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Freedom as a source of constraint:

Expanding market discipline through free movement

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FREEDOM AS A SOURCE OF CONSTRAINT: EXPANDING MARKET DISCIPLINE THROUGH FREE MOVEMENT

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Abstract

Free movement increases the degree of market discipline within every Member State by exposing domestic workers and businesses to competitive pressures coming from other Member States. However, the nature of this amplifying effect on market discipline is fundamentally different depending on whether free movement is interpreted as requiring national treatment (chiefly in relation to workers, with the notable exception of posted workers) or mutual recognition (chiefly in the areas of goods, services and companies).

National treatment tends to subject domestic and incoming workers to the same regulatory standard, which is defined by the host State (level-playing field). As a result, domestic and incoming workers are engaged in a process of merit-based competition, in which superior merits tend to translate into higher market shares. To that extent, national treatment generates extra competitive pressures on domestic workers, who can be displaced by incoming workers showing superior merits. However, these extra competitive pressures are likely to be limited and not be felt as 'unfair', since they arise on a level-playing field.

By contrast, mutual recognition subjects domestic and foreign producers to different regulatory standards: domestic goods, services and companies must abide by the law of the host State, whereas incoming goods, services and companies remain subject to the law of their home State. As a result, competition between domestic and imported producers is based not only on merit, but also on the cost of compliance with national laws. Producers established in a low(er)-regulation home State enjoy a structural competitive advantage – originating in regulation – over domestic producers established in the host State, irrespective of their eventual superior merits. Consequently, the competitive pressures added by mutual recognition may be substantial and felt as 'unfair'; arguably, the so-called 'Polish plumber' is a mutual-recognition plumber, not a national-treatment plumber.

Keywords

Free movement; mutual recognition; national treatment; market discipline; social dumping

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Introduction

This working paper[1] describes the amplifying effect of free movement upon market discipline. Market discipline can be defined as the constraining force collectively exerted by competitors present on a market. As the number of potential outlets is limited, economic agents offering goods and services are exposed to the risk of being displaced by competitors. In order to mitigate this risk and preserve or increase their market shares, they are forced to adapt their behaviour: this constraining force is hereinafter designated as market discipline.

Academic research in the area of free movement law is often limited to a description of the legal obligations falling upon Member States, chiefly national treatment and mutual recognition. The present paper deals with another – less immediate but no less important – constraint originating in free movement, namely market discipline. Free movement increases the degree of market discipline within every Member State, by exposing domestic workers and businesses to competitive pressures coming from other Member States. In order to enquire this amplifying effect of free movement upon market discipline, it is useful to establish, in a first step, a typology of the policies available to Member States when regulating cross-border activities (first part). This typology will permit a structured approach to the effects of free movement on market discipline, and in particular of the fundamentally different impacts of national treatment and mutual recognition (second part).

Typology of policies available to member states when regulating cross-border activities

Member States may adopt one of three distinct policies when regulating cross-border activities: they can treat cross-border activities worse, equally or better than domestic ones. These three policies are usually captured by the concepts of discrimination, national treatment and mutual recognition.

Discrimination is the policy traditionally applied in trade relationships among States: it takes the form chiefly of customs duties and quotas or, in the most extreme cases, of economic embargos. Since the founding of the European Economic Community on 1 January 1958 by the Treaty of Rome (signed in 1957), discriminations on grounds of nationality or origin are as a rule incompatible with the freedoms of movement.[2] There are numerous examples of discriminatory measures struck down by the Court interpreting the Treaty provisions on free movement, including direct discriminations (such as nationality requirements)[3] and indirect ones (such as residence requirements).[4] Exceptionally, discriminatory measures may be upheld under free movement law: in such cases, the freedoms of

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[1] The author is référendaire at the Court of Justice of the European Union (LL.M. Harvard; Ph.D. EUI). Obviously, this working paper only reflects the views of the author, not that of the Court. This working paper has benefited from insightful comments and criticisms kindly offered by, in the alphabetical order, Bruno de Witte, Thierry Erniquin, Susanna Greijer, Ulrich Klinke and Charles-Henry Massa. The final version of this working paper will be published in P Koutrakos, J Snell (eds), Research Handbook on the Law of the EU's Internal Market (Cheltenham: Elgar, 2015, forthcoming).

[2] According to settled case law, the freedoms of movement include an 'in-built' rule of non-discrimination: see eg *Generali-Providencia Biztosító*, Case C-470/13, EU:C:2014:2469, paras 30–31; *Josemans*, Case C-137/09, EU:C:2010:774, paras 51–52. Article 18 TFEU applies independently only to situations for which the Treaty lays down no specific rules of non-discrimination. For a recent instance in which the Court applied 18 TFEU independently, since the freedoms of movement were not applicable, see *International Jet Management*, Case C-628/11, EU:C:2014:171. The Court ruled that Article 18 TFEU precluded a German legislation obliging non-German airlines to obtain permission to make inward flights in respect of charter flights, which required evidence that German airlines were not in a position to carry out the flights (a 'non-availability declaration').

[3] See n 14 below.

[4] See n 15 below.

movement impose no particular legal obligation on Member States, which are granted a 'licence to discriminate'.[5] The Treaty FEU itself provides for several derogations to the freedoms of movement;[6] for instance, Article 51 TFEU grants Member States a licence to discriminate in relation to activities that are connected 'with the exercise of official authority'.[7] However, the Court has notoriously adopted a restrictive stance towards derogations to free movement.[8]

Overall, and without denying the existence of certain derogations granting a licence to discriminate to Member States, the upholding of discriminations on grounds of nationality remains exceptional under free movement law. Of much greater relevance are the obligations of national treatment and mutual recognition.

National treatment: treating cross-border and domestic activities equally

The second policy available to Member States, namely national treatment, consists in treating domestic and cross-border activities equally. The general idea conveyed by the expression 'national treatment' is that Member States must 'treat' nationals of other Member States as their own 'nationals'. It is important to underline that an obligation of national treatment does not compel Member States to treat cross-border activities better than domestic ones, by contrast with an obligation of mutual recognition (see next section).

Under free movement law, obligations of national treatment are mostly imposed in relation to citizens and workers (with the notable exception of posted workers[9]). The regulation of migrant workers aptly illustrates the concrete functioning of the obligation of national treatment. Article 45(2) TFEU provides that the freedom of movement for workers shall entail the abolition of any discrimination based on nationality between workers of the Member States as regards employment, remuneration and other conditions of work and employment. National treatment means that, as a rule, the State of employment ('host State') is bound to apply the laws governing the activities of its own nationals ('host law') to incoming workers. This obligation of national treatment for migrant workers has been implemented by Regulation 492/2011 in relation to conditions of employment and work[10] and by

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[5] See for instance *Dano*, Case C-333/13, EU:C:2014:2358 (refusal to grant certain special non-contributory cash benefits in Germany to nationals of other Member States who are not economically active, whereas those benefits are granted to German nationals in the same situation); *Josemans*, Case C-137/09, EU:C:2010:774 (municipal rules adopted in Maastricht in order to restrict the admission to coffee-shops to Netherlands residents); *Geven*, Case C-213/05, EU:C:2007:438 (requirement of residence and/or substantial employment in Germany to receive child-raising allowance); *Baldinger*, Case C-386/02, EU:C:2004:535 (Austrian nationality requirement to receive a compensation a monthly allowance for former prisoners of war).

[6] See especially Articles 36 TFEU (goods); 45(4) TFEU (workers); 51, 52(1) and 62 TFEU (establishment and services*);* 65(1)(a) TFEU (capitals)

[7] See Case C-438/08 *Commission/Portugal*, EU:C:2009:651, para 36 and case law cited.

[8] See C Barnard, 'Derogations, Justifications and the Four Freedoms: Is State Interest Really Protected?' in C Barnard and O Odudu (eds), *The Outer Limits of European Union Law* (Hart Publishing: Oxford, 2009), 273–305. According to the Court's settled case law, the freedoms of movement must be interpreted broadly, and correlatively any derogation must be interpreted strictly: see inter alia *Commission/Germany*, Case C-319/05, EU:C:2007:678, para 88 (goods); *Omega*, Case C-36/02, EU:C:2004:614, para 30 (services); *Ziebell*, Case C-371/08, EU:C:2011:809, para 81 (workers); *Bozkurt*, Case C-303/08, EU:C:2010:800, para 56 (persons); *Verest and Gerards*, Case C-489/13, EU:C:2014:2210, para 26 (capital); *Commission v France*, Case C-50/08, EU:C:2011:335, para 74 (establishment); *Insinööritoimisto InsTiimi Oy*, Case C-615/10, EU:C:2012:324, para 35 (freedoms of movement in general).

