageous tax treatment of inheritance, which reduces its value, on the basis of the residence of the taxpayer concerned.[193]

Differentiated tax treatment of incomes depending on the residence of the taxpayer (e.g., the availability of tax refunds, tax exemptions, recovery of advance corporation tax (and advantageous arrangements for the recovery of advance corporation tax), tax credit, tax deductions, tax shields, tax caps or other tax advantages),[194]

- residence in the Member State concerned, as opposed to the actual tax situation of the taxpayer, cannot be the basis for taxing income in cross-border situations,[195]
- the linking of a tax benefit to meeting national legislative requirements makes the discrimination based on residence

[188] Para. 27, Case C-478/98 Commission v Belgium.
[189] See the prior authorization and notification/prior declaration case law, n. and n.
[190] Paras. 22-24, Case C-489/13 Verest.
[191] Paras. 28-31, Case C-282/12 Itelcar (here, in Member State–third country relations).
[192] Paras. 38-39, Case C-512/03 Blanckaert ECLI:EU:C:2005:516.
[193] Para. 23, Case C-181/12 Welte; para. 62, Case C-364/01 Barbier. Contrast with para. 46, Case C-513/03 Van Hilten.
[194] Inter alia, paras. 20-22, Case C-319/02 Manninen; para. 64, Case C-47/12 Kronos; paras. 44-55, Case C-375/12 Bouanich (established with reference to incoming investment and investors in other Member States); paras. 41-42, Case C-310/09, Accor (also in parent company–subsidiary relations).
[195] Para. 63, Case C-47/12 Kronos.

easier to establish;[196]

- it is not affected by the possibility that in certain cases the tax burdens can be reduced or eliminated,[197]

- the right to choose fixed levies when they lead to a favourable tax treatment of taxpayers compared to the normal rate of tax, which is only available in case of domestic investments, entails a discriminatory treatment of foreign investment possibilities,[198]

- the requirement of having a registered office in the Member State concerned is similarly problematic,[199]

- the requirement that the shares must have been in the continuous ownership of the same taxable person for longer than a year could also augment the restrictive nature of the tax discrimination,[200]

- proceeding under the double taxation convention could be irrelevant, as they must observe the equal treatment requirement inherent in Article 63 TFEU,[201]

- when the equal tax treatment of nationally- and foreign-sourced dividends is ensured, the Member States are free to determine different tax imposition methods (i.e. the exemption method and the imputation method) on dividends paid by a resident and a non-resident company,[202]

    - the different tax imposition methods will not lead to discriminatory treatment when the tax rates applied are equal and the tax credit provided 'is at least equal to the amount paid in the State of the company making the distribution, up to the limit of the tax charged in the Member State of the company receiving the dividends',[203]

    - in contrast, the different tax imposition methods will lead to unequal treatment, when the tax rates applied for nationally-sourced and foreign-sourced dividends are different and different levels of taxation occur by

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[196] Para. 40, Case C-190/12 Emerging Markets and paras. 29-32, Case C-493/09 Commission v Portugal ECLI:EU:C:2011:635.
[197] Para. 12.
[198] Paras. 22-24, Case C-334/02 Commission v France ECLI:EU:C:2004:129.
[199] Para. 41, Case C-190/12 Emerging Markets (it 'prevents non-resident investment funds from accessing the exemption from deduction of the tax at source, even though those dividends might possibly benefit from a lower tax rate under a double taxation convention.').
[200] Paras. 29-32, Case C-493/09 Commission v Portugal.
[201] Paras. 65-68, Case C-47/12 Kronos.
[202] Para. 66, Case C-47/12 Kronos.
[203] Ibid. In such circumstances, the Member States can decide to apply the imputation method for nationally-sourced dividends and the exemption methods for foreign-sourced dividends, para. 67, ibid.

reason of a change to the tax base as a result of certain exceptional reliefs,[204]

- nevertheless, the different tax imposition methods will not immediately cease to be equivalent when there is a difference between the nominal rate of tax and the effective level of taxation as that difference can be exceptional in nature (which is for the national court to determine),[205]
- when that difference is not exceptional, the application of the different tax imposition methods will lead to discriminatory treatment.[206]

The territorial restriction on the availability of tax advantages (e.g., tax exemptions, deduction of losses and other advantages) by not making them available for cross-border situations[207] or territorially determined tax burdens capable of reducing the value of cross-border transactions and subjecting them to higher tax liability (differentiated tax treatment),[208]

- linking tax exemption to immovable property being situated in the territory of the Member State concerned,[209]
- subjecting tax advantage on inheritance to the condition that the asset transferred is situated in the territory of the Member State concerned,[210]
- allowing the deduction of losses arising from the transfer of immovable property for property situated in the Member State concerned, which in any event cannot be considered as the consequence of two Member States exercising their parallel powers of taxation but of the Member State concerned exercising its taxation powers in a particular way,[211]
- applying in inheritance tax a different limitation period for the

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[204] Paras. 41-52, Case C-35/11 Test Claimants in the FII Group Litigation.
[205] Para. 49, Case C-35/11 Test Claimants in the FII Group Litigation.
[206] Paras. 51-52, Case C-35/11 Test Claimants in the FII Group Litigation.
[207] Paras. 20-21, Case C-133/13 Q ECLI:EU:C:2014:2460; paras. 19-27, Case C-87/13 X ECLI:EU:C:2014:2459; paras. 29-31 Case C-322/11 K.
[208] Measures whose effect is to reduce the value of a gift by a resident of a Member State other than that in which the property concerned is located and which taxes the gift of that property, para. 26, Case C-510/08 Mattner. See also paras. 17-24, Case C-181/12 Welte, inheritance tax allowance (tax-free allowance for the inheritance of immovable property) lower for residents of a third State than for those residing in the Member State concerned at the time of death: such linkage of tax benefits to residence in the Member State concerned leads to the transaction (succession) being subject to a higher tax liability than that applicable to transactions involving residents and, therefore, has the effect of reducing the value of that transaction.
[209] Paras. 20-21, Case C-133/13 Q. See also the preferential tax treatment offered to owners of listed historic buildings situated in the national territory condemned in paras. 19-27, Case C-87/13 X because it results in a difference in treatment between taxpayers ccording to whether or not they live in national territory, which is liable to deter taxpayers who live in a historic building situated in the territory of a Member State from carrying on their activities in another Member State.
[210] Paras. 28-35, Case C-256/06 Jäger ECLI:EU:C:2008:20.
[211] Paras. 29-31, Case C-322/11 K.

valuation of registered shares depending on the location of the issuing company's centre of effective management, when the longer limitation period affecting the heirs of investments made in another Member States by maintaining a longer period of uncertainty regarding the possibility of being subject to a tax adjustment.[212]

Subjecting the availability of a tax advantage to the States concerned having concluded an international convention on administrative assistance in taxation matters.[213]

Refusal to authorise the deduction from tax of gifts on the ground that the recipient public body or public institutions resides in another State.[214]

Imposing a flat-rate tax, which does not take into account fluctuations in the value of the investment or the length of time for which the investment is held, on capital gains made by non-resident taxpayer in the event of non-compliance with obligations of communication and publication laid down in national law,[215] and

- the taxpayer is not afforded the opportunity to produce evidence or information concerning the actual size of the income (procedural fairness),[216]
- it is not affected by the tax advantages that may be available when the tax is imposed,[217]
- communication and publication requirements are imposed in national law on taxpayers that are not active in the domestic market and do not actively target that market (these requirements are irrational (do not pursue genuine aims).[218]

A flat tax treatment of cross-border loans free of charge motor vehicles which does not take into account the duration of use of those vehicles, and

- the taxpayer is not afforded a right of tax exemption or a right to tax reimbursement when a vehicle is not used on a permanent basis.[219]

Using a mathematical formula for allowing the deduction of withholding tax paid in another Member State when determining income tax in the Member State concerned, which enables resident taxpayers to benefit from the tax allowances available but which

[212] Paras. 22-25, Case C-132/10 Olivier Halley.
[213] Paras. 26-29, Case C-72/09 Rimbaud.
[214] Paras. 21-27, Case C-10/10 Commission v Austria ECLI:EU:C:2011:399.
[215] Paras. 26-38, C-326/12 van Caster.
[216] Ibid.
[217] Para. 31, ibid.
[218] Paras. 34-37, ibid.
[219] Paras. 37-40, Joined Cases C-578/10 to C-580/10 van Putten.

fails to guarantee the same allowances when part of the income was received abroad,[220]

- when the tax allowances correspond with the lifestyle or the personal and family circumstances of the person concerned, it is the Member State of residence to take these into account when assessing the taxpayer's ability to pay tax, and the Member State in which the income originated may only be required to take these into account when the taxpayer receives almost all or all of his taxable income in that Member State and the Member State of residence is not in a position to calculate and grant him the advantages based on his personal and family circumstances.[221]

Imprecise determination of tax rate (when that is essential for calculating a tax credit so as to avoid double taxation) and using instead a simple estimate of the relevant rate,[222]

- in such a case, the Member State requiring the taxpayer to submit a certificate regulated in national law to initiate the granting of this tax credit, without any opportunity for the taxpayer of 'showing, by other factors and relevant information, the tax actually paid, constitutes a disguised restriction on the free movement of capital'.[223]

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[220] Paras. 36-42, Case C-168/11 Beker.
[221] Paras. 43-44, ibid.
[222] Para. 36, Case C-262/09 Meilicke. The difficulties that may arise in determining this or the tax actually paid cannot justify a restriction on the free movement of capital, para. 39, ibid and infra.
[223] Para. 40, ibid. See the similar conclusion reached in examining the proportionality of restrictions, infra.

4 Immunities and other delimitations of EU restrictions

The restrictions following from EU law on national policies and regulations are not absolute. The EU's competences may be explicitly limited, the circumstances of individual Member States or of individual cases may require the suspension of the normal operation of EU policies, or the political influence and power of the Member States may be relied upon to depart from the common obligations.

4.1 The principle of neutrality (regarding the regulation of ownership)

Incomplete immunity

Article 345 TFEU governing the impact of EU law on national property ownership regimes, in principle, enables the Member States to make the fundamental decisions regarding public and private ownership unfettered by interferences from EU obligations. Under this principle, the Member States are entitled – as a general rule – to decide on nationalising or privatising undertakings or economic sectors.[224] Regarding immovable property, it has been held that the Member States are entitled to establish systems 'for the acquisition of immovable property which lays down measures specific to transactions relating to agricultural and forestry plots.'[225] However, according to the jurisprudence of the EU Court of Justice, these decisions of the Member States must comply with the fundamental rules of the Treaties including Article 63 TFEU.[226] The policy or other rationales of Member State decisions affecting property ownership may be taken into account as an overriding reason in the public interest capable of justifying interferences with Treaty rules.[227] As a result, Article 345 TFEU can hardly be considered as providing genuine legal immunity for the Member States from their EU obligations. The regulation of national ownership regimes by the Member States – which has an impact on economic activity in the national and European markets – will be subjected to legal scrutiny under EU law and be rendered legitimate or illegitimate depending on its legal justifiability within usual framework of EU rules.

4.2 Emergency measures

[224] Paras. 29-31, Joined Cases C-105/12 to C-107/12 Essent.
[225] Para. 24, Case C-452/01 Ospelt.
[226] Paras. 33-37, Joined Cases C-105/12 to C-107/12 Essent. Relating to national systems governing the acquisition of immovable property, para. 24, Case C-452/01 Ospelt and paras. 28-31, Case C-515/99 Reisch.
[227] Para. 53, Joined Cases C-105/12 to C-107/12 Essent. This assessment can be deferred to the national court, para. 55, ibid.

As recognised explicitly by the EU policy maker, the liberalisation of capital markets cannot entail that the Member States and their economies are left defenceless against harmful, (exceptionally) large and volatile capital movements.[228] For this purpose, due to the silence of the Treaties on this matter, EU legislation was adopted, first, to harmonise national laws so as to ensure that the necessary measures are available to national authorities, and, second, to create the possibility for the Member States to introduce emergency measures restricting capital movements. The introduction of emergency measures, which is regulated distinct from the usual set of exemptions from Treaty obligations, is not within the discretion of the Member States.[229] Their separate regulation also means that their rationales – for example, the imminent breakdown of the national monetary system and the national economy as a result of volatile capital movements – are not available to justify Member State restrictions on capital movements under Article 65 TFEU. Because of their political sensitivity and also because of their socio-economic importance, the introduction of emergency measures could be subject to the political assessment of the Member States in the Council.[230]

Substantively and procedurally confined emergency measures

Their first regulation in the 1972 Capital Directive, which was adopted for the purpose of ensuring that Member State authorities are equipped with the appropriate means to address emergency situations, obliged the Member States to make instruments available to their 'monetary authorities' for the 'effective regulation of international capital flows' and for 'the neutralization of those effects produced by international capital flows on domestic liquidity which are considered undesirable' (Article 1).[231] It also provided that these instruments should be used, where necessary, with immediate effect without resorting to further enabling measures (Article 1).

The 1972 Capital Directive

The 1988 Capital Directive provided that Member State protective measures may only be introduced following the authorisation of the Commission, an

The 1988 Capital Directive

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[228] Infra

[229] It follows from Article 4 of the 1988 Capital Directive (This Directive shall be without prejudice to the right of Member States to take all requisite measures to prevent infringements of their laws and regulations, inter alia in the field of taxation and prudential supervision of financial institutions, or to lay down procedures for the declaration of capital movements for purposes of administrative or statistical information. Application of those measures and procedures may not have the effect of impeding capital movements carried out in accordance with Community law.).

[230] The revision clause in Article 3(5) of the 1988 Capital Directive enables the Council to examine whether the possibility of introducing emergency protective measures 'remain appropriate, as regards their principle and details, to the requirements which they were intended to satisfy.'

[231] The regulatory measures include: rules governing investment on the money market and payment of interest on deposit by non-residents, and the regulation of loans and credits which are not related to commercial transactions or to provisions of services and are granted by non-residents to residents (e.g., securities investments). The neutralisation measures include: the regulation of the net external position of credit institutions, and the fixing of minimum reserve ratios, in particular, for the holdings of non-residents.

authorisation which also extends to the conditions and details of the measure in question (Article 3(1)).[232] Before deciding on the authorisation, the Commission must consult the Monetary Committee and the Committee of Governors of the Central Banks. The Member States themselves may take protective measures only in case of urgency and only when it is necessary. The Member State introducing such measures is under an obligation to inform the Commission and the Member States,[233] and the Commission is empowered to override the assessment of the Member State concerned and to decide whether the measure in question can continue to be applied, should be amended, or should be abolished (Article 3(2)). Before deciding on the protective measure, the Commission must consult the Monetary Committee and the Committee of Governors of the Central Banks.

Both decisions of the Commission are subject to a political override in the Council which, acting by a qualified majority, may revoke or amend the Commission decision (Article 3(3)).

The Directive maximised the application of protective measures in 6 months (Article 3(4)).

4.3 Delimiting the temporal effects of judgments by the EU Court of Justice

Legal certainty

In principle, the Member States – having been found to have violated their obligations under Article 63 TFEU – may apply for the EU Court of Justice to restrict the temporal effect of its judgments. The rationale of this legal possibility is to protect – under the principle of legal certainty – legal relationships established by individuals in good faith during the non-compliant conduct of the Member State concerned. For the Member States, its benefit is that they may be able to avoid legal responsibility for their unlawful conduct prior to the date determined by the Court and they will be obliged to adjust their conduct to meet their EU obligations only following that particular date. It is allowed only exceptionally subject to the rather demanding dual condition that the persons affected have acted in good faith and that there is a risk of serious difficulties.[234]

The criteria

The Court of Justice has found that these two criteria are met when there was a 'risk of serious economic repercussions owing in particular to the large number of legal relationships entered into in good faith on the basis of rules considered to be validly in force' and individuals and Member State authorities had adopted practices in breach of EU law law 'by reason of

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[232] The scope of protective measures is restricted to capital movements indentified in Annex II of the Directive.

