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Member State Preferences and the Free Movement of Capital: has there ever been an appetite for open capital markets?

Marton Varju

Hungarian Academy of Sciences

Lendulet-HPOPs Research Group

varju.marton@tk.mta.hu

This paper looks at the evolution of the law on the free movement of capital under Article 63 TFEU from the perspective of the Member States' engagement with the agenda of liberalizing and integrating national capital markets. It argues that because the law – at Treaty level, in secondary legislation and in the jurisprudence of the EU Court of Justice – shows particular characteristics in its development, which distinguish it from the law under the other fundamental freedoms and which provided for a controlled and balanced realization of the central liberalization agenda, the appetite of the Member States for open capital markets in Europe has never been particularly large. The reluctance of the Member States to promote uncritically free capital movements has a number of explanations. Firstly, global experiences with the negative consequences of large and volatile capital movements showed that States must be prepared to control and restrict cross-border capital movements in case of serious disturbances in capital markets. Secondly, the liberalization of capital movements affects the core of national economic and tax policies where, especially when the EU lacks competences or EU measures have not been introduced to regulate certain areas, the Member States are more than willing to pursue their own particular preferences.

The main argument of the paper is developed in the following order. Firstly, a short overview of the law on the free movement of capital is provided with emphasis on its particular course of development. Secondly, based on the assumption that these particular characteristics in the development of Member State obligations under Article 63 TFEU reflect a cautious attitude from the Member States towards liberalized capital movements we examine the potential explanations for the Member States preferring a balanced and sustainable policy framework for the free movement of capital. In this connection, we will first look at the risks associated with large and volatile capital movements as recognized in the EU policy documents and as addressed in the law created under Article 63 TFEU. This is followed by a selective overview of economic and tax policy areas which are considered as sensitive by the Member States. We examine, in particular, the compromise solution created by the Court of Justice in connection with Member State practices controlling the acquisition of agricultural land and how in the area of tax policy the autonomy of the Member States is reconciled with the strict control of national tax measures under Articles 63 and 65 TFEU.

The development of the law on the free movement of capital

It is well known that the free movement of capital is the only fundamental freedom where the liberalization and integration agenda was achieved without radical interferences from the Court of Justice following the original intentions of the Treaties.[1] The liberalization of capital movements took place not by means of enforcing directly effective Treaty obligations through national courts against the Member States but through regulating the scope and detail of liberalization obligations in secondary legislation. This was obviously helped by the original wording of Article 67(1) of the EEC Treaty which provided that the Member States, 'to the extent necessary for the proper functioning of the Common Market', 'progressively abolish' restrictions on intra-Union capital movements and any other discriminatory treatment based on the nationality or the residence of the person concerned.[2] The refusal of the Court of Justice to grant direct effect to Article 67 EEC also indicated that it is not prepared to follow a strategy of judicial deregulation to achieve the corresponding objectives of the Treaties.[3]

Without a general judicially recognized free movement principle for capital movements, which was enacted only in the 1988 Capital Directive[4] and in the subsequent introduction of a new Treaty article on capital movements in the Maastricht Treaty, the liberalization of capital movements in Europe was achieved through secondary legislation adopted in the EU legislative process under the political control of the Member States in the Council. The First Capital Directive[5] 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. It introduced a number of different obligations, which were of different severity depending on the type of capital movements, on the Member States:

- to grant foreign exchange authorisations for List A capital movements (Article 1(1)),
- to grant general permissions for capital movements between the Member States (Article 2(1)),
- to grant foreign exchange authorisations for List B capital movements (Article 3(1)),

[1] John Usher, Monetary movements and the internal market, in NN Shuibhne, Regulating the Internal Market (Elgar, 2006) 181-209, at 181 and 186.
[2] See further indications of a reserved gradual approach to the free movement of capital in Articles 68-71 EEC.
[3] Case 203/80 Casati [1981] ECR 2595. Under Article 67(2) EEC, current payments connected with capital movements had to be freed by the end of the first stage of the transitional period. The Court of Justice, however, refused to allow economic operators to rely on this provision to contest Member State restrictions on capital movements when it maintained in Joined Cases 286/82 and 26/83 Luisi and Carbone [1984} ECR 377 a distinction between capital movements ('financial operation') and current payments (a 'consideration').
[4] Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty, OJ L178, 08/07/1988 P. 0005 – 0018.
[5] Council Directive 60/921/EEC (First Council Directive for the implementation of Article 67 of the Treaty), OJ L43, 12.7.1960, p. 921–932. It divided capital movements into four groups with different degrees of liberalization obligations (Lists A-D). This was amended by Directive 86/566/EEC, OJ 1986 L33 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.

