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Unravelling the General Good Exception.
The case of Financial Services

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Unravelling the General Good Exception The case of Financial Services

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Abstract

In this paper we try to analyze the scope and significance of the general good exception, which has been construed by the Court of Justice as a mitigation of the general prohibition of all restrictions, whether discriminatory or not, to free movement of services and freedom of establishment. After an overview of the case law of the Court ofJustice relating to these freedoms, we examine the conditions attached to the possibility for the member states to invoke the general good in order to maintain their national regulation restricting free movement..
Notwithstanding the existence of EU directives in the area of financial services with a view to create an internal market, there still is a wide scope for applying the general good by the member states at the level of financial product regulation. In view of the difficulties and the uncertainties surrounding the general good clause, we finally look at possible alternatives which aim at reducing information costs and enhance transparency with respect to the practical application of the general good clause by the member states.

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Introduction

The ever widening interpretation of the Treaty freedoms given by the Court of Justice in its jurisprudence over the last decade raises new questions as to the scope and limits of these freedoms. As the case law at present seems to promulgate the prohibition of all restrictions to free movement, whether discriminatory or not, as a general principle of Community law common to all Treaty freedoms, the discussions shift to another level: on the one hand, questions arise as how to circumscribe the notion of 'restriction' to free movement. The step backwards taken by the Court in *Keck* illustrates the complexities of the issue, and the consequences of an uncontrolled extension of the Court's scrutiny of national law in the past. On the other hand, the more national law is caught by the general 'restriction based' prohibitions to free movement, the more interpretation problems will arise with respect to the possibilities for Member States to uphold restrictive rules under the heading of the 'general good'.

In reality, the 'general good' has evolved over the past decade as a central, but yet very vague, notion in the balance of interests between Treaty freedoms and legitimate regulatory interests of the EU Member States. Furthermore, the 'general good'-clause continues to play an important role in the operation of many directives enacted by the Community institutions within the framework of the 1992 Internal Market Programme. Notably, the legal uncertainty surrounding the interpretation of the general good-clause in the banking and financial services directives has emerged as one of the most controversial interpretation issues in the operation of the directives, both among legal scholars, and at institutional level (supervisory authorities, member states and the European Commission). The European Commission for its part has provoked a public discussion on the issue and published a communication ('*the Interpretative Communication*'), which provides its (non-binding) view on the interpretation of the general good-clauses in the banking directives.[1] [2] A similar communication has been published in the field of insurance[3], while a draft communication is said to be prepared in the area of investment services.

The present chapter will try to provide some elements in circumscribing the notion of general good within the context of financial services in general and of the EU-directives on banking and investment services in particular. This will enable us to take position on the

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1 See COMMISSION OF THE EUROPEAN COMMUNITIES, *Commission interpretative Communication. Freedom to provide services ant the interest of the general good in the Second Banking Directive*, *OJ*, C 209/6 of 10 July 1997. See also URL: http://europa.eu.int/comm/dg15/en/finances/banks/

2 It would seem that the Commission has waited to launch its Interpretative Communication until the judgment of the Court of Justice in the so-called *pension funds* case, concerning the action for annulment introduced by the French Republic against a Communication by the Commission to the Member States on the investment rules for pension funds. (ECJ, 20 March 1997 case C-57/95, *France v. Commission*, not yet reported in the E.C.R.) The outcome of this case had a direct bearing on the question whether the Commission would be further allowed to use the communication as a useful means to provide its point of view on questions of interpretation of the EC Treaty and other binding legal instruments (directives etc). Although the Court quashed the said communication, it may be submitted that the motives underlying the Court's ruling do not create a specific risk as to the validity of the Commission's Interpretative Communication.

3 OJ, C 43, 16 February 2000, p. 5.

Commission's Interpretative Communication with respect to this issue. As the general good-doctrine originates in the case law of the Court of Justice with respect to the Treaty freedoms, we shall first briefly recall the Court's view on the scope of these freedoms (Part I). Part II will focus on the notion of general good, both in the overall context of freedom to provide services and in the case of financial services in particular. Part III will proceed with an analysis of the general good provisions in the Second Banking Directive and the Investment Services Directive, from the angle of both the material scope of these clauses and their procedural aspects, in particular the question of the notification of general good provisions by the host states' competent authorities. Finally, in Part IV we will try to shed some light on a issue which is highly relevant for the provision of cross-border (financial) services, namely the relationship between the general good, rules of contract law and private international law rules in the member states.

Part I — The Roots of the General Good — the Court's Case Law on the Treaty Freedoms

A. Overview of the relevant case law[4]

The general good, as is well known, is a concept which finds no explicit legal basis in the Treaty, but which has been created by the Court of Justice. The general good-doctrine must be seen as the necessary counterweight for the Court's judicial activism in widening the scope of the Treaty freedoms from mere non-discrimination principles to general prohibitions on all measures, whether discriminatory or not, which constitute a *restriction* to free movement across borders. More specifically, the general good exception mitigates the effects of the restriction based approach to the Treaty freedoms, thus striking a balance between the interests of free movement as a precondition for market unification on the one hand, and the preservation of other social values by the member states on the other.

This tendency was first clearly identified in the area of free movement of goods: in *Dassonville*[5], the Court considered as contrary to free movement of goods all measures which directly or indirectly, actually or potentially hindered trans-border trade, unless they could be reasonably justified. This latter 'rule of reason' was further refined in the landmark *Cassis de Dijon* case: a member state may uphold its restrictive regulation as far as it finds a reasonable justification in imperative reasons relating to the general good.[6] In a positive sense, the Court's position came down to formulating a principle of mutual recognition: a good legally manufactured and marketed in its member state of origin, should in principle be offered on the market of other member states under the same conditions as in its member state of origin. The host member states are entitled to apply their own laws only under two circumstances: (1) either they do not qualify as restriction to the free movement of the imported good, or (2) when they do constitute a restriction on cross-border free movement, they should be properly justified by an imperative reason relating to the general good.[7] It is well known that this mutual recognition principle later served as the regulatory model for the Commission's single market programme.

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4 As part of its continuous efforts to inform citizens and business operators, the European Commission has recently drafted an extensive guide to the Court's case law on freedom to provide services: see EUROPEAN COMMISSION, *Guide to the case law of the European Court of Justice on Articles 59 et seq. EC Treaty. Freedom to provide services*, 1999, 190 p. (URL: http://europa.eu.int/comm/dg15/en/services/services/art59en.pdf).

5 ECJ, 11 July 1974, case 11/74 (*Dassonville*), E.C.R., 1974, at 837.

6 ECJ, 20 February 1979, case 120/78 (*Rewe v. Bundesmonopolverwaltung für Branntwein*), E.C.R., 1979, at 649. Hereafter referred to as '*Cassis de Dijon*'.

7 Compare the Commission's viewpoint in a Communication issued shortly after the *Cassis de Dijon*-case: *OJ*, C 256, 3 October 1980, pp. 2-3.

The Court of Justice gradually extended its broad interpretation of the free movement principle and the general good-exception as mitigation of the rule, to the other Treaty freedoms. The *German insurance case*[8] witnessed the Court's firm determination to transpose the *Cassis de Dijon*-model to services.[9] However, it was not until the *French tourist*[10] and the *Säger* cases[11] that the Court unequivocally prohibited all, even non-discriminatory, restrictions on free movement of services, unless they were duly justified by an exception provided for in the Treaty (public order, art 46) or by the general good.