[233] At the latest, by the date of entry into force of the measure in question.

[234] Para. 37, Case C-292/04 Meilicke.

objective, significant uncertainty regarding the implications of European Union provisions, to which the conduct of other Member States or the Commission may even have contributed.'[235]

Limited to the actual judgment

The restriction may only be allowed in the actual judgment providing the interpretation requested by the national court.[236] This excludes that interpretations provided in earlier judgments and reaffirmed in a later judgment could be restricted at that later time. In the Court of Justice`s view the principle that a restriction may be allowed only in the actual judgment which provided that interpretation of law 'guarantees the equal treatment of the Member States and of other persons subject to Community law, under that law, fulfilling, at the same time, the requirements arising from the principle of legal certainty.'[237]

Burden of proof

The burden of proof rests on the Member State concerned. Following the legal test above, it needs to establish the following.

How the Commission and other Member States have specifically contributed to the objective, significant uncertainty regarding the implications of EU law,[238]

- in this regard, that the situation is different from when it is for the Member State to assess the compliance of its provisions with general rules of EU law, especially when the legal situation under the applicable legal test is rather straightforward in the particular case;[239]

That the Member State concerned actually risks incurring serious economic repercussions as supported by sufficient data,[240]

- in this regard, that the disadvantages go beyond the financial consequences (e.g. far-reaching consequences for the national budget) which might ensue for a Member State from a judgment from the EU Court of Justice.[241]

4.4 The temporal effect of Treaty obligations

The obligations laid down in the Treaties do not apply prior to the date of accession of the Member State concerned to the EU.[242] As to their impact on private law relationships (here, a registration of a mortgage taken out in a foreign currency) established before the date of accession of the Member State concerned, the Court of Justice held that the nullity of those

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[235] Para. 60, Joined Cases C-338/11 to C-347/11 Santander Asset Management.
[236] Paras. 36-37, Meilicke.
[237] Para. 37, ibid.
[238] Para. 61, Joined Cases C-338/11 to C-347/11 Santander Asset Management.
[239] Ibid.
[240] Para. 62, Joined Cases C-338/11 to C-347/11 Santander Asset Management
[241] Ibid.
[242] Para. 22, Case C-464/98 Stefan.

relationships, which under national law is absolute and incurable from the outset and operates to render such registration non-existent, cannot be remedied by the entry into force of EU law in a Member State.[243]

4.5 The flexible application of EU obligations

Differentiation

Article 63 TFEU has not been applied in the same way in every Member State. The flexible application of EU obligations in the area of the free movement of capital has led to differentiated integration in some domains of the European capital market. At different points of their EU membership, as part of the negotiation of their accession as recognised in the respective Acts of Accession[244] or in the Founding Treaties, or as a condition of the adoption of a piece of EU legislation, some Member States managed to negotiate a temporary preferential treatment of their regulation of capital movements.[245]

Hungarian derogations

For Hungary, these include two main derogations. Firstly, the broadly interpreted[246] cut-off date (31 December 1999)[247] set in Article 64(1) TFEU for Bulgaria, Estonia and Hungary for maintaining restrictions introduced with respect to 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. Secondly, the derogation in Annex X of the Treaty of Accession[248] (Point

[243] Paras. 23-24, ibid.

[244] See Case C-300/01 Salzmann where it was held that national provisions adopted after the date of accession are not, by that fact alone, automatically excluded from derogations laid down in the Act of Accession, and thus, 'if it is in substance identical to the previous legislation or if it is limited to reducing or eliminating an obstacle to the exercise of Community rights and freedoms in the earlier legislation, it will be covered by the derogation' (para. 54). This criterion of 'substantive identity' must be interpreted strictly and 'later legislation which is based on an approach which differs from that of the previous law and establishes new procedures cannot be treated as legislation existing at the time of accession' (a number of significant differences exclude the application of derogations laid down in the Act of Accession to measures adopted subsequently) (para. 55). This latter is for the national court to determine (para. 56).

[245] E.g., Spain, Portugal, Greece and Ireland, and also Belgium and Luxembourg, as recognised in Articles 5 and 6 of the 1988 Capital Directive. See also the exemptions and the transitional provisions of Directive 2003/48/EC. See Case 194/84 Commission v Greece ECLI:EU:C:1987:521 concerning the failure of Greece to comply with its gradual liberalisation obligations set out in a timeframe in its Act of Accession and rejecting claims that Greece had been discriminated against the other Member States and that the liberalisation obligations must be interepreted narrowly.

[246] According to the case law, these measures must be introduced before the date set in the Treaty (temporal condition) and in case they are adopted subsequently, they could be exempted in case they are, in essence, identical to the previous legislation (identical approach to regulating), or limited to reducing or eliminating an obstacle to the exercise of rights and freedoms established by EU law in the earlier legislation (material condition), paras. 47-52, Case C-190/12 Emerging Markets.

[247] The general cutoff date was 31 December 1993.

[248] OJ L236 (2003), 17-930.

3(2)) – subject to the general equal treatment principle[249] – allowing Hungary to 'maintain in force for seven years from the date of accession the prohibitions laid down in its legislation existing' at the time of the signing of the Act of Accession 'on the acquisition of agricultural land by natural persons who are non-residents or non-nationals of Hungary and by legal persons'. The conditions of this latter derogation are delineated below.

> The derogation does not apply to 'nationals of another Member State who want to establish themselves as self-employed farmers and who have been legally resident and active in farming in Hungary at least for three years continuously' and they must not be subject to 'any rules and procedures other than those to which nationals of Hungary are subject'.
>
> Based on the conditions laid down in the jurisprudence of the Court of Justice,[250] in case Hungary applies authorisation procedures for the acquisition of agricultural land during the derogation period 'they shall be based on objective, stable, transparent and public criteria' and the criteria must be applied 'in a non-discriminatory manner' and must not 'differentiate between nationals of the Member States residing in Hungary'.
>
> The derogation was regulated in a way that in the third year following the date of accession it was subject to a centralised general review by the Commission and the Council, which latter could have decided to shorten or terminate the derogation period.
>
> The maximum three year extension of the derogation period was also offered, which could be requested by Hungary from the Commission in case there is 'sufficient evidence that, upon the expiry of the transitional period, there will be serious disturbances or a threat of serious disturbances on the agricultural land market of Hungary'.[251]

4.6 Political override over EU obligations

Council powers

Having regard to the sensitive nature of capital movements liberalisation, the regulation of free movement of capital in the Treaties and in secondary legislation has always enabled the Member States – in a limited domain – to regain political control over their legal obligations laid down in the Treaties or concretised in individual procedures.

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[249] The derogation comes with the restriction that 'in no instance may nationals of the Member States or legal persons formed in accordance with the laws of another Member State be treated less favourably in respect of the acquisition of agricultural land than at the date of signature of the Accession Treaty' and that 'in no instance may a national of a Member State be treated in a more restrictive way than a national from a third country.'

[250] Infra.

[251] This was granted in 2011. The new legal conditions applicable after the 1 May 2014 date are reflected in Act 2013: CXXII on Agricultural Land which no longer excludes nationals of other Member States from the acquisition of agricultural land in Hungary (Section 9).

The avenues for recouping political control available in the current legal framework are delinated below.

Declaring the compatibility of national tax measures

The possibility in Article 65(4) TFEU for the Council to declare[252] – in an unanimous decision on application by a Member State – restrictive tax measures adopted by a Member State concerning third countries to be compatible with the Treaties, provided that they are justified by one of the objectives of the Union and compatible with the proper functioning of the internal market.

A step back from the liberalisation agenda

The possibility in Article 64(3) TFEU for the Council to adopt – following a special legislative procedure requiring unanimity and consulting the European Parliament – 'measures which constitute a step backwards in Union law as regards the liberalisation of the movement of capital to or from third countries'.

The override of unilateral emergency measures

The political override in Article 3(3) of the 1988 Capital Directive by the Council of Commission decisions concerning authorised and notified protective emergency measures.

4.7 The Member State acting in a private capacity

The State as a private operator

In principle, EU obligations may not apply when the Member State acts in its capacity as a private operator instead of acting in its capacity as a public authority.[253] In case of regulatory measures implementing public policy, this is nearly impossible to establish, even when they 'regulate the tax aspects of the loan to be contracted' by the Member State concerned.[254] Claims made by the Member States as to them acting in their capacity as a private operator (e.g., acting as a borrower and agreeing on a contractual term with the financial intermediaries) must be genuine and be made out adequately.[255] Introducing changes affecting the free movement of capital through modifying an undertaking's articles of association will not qualify as a 'normal operation of company law' and will not render the Member State acting as a private operator when that modification was to be approved by a government minister.[256] In other words, the introduction of special shares

[252] In the absence of measures pursuant to Article 64(3), the Commission or, in the absence of a Commission decision within three months from the request of the Member State concerned.

[253] Raised by Belgium in Case C-478/98 Commission v Belgium.

[254] Paras. 22-24, ibid.

[255] Para. 26, ibid, the State regulating the terms of loans in statutes is unlikely to be regarded as being similar to a private borrower negotiating a contractual condition.

[256] Para. 78, Case C-98/01 Commission v UK.

into the memorandum and articles of association of privatised corporation as a result of decisions taken by the Member State concerned with a view to reserving a certain number of special rights under the companies' statutes is a State measure.[257]

[257] Para. 22, Case C-282/04 Commission v Netherlands.

5 Exemptions from Treaty obligations

Safeguarding national policies

The system of exemptions available in the Treaties, as developed and interpreted in the jurisprudence of the EU Court of Justice, enables the Member States to safeguard national policies and regulations from the prohibitions included in Article 63 TFEU. The exemptions which the Member States can rely upon are filtered and moderated by EU law accepting only those as legitimate which contribute in an adequately regulated and governed manner to establishing and maintaining a balanced and sustainable integrated capital market in Europe. In case EU legislation was adopted to cover the particular matter (e.g., cross-border administrative cooperation), the possibilities for the Member States to raise the same or similar concerns in support of national measures or unilateral conduct contradicting Treaty prohibitions will necessarily be narrower.

Legal benchmarks

When the Member States aim to pursue policies within the framework of exemptions, they need to take into account a number of general and more concrete benchmarks developed in the jurisprudence. Primarily, they need to observe that the general principle governing the use of exemptions, which are different in the different contexts where the free movement of capital is applicable and which comes with qualifications and conditions affecting its application, are met. The Member States must also ensure that the ground of exemption raised will be deemed as genuine and legitimate and that the national measure and its application are necessary and proportionate. As to the more concrete benchmarks, the Member States are prevented from adopting measures and procedures which constitute means of arbitrary discrimination (equal treatment) or which in disguise undermine the prohibitions laid down in Article 63 TFEU (no frustration of EU policy).

5.1 The general principle

As a general principle, restrictions on the free movement of capital must be justified either under the grounds mentioned in Article 65 TFEU or on the basis of overriding reasons in the public interests as recognised by the jurisprudence of the EU Court of Justice.[258] Article 65 TFEU recognises the following rights of the Member States.[259]

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[258] Inter alia, para. 63, Case C-375/12 Bouanich; para. 44, Case C-181/12, Welte; para. 32, Case C-282/12 Itelcar; para. 49, Joined Cases C-197/11 and C-203/11 Libert.

[259] See the interprteation of the similarly worded provisions of the 1988 Directive in paras. 20-28, Case C-358/93 Bordessa emphasising that (a) measures designed to prevent illegal activities of comparable seriousness, such as money laundering, drug trafficking or terrorism can be permitted, (b) prior authorisation obligations may represent an excessive interference as it may entail the unconstrained use of discretion by national authorities, and (c) prior declaration obligations are acceptable interferences on account of their low degree of

To apply the 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.

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 financial institutions.

To lay down procedures for the declaration of capital movements for purposes of administrative or statistical information.

To take measures which are justified on grounds of public policy or public security.

General benchmarks

The general principle is qualified by the general fundamental benchmarks[260] that the Member States are required to observe the fundamental equal treatment principle (Article 65(3) TFEU on arbitrary discrimination), that they have to avoid frustrating the free movement of capital (Article 65(3) TFEU on disguised restrictions), and that they have to exercise their discretion in defining the objectives in the public interest they wish to promote in accordance with EU law.

Further benchmarks qualifying the application of the general principle include the principles below.

Abuse of exemptions

Abusive uses of the exemptions must be avoided, especially that the national measure in question must serve the interest claimed and not a different interest,[261]

- this also means that the Member States must strictly separate the different grounds of justification and address the distinct ground adequately without mixing the arguments relevant for the respective grounds.[262]

Breach of logic and effectiveness

The logic of the applicable provisions must not be contradicted and the principle of the free movement of capital must not be deprived of any practical effect when the exemptions are used,[263]

- for instance, the aims of effective fiscal supervision or the

restrictiveness. Combatting tax evasion and the effectiveness of fiscal supervision were recognised as objectives available for the Member States to pursue in para. 38, Case C-478/98 Commission v Belgium.

[260] Para. 32, Case C-10/10, Commission v Austria and supra.

[261] Para. 46, Case C-296/12 Commission v Belgium ECLI:EU:C:2014:24.

[262] Paras. 65-67, Case C-190/12 Emerging Markets, essentially the limited terrirorial scope of EU law is the cause of the unlawful differentiated tax treatment introduced in national law.

[263] Ibid. See also para. 34, Case C-439/97 Sandoz arguing that the objective of equal treatment of taxpayers is in fact undermined by the discriminatory imposition of a duty on foreign- and domestically-contracted loans.

effective collection of tax cannot be raised when the national measure preventing taxpayers from submitting evidence or information to establish his taxable income contradicts that aim.[264]

Excessive restrictions

Excessively restrictive interferences are likely to be denied justifiability by way of an exemption, either when examining the legitimacy of the ground raised or during the examination of the necessity of the interference.[265]

Lack of EU measures

As a further qualification to the application of the general principle, which follows from the logic of regulating the Single Market and which is taken into account when examining the ground raised by the Member State concerned,[266] exemptions are allowed only 'to the extent that there are no harmonising measures at the European Union level ensuring the protection of those interests'.

Context specific interpretations

The general principle has been interpreted to represent different possibilities in different environments and it has been supplemented in judicial interpretation by further general conditions specific to the particular context. Distinct interpretations of the general principle have emerged in the three different areas of potential restrictions under Article 63 TFEU.

Tax discrimination and objective comparability

Under Article 65(1)a concerning differentiated tax treatment, the national measure must relate to situations 'which are not objectively comparable, such comparability being required to be assessed on the basis of the object and content of the national provisions at issue in the main proceedings',[267]

- this is supported by the general distinction recognised in the jurisprudence between permissible unequal tax treatments and practices of discrimination that are prohibited under Article 65(3) TFEU,[268]
- this possibility must be interpreted strictly, and 'it cannot, therefore, be interpreted as meaning that all tax legislation which draws a distinction between taxpayers on the basis of their place of residence or the Member State in which they invest their capital is automatically compatible with the Treaty'.[269]

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[264] Para. 57, Case C-326/12 van Caster.
[265] Para. 81, Case C-387/11 Commission v Belgium; para. 49, Case C-326/12, van Caster; paras. 44-45, Case C-493/09, Commission v Portugal.
[266] Para. 32, Case C-282/04 Commission v Netherlands.
[267] Para. 22, Case C-133/13, Q; para. 27, Case C-87/13 X; para. 44, Case C 181/12, Welte.
[268] Para. 63, Case C-375/12 Bouanich; para. 44, Case C-181/12, Welte; para. 45, Case C-387/11 Commission v Belgium.
[269] Inter alia, para. 42, Case C-181/12, Welte; para. 43, Case C-387/11 Commission v Belgium; paras. 25-26, Case C-489/13 Verest; para. 55, Case C-190/12 Emerging Markets.