- to simplify – as far as possible – the authorisation and control formalities for capital movements (Article 5(2)),
- to endeavour not to introduce any new exchange restrictions for liberalised capital movements or to make existing provisions more restrictive (Article 6), and
- to notify the Commission of national provisions governing capital movements and of the provisions implementing the directive (Article 7).

The Second Capital Directive[6] pursued the agenda of consolidating the liberalisation of capital movements and of contributing through the 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'. It 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 Capital Directive the scope of its Article 2(1) on granting general permissions on capital transactions and transfers (Article 1). The Second Capital Directive also modified the nomenclature adopted for capital movements in the First Capital Directive.

The 1988 Capital Directive, which repealed the First Capital Directive and the 1972 Capital Directive,[7] in order for the Single Market for capital movements and payments to be completed, by introducing a general free movement principle made Member State obligations simpler and more robust at the same time. Under Article 1(1), which provided that general principle of free movement missing from the Treaties, the Member States were required to abolish restrictions on all intra-Union capital movements. The graduality of Article 67 EEC was, however, kept with regards third country capital movements regarding which the Member States were only obliged to endeavour to attain the same degree of liberalisation as that applicable within the Union (Article 7(1)).

Article 1(1) of the 1988 Capital Directive changed the nature of Member State obligations in connection with the free movement of capital radically when its direct effect was recognised by the Court of Justice.[8] This change, however, has its roots in the political determination of the Member States to further the liberalisation agenda under Article 67 EEC by adopting that directive containing the general free movement principle. The political willingness of the Member States to complete the single market for capital was expressed ultimately in the new Article 56 of the EC Treaty as introduced by the Maastricht Treaty. It has direct effect[9] and its implementation at the Member State level does not depend on the adoption of secondary EU legislation. In its current form (Article 63 TFEU), it holds that all restrictions on the movement of capital and payments between Member States and between Member States and third countries are prohibited.

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[6] Council 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, 22.1.1963, p. 62–74.

[7] Council Directive 72/156/EEC of 21 March 1972 on regulating international capital flows and neutralizing their undesirable effects on domestic liquidity Official Journal L 091 , 18/04/1972 P. 0013

[8] 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 Article 1 were recognised in para. 33, Case C-358/93 Bordessa ECLI:EU:C:1995:54.

[9] Paras. 41-47, Joined Cases C-163, C-165 and C-250/94 Sanz de Lera [1995] ECR I-4821.

Has there ever been an appetite for open and integrated capital markets in Europe?

The previous short overview of the development of the law under what is now Article 63 TFEU indicates that the liberalization of capital movements in the Union has from the beginning been subject to the political control of the Member States. The intention of the Member States to keep the creation of an open capital market in Europe under restraint is expressed not only in the original Treaty provision prescribing for the Member States a qualified and gradual obligation only but also in how liberalization was achieved through secondary legislation the obligations of which differed with respect to different capital movements and were gradually enhanced by the subsequent modifications of the First Capital Directive.[10] The radical changes of the 1988 Capital Directive and the Maastricht Treaty followed only when the Member States became convinced that 'completing the internal market' was the way forward for European integration[11] and that the even further step of establishing the EMU necessitated the complete liberalization of capital movements.[12] These indicate that the Member States were interested in developing a balanced and sustainable integrated market for capital rather than pursuing myopically a simple liberalization agenda.

Member State intentions of a controlled and balanced realization of the free movement of capital are reflected in the broader constitutional framework provided in the Treaties. As it now stands under Articles 63 to 66 TFEU, the benefits of free capital movements are balanced against their risks and the central liberalization agenda is accompanied by parallel policy considerations so as to ensure the internal balance of the policy. The liberalisation obligations of Article 63 are supplemented by Article 65 which allow the Member States to introduce differentiated tax treatment of taxpayers that are not in an objectively comparable situation, and 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.

Further instruments 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 which empowered the Member States to take protective measures for the protection of national economies. Even the First Capital Directive 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)).[13] In

[10] Mainly, through the amendments of the different 'Lists' for capital movements annexed to the directive.