More recently, the Court extended the same restriction based interpretation to the freedom of establishment: although the Court initially showed some reluctance in fully transposing the principles (*Vlassopoulou*[12] and *Kraus*[13] cases), the judgment in *Gebhard* left no doubts as to the willingness of the Court to read in article 43 EU-Treaty a general ban on all restrictions to the freedom of establishment. Finally, the Court seems inclined to adopt the same restriction-based approach in the area of capital movements, although the case law — in particular the *Veronica*[14] and *Svensson*[15] cases — initially appeared less pronounced in this sense.[16] The Court's judgment in *Trummer*[17] however seems to adhere to the mentioned broader interpretation.

The evolution of the Court's case law over the last few years thus clearly indicates a movement of convergence in the interpretation of all Treaty freedoms. This was amply demonstrated in the *Gebhard*-judgment[18], where the Court affirmed the restriction based concept of free movement as a general principle common to all Treaty freedoms. Hence, after *Gebhard* the general good will serve as a common standard for the justification of restrictions on the free movement in the context of all Treaty freedoms (goods, services, persons — both workers and self-employed — and capital).

Taking *Cassis de Dijon* as a model, the extension of the restriction based concept of free movement may be positively translated into a principle of mutual recognition: in the area of services, this means that a service legally provided in one member state may be offered under the

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8 ECJ, 4 December 1986, case 205/84 (*Commission v. Germany)*, E.C.R., 1986, at 3755.

9 One should note, however, that even before *Cassis de Dijon*, the *van Binsbergen* case already contained some elements pointing in the direction of an interpretation of the Treaty free movement of services extending beyond the non-discrimination principle.

10 ECJ, 26 February 1991, case C-154/89 (*Commission v. France*), *E.C.R.*, 1991, at I-659.

11 ECJ, 25 July 1991, case C-76/90 *(Säger)*, E.C.R., 1991, I-4239.

12 ECJ, 7 May 1991, case C-340/89 *(Vlassopoulou)*, E.C.R., 1991, I-2357; more recently confirmed in case C-104/91, decision of 7 May 1992 *(Aguirre Borrell a.o.*), E.C.R., 1992, I-3003; ECJ, 9 February 1994, case C-319/92 *(Salomone Haim)*, E.C.R., 1994, I-425.

13 ECJ, 31 March 1993, case C-19/92 *(Dieter Kraus)*, E.C.R., 1993, I-1663.

14 ECJ, 3 February 1993 in case C-148/91 *(Vereniging Veronica Omroep Organisatie,)*, E.C.R., 1993, I-487.

15 ECJ, 14 November 1995, case C-484/93 *(Svensson and Gustavsson)*, E.C.R., 1995, I-3955.

16 The restriction based interpretation of the free movement of capital is however widely accepted in legal writing: see, *inter alia*, HAUPTMANN, J.-M., "Article 73 B", in *Traité sur l'Union européenne*, V. CONSTANTINESCO, R. KOVAR, D. SIMON (eds.), Paris, Economica, 1995, 176-177; OHLER, CH., "Die Kapitalverkehrsfreiheit und ihre Schranken", *WM*, 1996, (1801), 1806; PFEIL, W., "Freier Kapitalverkehr und §110 I Nr. 2 BewG", *RIW*, 1996, (788), 790; USHER, J.A., *The Law of Money and Financial Services in the European Community*, Oxford, Clarendon Press, 1994, pp. 38-39 and 73; RESS, H.-K., *JZ*, 1995, 1010; WEBER, S., "Kapitalverkehr und Kapitalmärkte im Vertrag über die Europäische Union", *EuZW*, 1992, (562), p. 562-563; ZÄCH, R., WEBER, U.M., "Die Entwicklung des freien Kapitalverkehrs im Recht der Europäischen Gemeinschaft", in *Aspekte des Wirtschaftsrecht. Festgabe zum Schweizerischen Juristentag 1994*, H.U. WALDER, T. JAAG, D. ZOBL (eds.), Zürich, Schulthess, 1994, (405), 417-418. See on the contrary PERTSCH, PH.E., "Libre circulation des capitaux: jurisprudence récente et perspectives", *J.T.D.E.*, 1996, (97), p. 101, no. 15, who regards this interpretation as premature.

17 ECJ, 16 March 1999, case C-222/97 (*Trummer*), E.C.R., 1999, I-1661, *Euredia*, 1999/3, p. 399, note J. USHER.

18 ECJ, 30 november 1995, case C-55/94 *(Gebhard)*, E.C.R., 1995, I-4165.

same conditions in the other member states, thus prohibiting the host member state from imposing additional — by assumption restrictive — requirements on the foreign service provider. As an exception to the mutual recognition principle, the host member state may continue to apply to the imported service those provisions of its laws which are justified by the general good. The same principle applies with respect to establishment: a EU national may not be subjected to additional — and by assumption restrictive — conditions by the host member state when setting up an establishment in that state, except when the general good provides a reasonable justification for the application of the host state's laws.

The mutual recognition principle is thus based on the assumption that disparities amongst member states' laws may by themselves be tantamount to a restriction on free movement, although this is not necessarily the case.[19]

B. Material scope of the Treaty freedoms

A second question with respect to the interpretation of the Treaty freedoms concerns its material scope: which rules in the host states should qualify as a restriction on cross-border free movement ? The issue was for long considered of minor importance in both the Court's case law and in legal writing. It is only with the judgment in *Keck* and in subsequent cases that the discussion appeared at the forefront. Indeed, the definition of a 'restriction' to free movement has a direct bearing on the scope of the general good-exception: host state rules which by their nature are considered not to have a restrictive effect on free movement, can be applied in cross-border situations without the need to satisfy the general good test. Only the general non-discrimination principle would then apply for these rules.

1. General principles

In general, the Court's approach in the interpretation of the Treaty freedoms has been characterised by a functional approach to the notion of 'restriction': the restrictive character of a member state's measure is determined not by its nature, but by its *effects* on cross-border free movement. This implies that in principle, and irrespective of the freedom at stake, rules of both public and private law may run contrary to the Treaty freedoms, provided they are likely to produce a restrictive effect on cross-border free movement. This conclusion is supported by the Court's judgment in *Hubbard*, involving the application of the *cautio iudicatum solvi* in a national court to a foreign service provider. The Court stated that 'the effectiveness of Community law cannot vary according to the various branches of national law which it may affect'.[20] The European Commission takes the same view, in particular with respect to the private law relating to financial services.[21]

It should be noted that the Court until now never explicitly applied the general prohibition of non-discriminatory restrictions to regulations in the private law area. Neither did it however at any time reject such application. It is true that in the Koestler-case, involving the prohibition under German law to recover debts incurred in speculative securities transactions, the Court only applied a non-discrimination test, and concluded that the German law did not infringe the principle of free movement of services.[22] The Court's approach of the case should however be situated within its proper context, as it was decided in 1978, even before the *Cassis de Dijon*-case. Other cases in which the Court had to decide on the compatibility of private

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19 See *inter alia* ECJ, 14 July 1994, case C-379/92 (*Peralta*), E.C.R., 1994, I-3453. On the definition of a 'restriction', see *infra*.