[9] See n 63 to n 73 below and accompanying text.

[10] Regulation (EU) 492/2011 of the European Parliament and of the Council of 5 April 2011 on freedom of movement for workers within the Union [2011] OJ L 141/1. See in particular Article 1(1) on equal treatment in relation to the right to

Regulation 883/2004 in the field of social security.[11] Both regulations have been the object of ample case law.[12]

The overall effect of these provisions is to trigger a change of law whenever a worker takes up an employment in another Member State: the regulatory powers of the former country of employment (home country) are pre-empted to the benefit of the new country of employment (host country). As nicely coined by AG Fennelly, 'the migrant worker must take the national employment market as he finds it'.[13]

However, national treatment does not always amount to the mere extension of host law to incoming workers: national treatment may require the host State to adapt host law and be 'other-regarding', by taking into account facts or events occurring in the home State. Indeed, the mere application of host law (namely the laws governing the activities of nationals) will prevent direct discriminations, by precluding the host State from treating non-nationals differently from its own nationals.[14] But applying host law to non-nationals could still lead to indirect discriminations, especially when it relies on facts and events occurring on the territory of the host State. Residence requirements represent one classical example of such indirect discriminations:[15] even where they apply to both nationals and non-nationals, residence requirements are 'liable to operate mainly to the detriment of nationals of others Member States, as non-residents are in the majority of cases foreign nationals'.[16] Therefore, unless justified, residence requirements are incompatible with an obligation of national treatment.[17]

(Contd.)

take up and pursue an activity as an employed person in another Member State; Article 7(1) on equal treatment with regard to conditions of employment and work; Article 7(2) on equal treatment with regard to social and tax advantages.

[11] Regulation (EU) 883/2004 of the European Parliament and of the Council of 29 April 2004 on the coordination of social security systems [2004] OJ L 166/1. See in particular Article 4 on equal treatment with regard to benefits and obligations; Articles 11(1) and 11(3)(a) according to which employed or self-employed persons shall be only subject to the legislation of the Member State of employment.

[12] On the interpretation of Article 1(1) of Regulation 1612/68, predecessor of Article 1(1) of Regulation 492/2011, see eg *Commission v Greece*, Case C-290/94, EU:C:1996:265; *Commission v Belgium*, Case C-37/93, EU:C:1993:911. On the interpretation of Article 7(1) of Regulation 492/2011, see *Zentralbetriebsrat der gemeinnützigen Salzburger Landeskliniken*, Case C-514/12, EU:C:2013:799. On the interpretation of its predecessor, Article 7(1) of Regulation 1612/68, see eg *Commission v Italy*, Case C-371/04, EU:C:2006:668; *Köbler*, Case C-224/01, EU:C:2003:513. On the interpretation of Article 7(2) of Regulation 1612/68, predecessor of Article 7(2) of Regulation 492/2011, see eg *Giersch*, Case C-20/12, EU:C:2013:411; *Commission/Netherlands*, Case C-542/09, EU:C:2012:346; *Hartmann*, Case C-212/05, EU:C:2007:437; *Commission v Luxembourg*, Case C-299/01, EU:C:2002:394; *Zurstrassen*, Case C-87/99, EU:C:2000:251. On the interpretation of Article 3(1) of Regulation 1408/71, predecessor of Article 4 of Regulation 883/2004, see eg *Landtová*, Case C-399/09, EU:C:2011:415; *Chateignier*, Case C-346/05, EU:C:2006:711; *Laurin Effing*, Case C-302/02, EU:C:2005:36; *Offermanns*, Case C-85/99, EU:C:2001:166.

[13] AG Fennelly, *Graf*, Case C-190/98, EU:C:1999:423, para 32.

[14] A different treatment may take the form of an additional obligation (eg higher tax rate, extra requirement to exercise a profession) or a denied benefit (eg tax benefit, social benefit). Nationality requirements represent a common form of direct discrimination: see eg *Reyners*, Case 2/74, EU:C:1974:68 (nationality requirement to exercise the profession of lawyer in Belgium); *Commission v Belgium (Notaries)*, Case C-47/08, EU:C:2011:334 (nationality requirement to exercise the profession of notary in Belgium); *Landtová*, Case C-399/09, EU:C:2011:415, paras 41–43 (nationality requirement to receive a supplement to old age benefit in Czech Republic); *Haralambidis*, Case C-270/13, EU:C:2014:2185 (nationality requirement to become president of a port authority in Italy).

[15] See eg *Landtová*, Case C-399/09, EU:C:2011:415, paras 44–46 (residence requirement to receive a supplement to old age benefit in Czech Republic); *Commission/Netherlands*, Case C-542/09, EU:C:2012:346, paras 52–55 (residence requirement to receive portable studies funding); *Giersch*, Case C-20/12, EU:C:2013:411, paras 41–46 (residence requirement in Luxembourg to receive studies funding).

[16] See inter alia *Giersch*, Case C-20/12, EU:C:2013:411, paras 42–45.

[17] Analytically, accepting the equivalence of a residence in another State is tantamount to removing the requirement of a residence in the host State altogether.

Several cases decided by the Court in the field of social security further illustrate this obligation to accept the equivalence of facts and events occurring on the territory of another State. *Reichel-Albert* concerned a German legislation which provided that, for the purposes of the granting of an old-age pension, child-raising periods completed in another Member State were, as a rule, not taken into account, unlike those completed in the national territory (para 37).[18] The Court ruled that such legislation was contrary to the principle of equal treatment (paras 41–42) and that Article 21 TFEU required Germany to take account of child-raising periods completed in another Member State as though those periods had been completed on its national territory (para 45). This judgment did not preclude Germany, as host country, from applying the standard of its choosing (national treatment); but it did oblige Germany to adapt its laws in order to take into account an event that occurred in Belgium 'as though this event occurred on its national territory' (obligation to be other-regarding).[19] This obligation has been codified in Article 5 of Regulation 883/2004 on the coordination of social security systems, headed 'equal treatment of benefits, income, facts or events', which provides that the competent State must treat, as though they had taken place on its own territory, the receipt of social security benefits or other income and the occurrence of facts or events in another Member State.

In the field of diplomas, the *Vlassopoulou* judgment provides another illustration of national treatment qualified by an obligation to be other-regarding.[20] Mrs Vlassopoulou applied to the German authorities for admission as a Rechtsanwältin. Her application was rejected because she did not meet the formal requirements imposed under German law, although she held a law degree from a Greek university, a doctorate in law from a German university and a working experience with a German law firm. The Court ruled that, in the absence of harmonization of the conditions of access to a particular occupation, Member States were entitled to lay down the knowledge and qualifications needed in order to pursue it (paras 9–12: national treatment).[21] Nevertheless, the host State had to take into consideration the diplomas, certificates and other evidence of qualifications acquired in other Member States (paras 15–23: obligation to be other-regarding).[22] The Court applied a similar reasoning in the *Gebhard* case.[23] Italy was entitled to lay down conditions, and enforce them upon non-nationals, for the taking-up and pursuit of certain self-employed activities such as the profession of lawyer, and for the use of professional titles such as 'avvocato' (paras 35–36: national treatment). Nevertheless, Italian authorities had to take into consideration the knowledge and qualifications already acquired in another Member State (paras 37–38: obligation to be other-regarding).

To sum up, an obligation of national treatment compels the host State to treat non-nationals as its own nationals. As a rule, the host State is bound to extend the laws governing the activities of its nationals to workers coming from other States. Nevertheless, an obligation of national treatment may also require the host State to adapt host law by treating facts or events that occurred in another State as though they had occurred on its own territory.

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[18] *Reichel-Albert*, Case C-522/10, EU:C:2012:475.

[19] Similar decisions in the field of social security, in which the Court obliged the host State to accept the equivalence of facts and events that occurred in the home State, include *Dumont de Chassart*, Case C-619/11, EU:C:2013:92; *Klöppel*, Case C-507/06, EU:C:2008:110; *Öztürk*, Case C-373/02, EU:C:2004:232.

[20] *Vlassopoulou*, Case C-340/89, EU:C:1991:193.

[21] See also *Bouchoucha*, Case C-61/89, EU:C:1990:343, para 16, in which the Court allowed a Member State (France) to preclude one of its nationals, who held a diploma in osteopathy from another Member State (UK), from pursuing this activity on its territory where it was restricted to persons holding the qualification of doctor of medicine.

[22] For a recent application of this comparison exercise, see *Peñarroja Fa*, Joined Cases C-372/09 and C-373/09, EU:C:2011:156, paras 76–78.

[23] *Gebhard*, Case C-55/94, EU:C:1995:411.