Tax discrimination and public interest grounds

Under Article 65(1)b and under overriding reasons in the public interest concerning differentiated tax treatment, the national measure must be appropriate for ensuring the attainment of the objective in question and must not go beyond what is necessary to attain it,[270]

- this possibility is available where there are no harmonising instruments of EU law providing for measures necessary to ensure the protection of those public interest grounds.[271]

Indistinctly applicable measures and public interest grounds

Under Article 65(1)b and under overriding reasons in the public interest concerning indistinctly applicable (regulatory) measures,[272] the national measure must be appropriate for ensuring the attainment of the objective in question and must not go beyond what is necessary to attain it.[273]

The jurisprudence has also indicated a number of special conditions applicable in the interpretation of the general principle. These are delinated below.

Specific benchmarks

Connected advantages

Unfavourable tax treatment differentiating between domestic and cross-border transactions violating a fundamental freedom cannot be regarded as compatible with EU law because of the existence of other connected advantages, even when such advantages are assumed to exist,[274]

- in particular, a Member State cannot rely on the existence of a tax advantage granted unilaterally by another Member State in order to escape its obligations under the Treaty.[275]

Tax burdens imposed outside jurisdiction

The Member States can be held liable under EU law for tax burdens imposed outside of their jurisdiction (i.e., in another Member State) when the unfavourable tax treatment differentiating between domestic and cross-border transactions follows from the parallel application of the tax rules – affected by a double taxation convention – of the Member State concerned and of the other Member State involved.[276]

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[270] Inter alia, para. 65, Case C-375/12 Bouanich; para. 44, Case C 181/12 Welte; para. 74, Case C-387/11, Commission v Belgium.
[271] Para. 74, Case C-387/11 Commission v Belgium.
[272] Measures capable of hindering the exercise of fundamental freedoms guaranteed by the FEU Treaty or of making it less attractive.
[273] Inter alia, para. 32, Case C-296/12 Commission v Belgium; para. 32, Case C-282/12 Itelcar; para. 49, Joined Cases C-197/11 and C-203/11. Libert.
[274] Para. 53, Case C-387/11 Commission v Belgium.
[275] Para. 69, Case C-11/07 Eckelkamp.
[276] Paras. 55-56, Case C-387/11 Commission v Belgium.

Offset by double taxation conventions

Unfavourable tax treatment differentiating between domestic and cross-border transactions cannot be offset by double taxation conventions alone, unless the application of such a convention allows the effects of the difference in treatment under national legislation to be compensated for,[277]

- this is not the case when the double taxation convention, instead of excluding the domestic taxation of foreign income, imposes a tax comparable to that applicable in domestic law for foreign, but not for domestic income.[278]

Equal treatment principle

When the unfavourable tax treatment differentiating between domestic and cross-border transactions is examined on the basis of the general equal treatment principle the legal test could be similar to that pursued when justifying exemptions from Article 63 TFEU, which would involve considering

- whether in the circumstances of the actual case the situation of the different tax subjects is objectively comparable, and
- 'whether they were treated equally',
- 'or, if they were treated differently, whether the difference was justified by an overriding reason in the general interest',
- 'and, finally, whether the measure at issue is consistent with the principle of proportionality';[279]

Administrative burdens and disadvantages

The administrative burden on the Member State concerned complying with EU obligations and any related administrative disadvantage (e.g., when the taxpayers must be provided a legal opportunity to submit evidence capable of demonstrating their actual income) are not alone sufficient to justify imposing a barrier to the free movement of capital.[280]

Burden of proof

The burden of proof rests on the Member State concerned.[281] The relevant requirements also indicate – as benchmarks for national regulation – how the Member States should prepare and design their measures in case they aim to secure its justifiability as an exemption. In the formulation of the

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[277] Para. 34, Case C-342/10 Commission v Finland.
[278] Para. 34, ibid.
[279] Paras. 42-44, Joined Cases C-578/10 to C-580/10 van Putten.
[280] Para. 56, Case C-326/12 van Caster; para. 54, Case C-319/02 Manninen. It would enable the Member States to jeopardise unilaterally the uniform and effective application of EU law in the Union, and they would be able to rely on their own misconduct to avoid meeting their legal obligations.
[281] This also applies when the Member State wants to rely on Article 106(2) TFEU to establish that Article 63 TFEU will jeopardise the performance of tasks of general economic interest, para. 82, Case C-463/00 Commission v Spain.

jurisprudence, the national authorities must be able to show in each individual case when they adopt a measure in derogation from EU law that the national measure is appropriate and proportionate and that this is substantiated by specific evidence.[282]

However, as it follows from the system and the purpose of the exemptions allowed, the Member States are entitled to verify the nature and reality of transactions and transfers in question 'with a view to satisfying themselves that such transfers will not be used' for the illicit purposes indicated in Article 65 TFEU.[283] This implies that Member State restrictions implemented for this aim are likely to be found necessary and proportionate.[284]

Public policy and security

As to the use of the public policy and public security ground,[285] the Court of Justice in *Église de Scientologie* maintained

that while Member States are still, in principle, free to determine the requirements of public policy and public security in the light of their national needs, those grounds must, in the Community context and, in particular, as derogations from the fundamental principle of free movement of capital, be interpreted strictly, so that their scope cannot be determined unilaterally by each Member State without any control by the Community institutions (…). Thus, public policy and public security may be relied on only if there is a genuine and sufficiently serious threat to a fundamental interest of society (…). Moreover, those derogations must not be misapplied so as, in fact, to serve purely economic ends (…). Further, any person affected by a restrictive measure based on such a derogation must have access to legal redress (…).[286]

5.2 The legitimacy of the exemption

Close scrutiny of exemptions

In the law of the free movement of capital, the legitimacy of exemptions claimed by the Member States – foremost in connection with national fiscal (tax) measures – receives a close scrutiny by the EU Court of Justice. The intensity and high detail of the legal benchmarks addressed to the Member

[282] Para. 33, Case C-296/12 Commission v Belgium.
[283] Para. 37, Joined Cases C-163, C-165 and C-250/94 Sanz de Lera. See also paras. 31 and 33, Joined Cases 286/82 and 26/83 Luisi and Carbone.
[284] See para. 38, Joined Cases C-163, C-165 and C-250/94 Sanz de Lera.
[285] E.g., the safeguarding of supplies of petroleum products in the event of a crisis and ensuring a minimum supply of petroleum products at all times, para. 47, Case C-483/99 Commission v France and para. 46, Case C-503/99 Commission v Belgium; safeguarding supplies in the petroleum, telecommunications and electricity sectors in the even of a crisis, para. 71, Case C-463/00 Commission v Spain. However, it must be established that the measure in question is capable of securing the public security interest, para. 40, Case C-174/04 Commission v Italy (suspending the voting rigths of shareholders is not a suitable measure).
[286] Para. 17, Case C-54/99 Église de Scientologie. See also para. 48, Case C-483/99 Commission v France and para. 47, Case C-503/99 Commission v Belgium, and para. 72, Case C-463/00 Commission v Spain

States follow from the highly technical nature of some of the grounds of exemption and also from the need to avoid an overly extensive, possibly abusive interpretation of some of the more general grounds. Despite the explicit recognition of the general discretion available to the Member States to regulate the relevant matters,[287] the choices of the Member States are closely tested. This ensures that Member State restrictions are imposed for the permitted objectives only, that the permitted objectives are taken seriously by the Member States, and that the national measures will actually deliver the declared legitimate outcome. With this, EU law interferes rather intensively with Member State autonomy in areas where the Member States recognisably enjoy the general competence to regulate and develop policies.

A generous list

In defining the objectives which could be legitimately pursued by Member State action, the law has been generous. It has recognised a broad range of general and specific objectives and the general conditions they are expected to satisfy are not particularly strenuous. In principle, the Member States can rely on the objectives listed in Article 65 TFEU, the objectives related to the operation of national tax systems, and other overriding reasons in the public interest.

Taxation objectives

The objectives relating to the operation of national tax systems ensure that in the integrated European capital market the fiscal sovereignty and taxation powers of the Member States are not undermined unduly. These specific objectives include the ones listed below.

Preserving the coherence of the tax system.[288]

Safeguarding the balanced allocation of powers of taxation between the Member States.[289]

Ensuring effective fiscal supervision.[290]

Combating tax avoidance and tax evasion (separately from effective supervision).[291]

Effective collection of tax.[292]

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[288] Inter alia, para. 69, Case C-375/12 Bouanich; para. 35, Case C-296/12 Commission v Belgium.
[289] Inter alia, para. 81, Case C-375/12 Bouanich; para. 75, Case C-387/11 Commission v Belgium.
[290] Inter alia, para. 42, Case C-296/12 Commission v Belgium; para. 71, Case C-190/12 Emerging Markets; para. 63, Case C-181/12 Welte.
[291] Inter alia, para. 34, Case C-282/12 Itelcar; para. 30, Case C-132/10 Olivier Halley.
[292] Para. 46, Case C-326/12 van Caster.

The following general public interests grounds have been examined in the jurisprudence of the EU Court of Justice.

General objectives

Guaranteeing the stability and security of assets invested or available for investment (e.g., by means of prudential rules).[293]

Requirements relating to social housing policy.[294]

Financial equilibrium of national social security systems.[295]

Decisions on the public or private ownership of public service sectors,[296]

- certain concerns' relating to undertakings that were initially public and subsequently privatised, where those undertakings are active in fields involving the provision of services in the public interest or strategic services (in golden shares cases);[297]

- the undertakings affected must, however, serve the objective of providing public services and the Member State must establish – instead of referring to certain lines of business which in the past had some public connections – that there are particular circumstances as a result of which the undertakings concerned take 'responsibility for a public-service function.'[298]

Promoting national training and education.[299]

National cultural policy intending to safeguard, in the audio-visual sector, the freedom of expression of various beliefs and viewpoints.[300]

National media policy aiming to create a pluralistic and non-commercial broadcasting system.[301]

Protection of national (natural, historical and cultural) heritage (even against the interests of individuals, such as owners).[302]

National agricultural policy priorities, town and country planning objectives and the related agricultural land use objectives.[303]

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[293] Para. 31, Case C-39/11 VBV.
[294] Para. 52, Joined Cases C-197/11 and C-203/11 Libert.
[295] Para. 36, Case C-39/11 VBV.
[296] Para. 53, Joined Cases C-105/12 to C-107/12, Essent.
[297] Para. 47, C-367/98 Commission v Portugal; para. 43, Case C-483/99 Commission v France; para, 43, Case C-503/99 Commission v Belgium; para. 66, Case C-463/00 Commission v Spain; para. 38, Case C-282/04 Commission v Netherlands.
[298] Para. 70, Case C-463/00 Commission v Spain.
[299] Para. 38, Case C-10/10 Commission v Austria.
[300] Para. 9, Case C-148/91 VVOO ECLI:EU:C:1993:45.
[301] Ibid.
[302] Para. 24, Case C-133/13 Q; para. 29, Case C-87/13 X.

Ensuring undistorted competition on liberalized (public service) markets,

- combating cross-subsidisation in order to achieve transparency in markets,[304]
- preventing distortions of competition.[305]

Guaranteeing adequate investment in liberalized (public service) markets,

- combating cross-subsidisation,[306]
- energy security.[307]

Energy security,

- as a result of guaranteeing adequate investment.[308]

Consumer protection,[309]

- as a result of guaranteeing fair and undistorted competition,[310]
- the protection of beneficiaries of payments under a severance fund in their capacity as consumers.[311]

Reluctance to accept grounds

Despite the Court's openness to recognising numerous potential grounds for exemptions, the ability of the Member States to justify their measures and policies has been rather limited owing to the Court's reluctance to accept the grounds raised as legitimate.[312] This may follow from the actual ground raised which in the EU context may be impossible to accept (e.g., the administrative burdens of compliance with EU law, the difficulties of cross-border administration when EU instruments are available to facilitate administrative cooperation among the Member States, the economic nature

[303] Para. 27, Case C-370/05 Festersen and infra n.
[304] Para. 56, Joined Cases C-105/12 to C-107/12 Essent, including the prevention of exchanging strategic information.
[305] Ibid.
[306] Ibid.
[307] Para. 59, ibid. See also paras. 34-35, Case 72/83 Campus Oil; para. 46, Case C-503/99 Commission v Belgium; para. 41, Case C-174/04 Commission v Italy.
[308] Ibid.
[309] Para. 58, ibid.
[310] Ibid.
[311] Para. 35, Case C-39/11 VBV.
[312] This is a general trend in the past couple of decades in the free movement jurisprudence with the Court of Justice regarding itself empowered to examine the substance of the justification, see C. Barnard, 'Derogations, justifications and the four freedoms: is State interest really protected?', in C. Barnard and O. Odudu, *The Outer Limits of European Law* (Hart, 2009), 273-305, 281.

of the interest protected, or the reduction of state revenues). Often, the Member States are unable to satisfy the general and specific conditions laid down in the jurisprudence. However, this does not mean that the Member States would not be granted opportunities to regulate matters that are close to their interests. For example, the developments in the jurisprudence concerning the aim of guaranteeing a balanced allocation of taxation powers among the Member States allows the Member States to maintain bilateral tax agreements to determine the respective boundaries of their taxation powers and to ensure that economic double taxation is avoided.

Fundamentally incompatible grounds

The jurisprudence excludes specific grounds as being capable of justifying restrictions of the free movement of capital. This is in harmony with the general understanding of the law on the free movement of capital that only such Member State conduct will be supported which contributes to maintaining a balanced and sustainable integrated European capital market. It is also in accordance with the general legal benchmarks of Member State conduct under Article 63 TFEU (e.g., no frustration of EU policy).

Purely economic grounds

In particular, the law will not accept 'grounds of purely economic nature.'[313] This entails that public policy and public security grounds must not serve purely economic ends,[314] but reasons of an economic nature in the pursuit of an objective in the public interest may be legitimate.[315]

Grounds supporting EU policy

Confining legitimate Member State measures to those which support EU policy also appeared elsewhere in the jurisprudence. In *Essent*, the EU Court of Justice following the economic model designed for electricity markets by the EU legislator established that the aim of consumer protection will be examined as achievable through guaranteeing fair and undistorted competition in the market.[316] The Court's approach implied that means of consumer protection that may be incompatible with this model will not be considered as legitimately contributing to the consumer protection objective.

The diminution of tax revenue

The diminution of tax revenue[317] was refused as an overriding reason in the public interest in similar circumstances.[318] The Court found that the Member

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[313] Para. 51, Joined Cases C-105/12 to C-107/12 Essent; para. 52, Case C-367/98 Commission v Portugal; para. 37, Case C-174/04 Commission v Italy (competitiveness of a sector) and para. 50, Case C-436/00 X and Y (general financial interests of a Member State).

[314] Para. 29, Case C-39/11 VBV.

[315] Para. 52, Joined Cases C-105/12 to C-107/12 Essent.

[316] Para. 58, ibid.

[317] The Member States may try to distinguish this from the erosion of the national tax base which they regard as an objective with higher legitimacy under the EU framework, which attempts are normally rejected by the Court of Justice as the Member State fail to establish the difference between the two grounds, para. 42, Case C-168/01 Bosal ECLI:EU:C:2003:479. See also general fiscal interests excluded as legitimate grounds, supra n.