20 ECJ, 1 July 1993, case C-20/92 *(Hubbard)* , E.C.R., 1993, I-3777; see with respect to rules of criminal law already: ECJ, 21 March 1972, case 82/71 (*SAIL)*, E.C.R., 1972, 119.

21 Interpretative Communication, at p. 23.

22 ECJ, 24 October 1978, case 15/78 *(Koestler*), E.C.R., 1978, p. 1971.

law rules with the free movement of goods or services all concerned alleged discriminatory provisions.[23] Therefore, the Court was not given the opportunity to give a ruling on the general prohibition of non-discriminatory restrictions.[24]

In summary, one could consider that, in order to determine the material scope of the Treaty freedoms on the member states' laws, three main areas of law could be distinguished in which the free movement of services or goods and the freedom of establishment are likely to interfere:

(1) Rules relating to market access for offerors of goods and services. Mainly originating in public law, these rules concern the conditions under which the manufacturers and distributors of goods and services obtain access to the market (rules on the legal form and the internal organisation of the enterprise, including requirements originating in general company law, own funds requirements, professional rules,…) and the instruments through which these rules are enforced (registration with a public body, licensing, supervision by an administrative body, …);

(2) Rules on market behaviour by the goods and services offerors: these rules of both public and private law relate to the way in which goods and services are offered on the market, with respect to *inter alia* advertising, joint or tied offers and, in general, the rules on unfair competition. In some member states, the enforcement of these rules is entrusted to a public law body, while in others only private enforcement mechanisms are provided;

(3) Private law rules purporting to the contents or substance of the goods or services offered on the market: these 'product rules' relate to the proper characteristics of the material good (weight, composition, presentation, labelling) or of the service.[25] With respect to the latter, a service being immaterial by its very nature, the contractual relationship between service provider and receiver will play a central role (object of the contract, mutual rights and obligations of parties, liability rules, unfair or mandatory contract terms,…).

2. Material scope and proper function of the Treaty freedoms

In theory, the general prohibition of non-discriminatory restrictions may affect the member states' regulatory powers in all the aforementioned areas of law, on the sole condition that the obligation for the market participant to comply with the said rule qualifies as a 'restriction' to cross-border free movement. Surprisingly, the Court did never, except in the context of free movement of goods, clearly define the notion of 'restriction' itself. It may be submitted that the Court implicitly relied on the broad *Dassonville*-formula when extending its jurisprudence to the other Treaty freedoms. Consequently, all measures which directly or indirectly, actually or potentially affect the cross-border free movement will be caught by the prohibition. The Court will examine whether the rules under scrutiny in one way or another make the exercise of the freedom either impossible[26], more costly[27] or less attractive.[28]

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23 See e.g. ECJ, 24 January 1991, case C-339/89 (*Alsthom Atlantique*), E.C.R., 1991, I-107; ECJ, 13 October 1993, case C-93/92 (*Motorradcenter*), E.C.R., 1993, I-5009. With respect to rules of private procedure: ECJ, 29 October 1980, case 22/80 (*BoussacSaint-Frères*), E.C.R., 1980, 3427; ECJ, 1 July 1993, case C-20/92 *(Hubbard)* , E.C.R., 1993, I-3777; ECJ, 10 February 1994, case C-398/92 (*Mund & Fester*), E.C.R., 1994`, 467; ECJ, 26 September 1996, case C-43/95 (*Forsberg*), E.C.R., 1996, I-4661.

24 see however ECJ, 1 February 1996, case C-177/94 (*Perfili*), E.C.R., 1996, I-161, where the Court refused to decide whether the non-discriminatory procedural rule (*in casu* the rule in Italian law according to which a victim of a criminal offence who wishes to bring suit as a civil party in criminal proceedings should grant his representative a special power of attorney) could constitute a non-discriminatory restriction te free movement, with the argument that it did not dispose of the necessary elements in fact to make a judgment.

25 See in this respect the distinction drawn by the Court of Justice in *Keck* between 'product rules' and 'selling arrangements' as basis for the more lenient regime applying to the latter.

26 See the Court's approach in ECJ, 25 July 1991, case C-76/90 (*Säger*), E.C.R., 1991, p. I-4221, para 12:

Should one conclude from the *Gebhard* judgment that all Treaty freedoms today enjoy a convergent or even identical interpretation, implying that the law of a Member state which qualifies as a restriction to the freedom to provide services automatically consitutes a restriction to the freedom of establishment? The answer is negative, in so far as this conclusion omits to take account of the proper functions and objectives of the different Treaty freedoms. Indeed, a teleological approach to the interpretation of the Treaty freedoms may lead to varying results as to the material scope of the different freedoms considered separately. As a matter of fact, different objectives may be attributed to each Treaty freedom: it is clear that the free movement of goods is mainly concerned with mobility of material products across borders. In the same line, the free movement of services essentially involves the cross-border mobility of the immaterial product (the service), and, ancillary to the product mobility, the (temporary) cross-border mobility of the person providing or receiving the service.[29] On the other hand, the freedom of establishment and the free movement of workers are essentially concerned with the mobility of — natural and legal — persons across borders, and remain largely unrelated with the mobility of the goods or services manufactured or distributed by these persons: the establishment supposes the setting up of an entity integrated in the economy of the host member state[30], from where it will develop its activities. The free movement of capital finally relates to the free flow of all capital substance in any form.

Bearing in mind the specific objectives of each Treaty freedom, further refinements could be made as to what constitutes a 'restriction' to free movement. Thus, the freedom of establishment being related essentially to the movement of persons, only the member states' measures which are related to the mobility of the person, i.e. influencing the decision to set up or to maintain an establishment, or with respect to the internal organisation and functioning of the enterprise as such, will qualify as a restriction to cross-border establishment (so called 'enterprise-related' rules). Hence, it is difficult to see how non-discriminatory product-related rules (e.g. mandatory contractual clauses, rules on advertising for a given product) could be regarded as restricting the freedom of establishment, as these rules do not interfere with the proper function of that freedom. On the contrary, the same non-discriminatory product-related rules may amount to a restriction on the free movement of services, in the situation where the service provider does not maintain an establishment in the host member state: the host state's rules oblige the foreign service provider to modify the substance of the service or the way in which it is offered when extending his activities to the host state's market, and therefore directly affect the proper function of the free movement of services, *i.e.* the cross-border mobility of the service as an immaterial product. A restriction to free movement of services will therefore not necessarily amount to a restriction on the freedom of establishment, when the same activity would be taken up through an establishment in another member state. Measures which do not, by their very nature, influence the movement of the enterprise itself, but merely the way in which the activity is exercised, can

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27 See ECJ, 4 December 1986, case 205/84 (Commission v. Germany, *E.C.R.*, 1986, p. 3755, para 28, where the Court found in the requirement for a foreign insurance undertaking to have a permanent presence in the host country a restriction on free provision of services inasmuch as it increases the cost of insurance services in the State in which they are provided.

28 See ECJ, 30 November 1995, case C-55/94 (*Gebhard*), E.C.R., 1995, I-4188, para 37, which refers to the general prohibition of all national measures which "hinder or make less attractive" the exercise of fundamental freedoms. The general wording of the cases now refer to all measures which 'prohibit, impede or render less advanageous' the exercise of the freedom: see *inter alia* ECJ, 23 November 1999, case C-369/96 and 376/96, (*Arblade and Leloup*), *not yet reported*, para 33.