Mutual recognition: treating cross-border activities better than domestic ones

Whereas the obligation of national treatment compels the host State to treat nationals of other Member States as its own nationals, the obligation of mutual recognition goes beyond that by requesting the host State to treat nationals of other Member States better than its own nationals. In most instances, 'better treatment' means that some obligations imposed by the host State to domestic producers are not applicable to incoming goods, services or companies.

The best way to highlight the differences between national treatment and mutual recognition is to start with the seminal *Cassis de Dijon* judgment (1979), in which the Court established for the first time that free movement of **goods** could demand more than national treatment.[24] As is well known, this case concerned the import of a French fruit liqueur named 'Cassis de Dijon' into Germany. The German monopoly administration for spirits rejected the application for import, on the ground that 'Cassis de Dijon', whose alcohol content was between 15 and 20%, did not meet the minimum alcohol content of 25% required for the marketing of fruit liqueurs in Germany (paras 2–3). The Court first examined the possibility of this decision being 'necessary in order to satisfy mandatory requirements' (para 8):

> Obstacles to movement … resulting from disparities between the national laws relating to the marketing of the products in question must be accepted in so far as those provisions may be recognized as being necessary in order to satisfy mandatory requirements relating in particular to the effectiveness of fiscal supervision, the protection of public health, the fairness of commercial transactions and the defence of the consumer.

After reviewing the grounds of justification put forward by the German government (paras 9–13), the Court judged that the minimum alcohol requirement 'did not serve a purpose which is in the general interest and such as to take precedence over the requirements of the free movement of goods' (para 14). The Court concluded its reasoning by formulating the new principle on which it founded its ruling, namely mutual recognition (para 14):

> There is therefore no valid reason why, provided that they have been lawfully produced and marketed in one of the Member States, alcoholic beverages should not be introduced into any other Member State; the sale of such products may not be subject to a legal prohibition on the marketing of beverages with alcohol content lower than the limit set by the national rules.

If the Court had interpreted the free movement of goods as imposing a mere obligation of national treatment, as pleaded by the German government, it is undisputable that Germany would have won the *Cassis de Dijon* case: indeed, this minimum alcohol content requirement was not discriminatory, either directly or indirectly, against French liqueurs. German producers of fruit liqueurs with alcohol content lower than 25% were similarly barred from selling such products in Germany. Nevertheless, the Court ruled that Germany could not apply this requirement of minimum alcohol content to French imported liqueurs. Therefore, mutual recognition goes beyond national treatment by requesting the host State to treat goods from other Member States *better* than domestic goods.

Following *Cassis de Dijon*, the Court almost systematically ruled that national treatment was not sufficient to ensure free movement of goods, thereby extending the scope of the obligation of mutual recognition. In all those cases, the host State did not claim a licence to discriminate against foreign products, but merely sought to apply non-discriminatory host laws to domestic and foreign products (national treatment).[25] The Court established a derogation to the principle of mutual recognition in

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[24] Rewe-Zentral ('Cassis de Dijon'), Case 120/78, EU:C:1979:42.

[25] See eg *Rau Lebensmittelwerke*, Case 261/81, EU:C:1982:382 (para 12); *3 Glocken et Kritzinger*, Case 407/85, EU:C:1988:401 (para 10); *Guimont*, Case C-448/98, EU:C:2000:663 (paras 26–27); *Mars*, Case C-470/93,

Keck and Mithouard, which concerned a general prohibition on resale at a loss imposed under French law.[26] The Court confirmed the obligation of mutual recognition for 'product requirements' imposed by the host State (para 15), but imposed a mere obligation of national treatment for 'selling arrangements' (para 16). However, the scope of the *Keck* derogation for selling arrangements remained rather limited.[27]

The principle of mutual recognition has progressively pervaded other areas of free movement, chiefly the freedom to provide **services**. Arguably, the Court introduced the mutual recognition principle into the area of services in the *Säger* judgment, delivered in 1991. *Säger* concerned a German law making the provision of patent renewal services in Germany subject to the issue of an administrative licence for which the possession of certain professional qualifications, such as patent agent or lawyer, was required.[28] Manfred Säger, a patent agent, sued Dennemeyer, a UK company, for providing patent renewal services in Germany without the required licence. As in *Cassis de Dijon*, if the Court had interpreted the freedom to provide services as imposing a mere obligation of national treatment, it is undisputable that Manfred Säger would have won this case: indeed, this licence requirement applied in the same way, both in law and in fact, to service providers from Germany and from other Member States. However, the Court stated that (para 12):

> [Article 56 TFEU] requires not only the elimination of all discrimination against a person providing services on the ground of his nationality but also the abolition of any restriction, even if it applies without distinction to national providers of services and to those of other Member States, when it is liable to prohibit or otherwise impede the activities of a provider of services established in another Member State where he lawfully provides similar services.

The application of this licence requirement to services providers from other Member States constituted a restriction on the freedom to provide services, even if it applied in the same way, both in law and in fact, to service providers from Germany (para 14). Therefore, the Court ruled that the freedom to provide services compelled the host State to treat services providers from other Member States *better* than domestic service providers, by not applying this licence requirement, in accordance with the principle of mutual recognition. Echoing the 'mandatory requirements' of *Cassis de Dijon*, the Court added that (para 15):

> [T]he freedom to provide services may be limited only by rules which are justified by imperative reasons relating to the public interest and which apply to all persons or undertakings pursuing an activity in the State of destination, in so far as that interest is not protected by the rules to which the person providing the services is subject in the Member State in which he is established.

In the case at hand, however, the licence requirement could not be justified as it went beyond what was necessary to protect the recipients of patent renewal services (paras 17–18). In the wake of *Säger*, the Court increasingly considered non-discriminatory measures applied by the host State as restrictions

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EU:C:1995:224 (paras 11–15); *Commission v Italy*, Case C-14/00, EU:C:2003:22 (paras 69, 75, 78); *Commission v Denmark*, Case C-192/01, EU:C:2003:492 (paras 39–41).

[26] *Keck and Mithouard*, Joined Cases C-267/91 and C-268/91, EU:C:1993:905.

[27] The Court imposed mutual recognition in relation to non-discriminatory rules unrelated to product requirements: see eg *Association des Centres distributeurs Leclerc and Thouars Distribution*, Case 229/83, EU:C:1985:1, paras 23–26 and *Fachverband der Buch- und Medienwirtschaft ('LIBRO')*, Case C-531/07, EU:C:2009:276, paras 17–22 (requirements of minimum retail price for books); *Commission v Italy*, C-110/05, EU:C:2009:66, paras 50 and 55–58 and *Mickelsson and Roos*, Case C-142/05, EU:C:2009:336, paras 25–28; *Sandström*, Case C-433/05, EU:C:2010:184, paras 31–40 (restrictions on the use of motorcycle trailers and personal watercrafts).

[28] *Säger*, Case C-76/90, EU:C:1991:331.

to the freedom to provide services.[29] Mutual recognition is also the directing principle of the 'Bolkestein' Directive 2006/123 on services in the internal market.[30] This directive has vocation to apply to all services[31] and imposes a stringent obligation of mutual recognition. The host State is only allowed to apply its national laws where they satisfy three cumulative conditions: the law is not discriminatory with regard to nationality; it is justified for reasons of public policy, public security, public health or the protection of the environment; it is suitable and does not go beyond what is necessary to attain that objective (article 16).

In addition to goods and services, the Court also imposed an obligation of mutual recognition in relation to **companies**, in situations where a company formed in accordance with the law of one (home) State seeks to deploy its activities in another (host) State. In such 'entry' cases,[32] a company disputes the application of host law, even where the obligations imposed under host law apply equally, both in law and in fact, to companies incorporated in the host State. The seminal *Centros* case concerned a private limited company incorporated in England and Wales, which sought to register a branch in Denmark.[33] The Danish authorities refused to register the branch on the grounds that Centros, which did not trade in England and Wales, sought to circumvent the Danish rules on the paying-up of a minimum capital fixed at DKK 200.000 (para 7). As a matter of fact, the shareholders of Centros did not dispute the fact that they formed their company in the United Kingdom, where no requirement of a minimum share capital was imposed, for the purpose of avoiding the Danish rules on minimum paid-up capital (para 18).

Had the Court imposed a mere obligation of national treatment on Danish authorities, Centros would have been obliged to abide by this non-discriminatory requirement of a minimum paid-up capital of DKK 200.000. The Court however ruled that Danish authorities could not refuse to register a branch of Centros in Denmark, even if that branch was intended to enable the company to carry on all its economic activity in Denmark, with the result that the secondary establishment escaped national rules on minimum capital (para 30). As in *Cassis de Dijon* and *Säger*, the Court obliged the host State to treat businesses from other States better than domestic ones. *Centros* – and the principle of mutual recognition for companies – was confirmed in *Überseering* and *Inspire Art*.[34]

To sum up, the principle of mutual recognition requires the host State to treat cross-border activities better than domestic activities, by restraining itself from applying non-discriminatory measures to incoming goods, services or companies.