[318] Para. 59, Case C-35/98 Verkooijen [2000] ECR I-4071; para. 50, Case C-436/00 X and Y (a purely economic ground); para. 102, Case C-190/12 Emerging Markets.

States surrendering tax revenue to other Member States is a characteristic of an open and integrated capital market where conventions are adopted between the Member States to prevent double taxation.[319] It also held that the free movement of capital does not exclude the Member States taxing domestically-sourced incomes and abandoning, in the longer term, the prevention of double taxation by eliminating situations where double taxation may arise.[320] In another case, the Court explained that the free movement of capital necessarily implies that taxable income will leave the territory of the Member State concerned which will in turn reduce its ability to raise income for domestic public institutions through taxation.[321] Generally, the loss of revenue or the erosion of the domestic tax base resulting from compliance with EU obligations never received much sympathy from the Court of Justice as, in principle, it would enable the Member States to claim an exemption anytime the correct application of EU law entails costs at the national level.[322]

Comparing tax systems

The Court of Justice would also reject claims that the level of taxation in other Member States needs to be taken into account when assessing the compatibility of national tax legislation maintaining a differentiated tax treatment of foreign- and domestically sourced incomes.[323] Claims that restrictions on the free movement of capital could be compensated, for instance, by extending national tax legislation to foreign-sourced incomes to make foreign investment more attractive to resident taxpayers or by offering them tax advantages are also rejected.[324]

Trespassing into EU policy areas

The overlap of the public interest objective raised by the Member State concerned with parallel areas of EU policy could reduce its acceptability. The promotion of learning, teaching and research by one of the Member States – through national tax legislation channelling donations to institutions established in the national territory – was regarded with considerable suspicion when submitted as a legitimate public interest ground.[325] Ultimately, it was unacceptable on account of the national policy contradicting the aims of the EU policy in the same area.[326] Here, Member State action was not excluded because it was liable to undermine the EU

[319] Para. 103, ibid.
[320] Ibid.
[321] Paras. 39-40, Case C-10/10 Commission v Austria.
[322] A.P. Dourado and R. da Palma Borges (eds.), *The Acte Clair in EC Direct Tax Law* (IBFD, 2008), 87-88.
[323] Paras. 41-42, Case C-315/02 Lenz.
[324] Para. 43, ibid. See the principle that unfavourable tax treatment contrary to a fundamental freedom cannot be justified by the existence of other tax advantages, even supposing that such advantages exist, para. 61, Case C-35/98 Verkooijen and infra n.
[325] Paras. 32 and 34, Case C-10/10 Commission v Austria.
[326] Para. 37, Case C-10/10 Commission v Austria which is to promote fiscal cooperation among the Member States and not the national promotion of domestic policies through fiscal means.

policy on the free movement of capital, a policy which should acknowledge that capital movements may jeopardise the efforts of the Member States to raise funds to finance education and research. Instead, it was rejected because it unduly interfered with the EU's education and research policy objectives.

Synergies with EU policy areas

Conversely, synergies between the Member State justification raised and the objectives pursued by the EU measures regulating the area can enhance the acceptability of the public interest ground raised by the Member State concerned.[327] In *Essent*, the objectives of ensuring undistorted competition and guaranteeing investment in liberalised (public service) markets were accepted on the following grounds. Firstly, they followed from the objectives of the corresponding area of EU law as laid down in the case law and they corresponded with what the jurisprudence recognised as relevant public interest grounds. Secondly, they emerged as objectives pursued at the national level on account of the Member State concerned having implemented the relevant pieces of EU legislation.[328] However, the lack of such synergies, especially when an EU policy framework is missing or when the national policy objectives are at odds with the general EU policy framework, can lead to the rejection of the justification.[329]

Tax territoriality

Member State claims based on tax territoriality are generally rejected by the Court of Justice.[330] While developing national tax regimes on the basis of this principle, which would confine the exercise of tax jurisdiction to the territory of the state concerned, falls within the competence of the Member States, they are prevented from relying on the fiscal territoriality principle in order to defend a discriminatory tax treatment of foreign sourced incomes. Often, the national measure would have no connection with the principle and the principle would only be invoked to cover up a breach of the equal treatment principle. The jurisprudence also takes into account the fact that the allocation of tax jurisdiction among the Member States as well as the avoidance of double taxation among them are regulated by a network of international double taxation conventions and connected national measures.

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[327] See para. 40, Case C-452/01 Ospelt emphasising the synergies between the CAP and local policy on agricultural land use.

[328] Paras. 58-65, Joined Cases C-105/12 to C-107/12, Essent. Contrast with para. 45, Case C-471/04 Keller ECLI:EU:C:2006:143 where the argument that the national measure constituted an implementation of an EU directive was rejected as the Member States are obliged in the implementation of directives to observe their Treaty obligations.

[329] See para. 52 Case C-367/98 Commission v Portugal and para. 37, Case C-174/04 Commission v Italy concerning national economic policy objectives, namely, choosing a strategic partner, strengthening the competitive structure of the market concerned or modernising and increasing the efficiency of means of production. It is difficult to see how these are different from the instance when similar national economic policy grounds would be embraced by the available EU policy framework and would support their acceptability.

[330] The lack of a reference to territoriality in the directive applicable in the case may also support such a refusal, para. 41, Case C-168/01 Bosal.

In *Manninen*, the Court of Justice held that national tax legislation denying the equal treatment of foreign- and domestically-sourced incomes – through the equal provision of grant tax advantages – cannot be regarded as an emanation of the principle of territoriality, a principle which does not in fact preclude the granting of a tax advantage to foreign-sourced incomes.[331] The Court of Justice added that, in any event, the tax territoriality principle cannot be invoked to justify discriminatory tax measures.[332] The same prohibition was expressed in the formula that the principle of tax territoriality cannot be relied upon when the objective comparability of the taxpayers has been established.[333] However, when the equal treatment of taxpayers is ensured national measures which do in fact conform with the fiscal principle of territoriality (e.g., taxing non-resident taxpayers on profits and losses arising from their activities in the Member State concerned while taxing resident taxpayers irrespective of where their activities have been carried out) may be accepted as legitimate.[334]

The conditions

The specific conditions which must be observed by the Member States in case they want to ensure that the objectives pursued by national policies and measures are legitimate are delinated below.

The requirement that the legitimate aim pursued must be visible from the measure in question (expressly stated and/or can be inferred from individual provisions).[335]

The requirement that the legitimate aim must be the actual objective of the measure in question,[336]

- which must be the particular aim of the particular measure not the general aim of the general legal framework.[337]
- which must not be an aim pursued in a measure addressed to other individuals,[338]

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[331] Para. 38, Case C-319/02 Manninen. The national measure must be an application of that principle and discrimination in the taxation and in the granting of tax benefits of parent companies and subsidiaries established in different Member States does not qualify as such, para. 44, Case C-471/04 Keller.
[332] Para. 39, Case C-319/02 Manninen.
[333] Paras. 45-47, Case C-342/10 Commission v Finland.
[334] Paras. 20-22, Case C-250/95 Futura [1997] ECR I-2471 (under the freedom of establishment). The facts of the case and the national measure in question do have specific relevance in this regard as relying on Futura can be denied on account of distinguishing cases on their facts (i.e., primarily, whether the measure concerned tax territoriality or introduced tax differentiation with regards a certain cross-border element), paras. 38-40, Case C-168/01 Bosal.
[335] Paras. 24-26, Case C-133/13, Q; paras. 29-31, Case C-87/13 X.
[336] Para. 69, Case C-375/12 Bouanich.
[337] Ibid. and para. 30, Case C-39/11 VBV.
[338] Para. 30, Case C-39/11 VBV concerning national provisions providing the substantive content of the prudential rules applicable to investments, but not in any way whatsoever

- which aim must be pursued by a measure which belongs to an area of national law or policy dedicated to achieving that aim.[339]

The requirement that the legitimate aim must be correctly determined and that the abuse/extension of the grounds available for justification, in order to include aim which may be illegitimate or fall under a different ground, must be avoided.[340]

The requirement that there must be a direct relationship between aim and measure meaning that the measure is an appropriate means of attaining the aim (covering issues belonging to the necessity test).[341]

The requirement when the public policy and public security ground is raised that there must be a genuine and sufficiently serious threat to a fundamental interest of society.[342]

5.2.1 The legitimacy of the individual grounds of exemption

In the following, the conditions developed in the jurisprudence of the EU Court of Justice concerning the legitimacy of the individual grounds of exemption relied upon by the Member States are examined. The close judicial scrutiny of this matter has resulted in further benchmarks and signposts which Member State policy making and regulation needs to take into account.

5.2.1.1 Objective comparability in taxation

Strict intepretation

This ground enables the Member States to introduce and maintain differentiation in the tax treatment of different taxpayers on the basis of objective differences in their circumstances.[343] The objective comparability of the situation of taxpayers renders their differentiated tax treatment a breach of the equal treatment principle and of the Treaty prohibition in Article 65(3) TFEU on arbitrary discrimination.[344] The exemption 'must be

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designed to prevent infringement of the laws and regulations in the field of the prudential supervision of financial institutions.

[339] The Member State cannot rely on the objective of securing the financial equilibrium of national social security systems when the national scheme in question cannot, notwithstanding its social objective, be regarded, in the light of EU law, as forming part of the social security system of a Member State, para. 36, Case C-39/11 VBV.

[340] Xref to effective fisc supervision

[341] Para. 35, Case C 282/12 Itelcar. See also paras. 31-32, Case C-222/97 Trummer and Mayer; paras 39, Case C-279/00 Commission v Italy.

[342] Para. 29, Case C-39/11 VBV.

[343] It was raised that this provision could enable Member States to adopt tax measures that by favouring inward domestic investment would qualify as unlawful state aid under Article 107 TFEU, which issue, however, has not been litigated before the Court of Justice, Usher (2006), 199.

[344] There is a distinction between unequal treatment which is permitted under this derogation and arbitrary discrimination prohibited by the Treaties: tax differentiation is permitted when the difference in treatment concerns situations which are not objectively comparable or it is

interpreted strictly, cannot be interpreted as meaning that any tax legislation making a distinction between taxpayers by reference to the place where they invest their capital is automatically compatible with the Treaty.'[345] The focus of the Court's assessment is whether the persons concerned are in a similar factual situation as a matter of the applicable law.[346] Any further logical explanations for not offering the same taxation possibilities (e.g., deductions from taxable amount) will not be accepted.[347]

Residence as a distinguishing factor

In particular, as has been mentioned earlier, the Member States are prevented from relying on the place of establishment (or residence) of the persons concerned (taxpayers) as a valid criterion when distinguishing between them in tax law.[348] Therefore, they must be able to identify an objective distinguishing criterion between the persons concerned other than their place of establishment or residence.[349] The Member States need to be circumspect in their regulatory efforts as the EU Court of Justice will only accept[350] the relevant distinguishing criteria established by the national tax

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justified by overriding reasons in the general interest, and the difference in treatment does not go beyond what is necessary in order to attain the objective of the legislation, para. 29, Case C-319/02 Manninen and paras. 26-27, Case C-315/02 Lenz.

[345] Para. 28, Case C-319/02 Manninen and para. 27, Case C-315/02 Lenz. This strict interpretation of Article 65 TFEU may be able to ensure the coherence between this area of EU law and the developments under the other fundamental freedoms which operate with an absolute prohibition on discrimination, Usher (2006), 204.

[346] Paras. 17-18, Case C-513/04 Kerckhaert. The assessment could cover both Member States concerned and it can reach different conclusions as a matter of the applicable law, see paras. 55-56, 57-60, and 60-61, Case C-374/04 Test Claimants in Class IV of the ACT Group Litigation.

[347] Paras. 48-52, Case C-342/10 Commission v Finland; paras. 68-69, Case C-190/12 Emerging Markets.

[348] Para. 26, Case C-376/06 D ECLI:EU:C:2005:424; para. 35, Case C-10/10, Commission v Austria; para. 24, Case C-35/98 Verkooijen; paras. 42-44, Joined Cases C-338/11 to C-347/11 Santander Asset Management. See, for instance, the argument that the extension of Member State tax powers to foreign-sourced income puts domestic- and foreign-sourced income in a comparable situation, para. 51, Case C-87/11, Commission v Belgium, not affected by the fact that their tax burden is not heavier, because a) 'unfavourable tax treatment contrary to a fundamental freedom cannot be regarded as compatible with EU law because of the existence of other advantages, even assuming that such advantages exist' and b) 'setting off of the tax paid in Belgium against the tax payable in the other Member State, pursuant to the double taxation conventions, allows in every case the neutralisation of the difference of treatment resulting from the application of the provisions of national tax legislation or of those conventions whose effect is to reduce the rate of the deduction arising from the withholding tax' (paras. 52-57).

[349] This includes regulating the conditions of imposing tax with reference to the place of residence or of establishment of the persons concerned, for instance, in the applicable procedural rules (paras. 42-44, Joined Cases C-338/11 to C-347/11 Santander Asset Management) or in the granting of tax allowances (paras. 50-51, Case C 181/12 Welte).

[350] Para. 61, Case C-190/12 Emerging Markets; paras. 65-66, Case C-387/11, Commission v Belgium. This could mean that the Court of Justice rejects to examine comparability below the level of the investment vechicle and ignores the situation of unit-holders, which entails that tax treatment at the level of the unit holder (attributing the foreign tax paid to his personal tax liability or deducting that tax when the basis of tax is determined) cannot nullify the effect of a restriction, paras. 62-64, Case C-190/12 Emerging Markets Series. The same holds true when the residence of a company is mentioned in legislation for exercising tax

measure in question[351] and only at the level of distinction.[352] This also follows from the generally close scrutiny by the Court of Justice of the objective comparability of resident and non-resident taxpayers.[353] In this regard, the autonomy of the Member States and their competences in matters of direct taxation plays an important role:[354] whereas differentiated tax treatment on the basis of the residence of taxpayers of the source or destination of taxable income is not permitted, the Member States – on account of their autonomy in fiscal matters – are not required 'to manage the (negative) effects arising from the continued co-existence of different but non-discriminatory national tax regimes.'[355]

Residency requirement in different tax cases

The Court of Justice in *D* made the following distinction. In direct tax cases, the situations of residents and of non-residents are not, as a rule, comparable. In relation to income tax and wealth tax,[356] 'the situation of a resident is different from that of a non-resident in so far as the major part of his income is normally concentrated in the State of residence' and their differentiated tax treatment, for instance, in terms of granting certain tax benefits is permitted.[357] Conversely, when the non-resident receives no significant income in the Member State of residence and obtains the major part of his taxable income from an activity in the State of employment, resident and non-resident taxpayers engaged in comparable employment are not distinguishable on objective grounds so as to justify differentiated tax treatment.[358]

Benchmarks for national tax law

The jurisprudence provides further particular benchmarks and signposts for national tax legislation and administrative practice. These are presented in detail in the next pages.

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powers, and the residence of shareholders is not, paras. 27-28, Joined Cases C-338/11 to C-347/11 Santander Asset Management. Contast with para. 33, Case C-194/06 Orange European Smallcap Fund where residence of shareholder was made a condition of the tax advantage.

[351] Only the relevant distinguishing criteria will be examined and factual circumstances raised by the Member State concerned will not, paras. 27-28, Joined Cases C-338/11 to C-347/11 Santander Asset Management.

[352] Paras. 65-66, Case C-387/11, Commission v Belgium.

[353] Horsley (2012), 163.

[354] Supra n.

[355] Horsley (2012), 163.

[356] Regarding the latter, see paras. 34-42, Case C-376/06 D.

[357] Paras. 26-28, ibid. and paras. 31 and 33, Case C-279/93 Schumacker. In para. 28, Case C-376/06 D the Court held that the State generally has available all the information needed to assess the taxpayer's overall ability to pay, taking account of his personal and family circumstances.