29 See with respect to the latter Article 50, paragraph 2 EC-Treaty.

30 Compare on the notion of establishment ECJ, 25 July 1991, case C-221/89, (*Factortame II*), ECR, 1991, I-3905; ECJ, 30 November 1995, case C-55/94 (*Kraus*), E.C.R., 1995, I-1663, para 25; ECJ, 5 June 1997, case C-56/96 (*VT4*), E.C.R., 1997, I-3143, para 17 (in the context of Article 49 EC).

therefore be considered to remain outside the material scope of the freedom of establishment.[31]

An example will illustrate the former. According to Belgian law, enterprises offering mortgage credit have to register with the *Office de Contrôle des Assurances*, by whom they are supervised, in order to grant mortgage credit to consumers with habitual residence in Belgium.[32] The Law on mortgage credit further contains, for the sake of consumer protection, specific rules on contractual clauses, *inter alia* with respect to interest rate variability: parties must relate the interest rate of the credit to the rates for Belgian treasury bills when the credit is denominated in Belgian francs or in euro; moreover, the interest rate may not vary to the consumer's detriment during the first three years of the credit (art. 9). Finally, the law imposes specific requirements on advertising for mortgage credit and the availability of all useful information on the credit under the form of a prospectus (art. 47).

For a financial institution established and properly supervised in another EU member state, the obligation to register with and submit specific documents to the supervisory authorities in Belgium when offering mortgage credit contracts on the Belgian market, will undoubtedly constitute a restriction on free movement, irrespective of whether the activity is undertaken through a Belgian branch or directly under the freedom to provide services.[33] Indeed, the regulatory cost involved with the supervisory requirements directly influences the foreign institution's decision to set up an establishment in the host member state. It also clearly affects the freedom to provide services, as it imposes an additional burden on the financial institution wishing to offer its services without establishment.

On the contrary, the requirements with respect to interest variability and advertising by the mortgage credit enterprise are unrelated with the trans-border mobility of the financial institution as corporate entity, but solely concern the way the enterprise offers its products in the host member state. Hence, these non-discriminatory requirements under Belgian law may amount to a restriction to the free movement of services, because they prevent the financial institution from offering its services in the host state under the same conditions as in its home state. On the contrary, they do not constitute a restriction to the freedom of establishment, as they do not affect the setting up, the internal organisation or the functioning of the enterprise itself.

The further refinement operated above with respect to the varying significance of the 'restriction' according to the specific objectives of each Treaty freedom is not until now corroborated by the case law of the Court of Justice. Neither does the case law provide any argument against this approach. Indeed, the cases which formulated the restriction based concept of the freedom of establishment all, *Gebhard* included, concerned 'enterprise related' professional rules in national law. However, the recent *Centros* judgment indicates the willingness of the Court of Justice to consider the proper scope of the Treaty freedoms as foundation for their interpretation: with respect to the freedom of establishment, the Court held that Member States should, in combatting fraud by foreign companies, take account of the objectives of the Treaty freedoms. The Court further emphasised that the proper objective of the freedom of establishment consisted in guaranteeing the possibility for companies established in a member state to take up activities in other member states through a subsidiary, branch or agency. In view of this objective, the Court operated a distinction between rules relating to the creation of companies on the one hand, and rules on the exercise of professional activities on the other, to support its conclusion that the former category belonged to the very essence of establishment, and therefore could by no means be restricted by the host member state. Although the Court did not

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31 Compare the distinction operated by P. Troberg between 'institutional' and 'functional' regulation: TROBERG, P., "Artikel 59", in VON DER GROEBEN, H., THIESING, J., EHLERMANN, C.-D., *Kommentar zum EWG-Vertrag*, 4th ed., Baden-Baden, Nomos, 1991, p. 1064. See for a more extensive analysis of this proposition, and its possible applications to financial regulation: TISON, M., *De interne markt voor bank- en beleggingsdiensten*, Antwerp, Intersentia, 1999, paras 86-94, 167-184 and 284-309.

32 Art. 43 Law 4 August 1992 on mortgage credit, *Mon.*, 19 August 1992.

33 Compare the French cases which gave rise to the Court's judgment in *Parodi* (ECJ, 9 July 1997, case C-222/95 (*Parodi)*, E.C.R., 1997, I-3899) and its aftermath, in particular the outcome of the case in the judgment of the French Cour de Cassation of 20 October 1998. (On this case and subsequent judgments of French courts in similar cases, see TISON, M., "Rebondissements de l'affaire *Parodi* en France: entre nationalisme juridique et libertés communautaires", *Euredia*, 1999/4, p. 574).

conclude that rules on the exercise of a professional activity remained outside the restriction based interpretation of freedom of establishment, the Court nevertheless cleared the path for a 'variable geometry'-approach in interpreting the Treaty freedoms: in identifying the rules of the member states which constitute a restriction to one or another Treaty freedom, the objective of the freedom at stake will serve as primary reference. As a consequence, some rules will, by their very nature, more than others impair on the essence of the freedom and hence qualify as restriction.[34] In *Centros*, this was the case with rules which interfere in the possibility to set up an establishment: the likelihood of a reasonable justification for such restrictions will be far more reduced than for restrictions relating to the exercise of an activity in the host state through an establishment. In conclusion, *Centros* illustrates the move by the Court to identify the essence of the Treaty freedoms, in view of its objective in the Treaty system, as method for its interpretation and impact on national regulation.

In the context of freedom of establishment, the issue of delimiting the scope of the freedom as basis for its interpretation is not new. Several authors have made attempts to formulate criteria to delimit the material scope of non-discriminatory 'restrictions' with respect to freedom of establishment: distinction between rules on access to and exercise of a profession[35]; distinction between objective and subjective regulation[36]; criterion of market access as proper function of establishment.[37] None of these proposals lead to fully satisfactory results: the first is artificial and has been clearly rejected by the Court in *Gebhard*, the others are based on rather vague concepts which find no clear justifications in the Treaty itself. Although the *Centros* judgment could be invoked in support of a distinction between rules on market access and exercise of an activity in the host state through an establishment, it should be noted that this distinction served a specific purpose in the context of the facts of the case and the solution envisaged by the Court: the distinction made by the Court was intended to stress the 'untouchable' nature of rules on market access — and the setting up of a corporate entity in particular — in the light of the host state's competencies to counter alleged abuse of Treaty freedoms or fraud by the use of a pseudo-establishment.[38]

The distinction operated above between 'enterprise related' and 'product-related' rules necessarily determines the scope of the general good as exception to the prohibition of non-discriminatory restrictions to free movement: the measures in the law of a member state which are unrelated to the proper function of a Treaty freedom and therefore escape the restriction based prohibition, will not need any justification on grounds of general good: it is sufficient for these measures to satisfy the non-discrimination test, which forms part of the general principle of equal treatment in Community law.[39]

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34 The opposite is also true: as appears from *Keck and Mithouard* (cited *infra*, note 40), 'selling arrangements' which only have a limited effect on intra-Community trade because they intervene only in a late stage of distribution of goods, will not qualify as restriction to free movement.