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[29] See eg *Gourmet International Products*, Case C-405/98, EU:C:2001:135 (paras 35–40); *De Coster*, Case C-17/00, EU:C:2001:651 (paras 29–35); *Cipolla*, Joined Cases C-94/04 and C-202/04, EU:C:2006:758 (paras 56–60); *Direxta Alta Formazione*, Case C-523/12, EU:C:2013:831 (paras 21-24); *Citroën Belux*, Case C-265/12, EU:C:2013:498 (paras 35–36).

[30] Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on Services in the Internal Market [2006] OJ L 376/36.

[31] See definition of the notion of 'service' at Article 4(1). Nevertheless, Articles 1(2) to 1(7), 2(2), 3(1), 3(2), 17 and 18 establish a list of reservations, exclusions and derogations to the general applicability of Directive 2006/123.

[32] In 'exit' cases, a company formed in one (home) State seeks to transfer its registered office, central administration or principal place of business to another (host) State, which may entail the loss of its legal personality under home law: on the distinction between entry and exit cases, see *Überseering*, Case C-208/00, EU:C:2002:632, paras 61–73; *Inspire Art*, Case C-167/01, EU:C:2003:512, paras 102–103. Seminal exit cases include *Daily Mail and General Trust*, Case 81/87, EU:C:1988:456; *Cartesio*, Case C-210/06, EU:C:2008:723.

[33] *Centros*, Case C-212/97, EU:C:1999:126.

[34] *Überseering*, Case C-208/00, EU:C:2002:632, paras 78–82; *Inspire Art*, Case C-167/01, EU:C:2003:512, paras 99–101.

Expanding market discipline through free movement

The central submission of this paper is that free movement increases the degree of market discipline within every Member State, by exposing domestic workers and businesses to competitive pressures coming from other Member States. This amplifying effect of free movement on market discipline can be usefully decrypted in two steps: the switch from discrimination to national treatment and the switch from national treatment to mutual recognition.

As the freedoms of movement are only concerned with cross-border activities, and not purely internal situations[35], the obligations deriving from the freedoms of movement have no immediate effect on the degree of market discipline exercised by domestic competitors, namely competitors established within the host State. On the other hand, these obligations have very different effects on the market discipline exercised by competitors coming from other States, which are described in the next sections.

From discrimination to national treatment: promoting a level-playing field between domestic and imported productions

If the upholding of discriminations on grounds of nationality is exceptional under free movement law, what is the concrete impact of discriminatory policies on market discipline? Discriminatory policies impose extra burdens on workers and businesses coming from other States: they are either imposed an obligation not borne by domestic workers and businesses (direct extra burden) or denied a right enjoyed by the latter (indirect extra burden). In presence of such extra burdens, workers and businesses from other Member States are less or not able to compete on the basis of merit with domestic workers and businesses: schematically, their eventual superior merits are absorbed by the extra burdens imposed by the host State. As a result, discriminatory policies adopted by the host State tend to shield domestic workers and businesses from market discipline exerted by competitors from other States. This link between discriminatory policies and protectionism has long been established in the scholarship:

> Protectionism, essentially, is the protection of national production against competition from foreign trade. The non-discrimination principle in the field of trade was designed specifically to prohibit protectionism.[36]

Similarly, the Court has long associated discriminatory internal taxation with protectionism:

> [T]he aim of Article 110 TFEU is to ensure free movement of goods between the Member States in normal conditions of competition. It is intended to eliminate all forms of protection which may result from the application of internal taxation that discriminates against products from other Member States.[37]

Protected by discriminatory measures, workers and businesses in the host State tend to escape market discipline exerted by external competitors and be only subject to market discipline exercised by

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[35] According to settled case-law, the Treaty provisions on free movement ' cannot be applied to activities which have no factor linking them with any of the situations governed by EU law and which are confined in all relevant respects within a single Member State': see inter alia *Airport Shuttle Express*, Joined Cases C-162/12 and C-163/12, EU:C:2014:74, para 43; *Caixa d'Estalvis i Pensions de Barcelona*, Case C-139/12, EU:C:2014:174, para 42; order in *Szabó*, Case C-204/14, EU:C:2014:2220, para 19. See also MP Maduro, 'The Scope of European Remedies: the Case of Purely Internal Situations and Reverse Discrimination' in C Kilpatrick, et al (eds), *The Future of European Remedies* (Oxford, Hart Publishing, 2000); C Ritter, 'Purely Internal Situations, Reverse Discrimination, Guimont, Dzodzi and article 234' (2006) 31 *European Law Review* 690.

[36] G de Búrca, 'Unpacking the Concept of Discrimination in EC and International Trade law' in C Barnard and J Scott (eds), *The Law of the Single Market: Unpacking the Premises* (Hart: Oxford, 2002), 181–95, at 187.

[37] *Tatu*, Case C-402/09, EU:C:2011:219, para 34.

domestic competitors within the host State – assuming that the host State allows competition in the economic sector concerned.[38] In this process of merit-based competition, in which all domestic workers and businesses are subject to the same standards imposed by the host State, domestic competitors showing superior merits tend to progressively capture market shares.

The switch from discrimination to national treatment has the effect of removing the protections afforded by discriminatory policies. As explained above, national treatment, which is commonly applied in relation to migrant workers (with the notable exception of posted workers[39]), obliges the host State to treat domestic workers and incoming workers equally. As a consequence, an obligation of national treatment has the effect, in most situations, of subjecting domestic and incoming workers to the same regulatory standard, which is defined by the host State. The existence of a unique regulatory standard is obvious when the host State is merely required to extend the laws governing the activities of its nationals to incoming workers, for instance in relation to taxation, labour law or social security.[40] But even when the host State is obliged to adapt its national laws in order to take into account facts and events occurring in the home State (obligation to be other-regarding, which is sometimes erroneously analysed as mutual recognition), both domestic and incoming workers must abide by the same standard defined by the host State. For instance, in *Vlassopoulou*, the Court made clear that the level of qualifications required by the host State applied to everyone, including migrant workers (paras 9–12), even if the host State must take into account qualifications acquired in other States (paras 15–23).

The existence of a unique regulatory standard has one crucial effect in terms of market discipline: it allows migrant workers to offer their services in the host State under the same terms and conditions as national workers. Such a situation is often evoked as 'competition on an equal footing' or 'level-playing field', namely a situation in which domestic and cross-border activities operate under equal competitive conditions:

> [T]he regulatory ideal of the common market consisted in the creation of a 'level playing-field' on which all economic actors could operate under equal competitive conditions, and across which goods, persons and services could be exchanged unhindered.[41]

As they are subject to the same regulatory standard, domestic and migrant workers are engaged in a process of *merit*-based competition, in which superior merits tend to translate into higher market shares. Thus, migrant workers are able to gain market shares, at the expense of domestic workers, on the basis of their eventual superior merits. To that extent, domestic workers are exposed to extra competitive pressures imposed by migrant workers offering their services in the host State.

However, as they are based on merit, these additional competitive pressures generated by national treatment can be absorbed by the host society through the ordinary functioning of domestic markets, for at least two reasons. Firstly, the competitive pressures added by national treatment are likely to be limited. It is indeed unlikely that a wave of super-skilled migrant workers will settle in the host State and overwhelm domestic workers on the basis of their superior merits: some migrant workers will be

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[38] A State may indeed decide to exclude competition in a given economic sector, notably by entrusting a public or private monopoly with a specific economic activity such as the operation of games of chance, the sale of alcohol or tobacco, or the provision of health services. By way of illustration, on the exclusion of competition in the area of games of chance, see *Sporting Exchange*, Case C-203/08, EU:C:2010:307, para 58.

[39] See n 63 to n 73 below and accompanying text.

[40] For instance, by virtue of Article 7(1) of Regulation 492/2011, conditions of employment must be identical for national and migrant workers; by virtue of Article 7(2) of Regulation 492/2011, migrant workers enjoy the same social and tax advantages as national workers.