[358] Para. 29, ibid and para. 36, Case C-279/93 Schumacker.

In case of territorially-bound values and public goods ('national public goods'), the introduction of differentiated tax treatment may be less contentious,[359]

- for example, the Member States cannot be required to extend protection, benefits or advantages to public goods and values located outside of its territory and they are entitled to confine protection, benefits or advantages to public goods and values located in their territory.[360]

Distinctions introduced in national social law regarding social security entitlements between insured and non-insured taxpayers are acceptable as based on objective differences,[361]

- this also follows from the autonomy of the Member States to organise their own social security systems and to determine the range of insured persons, the level of contributions payable and the respective reductions, as well as the processes which allow entitlement to reductions to contributions only to persons liable to pay them.[362]

Legal difficulties and national legal particularities, on their own, do not make taxation situations objectively incomparable when the actual tax treatment is a simple case of tax differentiation.[363]

The equal treatment principle extends to expenses, such as business expenses, which are directly linked[364] to an activity which has generated taxable income in a Member State,

- denying for non-residents the right to deduct such expenses constitutes indirect discrimination on grounds of nationality,[365]

- not affected by the fact that income paid to non-residents is subject to withholding tax, as they are taxed on income on which resident persons are not and the different treatment is, therefore, not a question of providing for different taxation procedures depending on the place of residence of the person concerned.[366]

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[359] Paras. 27-28, Case C-133/13, Q and para. 33, Case C-87/13 X (falls under the scope of national legislation and the legislation of another Member State when national legislation is aiming to protect a 'national" public good (i.e., values and public goods linked to the territory of a Member State)).
[360] Ibid.
[361] Paras. 44-50, Case C-512/03 Blanckaert.
[362] Para. 49, ibid.
[363] Paras. 65-68, Case C-364/01 Barbier.
[364] They are, accordingly, necessary in order to carry out that activity, para. 30, Case C-559/13 Grünewald ECLI:EU:C:2015:109.
[365] Para. 40, Case C-450/09 Schröder [2011] ECR I-2497.
[366] Para. 44, Case C-342/10 Commission v Finland.

Objective comparability cannot be contested when

- the persons concerned are treated identically as a matter of tax legislation but they are of different legal form,[367]
- the persons concerned carry out their respective activities in different Member States, as this factual circumstance can change,[368]
- when the law created a direct link between the expenses and the taxable income of resident and non-resident persons,[369]
- the amount of the tax is not calculated having regard to the residence of the persons concerned but on the basis of the value of the asset and the personal situation of the person concerned.[370]

Differentiated tax treatment may not be introduced in cross-border situations when

- a double taxation convention treats foreign- and domestically-sourced incomes in the same way under law,[371]
- a double taxation convention does not exclude the application of domestic tax law,[372]
- the national measure is aimed at attenuating the effects of double taxation and without it the different incomes would be subjected to the same tax treatment,[373]
- the equal treatment of foreign- and domestically-sourced incomes is ensured under a system for addressing double taxation or the imposition of series of changes and the different incomes face the same tax burden.[374]

Measures aiming to prevent or mitigate the imposition of a series of charges to tax or cross-border double taxation do not alone ensure

[367] Paras. 59-61, Case C-387/11, Commission v Belgium.
[368] Paras. 62-64, ibid.
[369] Paras. 41-43, Case C-342/10 Commission v Finland through the application of the technique of assimilation, instead of other techniques, such as tax exemptions.
[370] Paras. 48-49, Case C-181/12, Welte (this is not affected by the availability of a tax-free allowance when that allowance is not calculated on the basis of the taxable value but on the basis of the personal situation of the person concerned making the person in question comparable, for the purposes of accessing the tax allowance, to those in a different personal situation, paras. 53-56).
[371] Paras. 42-46, Case C-322/11 K (the difference in treatment, so far as concerns the possibility of deducting losses sustained on the sale of immovable property, cannot be justified by a difference in circumstances related to the place where the property concerned is situated, para. 48).
[372] Para. 47, ibid.
[373] Paras. 29-33, Case C-315/02 Lenz.
[374] Paras. 35-37, Case C-319/02 Manninen and para. 30, Case C-262/09 Meilicke.

that the differentiated tax treatment of (resident and non-resident) taxpayers is justifiable,[375]

- measures aiming to prevent or mitigate the imposition of a series of charges to tax or cross-border double taxation do not alone ensure that the differentiated tax treatment of (resident and non-resident) taxpayers is justifiable,[376]

    - submitting foreign- and domestically-sourced incomes to the same tax treatment, either unilaterally or by way of a double taxation convention, can make the situation of resident and non-resident taxpayers comparable,[377]

    - the inability of national law aiming to prevent double taxation to eliminate or even mitigate the consequences of the Member State exercising its tax powers over foreign-sourced income will exclude justifiability,[378]

    - introducing a tax relief (e.g., a tax cap) for foreign-sourced incomes brought under national tax jurisdiction (to be taxed and/or added to the domestic tax base) may secure justifiability,[379]

    - under a double taxation convention, when income from immovable property situated in another Member State is not taxed, the equal treatment of foreign- and domestically-sourced income can be ensured by allowing the tax authorities to take account of that income for the purpose of determining, in accordance with the method of 'maintenance progressivity', the tax rate applicable to domestically-sourced incomes.[380]

Not falling under the EU uniform regulatory framework for the given economic activity (e.g., the UCITS Directive) is alone insufficient to find that the taxpayers concerned (EU and third-country) are in a different situation and could be subject to differentiated tax treatment.[381]

5.2.1.2 Preserving the coherence of the tax system

Tax deferral

This ground ensures that the free movement of capital does not undermine the integrity of national tax systems in the sense that the Member States are

[375] Para. 48, Case C-387/11, Commission v Belgium; para. 58, Case C-190/12 Emerging Markets.
[376] Ibid.
[377] Para. 49, Case C-387/11 Commission v Belgium
[378] Para. 60, Case C-190/12 Emerging Markets.
[379] Paras. 47-48, Case C-375/12 Bouanich. In particular, the aim is the consistent application of the national tax system to non-residents or to foreign income.
[380] Paras. 29-31, Case C-489/13 Verest.
[381] Paras. 65-69, Case C-190/12 Emerging Markets.

allowed to regulate tax advantages in a way that they are matched by a tax burden imposed.[382] As a matter of domestic (tax) policy, the Member States can decide to forgo a tax burden temporarily – in national law or in a double taxation convention – on the condition that the revenue will be collected at a later time.[383] This arrangement can be put in jeopardy by the taxpayers exercising their right under Article 63 TFEU to move their taxable income to the tax jurisdiction of another Member State. The Member States would, therefore, have an interest in denying the granting of tax advantages in situations and transactions with a potential cross-border element or in making the revenue claim when the tax subject decides to make his exit for another tax jurisdiction.

The requirement of a direct link

Because by using this ground, the Member States essentially aim to prevent the loss of tax revenue, which as an individual ground cannot be claimed legitimately under EU law,[384] the EU Court of Justice has interpreted this exemption narrowly holding that, following a 'logic of symmetry',[385] a direct link must be established and preserved between a tax advantage (e.g., tax credit, tax exemption, tax cap, tax shield, tax restitution, tax deduction) and a corresponding disadvantage offsetting that advantage by a particular tax levy.[386]

Micro- v macro level tax equity

Generally, since after the strongly criticised judgment in *Bachmann*[387] which first recognised and then accepted such a justification submitted by a Member State, the EU Court of Justice has been reluctant to grant an exemption under this ground.[388] The Member States would submit that fiscal coherence (cohesion) needs to be ensured at an individual or micro-level and the effects of bilateral tax treaties allowing the single taxation of incomes transferred to another Member States need to be compensated by restrictions imposed on individuals. Following *Wielockx*, the Court of Justice would reject these claims on the grounds that since overall fiscal coherence (and a revenue balance at a macro-level) has been achieved through the

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[382] It follows from the idea that national tax systems aim to maintain a close relationship between a tax advantage granted at a particular time and a tax obligation imposed at another time.
[383] The aim is not the reduction of the level of taxation of income on which the Member State concerned exercises its power of taxation, paras 72-73, Case C-375/12 Bouanich.
[384] Infra. See also para. 40, Case C-315/02 Lenz.
[385] EZ JO? Paras. 67-68, Case C-322/11 K.
[386] Inter alia, para. 69, Case C-375/12 Bouanich; para. 28, Case C-204/90 Bachmann [1992] ECR I-0249; para. 52, Joined Cases C-338/11 to C-347/11 Santander Asset Management.
[387] Case C-204/90 Bachmann and Case C-300/90 Commission v Belgium [1992] ECR I-0305. The judgment in Bachmann, focusing primarily on revenue compensation and not on system coherence, allowed discrimination on the basis of establishment/residence without considering that cross-border revenue collection could be ensured through administrative cooperation facilitated by EU legislation and that the cross-border provision of financial services can be seriously undermined by such national requirements. The cross-border administrative cooperation element was specifically emphasised in para. 26, Case C-80/94 Wielockx overturning Bachmann.
[388] Dourado and da Palma Borges (2008), 90; Barnard (2009), 291; Usher (2006), 202.

use of bilateral tax treaties regulating on the basis of the reciprocity principle the allocation of tax jurisdiction among the Member States there is no need to exempt restrictive national measures aimed at individuals on this ground.[389]

Strict intepretation

In any case, even when there is a direct link between the tax advantage and corresponding tax burden, the Member States will still find it impossible to convince the Court of Justice when situations or transactions with a cross-border dimension are subjected to differentiated (discriminatory) treatment,[390] for instance, in a simple case of overtaxation of foreign taxpayers or foreign-sourced incomes.[391] Similarly, national tax measures having the effect of increasing the disparity between the overall tax burden on the profits of domestic companies and on the profits of companies established in other Member States will not be accepted.[392] The Member States have a genuine chance to rely on this ground successfully when the national measure concerns a clear case of tax collection deferral.[393]

Qualifications to the direct link requirement

As to the existence of a direct link between the tax advantage and the tax subsequently claimed, the case law produced the following qualifications: firstly, the tax advantage and the disadvantage must be incurred under the same taxation framework and by the same person,[394] and secondly, the tax advantage must be actually offset by a particular levy on a particular income.[395]

5.2.1.3 Safeguarding the balanced allocation of tax jurisdiction among the Member States

Fair sharing of revenue

Under this ground, EU law ensures that the free movement of capital does not undermine the ability of the Member States to assume taxation powers and to safeguard their tax jurisdiction from the taxation powers of other

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[389] Paras. 24-26, Case C-80/94 Wielockx reversing Bachmann. See also paras. 22-26, Case C-242/03 Weidert ECLI:EU:C:2004:465; para. 53, Case C-436/00 X and Y (the Member States, in absence of EU rules, remain free to establish coherence at this level through international conventions).

[390] See, for instance, paras. 37-40, Case C-493/09 Commission v Portugal, paras. 41-42, Case C-279/93 Schumacker; paras. 53-57, Case C-436/00 X and Y.

[391] Para. 30, Case C-168/01 Bosal.

[392] Para. 38, Case C-315/02 Lenz.

[393] Dourado and da Palma Borges (2008), 91. Based on the examination of the objective pursued by the tax measure in question, para. 43, Case C-319/02 Manninen; para. 27, C-292/04 Meilicke. In paras. 43-46, Case C-319/02 Manninen the question was whether the tax credit was made available in order to ensure the coherence of the Finnish tax system or to avoid the double taxation of incomes, which in any event was found to be achievable through the use of less restrictive means.

[394] Inter alia, para. 69, Case C-322/11, K; para. 30, Case C-168/01 Bosal; paras. 41-43, Case C-471/04 Keller (parent companies and their subsidiaries are distinct legal persons and are taxed separately).

[395] Inter alia, paras. 22-26, Case C-242/06 Weidert; paras. 72-73, Case C-375/12 Bouanich; para. 69, Case C-322/11, K; paras. 48-52, Case C-342/10 Commission v Finland; para. 30, Case C-168/01 Bosal. National law must be quite precisely regulated so that the advantage is connected to the tax burden (e.g., the size of profit or the failure to make profit in the given year to be taken into account), para. 35, ibid.

Member States.[396] It reflects the idea that in times of intensive cross-border economic activity and when the Member States are keen on extending their tax jurisdiction over incomes earned outside their territory the fair distribution of tax revenue among the Member States can only be secured when the Member States negotiate – in bilateral treaties on avoiding double taxation through the extra-territorial application of Member State tax powers – mutually agreed (reciprocal) concessions in respect of their exercising their respective taxation powers, in particular, with regards to foreign-sourced incomes. These conflict of jurisdiction rules leading to a perceived equitable or fair sharing of cross-border tax revenue may be seen as directly conflicting with Article 63 TFEU and the related equal treatment principle which require an undifferentiated tax treatment of incomes irrespective of their source.[397]

Area of application

This exemption covers circumstances when it may be necessary to apply to the economic activities of taxpayers established in one of the Member States only the tax rules of that Member State[398] or when there is a system designed to prevent conduct capable of jeopardising the right of a Member State to exercise its fiscal jurisdiction in relation to activities carried out in its territory.[399]

Main trends

Member State administrations need to be aware of the following domains distinguished in the jurisprudence. First, a justification under this ground will receive different legal treatment when the restriction under scrutiny involves and when it does not involve a bilateral tax treaty regulating the allocation of tax powers and the avoidance of double taxation. The *Marks&Spencers* jurisprudence relating to the latter situation is quite distinct from the jurisprudence commenced in *Commission v France (avoir fiscal)*[400] dealing with what can be lawfully regulated in bilateral tax treaties under Article 63 TFEU. Second, the current jurisprudence on the compatibility of bilateral tax treaties with EU law clearly departed from the previous jurisprudence. The legal test laid down in *Commission v France (avoir fiscal)* was replaced by a different test which allows the Member States to regulate matters of substantive tax law – alongside the issue of allocating taxation powers – which previously was not permitted.

Marks & Spencers

In the *Marks&Spencers* jurisprudence, it is recognised that the unfettered choice for taxpayers to choose jurisdictions to have their losses or profits taken into account, specifically, that losses are taken into account in high-taxation jurisdictions and profits in low-taxation jurisdictions, 'could seriously

[396] Beyond equal treatment, the rationale is that the Member State concerned is not made to waive its right of taxation on income generated in its territory, para. 79, Case C-387/11 Commission v Belgium.
[397] Dourado and da Palma Borges (2008), 107.
[398] Para. 50, Case C-322/11 K; para. 61, Case C-311/08 SGI ECLI:EU:C:2010:26.
[399] Inter alia, para. 41, Case C-326/12 van Caster; para. 60, Case C-311/08 SGI.
[400] Case 270/82 Commission v France (avoir fiscal) [1986] ECR 273.

undermine a balanced allocation of the power to impose taxes between the Member States since the tax based would be increased in one of the States in question, and reduced in the other, by the amount of the losses or profits transferred."[401] In such circumstances, the Member State of residence, which could be granting tax advantages to the taxpayer concerned, 'would be forced to renounce its right (...) to tax its income in favour, possibly," of another Member State.[402] In essence, taxpayers cannot rely on Article 63 TFEU to have access to the most beneficial tax arrangements for them and damage, as a result, the taxation possibilities of the Member States concerned.[403]

Grünewald

In the recent judgment in *Grünewald*, the Court of Justice rejected the German claims based on a 'principle of correspondence', according to which, where the person obliged to make the payment has a right to have it deducted, the recipient of the payment must be liable to tax, in the context of derogations based on the balanced allocation of taxation powers and on the necessity to safeguard the internal coherence of national tax systems. Concerning the first ground for derogation, the Court argued that the principle as applied by Germany was hypothetical and had no connection with the circumstances of the given case, and it was applied in a discriminatory manner.[404] Under the second ground for derogation, the German claim was refused on the basis of the main criteria developed in the jurisprudence that in the given case there was no direct link between the tax advantage and the tax burden.[405]

Commission v France (avoir fiscal)

Under the previous jurisprudence anchored in *Commission v France (avoir fiscal)*, tax treaties between the Member States were found compatible with EU law in so far as they allocate tax jurisdiction between the Member States concerned and deal with the avoidance of double taxation, with which EU law expressed that it respects the efforts of the Member States to address the issue of inter-jurisdictional equity (fair distribution of tax revenue).[406] In contrast, the Member States were prevented from going beyond regulating the allocation of tax powers in these treaties and when they included substantive advantages or disadvantages discriminating – as perhaps dictated by the logic of these bilateral taxation compromises – between different tax subjects there was a clear breach of EU law.[407] With this, the jurisprudence denied that taxpayer equity would be an issue which could be legitimately pursued by the Member States under the EU legal framework.