35 See e.g. EVERLING, U., "Das Niederlassungsrecht in der Europäische Gemeinschaft", *Der Betrieb*, 1990, (1853), 1858; ROEGES, L., "L'exercice de l'activité bancaire par la voie d'une succursale après la deuxième directive bancaire", *Revue de droit bancaire et de la bourse*, 1994, p. 19 and p. 115.

36 ROTH, W.-H., "Niederlassungs- und Dienstleistungsfeiheit - Grundregeln", in *Handbuch des EG Wirtschaftsrecht*, M.A. DAUSES (ed.), Munich, Beck, looseleaf (1993), E.1, p. 22; ROTH, W.-H., "The Freedom of Establishment and the Free Provision of Services in the Financial Services Sector", in *The European Economic Area EC-EFTA. Institutional Aspects and Financial Services*, J. STUYCK, and A. LOOIJESTIJN-CLEARIE, (eds.), Deventer, Kluwer, 1994, (75), p. 86.

37 See WOUTERS, J., "Conflicts of Laws…", cited *supra* note 37, p. 201-203.

38 Comp. KIENINGER, E.M., "Niederlassungsfreiheit und Rechtswahlfreiheit", *ZGR*, 1999, p. 743; DE WULF, H., "Brievenbusvennootschappen, vrij vestigingsrecht en werkelijke zetelleer", *Vennootschapsrecht & Fiscaliteit*, 1999/1, p. 10, para 37.

39 This is confirmed by the Court's case law which analyses the Treaty freedoms primarily as a specification of the general non-discrimination principle, as laid down in Article 2 EC.

3. Effects of the Keck-jurisprudence

An additional difficulty in delimiting the material scope of the prohibition of non-discriminatory restrictions on free movement stems from the *Keck and Mithouard*[40] and subsequent cases, in which the Court held that the regulation of selling arrangements which does not imply any unequal treatment in law or in fact to the detriment of imported goods, could no longer be considered to unduly restrict the free movement. Apparently, the Court thus excluded a specific category of laws ('selling arrangements') from the prohibition of non-discriminatory restrictions. Other cases illustrate that the 'selling arrangements' also include rules on advertising for goods.[41]

It is not possible to enter in the present contribution into further details on the interpretation of *Keck*.[42] With respect to financial services however, two specific questions arise: is *Keck* likely to be applied to the other Treaty freedoms; and if so, under which conditions should it apply ?

As to the first question, the movement of convergence witnessed in the interpretation of the Treaty freedoms suggests that the development in the field of goods could equally be mirrored in the other Treaty freedoms. As demonstrated in *Alpine Investments,* the Court does not exclude a transposition of *Keck* to the area of (financial) services.[43]

On the contrary, it may be doubted whether *Keck* could receive a useful application in the area of freedom of establishment. Given the proper function of the freedom of establishment — promoting the mobility of persons and enterprises — the present case law already seems to exclude product-related regulation from the scope of the freedom of establishment: the 'selling arrangements', which relate to the way a product is offered on the market, will therefore only infringe the freedom of establishment when containing an overt or disguised discrimination on grounds of nationality. The interpretation of the freedom of establishment suggested above is therefore already in line with the *Keck*-jurisprudence.[44]

The second question — under which conditions could *Keck* apply in the area of services — is more difficult to answer. In our opinion, the rule in *Keck* was not intended to overrule all previous jurisprudence on the application of *Dassonville* in the field of 'selling arrangements', but merely wanted to return to the basics of the restriction based interpretation of the free movement of goods, *i.e.* prohibiting the measures in the member states which, without operating any formal or material discrimination, nevertheless result in an unequal treatment of imported goods due to their submission, in their member state of origin, to equivalent rules. The factual context in *Keck* and similar cases specifically concerned selling modalities which intervened in an advanced stage of distribution within the host member state, and therefore could be largely assimilated to internal situations. On the contrary, the regulation of selling arrangements which more directly affect the cross-border movement of goods, remains in our view subjected to the prohibition of all

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40 ECJ, 24 November 1993, case C-267-268/91 (*Keck and Mithouard*), E.C.R., 1993, I-6097.

41 See, *inter alia*, ECJ, 5 December 1993,case C-292/92 *(Hünermund)*, E.C.R., 1993, I-6787; ECJ, 9 February 1995, case C-412/93 *(Leclerc-Siplec vs TF1 and M6)*, E.C.R., 1995, I-179.

42 See WEATHERILL, S., "After *Keck*: Some thoughts on how to classify the clarification", *CMLR*, 1996, p. 885 *et seq.* For an extensive analysis of the *Keck*-ruling and its possible consequences for cross-border activities of financial institutions, see TISON, M., *De interne markt voor bank- en beleggingsdiensten*, *supra* note 31, paras 488-520.

43 ECJ, 10 May 1995, case C-384/93 *(Alpine Investments)*, E.C.R., 1995, I-1141. The rejection of the *Keck*-rule by the Court in *Alpine Investments* may be attributed to the specific facts of the case, which concerned an export restriction — the prohibition of cold calling for financial products towards customers in other member states — directly affecting the *access* of the service provider to the market of another member state. The Court did not exclude the application of the *Keck* rule in cases where the host member state would impose a similar non-discriminatory prohibition on services provided in its territory by an enterprise established abroad

44 See however WOUTERS, J., "Conflicts of Laws…", cited*supra* note 37, p. 207-208.

restrictions (e.g. the prohibition of direct advertising by the foreign distributor for his goods in the host country).[45]

This interpretation of *Keck* has important consequences for its transposition to services. The cross-border element in trans-border services usually relates to the service provider and receiver being established or resident in different member states. Moreover, unlike goods, the distribution of services usually does not take place through extensive distribution channels, but most of the time directly between the 'manufacturer' (provider) and the receiver (consumer) of the service. Consequently, the regulation in a member states with respect to 'selling arrangements' of a service will usually directly affect the cross-border flow of services, and therefore continue to be subjected to the general prohibition of non-discriminatory restrictions. Only in the hypothesis that the service is offered in the host state through the intervention of intermediaries, could *Keck* be applied by analogy on the regulation restricting the use of 'selling arrangements' by the intermediary.[46]

C. Conclusions on the Court's case law with respect to the Treaty freedoms

The analysis of the Court's case law on the Treaty freedoms shows a clear movement of convergence in the interpretation of all freedoms as prohibiting not only the — overt or disguised — discriminations on grounds of nationality, but also all other non-discriminatory measures which restrict cross-border free movement. However, the general prohibition of all restrictions needs further refinement in the light of each freedom's proper objectives, which in turn will affect the extent to which the general good-exception applies. On the other hand, the *Keck* jurisprudence does not seem to produce a significant effect in the fields of establishment and services in general, and financial services in particular.