[41] M Dougan, 'Minimum Harmonization and the Internal Market' (2000) 37 *Common Market Law Review* 853–885, at 860.

more skilled, some will be less skilled, and most of them will have to overcome cultural and language barriers.[42]

Second, there is a sense of fairness in the merit-based competition triggered by national treatment, which makes the competitive pressures added by incoming workers acceptable. Under national treatment, incoming workers are subject to the same regulatory standard as domestic workers; as a consequence, incoming workers can only gain market shares by showing equal or superior merits vis-à-vis domestic workers. The fact that this competitive process is based on merit fulfils a legitimating function of the market discipline exerted by workers coming from other States: arguably, most European citizens accept that plumbers, accountants or bakers from other States find an employment in their country if they are subject to the same obligations and work better than domestic plumbers, accountants or bakers. Although a minority of European citizens would prefer discriminatory policies (national 'preference'), the limited competitive pressures generated by national treatment were of the kind envisioned by every Member State upon joining the EU. Interestingly enough, the Spaak Report (1956), which prepared the adoption of the Rome Treaty a year later, expected national treatment to spontaneously lead the number of migrant workers – and the labour market – towards 'equilibrium':

> [I]f, on the one hand, discrimination is prohibited between national workers and migrant workers and if, on the other hand, a drop in salary is as a rule excluded either by State legislation of by action of trade unions, employers would have no incentive to have recourse to more migrant workers than they actually need to fill any vacancy. This way, pressure on remuneration levels is avoided and the labour market tends towards equilibrium.[43]

To sum up, national treatment tends to subject domestic and migrant workers to the same regulatory standard (level-playing field); accordingly, it exposes domestic workers to merit-based competitive pressures exerted by workers coming from other Member States.

From national treatment to mutual recognition: granting a structural competitive advantage to producers from low-regulation states

As explained above, mutual recognition is the prevailing obligation in the area of goods (*Cassis de Dijon*), services (*Säger*) and companies (*Centros*).

Whereas domestic and foreign producers are subject to the same regulatory standard under national treatment, they are subject to different regulatory standards under mutual recognition. By way of illustration, in *Cassis de Dijon*, Germany was deprived of the power to enforce a minimum alcohol requirement to imported French liqueurs, which remained subject to the sole French law: '*Cassis* introduces the principle of home state control and, in so doing, gives extraterritorial effect to the laws and standards laid down by the home state'.[44] In practice, the host State loses the power to regulate imported products placed on its domestic market, and only retains the power to regulate domestic

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[42] As explained in the next section, national treatment may even impose, in certain situations, a competitive disadvantage on incoming workers, which further limits the competitive pressures added by national treatment.

[43] Comité Intergouvernemental créé par la Conférence de Messine, 'Rapport des Chefs de Délégation aux Ministres des Affaires Étrangères' (Rapport Spaak), 21 April 1956, available at aei.pitt.edu/996/01/Spaak_report_french.pdf, 89, free translation.

[44] C Barnard, *The Substantive Law of the EU: the Four Freedoms*, 4th edn (Oxford University Press: Oxford, 2013) 93-94; see also Saydé (n 45) 242 et seq; A Saydé, 'One Law, Two Competitions: An Enquiry into the Contradictions of Free Movement Law' (2010-2011) 13 *Cambridge Yearbook of European Legal Studies* 365–413.

producers:[45] following *Cassis de Dijon*, Germany merely retained the power to enforce its minimum alcohol requirement on German producers of liqueurs.[46]

Given this coexistence of several regulatory standards, what is the effect of mutual recognition on market discipline? As they are subject to different regulatory standards, the competition between domestic and imported goods[47] is based not only on merit, but also on the cost of compliance with national laws. Depending on whether compliance with home law (applicable to imported goods) is more, equally or less costly than compliance with host law (applicable to domestic goods), imported goods will suffer from a structural competitive disadvantage, be on a level-playing field or enjoy a competitive advantage vis-à-vis domestic goods.

The revolution triggered by the Court in *Cassis de Dijon*, *Säger* and *Centros* lies precisely in the fact that, under an obligation of mutual recognition, producers established in a low(er)-regulation home State[48] enjoy a *structural competitive advantage* over domestic producers established in the host State. Discrimination, which is traditionally applied in trade relationships outside the EU through customs duties and quotas, imposes a competitive disadvantage on foreign production. National treatment, which arguably was the policy elected by the Treaty of Rome (1957),[49] aims at promoting a level-playing field between domestic and foreign productions. It is only under mutual recognition that production coming from a low-regulation State is granted a structural competitive 'bonus', originating in regulation.

The motives that spurred the Court to trigger this revolution in the area of goods (*Cassis de Dijon*) are well known. In essence, mutual recognition was intended to relieve imported goods from a specific competitive disadvantage which may flow from national treatment. Indeed, the switch from home law to host law may entail a specific cost for imported goods and services, which is not borne by domestic goods and services as they remain subject to the sole host law. AG Van Gerven observed:

> The main consideration underlying [Cassis de Dijon] is that such disparities between national laws may result in serious obstacles to intra-Community trade since they may necessitate extra expense or additional efforts in order to make the manufacture or the marketing of the product comply with laws differing from one Member State to another.[50]

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[45] W Kerber and R Van den Bergh, 'Mutual Recognition Revisited: Misunderstandings, Inconsistencies, and a Suggested Reinterpretation' (2008) 61 *Kyklos* 447, 453–54; see also A Saydé, *Abuse of EU Law and Regulation of the Internal Market* (Hart Publishing: Oxford, 2014), at 272.

[46] The Court has regularly highlighted the impossibility for the host State to enforce its stricter standard in a context of mutual recognition: in relation to the mutual recognition of driving licences, see eg *Akyüz*, Case C-467/10, EU:C:2012:112, para 56; *Hofmann*, Case C-419/10, EU:C:2012:240, para 84.

[47] This reasoning only refers to 'goods' in order to preserve readability, but applies equally to services and companies.

[48] Namely a home State in which compliance with home law is less costly than compliance with host law.

[49] Even in their last version adopted in Lisbon in 2007, the Treaty provisions establishing the freedoms of movement do not evoke once the existence of an obligation of mutual recognition. Article 53(1) TFEU merely establishes the possibility for the Union legislature of adopting directives for the mutual recognition of diplomas. Furthermore, the actual wording of the Treaty provisions establishing the freedoms of movement is more reminiscent of an obligation of national treatment: Articles 28 and 30 TFEU prohibit customs duties and all charges having equivalent effect; Articles 34 and 35 TFEU prohibit quotas and all charges having equivalent effect; Article 37 TFEU requires Member States to adjust State monopolies of a commercial character so as to avoid discrimination; Article 45(2) TFEU prohibits discriminations among workers of the Member States; Article 49, second sentence, TFEU imposes national treatment for self-employed persons; Article 54, first sentence, TFEU imposes national treatment for companies; Article 55 TFEU imposes national treatment in relation to participation in the capital of companies; Article 61 TFEU prohibits discriminations in relation to the provision of services.

[50] AG Van Gerven, *Torfaen Borough Council v B & Q (Sunday Trading)*, Case 145/88, ECLI:EU:C:1989:279, para 15.

This extra cost is easily identified when goods have to be modified or repackaged in order to be placed on the market of the host State, as in *Cassis de Dijon*. In such situations, the choice between national treatment and mutual recognition amounts to a choice between a competitive disadvantage for imported goods (national treatment) and a competitive advantage for goods imported from a low-regulation country (mutual recognition). Yet in other situations, the switch from home law to host law does not entail a specific cost for imported goods and services, so that national treatment tends to create a level-playing field. For instance, the switch from home law to host law does not entail a specific cost for migrant workers: they become subject to tax, labour and social security obligations in the host State, whereas corresponding obligations in the home State cease to be applicable. Arguably, the same can be said of the selling arrangements addressed in *Keck*, the licencing requirement in *Säger* and the minimum capital requirement in *Centros*: in all those cases, the choice between national treatment and mutual recognition amounted to a choice between a level-playing field (national treatment) and a competitive advantage for goods, services or companies coming from a low-regulation country (mutual recognition).