[11] Completing the Internal Market: White Paper from the Commission to the European Council (Milan, 28-29 June 1985) COM(85) 310, June 1985 and the Single European Act.

[12] Report on economic and monetary union in the European Community (Delors Report), Presented 17 April1989 by the Committee for the Study of Economic and Monetary Union, and the Maastricht Treaty.

[13] 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 complies with the obligation to hold the securities for at

connection with 'List B' capital movements, it recognised that the Member States – having consulted the Commission – may maintain or reintroduce foreign exchange restrictions on capital movements[14] 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) and (3)).[15] The Commission may recommend that the restrictions are abolished (Article 3(3)), and it is entitled to examine whether measures for coordinating the economic policies of the Member States are available to address these difficulties and it – after consulting the Monetary Committee – shall recommend their adoption by the Member States (Article 3(2)).

The reluctance of the Member State to submit completely to the liberalisation obligations of a supranational policy is also expressed in the opportunities reserved for a political override of Member State obligations. These apply in strictly confined domains and enable the Member States to regain political control over their legal obligations laid down in the Treaties or concretised in individual procedures. In the current legal framework, the avenues for recouping political control include the possibility in Article 65(4) TFEU for the Council to declare[16] – 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, 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', and 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.

There are a number of areas in which the cautious approach of the Member States with liberalised capital movements is particularly visible. The first concerns the risks associated with open capital markets, especially, with large and volatile capital movements. The second is linked with sensitive areas of national economic policy and to core areas of national tax policies. In the following, the accommodation of these concerns in EU law will be examined.

The risks of free capital movements

The reluctance of the Member States to rush forward with the liberalization of capital movements and their determination to maintain a balanced legal and policy framework for the free movement of capital follow, primarily, from their realization of the considerable risks of open capital markets. It is clear from

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.

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

[15] 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.

[16] 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.

the available policy documents and from the legal texts that the Member States have always been aware of these risks, especially, those that are associated with large, volatile capital movements and that they aimed to create a European capital market which is not only open but also capable of addressing the risks. The Spaak Report,[17] which laid down the policy basis of the free movement of capital, listed its benefits for the Member States and urged convergence in the relevant Member State policies, discussed that national capital controls are introduced, in principle, to react to genuine economic and financial problems and recognised explicitly that volatile capital movements, which are capable of causing severe geographical imbalances, represent a risk for monetary stability. It introduced the ideas of graduality and flexibility which, as demonstrated in the earlier overview, became to characterise the development of law 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.

From the 1970s onwards, Member States concerns for the negative consequences of large and volatile capital movements were given express legal recognition at Union level. Large and volatile capital movements were recognised as not only capable of damaging national economies but also of hindering the related common policies (e.g., the Economic and Monetary Union).[18] It was accepted that 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 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. Its preamble claimed that exceptionally large capital movements 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. 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 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,

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

[18] See also Council Resolution of 9 May 1971 and Commission Staff Working Paper on the free movement of capital in the EU, SWD(2014) 115 final.

empowered 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.

The awareness of the risks of free capital movements of the Member States was expressed the earliest in law 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 just like Article 3 of the 1988 Capital Directive, ex Article 73 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 subjected to the political override by the Council which in a decision taken with qualified majority can 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.

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 73 EEC.[19] The original provisions applied to all Member States. Its current equivalent, Article 143 TFEU, applies only with regards 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'.[20] 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 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.

Based on the understanding that the liberalisation of capital markets cannot entail that the Member States and their economies are left defenceless against harmful, (exceptionally) large and volatile capital

[19] Para. 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.
[20] Article 139 TFEU.

movements, EU law enables the Member States to adopt so called emergency (protective) measures. For this specific purpose, 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.[21] 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 political reassessment by the Member States in the Council.[22]

Their first direct regulation in the 1972 Capital Directive, which was adopted as a counterbalance for the central liberalisation agenda 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).[23] It also provided that these instruments should be used, where necessary, with immediate effect without resorting to further enabling measures (Article 1).

The 1988 Capital Directive provided that Member State protective measures may only be introduced following the authorisation of the Commission, which authorisation also extends to the conditions and the details of the measure in question (Article 3(1)).[24] 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,[25] and the Commission is empowered to override the assessment of the Member State concerned and to decide whether the measure in question can be continued 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

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[21] 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.)

[22] 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.'

[23] 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.

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

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

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)).