Part II — The 'general good' exception and its application in the area of financial services

A. General principles

Although some attempts have been made to provide a general definition of the concept of general good[47], it should be stressed from the outset that the Court has always refrained from building upon an abstract approach to the concept of 'general good' in its jurisprudence. Indeed, given its evolutionary nature, a definition of the general good could at most point to the *functions* it fulfils within the system of the Treaty. The general good may then be circumscribed as an open-ended concept, embracing the possibility for member states to maintain, in the absence of Community legislation, their regulation which ensures the protection of specific social values which are not incompatible with the objectives of the Treaty. The general good thus operates an arbitrage between the fundamental Treaty freedoms and the member states' interests in the regulation of other, non-economic values.[48] The general good thus primarily proceeds from the

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45 Comp. in this respect the *GB-Inno-BM* case, decision of 7 March 1990, case C-362/88, E.C.R., 1990, I-667 (prohibition under Luxemburg law for a Belgian supermarket to announce in its publicity leaflets, distributed in Luxembourg, price reductions with mention of the old prices).

46 However, even in that case will the service, unlike the distribution of goods, create a contractual relationship between service provider and receiver. This specificity could plead against the transposition of *Keck* to the area of trans-border services.

47 PARDON, J., "Liberté d'établissement et libre prestation dans le domaine bancaire", *Revue de Droit Bancaire et de la Bourse*, 1991, (219), at 220.

48 EVERLING, U., "Sur la jurisprudence de la Cour de Justice en matière de libre prestation de services

member states' regulatory policies, but is to be balanced against the need to ensure free movement of products (goods and services) and of production factors (human and other capital).[49] This balancing of possibly conflicting interests implies that, due to the precedence of Community law, the member states' autonomy in defining and implementing the general good will find its limits in Community law. These limits are incorporated in the conditions formulated by the Court in order for the general good exception to prevail on the free movement principle. This approach also implies that the Court of Justice will be the final judge in deciding on the compatibility of member states' regulation with the general good exception, thus achieving more uniformity in the application of Community law.

This peculiar relationship between general good and free movement may be compared to the 'public order' exception to the Treaty freedoms: the question which measures qualify as 'public order' is a matter of national law, but its application is limited by the need to ensure a proper balancing of interests with the free movement principle.[50] The main difference between the 'public order' and 'general good' interests lies in the possibility for the former to justify discriminatory restrictions on free movement: The availability of the 'public order' exception is restricted to those social values, the disruption of which would affect one of the fundamental interests of society.[51] Therefore, it may be submitted that interests such as consumer protection are not that fundamental for the social order as to justify discriminatory restrictions to free movement of (financial) services.

B. Conditions attached to the general good

The conditions under which a member state is allowed to invoke the general good as barrier to the free movement, are well established in the Court's case law, and may be summarised as follows:

- justification by a general good motive
- absence of harmonisation;
- absence of discrimination on grounds of nationality;
- absence of duplication of home state rules;
- objective necessity (adequacy and proportionality).

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rendus dans d'autres Etats-membres", *Cah. dr. eur.*, 1984, 14; DUBUISSON, B., "Unité ou diversité des notion d'intérêt général, d'ordre public et de normes impératives dans les directives communautaires relatives aux assurances", in *L'Europe de l'assurance. Les directives de la troisième génération*, Antwerp, Maklu, 1992, (187), at p. 244, no 70; DUBUISSON, B., "L'intérêt général en droit communautaire de l'assurance. La réaction thermidorienne", *R.G.A.T.*, 1995, (809), 815, no. 4; VAN SCHOUBROECK, C., "The Concept of the general Good", in *The Law and Practice of Insurance in the Single European Market*, A. MCGEE, W. HEUSEL (eds.), Köln, Bundesanzeiger, 1995, (149), 151.

49 Some have however expressed their support for a qualification of the general good concept under Community law, instead of under national law: see concl. adv.-gen. VERLOREN VAN THEMAAT in case 286/81 of 15 December 1982 *(Oosthoek)*, E.C.R., 1982, (4575), at p. 4598.

50 See also the Court's decision of 15 March 1988 in case 147/86 *(Commission v. Greece)*, E.C.R., 1988, p. 1637; for an overview of the case -law with respect to the 'public order' see VAN GERVEN, W., WOUTERS, J., "Free Movement of Financial Services and the European Contracts Convention", in *EC Financial Market Regulation and Company Law*, M. ANDENAS, S. KENYON-SLADE (eds.), London, Sweet & Maxwell, 1993, (43), at pp. 51-55.
Inversely, the circumstance that a Member State considers a law to belong to its (internal) public order, does not automatically imply that it is exempted from the application of Community law. As correctly held by the Court of Justice in *Arblade and Leloup*, the precendence and uniformity of Community law require that the application of 'public order' laws which impose a restriction on free movement be justified by an overriding ground of public interest under Community law ('public order' or general good): see ECJ, 23 November 1999, *Arblade and Leloup*, case C-369/96 and 376/96, *not yet reported.*

51 See in particular the Court's decision of 27 October 1977 in case 30/77, *(Bouchereau)*, E.C.R., 1977, p. 1999.

1. General good motive

First, the member state has to justify the restriction on free movement with reference to a general good motive which is not incompatible with the objectives of the EC-Treaty. In general, the Court refuses, as within the context of the 'public order' exception, the recourse by the member states on motives of economic nature, such as the protection against foreign competitors, the reduction of inflation or of unemployment. These motives will, in view of their protectionist nature, automatically interfere with the aims of the Treaty in creating a single market and eliminating all distortions of competition.[52]

The Court's scrutiny of the compatibility of member states' general good motives with the Treaty objectives is effected on a case by case basis. In general, the Court will investigate whether the invoked motive is in line with the Treaty objectives, and whether the member state's measure effectively pursues the said motive. Hence, the Court is entitled to 'pierce the member state's veil' when it appears that the measures in reality pursue other, protectionist, goals.[53]

The motives of general good may relate to matters falling both within or outside the Community's competencies, in the former hypothesis on condition that the Community did not yet adopt harmonisation measures in the same field. Furthermore, the Court's scrutiny in this case would appear to be more severe: the Court will not limit itself to checking the conformity of objectives, but will also make sure that the member states' measures do not run against possible future harmonisation actions to be undertaken by the Community legislator.[54]

2. Absence of harmonisation

In order for a member state to justify a restriction on free movement by the general good, the matter — by hypothesis falling within the Community's regulatory competencies — may not have been the subject of harmonisation measures at Community level. The underlying idea is that the exercise by the Community of its regulatory powers will be regarded as the codification at Community level of the member states' powers under the general good.

However, the Court should in any case verify whether the Community harmonisation is sufficient to produce a complete substitution effect to the member states' powers on grounds of general good. This is well illustrated in the *German insurance case*: notwithstanding the harmonisation of supervisory standards for insurance companies by the first non-life insurance directive, the Court recognised that several supervisory issues were not covered by this directive, thus leaving room for the member state to regulate foreign insurers in the interest of the general

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52 See, respectively, Art. 3(a) and 3(f) EC-Treaty.

53 See for an application the Court's decision of 16 December 1992 in case C-211/91 *(Commission vs Belgium)*, E.C.R., 1992, I-6757, where the Court rejected the defendant's justification on grounds of cultural policy with the argument that the measure at stake in reality aimed at protecting the own market against foreign competitors; more recently: ECJ, 21 October 1999, case C-67/98 (*Zenatti*), *not yet reported in E.C.R.*, where the Court verified whether the limits on the organisation of commercial betting activities in Italy efectively pursued the aim of protecting consumers and the social order. See also GAVALDA, C. and PARLEANI, G., *Traité de droit communautaire des affaires*, 2nd ed., Paris, Litec, 1992, p. 73, no. 52-11.