Irrespective of the motives for imposing an obligation of mutual recognition, the crucial finding is that such an obligation grants a structural competitive advantage to producers established in a lower-regulation home State, which deeply alters the nature of the market discipline imposed on domestic producers established in the host State. Indeed, such structural competitive advantages originating in regulation interfere with merit-based competition by 'absorbing', partly of wholly, the superior merits of domestic producers. In other words, and by contrast with national treatment, superior merits do not tend to translate into higher market shares under an obligation of mutual recognition.[51] Domestic and imported producers are engaged in a second and parallel competition process, based on national laws, which is classically designated as 'regulatory competition':

> [T]he *Cassis de Dijon* principle, by requiring the receiving or 'host state' to open its markets to goods legitimately produced in any other Member State (the 'home state'), provides a vital additional mechanism for subjecting laws to the forces of regulatory competition. This is the essence of 'mutual recognition'. Consumers in the host state now have a choice of goods produced under different regulatory regimes. Competition between goods produced under different legal systems means, in effect, that the laws of those systems are thrown into competition with each other too.[52]

Consequently, the market discipline entailed by mutual recognition is of a radically different nature than that generated by national treatment, owing to the risk that domestic producers suffer from a structural competitive disadvantage vis-à-vis producers coming from a low(er)-regulation State. First, there is no reason to think that the competitive pressures generated by mutual recognition should be limited. Since goods and services coming from low-regulation States enjoy a structural competitive edge over domestic goods and services, they could potentially displace a substantial share of national production. The potential scope of the competitive pressures entailed by mutual recognition can be illustrated with statistics regarding posted workers in the building sector in Belgium.[53] According to Construction Confédération, an employer organization representing more than 15.000 businesses in the building sector in Belgium,[54] 17.000 jobs were lost during the period 2011-2014 (9,7% of the total number of jobs in the sector), despite a 2%-increase in activity. During the same period, the yearly number of 'Limosa declarations', which have to be filed by the employer before posting workers in

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[51] In this sense, the effect of mutual recognition on market discipline mirrors the effect of discrimination: when discriminatory policies are allowed, producers from other States are not able to compete on the basis of merits; conversely, under an obligation of mutual recognition, domestic producers are not able to compete on the basis of merits with producers coming from a low-regulation State.

[52] C Barnard and S Deakin, 'Market Access and Regulatory Competition' in Barnard and Scott (n 36), 197–224, at 203.

[53] P Lorent, '20.000 emplois menacés dans la construction', *Le Soir*, 30 April 2015.

[54] See the website of Confédération Construction, http://www.confederationconstruction.be.

Belgium, more than doubled to reach the number of 314.924 in 2014. Construction Confédération deems that posted workers currently occupy 33.000 full-time equivalents in the building sector in Belgium, and that this phenomenon could destroy 20.000 more jobs by 2019.

Secondly, law-based market discipline (mutual recognition) does not benefit from the legitimating function of merit-based market discipline (national treatment). Indeed, superior merits of domestic producers do not translate into higher market shares in the presence of a structural competitive advantage enjoyed by producers coming from low-regulation States. As a result, domestic workers and businesses feel a sense of unfairness when, irrespective of their merits, they cannot compete with businesses and workers coming from low-regulation States. By way of illustration, the competition waged by posted workers who remain subject to the less comprehensive social security of their home State is often labelled as 'unfair'.[55] The Court itself observed in the seminal *Laval* case that:

> [Article 3(1) of Directive 96/71] thus prevents a situation arising in which, by applying to their workers the terms and conditions of employment in force in the Member State of origin as regards [a limited list of] matters, *undertakings established in other Member States would compete unfairly against undertakings of the host Member State* in the framework of the transnational provision of services, if the level of social protection in the host Member State is higher.[56]

It follows from what precedes that the competitive pressures entailed by mutual recognition and national treatment are of fundamentally different natures. As exposed in the previous section, the competitive pressures generated by national treatment are likely to be limited and are never labelled as 'unfair', as they arise on a level-playing field. Conversely, the competitive pressures added under mutual recognition may be substantial and are felt as 'unfair' as they originate in the lower cost of compliance with the laws applicable in the home State. Arguably, the so-called 'Polish plumber' is a mutual-recognition plumber, not a national-treatment plumber.

In practice, when producers tend to structurally lose their capacity to compete in their own domestic market with producers established in low-regulation States, they are left with three options:

- cessation of activities: they can progressively abandon market shares to competitors from low-regulation States;
- deregulation: they can lobby for having the law in the host State amended in order to enable them to compete with businesses established in low-regulation States;57 or
- relocation: they can avoid the law in the host State by making use of their right to establishment in a low-regulation State, in order to regain the capacity to compete.

A cessation of activities is the least desirable option for businesses. Moreover, deregulation is hardly available in the short run, as national laws implement a longstanding social contract among various interest groups, chiefly between businesses and workers. As a consequence, relocation tends to become the main outlet for the competitive pressures created by mutual recognition for goods and services. In other words, mutual recognition for goods and services creates a pressure on producers in high-regulation States to relocate in low(er)-regulation States, in order to regain their capacity to compete. It is important to highlight that producers may decide to relocate in order to anticipate a risk of structural competitive disadvantage, namely before being actually exposed to it.

This pressure to relocate can be illustrated with the seminal *Viking* case.[58] Viking, a Finnish company, operated ferries plying the route between Helsinki and Tallinn, among which was the Rosella. The

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[55] See eg X Attout, 'La concurrence déloyale mine le secteur de la construction', *Le Soir*, 24 February 2015; P Lorent, '20.000 emplois menacés dans la construction', *Le Soir*, 30 April 2015.

[56] *Laval*, Case C-341/05, EU:C:2007:809, para 75, emphasis added.

[57] By way of illustration, Construction Confédération demands a 13%-reduction of salary costs in Belgium: see X Attout, 'La concurrence déloyale mine le secteur de la construction', *Le Soir*, 24 February 2015.

Rosella was under the Finnish flag, so that Viking was bound to pay Finnish crew wages. Other ferries plying the same route were under the Estonian flag, and therefore paid (lower) Estonian crew wages. Since activities on-board a ship are governed by the law of the flag State, Finland had no means to impose Finnish crew wages on Estonian ferries navigating to Helsinki, which amounted, in effect, to a situation of mutual recognition. In its judgment, the Court described the logical sequence leading from mutual recognition to relocation (para 9):

> The Rosella was running at a loss as a result of direct competition from Estonian vessels operating on the same route with lower wage costs. As an alternative to selling the vessel, Viking sought … to reflag it by registering it in either Estonia or Norway, in order to … enter into a new collective agreement with a trade union established in one of those States.

To paraphrase the Court, the Rosella suffered from a *structural competitive disadvantage* in the competition process with Estonian vessels operating on the same route with lower wage costs. Since a reduction of Finnish crew wages (*deregulation*) was not possible, Viking only had two options: either selling the vessel (*cessation of activities*) or reflagging it in order to enter into a new collective agreement (*relocation*). In other words, in order to survive under mutual recognition, Viking had to 'relocate' the Rosella under a low-regulation flag.

Claiming a step back to national treatment: legal challenges to mutual recognition

Given the upsetting nature of the competitive pressure generated by mutual recognition for every economic sector exposed to competition from low-regulation States, it should not come as a surprise that the principle of mutual recognition has been – and still is – the object of numerous legal challenges. Such legal challenges include the reverse discrimination defence, the dumping defence and the abuse defence. These legal challenges have two traits in common: they claim a step back from mutual recognition to national treatment, and they have been largely unsuccessful.

The 'reverse discrimination' defence as (unsuccessful) challenge against mutual recognition

The 'reverse discrimination' defence was one of the first legal challenges launched against the principle of mutual recognition. In essence, a reverse discrimination occurs whenever domestic products are subject to stricter regulatory standards than incoming products, thereby suffering a competitive disadvantage on their own domestic market.[59] As explained above, such reverse discriminations are mechanically produced by mutual recognition in all situations where compliance with host law is costlier than compliance with home law, with the consequence that goods and services produced in the host State suffer from a structural competitive disadvantage vis-à-vis goods and services imported from a low-regulation State.

This mechanical effect can be illustrated with the judgments in *Leclerc* and *Cognet*.[60] In *Leclerc*, the Court ruled that a French legislation imposing a minimum retail price for books was contrary to free movement of goods and could not, as a consequence, be applied to imported books. *Cognet* concerned

(Contd.)

[58] International Transport Workers' Federation et Finnish Seamen's Union ('Viking'), Case C-438/05, EU:C:2007:772.

[59] AG Léger, *Ritter-Coulais*, Case C-152/03, EU:C:2005:122, para 46; C Dautricourt and S Thomas, 'Reverse Discrimination and Free Movement Of Persons under Community Law: All for Ulysses, Nothing for Penelope?' (2009) 34 *European Law Review* 433, 433; D Garcia, 'Are There Reasons to Convert Reverse Discrimination into a Prohibited Measure?' (2009) 18 *EC Tax Review* 179, 180; A Tryfonidou, 'Reverse Discrimination in Purely Internal Situations: An Incongruity in a Citizens' Europe' (2008) 35 *Legal Issues of Economic Integration* 43, 46; Ritter (n 35) 691.

[60] Association des Centres distributeurs Leclerc and Thouars Distribution, Case 229/83, EU:C:1985:1; Cognet, Case 355/85, EU:C:1986:410.

the French legislative amendment implementing the *Leclerc* ruling, according to which the minimum price requirement did not apply, as a rule, to imported goods (para 5). The referring judge observed that, in such circumstances, 'French distributors were exposed to the disadvantages of competition without their being enabled to meet that competition with equivalent means and French traders and foreign exporters to France were no longer treated equally' (para 6). The Court was asked whether such a difference of treatment was contrary to the principles of equality and non-discrimination contained in the Treaty. The Court squarely ruled that '[Union] law does not apply to treatment which works to the detriment of national products as compared with imported products' (para 11).