Sensitive economic and tax policy areas

The derogations provided in Article 65 TFEU, with their focus on certain national tax policy issues, indicate, firstly, that the free movement of capital interferes with the Member States exercising their tax powers and, secondly, that the Member States want to control those interferences so as to ensure that in the integrated European capital market the ability of the Member States to collect revenues through taxation and to realize the relevant fiscal policy objectives is not unduly undermined. National economic policies, apart from the now repealed Article 3(2) of the First Capital Directive allowing the reinstatement of foreign exchange restrictions in the case when capital movements 'might form an obstacle to the achievement of the economic policy objectives of a Member State', are not given such priority treatment under the free movement of capital. The main reason is that they are likely to violate the general principle of equal treatment, closely followed in the law on the free movement in capital, by giving advantages to domestic economic operators or by disadvantaging the economic operators of other Member States.[26] In fact, under Article 63 TFEU the general principle that derogations of purely economic nature are rejected[27] and that public policy and public security derogations must not serve purely economic ends,[28] is strictly enforced. Nonetheless, there were instances where the obligations under Article 63 TFEU were strongly opposed by individual Member States on economic policy grounds of high national importance and EU law had to take notice, and often to accommodate one way or another economic policy interest raised by the Member States.

Integrating agricultural land into the open European capital market, because of considerations of financial, social or environmental nature and because of agricultural policy interest, has met opposition from a number of Member States. For instance, Hungary negotiated a derogation in Annex X of the Treaty of Accession[29] (Point 3(2) which allowed 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 derogation was not without restriction as it remained subject to the general equal treatment principle,[30] it did not apply to 'nationals of another

[26] In this respect, take note of the tax discrimination clause under Article 65(1) allowing the unequal treatment of taxpayers in case they are distinguishable on objective grounds.
[27] 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)
[28] para. 29, Case C-39/11 VBV— Vorsorgekasse AG.
[29] OJ L 236, 23.9.2003, p. 17–930
[30] 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.'

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', and based on the conditions laid down in the jurisprudence of the Court of Justice,[31] in case Hungary applied 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 subjected to a centralised general review by the Commission and the Council, which latter could have decided to shorten or terminate the derogation period. The derogation was allowed with the possibility of a maximum three year extension period 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'.[32]

For the Member States wanting to restrict the acquisition of agricultural land by citizens from other Member States, the principle of neutrality under Article 345 TFEU governing the impact of EU law on national property ownership regimes did not offer much protection. In principle, it enables the Member States to make the fundamental decisions regarding public and private ownership unfettered from interferences from EU obligations. 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.'[33] 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.[34] The policy or other rationales of Member State decisions affecting property ownership may be taken into account within the general framework of scrutiny of restrictions on the free movement of capital as an overriding reason in the public interest.[35]

The Member States were, however, allowed to establish and maintain prior authorisation schemes for the acquisition of agricultural property. In contrast with the jurisprudence on the prior authorisation of direct foreign investment (currency movements),[36] prior authorisation regimes for immovable property in general are treated in the case law with more lenience mainly because of the objectives pursued. In principle, objectives which are relevant for the acquisition, use and disposal of immovable property,

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[31] Infra.

[32] 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).

[33] para. 24, Case C-452/01 Ospelt ECLI:EU:C:2003:493 referring to Case 182/83 *Fearon* [1984] ECR 3677, paragraph 7, and *Konle*, cited above, paragraphs 7 and 22

[34] 33-37, Joined Cases C-105/12 to C-107/12 Essent Para. 48 C-367/98 Commission v Portugal para. 44 C-483/99 Commission v France; para. 44, Case C-503/99 Commission v Belgium para. 67, Case C-463/00 Commission v Spain see Case C-171/08 *Commission* v *Portugal*, paragraph 64 and the case-law cited, and *Commission* v *Poland*, paragraph 44. Relating to national systems governing the acquisition of immovable property, para. 24, Case C-452/01 Ospelt ECLI:EU:C:2003:493 referring to paras. 28-31, Reisch.

[35] Para.53, Essent. This assessment can be deferred to the national court, para. 55.