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[401] Para. 46, Case C-464/03 Marks&Spencers ECLI:EU:C:2005:763; para. 62, Case C-311/08 SGI.
[402] Ibid.
[403] See the same construction in connection with tax avoidance.
[404] Paras. 42-43, Case C-559/13 Grünewald.
[405] Paras. 47-49, ibid.
[406] Dourado and da Palma Borges (2008), 113.
[407] Ibid.

In *Commission v France (avoir fiscal)*, the EU Court of Justice in harmony with the fundamental principles governing the free movement of capital decided that international tax treaties between the Member States are not above their obligations under EU law and that unfavourable tax differentiation (tax discrimination) between domestic and foreign tax subjects cannot avoid meeting EU requirements (e.g., the equal treatment principle) by virtue of being included in an international tax treaty. It argued, when distinguishing between the provisions governing the allocation of taxation powers and the provisions regulating different substantive tax burdens or tax benefits for taxpayers, that the equal treatment principle aiming to establish a level playing field for economic operators in the single market is unconditional and cannot be made subject to the provisions of an international tax treaty and to a condition of reciprocity, a condition which is the main governing principle of such treaties.[408] Basically, the equal treatment of domestic and foreign tax subjects must be ensured irrespective of whether an international tax treaty secures mutual benefits in this regard between the Member States concerned. Thus, even if international tax treaties do not regulate the equal treatment of tax subjects in the EU, or they violate the equal treatment principle, that treatment will have to be provided under the general principles of EU law.

Bachmann* and *Manninen

The *Bachmann* judgment allowing differentiated tax treatment on the basis of a requirement of domestic establishment in the context of preserving the coherence of the national tax system clearly contradicted this.[409] In that judgment, the Court of Justice enabled the Belgian state to collect revenues despite the separation and allocation in international treaties of tax competences among the Member States. In *Manninen*, it was interpreted as the Court seeing no alternative solution to allowing the Member State concerned to secure revenues by means of making sure through the domestic establishment requirement that the taxes as indeed collected.[410] Crucially, *Manninen* was distinguished from *Bachmann* on the facts and the Court of Justice held that the Member State concerned cannot claim legitimately as to the less restrictive solution suggested by the Court of Justice to avoid the double taxation of foreign-sourced incomes that its tax receipts would be reduced, as it is excluded by the long established principle that reduction in tax revenue cannot be regarded as an overriding reason in the public interest.[411] Essentially, in the circumstances of the case the Member State's ability to exercise its tax powers over incomes made in another Member State and to collect tax revenues from such incomes was no longer deemed worthy of protection. The Court of Justice, however,

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[408] Para. 26, Case 270/82 Commission v France (avoir fiscal).
[409] Supra.
[410] Para. 44, Case C-319/02 Manninen.
[411] Paras. 48-49, ibid and para. 30, Case C-292/04 Meilicke.

emphasised that national legislation must address the issue of double taxation in a manner that foreign-sourced incomes receive equal tax treatment with domestically-sourced incomes.[412]

The new jurisprudence: selective non-discrimination

More recent jurisprudence, however, seems to have departed from this case law. Essentially, it established that tax treaties between the Member States enjoy primacy over EU obligations (e.g., equal treatment) not only in respect of regulating the allocation of taxation powers and the avoidance of double taxation,[413] but also when they regulate substantive advantages and disadvantages in taxation. In *D*, the Court of Justice accepted that refusing to extend the substantive rules of a bilateral tax convention to residents of other Member States – therefore, discriminating against all other Member States except for those that are a party to the treaty– is not a violation of the free movement of capital.[414] This jurisprudence, instead of pursuing a consistent and comprehensive non-discrimination agenda for the benefit of the Single Market, enables the Member States to introduce variable tax burdens on cross-border economic activity in bilateral double taxation conventions.[415] Provided that they are able to negotiate mutually beneficial bilateral tax treaties, it offers the Member States greater freedom to prioritise certain cross-border revenue streams within the Union depending on their assessment of their value.[416] Controversially, this line of case law recognises indirectly Member States expectations of maintaining tax revenues and of avoiding their diminution when that ground has consistently been rejected in the case law as capable of justifying restrictions on the free movement of capital.[417]

Member State possibilities

Concerning the general possibilities for the Member States under this ground, the jurisprudence has recognised that the Member States can regulate to maintain and secure their power of taxation on economic activities carried on in its territory.[418] However, in harmony with the earlier mentioned general benchmark, this should actually follow from the measure

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[412] Para. 53-54, Case C-319/02 Manninen, the calculation of tax credit granted in order to avoid double taxation must be calculated on the basis of the tax actually paid in another Member State.

[413] A difference in treatment between nationals of the two Contracting States that results from that allocation cannot constitute discrimination contrary to EU law as they flow, in the absence of any unifying or harmonising measures adopted in the EU context, from the Member States' power to define, by treaty or unilaterally, the criteria for allocating their powers of taxation, para. 52, Case C-376/03 D; para. 47, Case C-513/03 Van Hilten.

[414] Paras. 53-63, Case C-376/03 D; paras. 84-92, Case C-374/04 Test Claimants in Class IV of the ACT Group Litigation.

[415] Dourado and da Palma Borges (2008), 113.

[416] Ibid (this way, the Member States can address both inter-jurisdictional and taxpayer equity free from the interference of EU law).

[417] Infra n.

[418] Inter alia, para. 78, Case C-387/11 Commission v Belgium; para. 81, Case C-375/12 Bouanich.

in question.[419] Another important aspect is that the Member States can regulate in a double taxation agreement the allocation of powers of taxation with a view to preserving their own power of taxation. Howver, that alone will be insufficient to justify a tax rule (e.g., a tax advantage) violating EU obligations.[420]

The particular possibilities offered by the jurisprudence to the Member States are summarised below.

The Member States cannot be required to ensure that in cross-border relations incomes are relieved from a series of charges to tax or from economic double taxation,[421]

- in particular, they cannot be required to exempt such incomes from tax, or
- to grant tax advantages equal to the tax paid on such incomes.[422]

The Member States – in order to safeguard the symmetry between the right to tax incomes and the right to deduct losses[423] – can refuse the deduction of losses by taxpayers when that would allow them to choose freely the Member State in which it is most advantageous from a taxation perspective to take into account those losses,[424]

- in particular, the Member States are entitled to allow the deduction of expenses or costs – for the purpose of offsetting a foreign tax imposed on incomes – only when it is directly linked to the tax revenue collected under the tax powers of the Member State concerned, a possibility which has a particularly strong grounding when the allocation of tax powers among the Member States has been determined in international tax treaties (double taxation conventions).[425]

The Member States cannot be required as the State of residence of the taxpayer concerned to compensate for the failure to take into account in another Member State the taxpayer's personal circumstances when taxing the income earned in that State,[426]

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[419] Para. 85, Case C-375/12 Bouanich; paras. 36-38, Case C-296/12 Commission v Belgium (the loss of power of taxation does not follow from the double taxation agreement but from the transfer of residence of the person concerned); paras. 42-43, Case C-326/12 van Caster (the purpose of ensuring uniform tax treatment of domestic and foreign incomes in not such as to prevent conducts capable of jeopardising the taxation powers of the Member State concerned).

[420] Paras. 82-84, Case C-375/12 Bouanich.

[421] Ibid.

[422] Para. 78, Case C-387/11 Commission v Belgium.

[423] Para. 51, Case C-322/11 K.

[424] Paras. 52-55, ibid (they cannot be prevented from constraining taxpayers in choosing freely the Member State in which they want their profits to be taxed or their losses to be deducted, para. 51).

[425] Para. 55, Case C-168/11 Beker. In such cases, the right to deduct losses is not matched by a right to tax, as the deduction of losses takes place irrespective of the allocation of tax powers among the Member States in a double taxation convention, paras. 52-55, Case C-322/11, K.

[426] Para. 55, Case C-168/11 Beker. From the freedom of establishment, see paras. 28-38, Case C-279/93 Schumacker distinguishing between situations on the basis of the amount of

- however, this does not enable the taxpayer's Member State of residence to evade its obligation to grant the taxpayer allowances on the basis of his personal and family circumstances, to which allowances he is entitled under national law, unless the taxpayer received such allowances in another Member State – based on an international tax treaty or on the unilateral decision of that State – with respect to income earned in that State.[427]

The Member States cannot be required to extend tax advantages (e.g., the right to surrender an advanced payment of corporation tax to subsidiaries so as to ensure that the tax paid by that group of companies does not exceed their aggregate tax liability) to non-residents when that would prevent the Member State concerned from levying additional tax on foreign sourced income which was subject to a nominal rate of taxation lower than that applicable in that Member State.[428]

In contrast, the Member States, as it follows from the applicable general principles, may be prevented from introducing restrictions in defence of their taxation powers in the following cases.

The Member State has chosen not to tax resident taxpayers in receipt of nationally-sourced income (e.g., grants them a tax allowance)[429] (in relations both between Member States and between Member States and third countries),[430]

- in such instances, the Member State concerned has not foregone its tax jurisdiction to other Member States and does not apply lower taxes than in other domestic cases.[431]

Or when it is able to exercise its taxation power on foreign-sourced incomes, for instance, in the form of 'a counterbalance to the payments of contributions in respect of which a tax reduction was granted.[432]

Offsetting the tax disadvantage

In harmony with the earlier mentioned general benchmark, the offering of a tax advantage (e.g., deducting foreign taxation from the taxable amount) potentially capable of offsetting the disadvantage suffered as a result of a restriction does not make the restriction in question compatible with EU law (especially when the restriction is automatically applied when the taxpayer fails to make a choice).[433]

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income earned by the taxpayer in the Member State concerned and in other Member States (the more the income earned in the Member State concerned is, the less the possibility to introduce differentiated tax treatment is).

[427] Para. 56, Case C-168/11 Beker.
[428] Para. 110, Case C-35/11 Test Claimants in the FII Group Litigation.
[429] Para. 99, Case C-190/12 Emerging Markets.
[430] Para. 100, ibid.
[431] Para. 58, Case C-168/11 Beker.
[432] Para. 39, Case C-296/12 Commission v Belgium.
[433] paras. 61-62 ??? C-269/12 ???

5.2.1.4 Ensuring effective fiscal supervision

Equal treatment and cooperation

Under this ground, the Member States aim to claim that with the free movement of capital in cross-border situations it is more difficult to obtain information for the purpose of conducting tax proceedings and also to enforce tax obligations. As a consequence, cross-border transactions and cross-border situations in capital movements – departing from the equal treatment principle – should be treated differently from purely domestic transactions and situations. Because such claims challenge one of the fundamental principles of the free movement of capital and because the alleged difficulties can be evaded by the Member States through the use of cross-border administrative arrangements, this justification is practically never allowed.[434] While the jurisprudence recognises, in principle, the difficulties of the Member States and accepts that they are entitled to obtain information necessary for the adequate application of tax laws,[435] the Member States are constantly reminded that instead of imposing restrictions on the free movement of capital, mainly, by subjecting cross-border situations and transactions to unfavourable differentiated tax treatment, they should rely on the available EU and international (OECD)[436] measures on mutual assistance in taxation matters or to allow the taxpayers to produce the necessary information themselves.[437] This is also the case when the Member State claims the inapplicability of the said instruments, for instance, when it would contradict national arrangements for banking secrecy.[438] In the Court of Justice's view, 'the impossibility of requesting cooperation of that kind does not justify' restrictions of a fundamental freedom.[439]

The EU legal measures available

In principle, the Member States would be able to introduce and maintain administrative and other arrangements for the supervision of compliance with tax obligations in cross-border transactions and situations, in case the necessary frameworks for cross-border administrative cooperation were not available.[440] With the Mutual Assistance Directive (ex Directive 77/799/EEC, Directive 2011/16/EU), the UCITS Directive (ex Directive 85/611/EEC, ex Directive 2008/55/EC, Directive 2009/65/EC) and other measures (Directive 2003/41/EC) in place, it is rather difficult for the Member States to maintain that a national derogation from EU obligations is necessary so as to ensure that cross-border capital movements and effective cross-border fiscal

[434] Dourado and da Palma Borges (2008), 113.
[435] See Case C-250/95 Futura.
[436] OECD and Council of Europe Convention on mutual administrative assistance in tax matters, 1988.
[437] Para. 18, Case C-204/90 Bachmann; paras. 31-32, Case C-334/02 Commission v France.
[438] Para. 32, Case C-334/02 Commission v France; para. 13, Case C-300/90 Commission v Belgium.
[439] Para. 32, Case C-334/02 Commission v France.
[440] Para. 43, Case C-296/12 Commission v Belgium; paras. 72-79, Case C-190/12 Emerging Markets.

supervision are both ensured in the integrated European capital market. The same observations apply in connection with capital movements between third States and the EU Member States where international instruments may be available to address cross-border fiscal supervision issues.
In this framework, the Member States are prevented from defending under this ground, and, as a consequence, they are unable to introduce and maintain the administrative and other arrangements listed below.