As is well known, *Cognet* is but one of many instances in which the Court has consistently refused to sanction reverse discriminations.[61] In the more recent Italian chocolate case, the Court bluntly stated that it is 'irrelevant that the obligation established at Article 34 TFEU is capable of placing the national products of the host State at a disadvantage'.[62] In sum, the reverse discrimination defence has failed to limit the expansion of the obligation of mutual recognition.

The 'dumping' defence as (unsuccessful) challenge against mutual recognition

The dumping defence represents a second – largely unsuccessful – challenge against the principle of mutual recognition. The dumping defence is more commonly used in the area of services, and chiefly in relation to the posting of workers.[63] In essence, the dumping defence is a recasting of the reverse discrimination defence, whereby economic terminology ('dumping') replaces legal terminology ('discrimination'). The underlying idea remains however identical: under a regime of mutual recognition, domestic services suffer from a structural competitive disadvantage vis-à-vis services provided from a low-regulation State. In relation to posted workers, a low-regulation State means a State where social protection is less comprehensive:

> In relation to services the issue [of how far the principle of mutual recognition of regimes is to be enforced] is none other than the fundamental but often frustrating question of what is 'social dumping'. With regard to services involving the supply of labour, mutual recognition of regulatory regimes could mean that the labour law standards of the Member State of establishment will govern the employment terms of workers hired in the state of establishment by the provider of the services, even if the services are to be provided through those employees in another Member State (the 'host' Member State), which has higher regulatory standards.[64]

The Court's case law on posted workers has undergone a radical evolution, from endorsing national treatment in *Rush Portuguesa* to imposing mutual recognition in *Laval*. As the switch from home law to host law does not entail a specific cost for migrant workers,[65] the choice between national treatment and mutual recognition in the context of labour and social security obligations amounts to a choice between a level-playing field for all workers (*Rush Portuguesa*: national treatment) and a competitive

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[61] See, inter alia, *Grandes distilleries Peureux*, Case 86/78, EU:C:1979:64, para 32; *Hurd*, Case 44/84, EU:C:1986:2, para 55; *Mathot*, Case 98/86, EU:C:1987:89, para 9; *Peralta*, Case C-379/92, EU:C:1994:296, para 27; *Aubertin and Others*, Joined Cases C-29/94 to C-35/94, EU:C:1995:39, para 6 and 13; *Uecker and Jacquet*, Joined Cases C-64/96 and C-65/96, EU:C:1997:285, para 22-23; *Metock and Others*, Case C-127/08, EU:C:2008:449, para 76-78.

[62] *Commission v Italy*, Case C-14/00, EU:C:2003:22, para 73.

[63] Still, the dumping defence and related arguments are raised in relation to other economic activities. For instance, in the seminal *Säger* case, Mr Säger claimed that he was facing 'unfair competition' from Dennemeyer, a UK company providing patent renewal services in Germany without the administrative licence required under German law. See *Säger*, Case C-76/90, EU:C:1991:331, para 5.

[64] P Davies, 'Market Integration and Social Policy in the Court of Justice' (1995) 24 *Industrial Law Journal* 49, at 71.

[65] See n 50 above and accompanying text.

advantage for posted workers – and their employers – coming from a low-regulation country (*Laval*: mutual recognition).

Rush Portuguesa concerned a special contribution imposed by French authorities on a Portuguese company for bringing Portuguese workers from Portugal without permission, in order to carry out works for the construction of a railway line.66 The Court held that the host State could not preclude an undertaking established in another Member State from moving on its territory with his staff in order to provide services there (para 12). However, the Court allowed the host State to apply its ordinary labour laws to such posted workers (para 18):

> [Union] law does not preclude Member States from extending their legislation, or collective labour agreements entered into by both sides of industry, to any person who is employed, even temporarily, within their territory, no matter in which country the employer is established; nor does [Union] law prohibit Member States from enforcing those rules by appropriate means.

In other words, the Court endorsed national treatment in *Rush Portuguesa*, thereby thwarting the risk of social dumping: as both domestic and posted workers were subject to host law (level-playing field), they were engaged in a process of merit-based competition, and so were their respective employers. Professor Barnard wrote:

> Thus, in one (unreasoned) paragraph, the Court put a stop to a threat of social dumping – without using this language – by allowing the host state to extend its labour laws and conditions to the staff employed by service providers working in its country.[67]

However, the *Rush Portuguesa* ruling was delivered in 1990, and the impact of the subsequent *Säger* ruling (1991) was quickly felt in the field of posted workers. The restriction approach of *Säger* was transposed in *Vander Elst*,[68] and *Guiot* marked the conceptual shift to mutual recognition.[69] Indeed, *Guiot* reconstructed the principle of national treatment endorsed in *Rush Portuguesa* as a mere derogation justified by 'overriding requirements of public interest' in the sense of *Säger*, with the consequence that it could only apply when some 'public interest' was not safeguarded by the laws of the home State (paras 11–13). Therefore, the host State could only 'extend its legislation' in the sense of *Rush Portuguesa* where it was necessary to ensure the social protection of posted workers, which was not the case where they enjoyed a 'comparable' protection in the home State (paras 16–18). *Guiot* was confirmed in cases such as *Arblade*, *Finalarte* or *Portugaia Construções*.[70]

Against this context was issued the seminal *Laval* ruling, which concerned the conditions of employment of Latvian workers posted on a construction site in Sweden.[71] Swedish trade unions initiated a collective action to force their employer, Laval, to negotiate the rates of pay and sign the collective agreement for the building sector. The Court ruled that this collective action amounted to a restriction of the freedom to provide services (para 99). Moreover, if the protection of the workers of the host State against social dumping could constitute an overriding reason of public interest (para 103), this collective action could not be justified since the Latvian employer was only required to observe the nucleus of mandatory rules for minimum protection in the host State defined in Article

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66 *Rush Portuguesa*, Case C-113/89, EU:C:1990:142.

67 C Barnard, 'Fifty Years of Avoiding Social Dumping? The EU's Economic and Not So Economic Constitution' in M Dougan and S Currie (eds), *50 Years of the European Treaties* (Hart: Oxford, 2009), 311–42, at 314.

68 *Vander Elst*, Case C-43/93, EU:C:1994:310, para 14.

69 *Guiot*, Case C-272/94, EU:C:1996:147.

70 *Arblade and Others*, Joined Cases C-369/96 and C-376/96, EU:C:1999:575, para 41; *Finalarte and Others*, Joined Cases C-49/98, C-50/98, C-52/98 to C-54/98 and C-68/98 to C-71/98, EU:C:2001:564; *Portugaia Construções*, Case C-164/99, EU:C:2002:40.

71 *Laval*, Case C-341/05, EU:C:2007:809.

3(1) of Directive 96/71 (para 108). The Court confirmed *Laval* in *Rüffert*, by ruling that a minimum wage could not be enforced in Germany against a Polish subcontractor if it had not been fixed according to one of the procedures laid down in Articles 3(1) and 3(8) of Directive 96/71 (para 35).[72] In short, mutual recognition had become the rule, and national treatment the exception whose boundaries are strictly defined by Articles 3(1) and 3(8) of Directive 96/71.

To sum up, national treatment (*Rush Portuguesa*) formed a natural bulwark against social dumping, which was progressively dismantled by the expansion of mutual recognition (*Guiot*, *Laval* and *Rüffert*):[73] indeed, mutual recognition allows employers to 'import' their home law when posting workers from their home State. Just as the reverse discrimination defence, the dumping defence has failed to limit the expansion of mutual recognition.

The 'abuse' defence as (unsuccessful) challenge against mutual recognition

Defences based on the prevention of reverse discriminations and dumping have proved unsuccessful in challenging the expansion of mutual recognition in the area of goods and services. As a result of this expansion, businesses in every State are facing the risk of suffering from a structural competitive disadvantage vis-à-vis businesses established in a low(er)-regulation State. As illustrated above with the *Viking* case, this peculiar competitive pressure generated by mutual recognition is likely to create an incentive for businesses in high-regulation States to relocate in low(er)-regulation States, in order to regain their capacity to compete.[74]

The 'abuse' defence is specifically aimed at countering such strategies of relocation. It is raised by stakeholders established in the host State that have an interest in seeking the enforcement of host law, such as public authorities (in *Centros* or *Cadbury Schweppes*) or persons benefiting from the protection of host law (for instance, the seafarers in *Viking*). In essence, the argument put forward in this context is that businesses should not have the right to elect the national law of a low-regulation State, and then rely on mutual recognition to provide goods and services throughout the internal market. The concrete claim put forward in this context is, again, to substitute mutual recognition with national treatment – in other words, to allow the host State to apply its ordinary laws to businesses relocated in a low-regulation State.