[36] paras. 24-25, Bordessa, paras. 25-28, Sanz de Lera, para 15 Eglise de Scientologie

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, are likely to be accepted as legitimate by the Court of Justice.[37] They, nevertheless, must apply without discrimination in pursuance of a public interest ground and they must be proportionate in the sense that the same result cannot be achieved by less restrictive measures.[38]

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.[39] 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.[40] The results of a prior authorisation system may also be achieved effectively by less restrictive but effective prior notification scheme.[41] 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.[42] When grating prior authorisations is subject to requirements on which national law does not impose any substantive restrictions, or 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.[43]

In relation to prior authorisation/notification/declaration systems for agricultural land, the deferential approach of the jurisprudence is obvious. This follows from 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.[44] 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.'[45] 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

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[37] Para. 34 Reisch, para 40. Konle and para 46, Burtscher. The concern 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, Burtscher. The specific objectives of preserving agricultural communities and viable farms, the sympathetic management of green spaces and the countryside, encouraing a reasonable use of the available land by resisting pressure on land, and preventing natural disasters may also be accepted, paras. 37 and 39, Ospelt referring to para. 10, Fearnon.

[38] Paras. 32-33 Case 515/99 Reisch, para. 39 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

[39] Para. 34 Reisch and para. 48, 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, Burtscher.

[40] Para. 35 Reisch, paras 44-48 Konle, para. 52, Burtscher and paras. 49-50 Salzmann

[41] Para. 37 Resich.

[42] Para. 38 Reisch and para 51, Salzmann

[43] Para. 38 Reisch

[44] Paras. 43-45, Ospelt

[45] Para. 43, ibid.

management', and legal certainty, would thus be undermined.[46] This, however, does not mean that a review of proportionality would not be carried out.[47] 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.'[48] This is the case, especially, when less 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.[49]

The generous listing of derogations in the Treaties aimed at national tax policies seems to suggest that the fiscal sovereignty and autonomy of the Member States enjoys a considerable degree of immunity from the obligations laid down in Article 63 TFEU. This may also follow from the fact that the EU has not been endowed with powers of direct taxation and that these competences have remained with the Member States.[50] 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.[51] 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 another Member State),[52] and they are not obliged to ensure taxation 'which removes any disparities arising from national tax rules'.[53]

In the field of direct taxation,

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.[54]

In the field of avoiding double taxation,

in the absence of unifying or harmonising measures adopted by the European Union,[55] *the Member States retain competence for determining the criteria for taxation on income and capital with a view to*

[46] Para. 44, ibid.
[47] Para. 46, ibid.
[48] 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).
[49] 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).
[50] 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 in bilateral tax conventions between Member States.
[51] Para. 37 Joined Cases C-578/10 to C-580/10, van Putten para. 31Case C-157/10, Banco Bilbao Vizcaya Argentaria SA Para. 18, Case C489/13 Verest *Imfeld and Garcet*, C-303/12, EU:C:2013:822, paragraph 41 and the case-law cited.
[52] para. 39, , Case C-157/10, Banco Bilbao Vizcaya Argentaria SA
[53] para. 80, Case C-322/11, K.
[54] Para. 37, Case C-387/11, Commission v Belgium *Test Claimants in Class IV of the ACT Group Litigation*, paragraph 50; *Test Claimants in the FII Group Litigation*, paragraph 47; Case C-194/06 *Orange European Smallcap Fund* [2008] ECR I-3747, paragraph 30; and Case C-128/08 *Damseaux* [2009] ECR I-6823, paragraph 25, and *Commission* v *Germany*, paragraph 45
[55] Apart from Convention 90/436/EEC on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (OJ 1990 L 225, p. 10), no unifying or harmonising measure for the elimination of double taxation had yet been adopted at EU level and the Member States did not conclude any multilateral convention to that effect under ex Article 293 EC, para. 50, Case 376/03 D

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.[56]

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.[57]

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.[58]

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. Even in these domains, they are required to observe the principle of equal treatment[59] and they must ensure compliance with EU law, in particular, the free movement of capital.[60] 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,[61] 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.'[62] Again, these powers must be exercised in compliance with EU law, especially, the principle of proportionality.[63]

Although considerations of national tax policy, mainly because of competences issues, are placed nearly on an equal footing as to their relevance with the liberalisation obligations of Article 63 TFEU, the jurisprudence of the Court of Justice imposed considerable restrictions on the Member States pursuing these objectives. Generally, the ability of the Member States to justify their measures and policies has

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[56] Inter alia, Para. 18, Case C489/13 Verest *Imfeld and Garcet*, C-303/12, EU:C:2013:822, paragraph 41 and the case-law cited Case C-307/97 *Saint-Gobain ZN* [1999] ECR I-6161, paragraph 57; Case C-385/00 *de Groot* [2002] ECR I-11819, paragraph 93; Case C-265/04 *Bouanich* [2006] ECR I-923, paragraph 49.