54 For instance, the Court relied in *GB-Inno-BM* on the Council's consumer protection action programme to illustrate the Community's adherence to issues of consumer protection with respect to advertising: see ECJ, 7 March 1990 in case C-362/88 *(GB-Inno-BM)*, E.C.R., 1990, I-667; see also the German Insurance case, 205/84, E.C.R., 1986, 3755, where the Court paid attention to the draft second non-life insurance directive in deciding whether the defendant could maintain a licensing requirement for foreign insurers

good.[55]

The extinction of member states' powers in the interest of the general good as a consequence of sufficient Community harmonisation, is one of the cornerstones of the 'new approach' to harmonisation set forth in the 1985 Commission White Book on the Completion of the Internal Market, and put in practice in the internal market directives on, *inter alia*, financial services: the directives aim at reaching a minimum, but sufficient level of harmonisation, which corresponds to the codification of the general good, in order to produce full mutual recognition of regulatory standards. This 'perfect' mutual recognition does no longer entitle the member states to invoke the general good as a justification for the application of more restrictive rules in cross-border situations.

The 'sufficient' minimum harmonisation as mentioned above is to be distinguished from the 'partial' minimum harmonisation effected by other directives adopted or elaborated in the first half of the '80s, *inter alia* in the field of misleading advertising or consumer credit. These directives do not aim at exhaustively harmonising what otherwise would fall under the general good powers of the member states, but clearly only intended to achieve a partial harmonisation of specific issues, leaving room for the member states to introduce or maintain more restrictive standards.[56] However, in view of the jurisprudential developments in the field of free movement, member states should, where it produces restrictive effects on cross-border free movement, use this clause in accordance with the general good exception.

The recent decision of the Court of Justice in *Ambry*[57] illustrates the difficulties to ascertain whether harmonisation is to be considered as 'sufficient' or only 'partial'. The Court was asked whether the French law which obliged travel agencies to dispose of sufficient financial resources under the form of, for instance, a bank guarantee, could require that, when the guarantee was provided by a credit institution established in another EU member state, an additional agreement be concluded between that credit institution and a French bank or insurance undertaking in order to ensure the immediate availability of the payment under the guarantee. The Court of Justice ruled that the French law was contrary to both the Treaty freedom to provide services (Art. 49 EU-Treaty) and to the right to provide services under the Second Banking Directive. It then went on verifying whether the restriction could be maintained under the general good clause, but held the French law to create a disproportional restriction to free movement.

Without challenging the outcome of the case, it may be questioned whether the Court's reasoning was fully coherent in on the one hand acknowledging that the French law was contrary to the single passport provided in the Second Banking directive, which is based on "sufficient" harmonisation of prudential standards, and on the other hand proceeding to the general good test notwithstanding the existence of harmonisation. It is true that the Second Banking Directive did not specifically harmonise the conditions under which a credit institution is allowed to provide financial guarantees for travel agents.[58] It may however be submitted that the French law constituted a direct *access* barrier for foreign credit institutions to the extent that the latter were obstructed in the possibility to provide bank guarantees which would be recognised as equivalent to a guarantee offered by a domestic credit institution.

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55 ECJ, 4 December 1986, case 205/84 (*Commission v. Germany)*, E.C.R., 1986, at 3755.

56 See in particular Art. 7 Directive 84/450/EEC on misleading advertising; art. 15 Directive 87/102/EEC of 22 December 1986 on consumer credit.

57 ECJ, 1 December 1998, *Ambry*, case C-410/96, E.C.R., 1998, I-7875, *Euredia*, 1999/1, p. 55, note M. VEREECKEN.

58 In the absence of harmonisation of this specific issue — the recognition as financially sound guarantee for the sake of protection of clients of travel agencies — the general good clause would consequently fully apply: compare VEREECKEN, M., "Can a Member State require an additional guarantee agreement in the interest of the general good ?", *Euredia*, 1999/1, (59), p. 62; see also ROTH, W.-H., "Bancassurfinance and the European passport for financial institutuions", in *Bancassurfinance*, Cahiers AEDBF-Belgium, Brussels, Bruylant, 2000 (forthcoming), para 2.1.5.

3. Non-discrimination

The prohibition for a general good rule to contain any discrimination on grounds of nationality distinguishes, as already stated, the judge-made concept of the general good from the 'public order' exceptions contained in the Treaty with respect to the different freedoms. The non-discrimination principle should be understood in a broad sense: it includes both overt and disguised discriminations, the latter pointing to situations where the measure at stake makes use of a distinctive criterion not relating to nationality, but producing in practice, due to factual circumstances, the same effects as a distinction based on nationality.

It should be noted that the Court does not always seem to follow this principle with the same rigour: especially in tax matters did the Court envisage the possibility of justifying a restrictive measure, notwithstanding its discriminatory character, by the general good, *viz.* the coherence of the fiscal system.[59] However, as recent case law seems to have limited to a great extent the possibility of relying on the coherence of the fiscal system as general good justification (cf. *infra*), this should not bear major concern.

4. Absence of duplication of home state rules and controls

The non-duplication principle perfectly illustrates the background of the restriction based interpretation of the Treaty freedoms: a measure in national law will be regarded as impeding free movement because, although operating no discrimination towards foreign products or persons, the duplication with the home state rules results in additional costs for the foreign product or person when entering the host state market. The non-duplication requirement underlines, together with the proportionality rule, the need for the member states to have regard, within a unified economic area, to each other's laws before applying their own laws in cross-border situations.[60]

An analysis of the case law on free movement of services and the general good shows that the Court's attention for the non-duplication principle varies considerably: very often, the general good test is effected without having regard to the rules or controls to which the service provider is subjected in its home state. In matters where the cost of double regulation appears overtly, the Court would however more strongly emphasise the non-duplication principle. This was made most clear in the cases where the Court has to decide on the application of various host state's laws and regulations on the temporary posting of workers by EU based employers in the context of cross-border service contracts.. In *Vanderelst*[61] and more recently in *Arblade and Leloup*[62], the Court strongly objected against the imposition by the host state of social security contributions upon the workers or their employer which are aimed at covering interventions which are equally guaranteed by the home state and for which similar contributions are already paid in the home state. The duplication of financial burdens is clearly tantamount to a restriction which will put the employer in a competitive disadvantageous situation compared to its host state equivalent.[63]

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59 See in particular the decisions of 28 January 1992 in case C-204/90 *(Bachmann)*, E.C.R., 1992, I-249 and in case C-300/90 *(Commission vs. Belgium)*, E.C.R., 1992, I-305, which concerned the tax deductibility of life insurance premiums by Belgian residents, granting the benefit only when the insurance company had an establishment in Belgium. It has been rightly stressed that this rule in reality discriminated against companies established in other member states: comp. WOUTERS, J., "The Case-Law of the European Court of Justice on Direct Taxes: Variarions upon a Theme", *Maastricht Journal of European and Comparative Law*, 1994, (179), p. 189-190; FOSSELARD, D., "L'obstacle fiscal à la réalisation du marché intérieur", *Cah. dr. eur.*, 1993, (472), p. 492-493.