In the field of ship regulation, such relocation is achieved by reflagging a ship in a low-regulation State, as illustrated by the *Viking* case. In this context, the fight against abusive practices takes on the appellation of fight against 'flags of convenience', namely the practice of registering a ship in a (low-regulation) State of which the owner is not a national.[75] In its judgment, the Court held that the fight against flags of convenience was not a legitimate objective capable of justifying restrictions on freedom of establishment (para 88). In so far as it was intended to protect the conditions of employment of seafarers, the fight against flags of convenience could not be justified either, because it also covered situations in which the ship was registered in a State offering a higher level of social protection (para 89).

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[72] *Rüffert*, Case C-346/06, EU:C:2008:189.

[73] See European Economic and Social Committee (EC), 'The social dimension of the internal market' (Own-Initiative Opinion), 14 July 2010, OJ C 44/90, in particular no 1.6 and section 3.4.

[74] See n 58 above and accompanying text.

[75] International Transport Workers' Federation et Finnish Seamen's Union ('Viking'), Case C-438/05, EU:C:2007:772, para 8.

The seminal *Centros* ruling, already evoked above, provides another illustration of the phenomenon targeted by the abuse defence.[76] The shareholders of Centros were Danish residents who wished to carry out a wine trading business in Denmark. To that end, they formed a company in the United Kingdom, where no minimum capital requirement was imposed, with the avowed purpose of avoiding the Danish rules on minimum paid-up capital (para 18). The Danish public authorities refused to register a branch of Centros in Denmark on the ground that Centros sought to circumvent Danish law. They also argued that the minimum capital requirement was intended to protect a specific group of stakeholders, namely creditors. The Court famously ruled that forming a company in the State whose rules of company law seem the least restrictive, and thereafter setting up branches in other States, does not amount to abuse (para 27). In effect, the *Centros* ruling dismissed the abuse defence and imposed mutual recognition in the field of company law, at least in entry cases.[77]

In tax matters, the abuse defence is best known as fight against tax avoidance. Tax avoidance strategies set up in a cross-border context seek to shift profits from a high-tax jurisdiction to a low-tax jurisdiction. One recurrent issue is the extent to which multinational corporate groups may use related companies as conduits to shift profits across States and minimize their global tax bill. This issue is aptly illustrated by the *Cadbury Schweppes* case.[78] The parent company of the Cadbury Schweppes group was a public limited company incorporated in the UK, as such subject to income tax in the UK. The group incorporated two subsidiaries in the International Financial Services Centre ('IFSC') in Dublin, which were entrusted with intra-group finance activities. This double incorporation was meant to subject the profits yielded by intra-group finance to the convenient 10% tax rate applicable in the IFSC (para 18). Indeed, profits made by a related company established in another State are taxed as a rule in the latter State, namely Ireland (para 4), which amounts de facto to a situation of mutual recognition.

The UK raised an abuse defence in the form of 'CFC rules', namely tax rules applicable to 'controlled foreign companies'. The CFC rules provided that, if a UK company owns more than 50% in a foreign company (which is then 'controlled'), and the foreign company pays little or no taxes abroad,[79] then the parent company is taxed in the UK on the profits made by its foreign subsidiary, after deduction of the taxes paid abroad. This, once again, is a claim to national treatment: the UK wanted to apply UK taxes on profits made by the Irish subsidiaries, and not be forced to recognize the tax jurisdiction of Ireland.

The Court judged that, although they restricted the freedom of establishment, such CFC rules could be justified on the basis of the prevention of abuses, but only in so far as they targeted 'wholly artificial arrangements which do not reflect economic reality with a view to escaping the tax normally due on the profits generated by activities carried out on national territory' (para 55). The Court further qualified the notion of wholly artificial arrangements as 'fictitious establishments not carrying out any genuine economic activity' (paras 66–68). Since *Cadbury Schweppes*, the Court has consistently limited the scope of the abuse defence in tax matters to such wholly artificial arrangements.[80] As a consequence, the abuse defence can be defeated by any genuine economic activity carried out by a

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[76] See n 33 above and accompanying text.

[77] On the distinction between entry and exit cases, see n 32 above.

[78] Cadbury Schweppes et Cadbury Schweppes Overseas, Case C-196/04, EU:C:2006:544.

[79] More precisely, the condition was that the tax paid by the CFC be less than three quarters of the amount of tax which would have been paid in the United Kingdom (para 7).

[80] See, among many others, *SCA Group Holding*, Joined Cases C-39/13, C-40/13 and C-41/13, EU:C:2014:1758, para 42; *Itelcar*, Case C-282/12, EU:C:2013:629, para 34; *Felixstowe Dock and Railway Company and Others*, Case C-80/12, EU:C:2014:200, para 33; *Oy AA*, Case C-231/05, EU:C:2007:439, para 62; *Test Claimants in the Thin Cap Group Litigation*, Case C-524/04, EU:C:2007:161, para 74.

related company in a low-tax jurisdiction – such as intra-group finance in the *Cadbury Schweppes* case. As a matter of fact, Irish lawyers hailed the *Cadbury Schweppes* ruling as a 'tonic for Irish business',[81] while the Guardian described it as a 'court blow' suffered by the Treasury in offshore tax fight.[82]

Overall, the Court's case law has severely curtailed the room for the abuse defence in the context of free movement, thereby enabling businesses to relocate in a low-regulation State and subsequently rely on mutual recognition to offer their goods and services throughout the internal market. The abuse defence has failed to impede the expansion of mutual recognition.

Conclusion: from freedom of movement to obligation of movement

Member States can logically adopt three policies when regulating cross-border activities: they can treat cross-border activities worse (discrimination), equally (national treatment) or better (mutual recognition) than domestic activities. As a rule, discrimination is incompatible with the freedoms of movement, and Member States are alternatively requested to adopt national treatment (chiefly in relation to incoming workers, with the notable exception of posted workers) or mutual recognition (chiefly in the areas of goods, services and companies).

National treatment and mutual recognition have radically different impacts on the type of market discipline imposed on producers throughout the Union. National treatment tends to subject domestic and incoming workers to the same regulatory standard, which is defined by the host State (level-playing field). As a result, domestic and incoming workers are engaged in a process of *merit*-based competition, in which superior merits tend to translate into higher market shares. To that extent, national treatment generates extra competitive pressures on domestic workers, who can be displaced by incoming workers showing superior merits. However, these extra competitive pressures are likely to be limited and not be felt as 'unfair', since they arise on a level-playing field.

By contrast, mutual recognition subjects domestic and foreign producers to different regulatory standards: domestic goods, services and companies must abide by the law of the host State, whereas incoming goods, services and companies remain subject to the law of their home State. As a result, competition between domestic and imported producers is based not only on merit, but also on the cost of compliance with national laws. Producers established in a low(er)-regulation home State enjoy a structural competitive advantage – originating in regulation – over domestic producers established in the host State, irrespective of their eventual superior merits. Consequently, the competitive pressures added by mutual recognition may be substantial and felt as 'unfair'; arguably, the so-called 'Polish plumber' is a mutual-recognition plumber, not a national-treatment plumber.

Furthermore, the extra competitive pressures generated by mutual recognition are likely to create an incentive for domestic producers to relocate in low(er)-regulation States, in order to regain their capacity to compete (*Viking*). In other words, mutual recognition may actually impose an *obligation of movement* on domestic producers suffering from a structural competitive disadvantage vis-à-vis producers established in low(er)-regulation States. Given the upsetting nature of these competitive pressures, it should not come as a surprise that mutual recognition has been – and still is – the object of numerous legal challenges. Nevertheless, defences based on the fight against reverse discriminations, dumping or abusive practices have by and large failed to impede the expansion of the obligation of mutual recognition.

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[81] O'Donnell Sweeney, *ODS Update*, Autumn 2006.

[82] P Inman, 'Treasury suffers court blow in offshore tax fight', *The Guardian*, 13 September 2006.

The impact of the freedoms of movement can now be reassessed from the perspective of market discipline. Put in a slightly provocative way, the freedoms of movement are not intended to increase human freedom, but rather to constrain it through an ever-expanding market discipline. On a horizontal plane, the constant broadening of the scope of the freedoms of movement has subjected a constantly increasing volume of human activities to market discipline exerted by producers established in other States. On a vertical plane, the switch from national treatment to mutual recognition exposes human activities to a harsher type of market discipline, under which superior merits are not rewarded. Overall, the expansion of free movement subjects more human activities to more market discipline.