[57] Para. 40 ase C-35/11Test Claimants in the FII Group Litigation. Para. 40 ase C-35/11Test Claimants in the FII Group Litigation Case C-513/04 *Kerckhaert and Morres* [2006] ECR I-10967, paragraph 22, and Case C-157/10 *Banco Bilbao Vizcaya Argentaria* [2011] ECR I-13023, paragraph 31 and the case-law cited

[58] para. 31Case C-157/10, Banco Bilbao Vizcaya Argentaria SA see Case C-513/04 *Kerckhaert and Morres* [2006] ECR I-10967, paragraph 23

[59] Para. 40 ase C-35/11Test Claimants in the FII Group Litigation para. 37-40, Case C-157/10, Banco Bilbao Vizcaya Argentaria SA *ase C-279/93 Schumacker [1995] ECR I-225, paragraphs 21 and 26; Case C-80/94 Wielockx [1995] ECR I-2493, paragraph 16; and Case C-107/94 Asscher [1996] ECR I-3089, paragraph 36)*

[60] Inter alia, Para. 18, Case C489/13 Verest *Imfeld and Garcet*, C-303/12, EU:C:2013:822, paragraph 41 and the case-law cited Para. 37 Joined Cases C-578/10 to C-580/10, van Putten Para. 36, Case C-387/11, Commission v Belgium; para. 14, Joined Cases C-338/11 to C-347/11Santander Asset Management SGIIC SA; see, inter alia, Case C-374/04 *Test Claimants in Class IV of the ACT Group Litigation* [2006] ECR I-11673, paragraph 36.

[61] Infra n.

[62] Para. 33, Case C-282/04 Commission v Netherlands

[63] Ibid.

been rather limited owing to the Court's reluctance to accept the grounds raised as legitimate.[64] The approach of the Court seems to have been influenced by the fact that some of the grounds raised or their circumstances are incompatible with the idea of the Single Market and with Member State obligations of effective compliance with their obligations. For instance, the burdens of compliance with Article 63 TFEU for Member State tax administrations will be refused without much hesitation.[65] The availability of EU instruments addressing the substantive tax problem or problem of tax administration also reduce the opportunity for the Member States.[66]

The diminution of tax revenue[67] has been constantly refused as an overriding reason in the public interest by the Court of Justice.[68] It Court found that the Member 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.[69] 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.[70] 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 to domestic public institutions through taxation.[71] 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.[72]

In general, the treatment of tax policy derogations by the Court of Justice indicates that Article 63 TFEU will only accommodate considerations that are genuinely linked with national tax policy and that are necessary for the adequate attainment of genuine tax policy needs. Because Member State tax provisions which are caught by Article 63 TFEU would discriminate between taxpayers on the basis of their place of residence, would offer overly generous coercive and other powers to national tax

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[64] This is a general trend 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?, at 281

[65] Para. 56, van Caster para. 48, Case C-262/09 Meilicke Para. 54 Manninen see, to that effect, judgments in C-334/02 *Commission* v *France*, EU:C:2004:129, paragraph 29; C-386/04 *Centro di Musicologia Walter Stauffer*, EU:C:2006:568, paragraph 48, and C-418/07 *Papillon*, EU:C:2008:659, paragraph 54. 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 realy on their own misconduct to avoid meeting their legal obligations.

[66] Inter alia, paras. 48-49, Case C-493/09, Commission v Portugal Para. 55 Case C-326/12, van Caster Para. 33, 35, 36 Case C-132/10 Olivier Halley Para. 43, Case C 296/12 Commission v Belgium; paras. 72-79, Case C-190/12 Emerging Markets Series of DFA Investment Trust Company

[67] 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 failing to establish the difference between the two grounds, para. 42, Bosal. See also general fiscal interests excluded as legitimate grounds, supra n.

[68] 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 Series of DFA Investment Trust Company *Haribo Lakritzen Hans Riegel and Österreichische Salinen*, paragraph 126 Paras. 39-40Case C-10/10, Commission v Austria.

[69] Para. 103, Case C-190/12 Emerging Markets Series of DFA Investment Trust Company

[70] Ibid.

[71] Paras. 39-40Case C-10/10, Commission v Austria.