Excluding, a priori, that taxpayers provide documentary evidence supporting that in order to obtain a tax advantage they meet regulatory standards in the Member State of their residence, standards which are equivalent to those of the Member State concerned,[441]

- this entails that the Member State concerned must accept the evidence (information and documents) forwarded by the taxpayer, or

- that the Member State concerned receives the evidence forwarded by the tax authorities of the Member State of residence under a double taxation agreement,[442]

    - both of which are subject to the condition that the evidence submitted enables a clear and precise assessment of the matter at issue[443] or it 'does not, as a general rule, require a complex assessment'.[444]

Examining evidence and information submitted by non-resident persons in order to establish whether they are comparable in nature with persons established in the Member State concerned, even when the available EU measures do not specifically provide for such powers.[445]

Denying non-resident taxpayers the opportunity to submit evidence to prove that for the purpose of securing a tax advantage they meet the legal conditions laid down in national law for obtaining that tax advantage.[446]

Requiring taxpayers to use a single, disadvantageous avenue to provide the information necessary for determining the basis of tax assessment.[447]

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[441] Para. 80, Case C-190/12 Emerging Markets Series; paras. 44-45, Case C-493/09 Commission v Portugal (especially when there is an EU measure governing such situations, paras. 46-47).
[442] Ibid.
[443] Ibid.
[444] Para. 64, Case C-181/12 Welte.
[445] Paras. 72-79, Case C-190/12 Emerging Markets.
[446] Paras. 44-45, Case C-493/09 Commission v Portugal.
[447] Para. 49, Case C-326/12 van Caster (in the form of a publication in the electronic federal bulletin of official announcements accompanied by a certificate issued by a professional

Maintaining a tax advantage (exemption) for resident taxpayers only, even when residency is regarded as a condition for enforcing the applicable provisions of national law,[448]

Insisting, in contradiction with the general benchmarks of Member State conduct, that residency in the Member State concerned is a key factor ensuring the effective enforcement of national tax law.[449]

Administrative inconvenience

In harmony with the general principle that mere administrative inconvenience is not capable of justifying an obstacle to a fundamental freedom,[450] the preference of the Member State concerned for deduction at source over 'voluntary payment' of an amount corresponding to the applicable tax or a 'voluntary annual declaration of income' – it being an easier administrative operation – cannot be accepted as a justification under this ground.[451]

Cooperation with third States

In third State and EU Member State relations, justifications submitted under this ground may be more readily accepted, especially because of the different legal environment[452] and because EU measures similar to those available for intra-Union movements may not be available.[453] It needs to be examined whether there are legal arrangements in place between the States concerned (e.g., under the OECD framework) so that the necessary information and evidence can be submitted to the Member State authorities so as to assess whether a particular tax treatment (e.g., a tax advantage) should be provided.[454] However, when the necessary information and evidence is impossible to obtain, the Member State concerned is, in principle, entitled to deny the tax treatment the availability of which is dependent on the taxpayer concerned satisfying certain conditions.[455]

Complex cross-border taxation arrangements

As stated earlier, in complex cross-border taxation arrangements (e.g., capital movements between parent companies and subsidiaries for the purposes of tax optimisation) the Member States are entitled to require taxpayers to provide evidence proving that they meet the conditions of a tax advantage and to deny the tax advantage when the suitable evidence is not produced.[456] They can also introduce measures 'which enable the amount of costs deductible in that Member State, which were incurred in another

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authorised by law to provide tax advisory services confirming that the information was established in accordance with German tax law rules).

[448] Paras. 44-45, Case C-493/09 Commission v Portugal.

[449] Ibid.

[450] Supra n. and

[451] Paras. 47-48, Case C-315/02 Lenz and paras. 29-30, Case C-334/02 Commission v France.

[452] Para. 82, Case C-190/12 Emerging Markets.

[453] Ibid.

[454] Paras. 84-88, ibid.

[455] Para. 63, Case C-181/12 Welte; para. 44, Case C-72/09 Rimbaud.

[456] Para. 44, Case C-296/12 Commission v Belgium; para. 45, Case C-262/09 Meilicke.

Member State, to be ascertained clearly and precisely.'[457] These, however, must meet the requirements of the proportionality test. Also, the Member States are not permitted 'to impose different conditions' on the transactions in questions on the basis of the place of establishment of the taxpayer concerned.[458]

Proportionate restrictions

In overlap with examining the necessity/proportionality of the interference, the legitimacy of the justification under this ground could be denied having regard to the nature and weight of the restriction. Therefore, the Member States cannot deny non-resident taxpayers tax exemptions and other tax advantages completely – irrespective of the guarantees and evidence they may be able to provide, advantages which are available to resident taxpayers.[459] In a similar vein, it is prohibited to subject non-resident taxpayers to discriminatory treatment under either substantive or procedural tax law when they fulfil the domestic legal requirements applicable to resident taxpayers.[460]

5.2.1.5 Combatting tax avoidance and tax evasion

Specific and targeted measures

This ground, which is linked to the previous ground of ensuring effective fiscal supervision,[461] enables the Member States to defend measures aimed specifically at preventing and combatting illegal tax avoidance and tax evasion practices in cross-border situations. Through accepting the justifiability of Member State restrictions, economic operators are prevented from using the free movement of capital to engage in practices of tax avoidance or tax evasion (to use significant disparities between the basis of assessment or rates of tax applied in the different Member States so as to avoid the tax normally due in the resident Member State).[462] It is notoriously difficult to secure a derogation under this ground as the Member States are expected to produce specifically targeted measures which are suitable to achieve this particular aim.[463] General statutory presumptions of illegal conduct (e.g., that practices of 'thin capitalisation' are abusive') will not suffice.[464] This follows from the fact that this ground may be difficult to distinguish from objectives deemed illegitimate under EU law, such as

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[457] Para. 41, Case C-262/09 Meilicke; para. 31, Case C-250/95 Futura.
[458] Para. 55, Case C-347/04 Rewe Zentralfinanz ECLI:EU:C:2007:194.
[459] Para. 81, Case C-387/11 Commission v Belgium.
[460] Paras. 44-45, Case C-493/09 Commission v Portugal; para. 49, Case C-326/12 van Caster. See also in the context of the proportionality test infra n.
[461] The national measures affected will address both effective taxation and the effective supervision of taxation at the same time, see para. 74, Case C-436/00 X and Y.
[462] Paras. 47-48, Case C-464/03 Marks&Spencers; paras. 67-68, Case C-311/08 SGI (to prevent coporate groups to place losses in high-taxation jurisdictions and place profits in low-taxation jurisdictions).
[463] See para. 62, Case C-436/00 X and Y; para. 60, Case C-322/11, K.
[464] Infra n. (ibid)

pursuing the general economic and fiscal interests of the Member State concerned or avoiding the diminution of domestic tax revenue.[465]

Discriminatory measures

To the benefit of the Member States, the case law has defined certain situations where the Member States may successfully rely on this ground. Since *Commission v France (avoir fiscal)*, it is clear that discriminatory national tax rules cannot be exempted on the basis of this ground (in the context of freedom of establishment).[466] The same also follows from *Sandoz* which, proceeding under Article 65(1)b TFEU, held that imposing a duty on foreign-contracted loans so as to ensure their equal tax treatment domestically-contracted loans and to exclude domestic taxpayers avoiding their tax obligations is essential to prevent infringements of national tax laws, and examined under Article 65(3) TFEU whether it constituted arbitrary discrimination.[467]

Purely artifical arrangements

The case law distinguishes between wholly artificial arrangements designed to circumvent the national tax system and lesser forms of tax avoidance with a lower degree of artificiality.[468] Purely artificial arrangements are arrangements which are "devoid of economic reality, created with the aim of escaping the tax normally due on the profits generated by activities carried out on national territory".[469] The conditions of national measures capable of being justified under the ground of combatting tax avoidance and tax evasion were developed in connection with these latter tax arrangements: the anti-avoidance (-evasion) measure must be suitable and specifically targeted.[470] In the Court of Justice's interpretation, specifically targeted means that the measure must not regulate in general any situation that may arise in a taxation scenario[471] (they may not be as widely formulated so that they cover situations which do not involve tax avoidance).[472] In other words, it must make it possible to combat practices the sole aim of which is to enable natural persons to avoid paying the tax on capital in France, or at least to make such practices less attractive.[473] In particular, the measure must enable 'the amount owed by taxpayers to be ascertained clearly and

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[465] Paras. 40-45, Case C-478/98 Commission v Belgium. See the related case law supra n. A 'general presumption of tax evasion or tax fraud' indicates that the Member State aims to secure general fiscal interests rather than meeting the specific objective of combatting tax evasion or tax fraud, see para. 45, ibid and para. 44, Case C-28/95 Leur-Bloem [1997] ECR I-4161.

[466] Para. 35, C-153/08 Commission v Spain ECLI:EU:C:2009:618.

[467] Paras. 24-26, Case C-439/97 Sandoz.

[468] Paras. 47-48, Case C-464/03 Marks&Spencers and para. 65, Case C-311/08 SGI. See also para. 34, Case C-282/12 Itelcar; para. 25, Case C-112/14, Commission v UK; paras. 72-74, Case C-524/04 Test Claimants in the Thin Cap Group Litigation.

[469] Para. 66, Case C-311/08 SGI.

[470] Para. 65, ibid; para. 61, Case C-322/11, K.

[471] para. 62, Case C-322/11 K.

[472] Paras. 15-16, Case C-175/88 Biehl ECLI:EU:C:1990:186.

[473] Para. 36, Case C-72/09 Rimbaud.

precisely.'[474] National measures which are not specifically designed to address purely artificial arrangements (e.g., general prohibitions in tax law (on offsetting losses)) may, however, be justified in case they fall under this justification and the ground concerning the balanced allocation of tax powers between the Member States.[475]

The focus of EU restrictions

There is a clear connection – suggesting practices of good regulation and administration – between the requirements that the Member States must avoid making general presumptions that certain transactions will lead to tax avoidance and that the Member States must address tax avoidance in the form of 'purely artificial contrivances, the aim of which is to circumvent tax law' by specifically targeted measures.[476] This, as well as the presence of the individual conditions in the jurisprudence, follows from the general requirement that restrictions on the free movement of capital must satisfy the requirements of necessity and proportionality.[477]

Legal bechmarks for national measures

Principally, it is for the Member States to establish that the cross-border transaction actually involves an element of tax evasion or avoidance, and as stated earlier, general, irrefutable or irrebuttable presumptions in this regard introduced in national measures or established by national tax authorities will not be accepted,[478] mainly because they violate the principle of proportionality.[479] Specific, rebuttable anti-avoidance rules may fare better but the Member States need to be careful how they frame the burden of proof falling onto taxpayers, especially in light of the proportionality requirement.[480] Specifically, such national measures may not be formulated in a way so as they cancel the earlier mentioned obligation of the Member States to establish that tax avoidance has taken place. In *Rimbaud* and *ELISA*, the Court of Justice made it clear that the Member States, in the

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[474] Para. 35, ibid.
[475] Para. 66, Case C-311/08 SGI.
[476] See paras. 50-53, C-347/04 Rewe Zentralfinanz; paras. 35-38, C-433/04 Comission v Belgium.
[477] See paras. 34-35, Case C-72/09 Rimbaud.
[478] Para. 62, Case C-436/00 X and Y; para. 60, Case C-322/11 K.
[479] Paras. 31-33, Case C-132/10 Olivier Halley; para. 71, Case C-311/08 SGI. See further infra n. 'In order to be so justified, the national legislation must be suitable for securing the objective which it pursues and must not go beyond what is necessary in order to attain it, so as to accord with the principle of proportionality', para. 18, Case C-54/99 Église de Scientologie.
[480] See, paras. 82-83, Case C-524/04 Test Claimants in the Thin Cap Group Litigation (the full formula holds that, firstly, national legislation must provide for a consideration of objective and verifiable elements which make it possible to identify the existence of a purely artificial arrangement, entered into for tax reasons alone, and must allow taxpayers to produce, if appropriate and without being subject to undue administrative constraints, evidence as to the commercial justification for the transaction in question and, secondly, where it is established that such an arrangement exists, such legislation treats practices as illegal only in so far as they exceed what is appropriate), and para. 71, Case C-311/08 SGI (taxpayers must not be subjected to undue administrative constraints (e.g., they must be provided sufficient time to submit their evidence and they must be allowed to challenge administrative decisions before national courts, para. 73)).

absence of instruments ensuring administrative cooperation between the States concerned, may not exclude taxpayers from producing evidence that they consider necessary for the correct assessment of taxes and duties, especially that their objective is not one of tax evasion.[481] For instance, they could apply measures less restrictive than categorically denying a tax advantage (e.g., refusing the tax advantage when evidence is not produced).

The relevance of the circumstances

The burden on the Member States may, however, be different in different circumstances. In respect of the possibility of taxpayers themselves proving that their sole aim is not tax evasion, the Court of Justice introduced a crucial distinction between intra-Union and EU-third State tax arrangements on the basis of the instruments available to facilitate cross-border administrative cooperation. It found that because of the difficulties of obtaining the necessary information from third State authorities the Member States may be entitled to introduce and maintain more restrictive measures.[482] In contrast with *ELISA* where in an intra-EU context the categorical refusal to grant a tax advantage and to allow taxpayers to submit evidence was found unjustifiable, in *Rimbaud* involving an EU Member State and a third State, because of the different, less advanced regulatory framework governing administrative cooperation, similar restrictions were declared as necessary and appropriate.[483]

5.3 The necessity/proportionality of the restriction

Legal bechmarks and signposts

Member State exemptions from Article 63 TFEU need to be necessary and proportionate.[484] In taxation cases, with so much focus on the legitimacy of the ground raised, this element of the legal test may receive less emphasis. Often, the examination of legitimacy extends to questions relating to the necessity of the restriction. In other cases, mainly involving regulatory measures,[485] the legal scrutiny of the interference is geared towards establishing its necessity and proportionality. The relevant jurisprudence has produced a number of benchmarks and signposts for Member State policy making and regulation. Some of these are far reaching, especially when the availability of less restrictive alternative means is examined.[486]

[481] Paras. 37-38 Rimbaud and paras. 99-101, Case C-451/05 ELISA [2007] ECR I-8251.
[482] Paras. 39-44 Rimbaud (on the condition that 'it proves impossible' to obtain that information).
[483] Paras. 45-51, Rimbaud.
[484] It must be appropriate for securing the attainment of the objective it pursues and must not go beyond what is necessary to attain it, para. 42, Case C-262/09 Meilicke.
[485] As an example in a taxation matter, paras. 31-32, Case C-132/10 Olivier Halley.
[486] See in particular the case law on prior obligations of authorization, notification or declaration of direct investment and transactions with immovable property supra n. In this context, Member State arguments relating to the effectiveness of related parallel systems of

However, in the (exceptional) circumstance that the national measure is adequately targeted, precisely regulated and the discretion made available is duly delimited, judicial demands for less restrictive alternative measures are more confined.[487] In some instances, the matter will be deferred to the national level allowing the national court to assess and determine the proportionality of the interference in light of the circumstances of the case.[488] The legal benchmarks and signposts confining Member State action are presented in the next pages.

There were instruments available in EU law to ensure that the aim pursued by the Member State concerned is achieved,

- the Member State cannot rely on the difficulties of collecting information and of recovering tax debts in a cross-border situation in order to justify a restriction (absolute refusal to grant a tax exemption), when EU measures were available to ensure mutual assistance and cooperation in cross-border taxation matters (Directives 77/799/EEC and 2011/16/EU and Directives 85/611/EEC, 2008/55/EC and 2009/65/EC),[489]

- the Member States, when they have evidence to request other Member States, either through an EU mutual assistance framework (Directives 77/799/EEC, 2011/16/EU) or under a bilateral convention, to communicate to them information necessary for the exercise of taxation powers, cannot apply an extended recovery period aimed at a taxable item located in another Member State which is not specifically intended to have effective recourse to the mechanisms of mutual assistance between the Member States,[490]

    - this applies even when the EU mutual assistance framework does not apply to the tax in question (inheritance tax), as it would have been possible for the national authorities to have recourse to other mutual assistance instruments,[491]

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administration and law enforcement (e.g., prosecution of crimes) can be ignored, para. 29, Joined Cases C-163, C-165 and C-250/94 Sanz de Lera.

[487] See, for instance, para. 53, Case C-503/99 Commission v Belgium arguing that 'there is no certainty that planning designed to encourage natural gas undertakings to conclude long-term supply contracts, to diversify their sources of supply or to operate a system of licences would be enough, on its own, to permit a rapid reaction in any particular situation' and that 'the introduction of rules precisely defining the standards required of undertakings in the sector concerned, as proposed by the Commission, would appear to be even more restrictive than a right of opposition limited to specific situations.'

[488] Para. 67, Joined Cases C-105/12 to C-107/12, Essent (regulation of energy market according to EU legislation); para. 68, Joined Cases C-197/11 and C-203/11 Libert (obligation imposed on economic operators to implement social obligations under national social housing policy); Case C-148/91 VVOO (national cultural and media policy ensuring freedom of expression).

[489] Paras. 48-49, Case C-493/09 Commission v Portugal; para. 55, Case C-326/12 van Caster.

[490] Paras. 33, 35, 36, Case C-132/10 Olivier Halley

[491] Para. 37, ibid.