[72] Pp 87-88, Act Clair

authorities, or they would unsuitable to achieve the desired aim, the derogations are practically never allowed. This follows even from technical requirements that the aim pursued must be visible from the national measure in question,[73] that the ground raised must be the actual objective pursued by the measure in question,[74] or that the objective pursued must be correctly determined and the grounds available for derogation must not be abused or arbitrarily extended.[75] The derogation allowing differentiated tax treatment of taxpayers in objectively different circumstances is interpreted strictly as not allowing arbitrary discrimination prohibited in Article 65(3) TFEU,[76] and it '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.'[77] The ground of preserving the coherence of the national tax system is interpreted as allowing only clear cases of tax collection deferral by the Member States.[78] Concerning the ground of ensuring effective fiscal supervision, while the jurisprudence has recognised that the Member States may face considerable difficulties in cross-border tax administration,[79] it constantly reminds the Member States that instead of imposing restrictions on the free movement of capital they should rely on the available EU and international (OECD) measures on mutual assistance in taxation matters or they should make alternative administrative arrangements available to taxpayers so that they can provide the information necessary for domestic tax authorities.[80] In case of national measures combatting tax avoidance and tax evasion, only measures aimed specifically at preventing and combatting illegal tax avoidance and tax evasion practices are accepted[81] and general statutory presumptions of illegal conduct will not suffice.[82]

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[73] Paras. 24-26, Case C-133/13, Q; paras, . 29-31, Case C-87/13 X

[74] Para. 69 Case C-375/12 Bouanich.

[75] Xref to effective fisc supervision

[76] There is a distinction between the 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 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, Manninen and paras. 26-27 Lenz

[77] Para. 28, Case C-319/02 Manninen and para. 27. 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 with an absolute prohibition on discrimination, Usher 204.

[78] P. 91. Based on the examination of the objective pursued by the tax measure in question, para. 43, Manninen, para. 27, Case C-292/04 *Meilicke and Others* [2007] ECR I-1835 and Case C-9/02 *De Lasteyrie du Saillant* [2004] ECR I-0000, paragraph 67. In paras. 43-46, 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.

[79] Futura vestergaard

[80] Para. 18, Bachmann, paras. 31-32, Case C-334/02 Commission v France, Case C-55/98 *Vestergaard* [1999] ECR I-7641, paragraphs 26 and 28

[81] See para. 62, Case C-436/00 X and Y para. 60, Case C-322/11, K. Under the freedom of establishment, Case C-196/04 *Cadbury Schweppes and Cadbury Schweppes Overseas* [2006] ECR I-7995, paragraph 50; Case C-524/04 *Test Claimants in the Thin Cap Group Litigation* [2007] ECR I-2107, paragraph 73; Case C-105/07*Lammers & Van Cleeff* [2008] ECR I-173, paragraph 27; Case C-330/07 *Jobra* [2008] ECR I-9099, paragraph 37; and Case C-318/10 *SIAT* [2012] ECR, paragraph 38

[82] Para. 62, Case C-436/00 *X and Y* para. 60, Case C-322/11, K. See under other fundamental freedoms, Case C-196/04 *Cadbury Schweppes and Cadbury Schweppes Overseas* [2006] ECR I-7995, paragraph 50; Case C-524/04 *Test Claimants in the Thin Cap Group Litigation* [2007] ECR I-2107, paragraph 73; Case C-105/07*Lammers*

Conclusions

The law on the free movement of capital, as it developed in the Treaties, secondary legislation and in the case law of the Court of Justice, gives an accessible example of how the EU commitments of the Member States – based on national preferences expressed at a given point of time – can collide with their national preferences. These conflicts can be fed into the common policy framework, either as a common determination of the Member States to make the EU policy more balanced and sustainable, as we saw in the case of the risks of liberalised capital movements, or as a particular Member State position defended before the Court of Justice. In the latter case, as our examples showed, a balanced, compromise solution is achievable provided that the Member State interest can be accommodated under the idea of a balanced and sustainable policy framework for the free movement of capital. Both of these indicate that the appetite of the Member States for open capital markets in Europe has never been particularly ferocious and that they were interested rather in a balanced diet of free capital movements, controlled foreign investments, protected local economic assets and of effective tax powers.

& Van Cleeff [2008] ECR I-173, paragraph 27; Case C-330/07 *Jobra* [2008] ECR I-9099, paragraph 37; and Case C-318/10 *SIAT* [2012] ECR, paragraph 38