- beyond using the EU mutual assistance framework, Member State authorities could be required to obtain information by other means, for instance, in the case of shares quoted on the stock market, they could find out the value of those shares by looking at the information available in the press or on the internet.[492]

There were other instruments available (e.g., a bilateral assistance agreement, internal exchange of information between national tax authorities, and even 'consulting' the press or the internet) to ensure that the aim pursued by the Member State concerned is achieved.[493]

There were less restrictive measures available to the Member State concerned to achieve the aim pursued,[494]

- regulating the risks of a temporary transfer of tax residence instead of preventing that choice,[495] or addressing the specific risk of a definitive leave from tax jurisdiction of the taxpayer instead of applying a general restriction (exclusion from tax advantage) on all relevant transactions,[496]

- despite the restrictions introduced by the Member State concerned (in order to avoid the creation of a domestic loan market with tax and a Eurobond loan market with no tax), nothing prevented residents 'wishing to invest from acquiring loan securities issued on the Eurobond market by issuers other than the Kingdom of Belgium which are also not subject to Belgian withholding tax',[497]

- granting a tax credit, in order to avoid double taxation, that matches the tax owed in another Member State instead of calculating a tax credit with reference to the tax due in the Member State concerned,[498]

- requiring prior financial guarantees for the purpose of ensuring the recovery of tax debts instead of an absolute refusal to grant a tax exemption,[499]

- supporting the persons concerned – by direct subsidies or though subsidy mechanisms – to gain access to the property market instead of introducing a de facto prohibition on property

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[492] Para. 38, ibid.
[493] Para. 50, Case C-493/09 Commission v Portugal; paras. 53-54, Case C-326/12 van Caster; paras. 36-38, Case C-132/10 Olivier Halley.
[494] In infringement procedures, Member State defences can be rejected on the ground that the Member State concerned has failed to establish that there were no less restrictive alternative solutions, or that the without the measure the aim could not have been achieved, para. 48, Case C-296/12 Commission v Belgium; para. 38, Case C-10/10, Commission v Austria.
[495] Para. 54, Case C-9/02 de Lasteyrie du Saillant ECLI:EU:C:2004:138.
[496] Para. 69, Case C-436/00 X and Y.
[497] Para. 46, Case C-478/98 Commission v Belgium.
[498] Paras. 44-45, Case C-319/02 Manninen; paras. 31-32, Case C-292/04 Meilicke.
[499] Para. 50, Case C-493/09 Commission v Portugal.

ownership and rentals through applying restrictive regulatory conditions,[500]

- using information obtainable by other means or already available under statutory obligations in another Member State instead of requiring a company already active in other Member States to gain authorisation for its activities in the Member State concerned,[501]

- giving taxpayers the opportunity, without being subject to undue administrative constraints, to provide evidence of any commercial justification for the transaction in question instead of applying a general, unrebuttable presumption that the taxpayer was involved in an act of tax avoidance,[502]

- allowing taxpayers to adduce evidence to enable the tax authorities to ascertain, clearly and precisely, the information required to tax incomes instead of allowing them the use of a single avenue for providing information for the purpose of tax assessment,[503]

    - it cannot be excluded that taxpayers can obtain the information, in which they must be assisted by the national tax authority by determining the content, form and degree of detail of the information required,[504]

    - it cannot be maintained that allowing taxpayers to adduce evidence will jeopardise uniform taxation in the Member State concerned as that aim can be achieved by national tax authorities exchanging information,[505]

    - it cannot be maintained that otherwise the national authorities are prevented from obtaining the necessary information when there are EU measures available on mutual assistance and cooperation,[506]

    - the assessment of evidence must not be conducted too formalistically, and formats and presentations of evidence other than those accepted in the Member State concerned must be accepted if they enable the tax authorities to ascertain, clearly and precisely

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[500] Para. 56, Joined Cases C-197/11 and C-203/11 Libert.
[501] Para. 33, Case C-39/11 VBV.
[502] Para. 71, Case C-311/08 SGI.
[503] Paras. 49-50, Case C-326/12 van Caster; paras. 43-44, Case C-262/09 Meilicke. Labelled also as a breach of the principle of sound administration, para. 43, ibid.
[504] Paras. 51-52, Case C-326/12 van Caster; para. 45, Case C-262/09 Meilicke.
[505] Paras. 53-54, Case C-326/12 van Caster.
[506] Para. 55, Case C-326/12 van Caster; paras. 49-52, Case C-262/09 Meilicke. It is for each Member State to assess the specific cases in which information concerning transactions by taxable persons in its territory is lacking and to decide whether those cases justify submitting a request for information to another Member State, ibid.

whether the conditions of the tax advantage are met,[507]

- the administrative burdens of allowing the taxpayers to adduce evidence are irrelevant as dictated by the general benchmark that the administrative disadvantages of compliance with EU law are alone insufficient to justify a restriction.[508]

The measure must be suitable to achieve its aim,[509]

- the conditions laid down in the measure must reflect the socio-economic factors which bear relevance from the perspective of the aim pursued and it must ensure that the aim is actually met by way of applying the conditions which relate to those factors.[510]

The measure and its application adhere to practices of good regulation and good administration (the measure and its application must be adequately prepared and targeted),[511]

- the measure is 'predicated on an assessment of objective and verifiable elements',[512]

- following the principle of legal certainty, the scope of the measure must be defined with sufficient precision (e.g., it should be possible, at the outset, to determine its scope)(see also the adequate targeting of the scope of the measure),[513]

- following the principle of legal certainty, systems of prior authorisation of direct foreign investment must be regulated with precision so as to enable individuals to assess their rights and obligations under the Treaties,[514]

- following the principle of legal certainty, the regulation of 'golden shares' must be regulated with precision so as to enable individuals to assess their rights and obligations under the Treaties (e.g., the exercise of rights must be qualified by a condition which is more precise than the 'national interest', the conditions of accepting or refusing authorisation must be

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[507] Para. 46, Case C-262/09 Meilicke. Only when the taxpayer produces no information to enable the tax authority to make its decision may the tax advantage be refused, para. 47, ibid.
[508] Para. 56, Case C-326/12 van Caster; para. 48, Case C-262/09 Meilicke (regarding the inadequate flow of information).
[509] See, para. 63, Case C-436/00 X and Y.
[510] Paras. 54-55, Joined Cases C-197/11 and C-203/11 Libert.
[511] On the emerging requirement of good governance when proportionality is used, Barnard (2009), 294.
[512] Para. 37, Case C-282/12 Itelcar; para. 27, Case C-112/14 Commission v UK.
[513] See also para. 44, C-282/12 Itelcar.
[514] Paras. 19-20, Case C-54/99 Église de Scientologie. See also the case law on prior authorization of transactions with immovable property, supra n.

objectively determined, discretionary powers must be adequately regulated),[515]

- the proportionality of the system can be established when it is guaranteed, 'on the basis of objective criteria which are subject to judicial review', that it is used for legitimate purposes of domestic policy[516] (no prior approval is needed (a system of subsequent opposition of company decisions by minister), ministerial intervention is made dependent upon the initiative by authorities, strict time-limits are introduced, the scope of interference is precisely delimited (e.g. relating to strategic assets), the conditions of interference are precisely regulated (e.g., there is a threat that the objectives of domestic policy may be compromised), interventions must be supported by a formal statement of reasons, and interventions may be subject to an effective review by the courts),[517]

- the special rights reserved for the Member State concerned must be limited to the public service activity, their exercise must be based on precise criteria, and must be backed by statement of reasons which make effective judicial review possible,[518]

○ the measure must meet the requirements of legal certainty, 'in accordance with which rules of law must be clear, precise and predictable as regards their effects, especially where they may have unfavourable consequences for individuals and companies'.[519]

- the relevant regulatory conditions must not be vaguely determined and they must specify the situations in which they will be met in individual cases,[520]

○ in each case, when the measure is applied the person concerned is given the opportunity – 'without subjecting him to undue administrative constraints' – to justify their conduct or establish that their conduct was lawful with evidence,[521]

○ national procedures involving discretionary assessment by national authorities in the application of the measure cannot negate the effectiveness of EU law and they must be based on objective, non-discriminatory criteria known in advance to the

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[515] Paras. 50-52, Case C-483/99 Commission v France; paras. 74-76, Case C-463/00 Commission v Spain.
[516] Legitimate purposes of domestic and EU energy policy with a view to fulflling public service obligations, see, para. 52, Case C-503/99 Commission v Belgium.
[517] Paras. 49-52, ibid. In such instances, it is extremely difficult to establish that there were less restrictive alternative means, para. 53, ibid. Used to examine systems set up in other Member States, paras. 78-80, Case C-463/00 Commission v Spain.
[518] Para. 40, Case 282/04 Commission v Netherlands.
[519] See also para. 44, C-282/12 Itelcar, which also states that 'as it is, rules which do not meet the requirements of the principle of legal certainty cannot be considered to be proportionate to the objectives pursued'.
[520] Para. 58, Joined Cases C-197/11 and C-203/11 Libert.
[521] Para. 37, Case C-282/12 Itelcar; paras. 27-28, Case C-112/14 Commission v UK.

persons concerned 'in such a way as to adequately circumscribe the exercise of the national authorities' discretion',[522]

- the application of the measure must be confined to the actual conduct which was found in breach of legal obligations (e.g., the corrective tax measure must cover only that aspect of the transaction which went beyond what was appropriate),[523]
    - the scope of the application of the measure must be reduced to the situations actually addressed by the measure (e.g., instead of every transaction the measure must address only those which lead to tax avoidance),[524]
    - this, however, will not remedy the shortcomings of the measure when such a limitation of the scope of the measure in the course of its application does not follow from the 'wording' of the measure in question,[525]
- the scope of the measure must be confined to the specific conducts deemed undesirable by the legislator
    - to target wholly artificial arrangements which do not reflect economic reality and which are carried out for tax purposes alone, and leave arrangements the economic reality of which cannot be disputed unaffected,[526]
    - to apply a corrective tax measure for transactions which go beyond 'what the companies concerned would have agreed under fully competitive conditions', which is confined to the part 'which exceeds what would have been agreed if the companies did not have a relationship of interdependence.'[527]

Restrictions which fail to meet the general legal principles governing Member State conduct, for instances, the equal treatment principle, will not satisfy the necessity/proportionality test. Examples for when the law would regard restrictions disproportionate are presented below.

Disproportionate Member State practies

Deduction of losses in a cross-border situation

in a cross-border scenario (involving subsidiaries established in another Member State), the deduction of losses – a possibility which is available in the case of domestic transactions – is not permitted by the Member State concerned, when the opportunities in the other

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[522] Para. 57, Joined Cases C-197/11 and C-203/11 Libert.
[523] Para. 38, Case C-282/12 Itelcar.
[524] Paras. 39-42, ibid.
[525] Para. 43, ibid.
[526] Para. 28, Case C-112/14 Commission v UK. This point is also raised in the context of examining the legitimacy of the public interest aim claimed.
[527] Para. 72, Case C-311/08 SGI.

Member State to take losses into account for taxation purposes have been exhausted.[528]

Double administratve burdens in a cross-border situation

In a cross-border setting, the national authorities demand that authorisation is obtained for activities which have already been authorised in another Member State and subject the person concerned to special supervision on a continuous basis.[529]

Taking into account the tax law of another Member State in a cross-border situation

In a cross-border scenario, the deduction of losses is not permitted and that possibility has not been offered to any taxpayer as

- in the contrary situation, the Member State where the taxpayer resides would be obliged 'to bear the adverse consequences arising from the tax legislation adopted by the Member State in which the property situated',[530] and
- it would contradict the general legal benchmarks that a 'Member State cannot be required to take account, for the purposes of applying its tax law, of the possible adverse consequences arising from particularities of legislation of another Member State'[531] and that the Member States cannot be required to adjust their tax rules to those of other Member States in order to ensure, in all circumstances, that disparities are removed from the application of national tax rules.[532]

The legitimacy of the ground and proportionality

As indicated earlier, examining the legitimacy of the ground raised by the Member States to justify a restriction on the free movement of capital can involve elements which raise questions about the necessity of the interference. Sometimes, when scrutinising the necessity/proportionality of Member State conduct the EU Court of Justice may touch upon issues which may also be considered when examining the legitimacy of the objective pursued by the Member State concerned. For example, the Court could reach the following conclusions.

Whilst the Member States may use either the imputation- or the exemption method so as to avoid double taxation, for the purpose of maintaining the cohesion of the tax system it is not necessary for them to take account, on the one hand, of the effective level of taxation to which incomes have been subject to calculate the tax advantage when applying the imputation method and, on the other, of only the nominal rate of tax chargeable on the incomes when applying the exemption method.[533]

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[528] Paras. 44-51, Case C-464/03 Marks&Spencers.
[529] Para. 32, Case C-39/11 VBV.
[530] Para. 78, Case C-322/11 K.
[531] Para. 79, ibid.
[532] Para. 80, ibid.
[533] Paras. 60 and 63, Case C-35/11 Test Claimants in the FII Group Litigation.

As to the concrete choice between taking into account the effective level of taxation or the nominal rate of tax imposed, the decision to rely on the nominal rate of taxation when using the exemption method was regarded as resembling a 'grant of a tax credit calculated by reference to that nominal rate of tax,[534] and the choice of taking into account the nominal rate of tax when using the imputation method was considered as being appropriate for preventing double taxation and for ensuring the internal cohesion of the tax system 'while being less prejudiciation to freedom of establishment and the free movement of capital'.[535]

As to this latter choice, while it may still lead to a less favourable tax treatment of foreign-sourced incomes, that unfavourable treatment results from 'the exercise in parallel by the different Member States of their fiscal sovereignty', which under the Treaties – in harmony, with the general rules on competences in taxation matters, is not prohibited.[536]

Residency requirements and proportionality

Under the proportionality test, it may be particularly difficult to justify a residency requirement.[537] In Festersen, the residency requirement introduced in connection with the acquisition of agricultural property – and, in fact, in connection with the acquisition of any kind of property as the particular circumstances relating to individual characteristics of agricultural land were found irrelevant – was rejected by the Court of Justice on the following grounds[538] listed below.

The residency requirement was not coupled with a requirement to farm the property personally, which made it unsuitable to achieve the objective of preserving the traditional form of farming by owner-occupiers.

While the residency requirement is likely to contribute, by definition, to preserving an agricultural community, in light of the phenomena of reduction in the number of farms and of regrouping of farms, that objective cannot be met when the acquisition is made by a farmer who is already resident on a another farm, which made it unsuitable to achieve that objective.

While the residency requirement can reduce the number of potential acquirers and reduce the pressure on agricultural land, and is, thus, suitable to achieve the objective of excluding acquisitions for purely for speculative reasons and the objective of facilitating the preferential appropriation of land by persons wishing to farm it, it goes beyond what is necessary to achieve those aims as it adversely affects the fundamental right of movement protected under the European Convention of Human Rights (ECHR) and there are less restrictive measures to achieve the aims.

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[534] Para. 61, ibid.
[535] Para. 62, ibid.
[536] Para. 64, ibid.
[537] Contrast with the deference showed towards authorization, notification or declaration regimes applied in connection with the acquisition of agricultural property, supra n.
[538] Paras. 29-48, Case C-370/05 Festersen.

In connection of the availability of less restrictive measures, it was found that the requirement of maintaining residency for at least eight years is overly restrictive, especially, that it affects the fundamental right of movement protected under the ECHR, and that the power of waiver of the responsible minister from the residency requirement, which in any event was regulated in breach of the requirement of legal certainty and in the application of which the discriminatory treatment of the citizens of other Member States was not excluded, was strictly limited to exceptional cases and was to be applied restrictively.