60 See also VAN SCHOUBROECK, C., "The Concept of the general Good", cited *supra* note 48, p. 155, no. 2.

61 ECJ, 9 August 1994, *Vander Elst*, C-43/93, *E.C.R.*, 1994, I-3803.

62 ECJ, 23 November 1999, *Arblade and Leloup*, case C-369/96 and 376/96, *not yet reported.*

63 See *Arblade and Leloup*, at para 50.

The comparison with the rules of the member state of origin of the product or the person in assessing the non-duplication requirement, implies that the general good-test may produce different results depending on the law applicable in the member state of origin of the product or person, the one disposing of equivalent rules while the other does not. Theoretically therefore, a member state should, when drawing up lists of general good rules applying to a foreign service provider[64], make a different list for each member state of origin separately.

5. Objective necessity (appropriateness and proportionality)

The proportionality or necessity requirement has emerged in the Court's case law as the cornerstone in the general good test, as it is the condition through which the arbitrage between the Community interest and the member states' regulatory interests is effected. The test in reality involves a double requirement: first, the member state's measure must be useful and appropriate to reach the general good objective, *i.e.* it must be possible for the public interest to be effectively achieved through the measures invoked (*appropriateness*); second, the measure must be *necessary* for achieving the general good objective. This necessity requirement itself contains both a positive and a negative element: in a positive sense, the restriction provoked by the general good measure must be in proportion with the benefits resulting from the measure for the attainment of the general good objective (*proportionality*); in a negative sense, there should be no equivalent alternative available which is less restrictive to cross-border free movement.

The latter requirement leaves ample room for jurisprudential activism in the application of the general good test, as it allows the judges to decide on the equivalence of different policy alternatives against the background of the free movement. As an example, the *GB-Inno-BM* case illustrates a clear policy choice with respect to consumer protection: by expressing its preference for sufficient information to consumers as equivalent alternative for prohibitive regulation, the Court rejected the traditional 'paternalistic' approach to consumer protection as a necessary precondition for market integration.

The division of powers between the Court of Justice and the national judge in preliminary procedures in the context of the general good-test has been summarised by advocate-general VAN GERVEN as follows:

- The national judge must provide the Court of Justice all factual elements which are important for the interpretation of the Treaty;
- It is up to the Court of Justice to lay down the general contents of the proportionality requirement, and the criteria according to which the proportionality of the member state's measure should be measured;
- The actual decision on the proportionality lies with the national courts, as it concerns an application of the abstract criteria to the factual elements of the case.

In reality, the Court of Justice very often rules itself on the proportionality issue, given the circumstance that it disposes of all necessary elements of fact to give guidance to the national judges. This approach further strengthens the Court's activism, and is likely to promote the unity in the application of Community law. However, the Court seems more reluctant in applying the proportionality test when the case appears more sensitive. This was demonstrated in the *Parodi*-case, involving the compatibility with Art. 49 EU Treaty of the French banking law which required EU credit institutions offering banking services in France prior to the entry into force of the Second Banking Directive to obtain a license with the French banking authorities, and even to have an establishment in France. The impact of the question was considerable as several dozens of cases had been brought before the French courts by borrowers who invoked the infringement of the banking law as ground for the annulment of the credit agreements and security interest. The Court stated that it did not dispose of sufficient elements on the objectives of the French banking law to proceed to the proportionality and necessity test. The result of it was that the French *Cour de Cassation* ruled the French law to satisfy the general good test, and declared void all transactions

64 See on this issue *infra*, Part III, E.

entered into by the foreign bank in contravention to the licensing requirement.[65] Interestingly, some lower French courts in very recent decisions openly deviate from the ruling of the Cour de Cassation and come to opposite conclusions on basis of another interpretation of the judgment of the Court of Justice in *Parodi*.[66]

6. Burden of proof

As an exception to the basic freedoms of the Treaty, the burden of proof with respect to the general good justification lies with the person who invokes it.[67] For example, when a financial services provider claims the benefit of the free movement of services against the application by the host state of its supervisory regulations, the service provider will be entitled to claim the benefit of free movement simply by demonstrating that he falls within its ambit: existence of a cross-border service, and existence of a restriction on the free movement of services (e.g. submission to equivalent rules in the home member state). It will then be up to the host state's supervisory authorities to prove that the application of its regulations satisfies the general good test.

The same principles apply when the issue is raised in a direct procedure of the Commission against a member state. The latter will have to demonstrate that its laws, the restrictive effect of which has been demonstrated by the Commission, can be maintained on grounds of general good.

C. The general good exception in the field of financial services

As mentioned above, the 'general good' by its very essence is an open-ended concept, which implies that over time new legitimate motives might emerge in the case law of the Court of Justice. With the relative growth of cases in the field of free movement of services in recent years, the potential for further refinements and innovations in the general good doctrine has increased. This is also illustrated in the case law on financial services, which, though still limited, enables to give some useful guidance on the importance of the general good clause. These cases bear specific importance in further clarifying the general good clauses contained in the internal market directives on financial services.

Within the inventory of general good motives currently accepted by the Court of Justice[68], mainly five motives should deserve specific attention for the area of financial services:

- Consumer protection
- The fairness of commercial transactions
- The integrity of the financial system
- The coherence of the fiscal system
- The effectiveness of fiscal supervision

1. Consumer protection

The protection of the consumer of financial services has received special attention in the

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65 Cass. fr., 20 October 1998, *Euredia*, 1999/1, p. 65, note B. SOUSI-ROUBI, *Recueil Dalloz*, 1999, jurispr., p. 10, note B. SOUSI-ROUBI, *Dalloz Affaires*, 1999, p. 69, note X.D, *RTDCom.*, 1999, p. 166.

66 For a comment on these cases, see TISON, M., "Les rebondissements de l'affaire *Parodi* en France: entre nationalisme juridique et liberté communautaire", *Euredia*, 1999/4, cited *supra*, note 33.

67 Compare with respect to the banking directives: TISON, M., "Europese bankintegratie en het algemeen belang", *Revue de la Banque*, 1993, (211), at p. 227-228, no. 51; BERNITZ, U., MOHAMED, S., "National Prudential Rules Override Capital Freedom", *JIBL*, 1996, (235), at p. 236. This seemed not always to have been the leading opinion: see conclusions of advocate-general SLYNN in case 279/80 *(Webb)*, E.C.R., 1981, (3305), p. 3335, putting the burden of proof on the service provider; see also BFH 19 July 1994 , *RIW*, 1994/11, (984), p. 986 sub ee).

68 See for an overview of the current situation the Interpretative Communication, p. 17.

Court's jurisprudence since the *German insurance case.*[69] The case showed the Court's consideration for the protection of the weak party in complex financial services, such as insurance products, as a justification for the submission of foreign insurers to a licensing requirement under German law.

In the view of the Court, the necessity and extent of consumer protection is not a monolithic concept in the context of financial services, but will vary according to the type, risk-level and complexity of the financial service on the one hand, and of the degree of sophistication of the recipient of the service on the other. With respect to insurance products, these criteria led to a further distinction between large and other risks, where only the latter could reasonably justify specific protective measures in the absence of sufficient community harmonisation.

In *Parodi*, the Court confirmed this approach with respect to banking services.[70] In considering the necessity of the host state's law imposing an additional banking license for a credit institution duly licensed in its home state and providing banking services in the host state, the Court indicated to the national judge that a further refinement should be made according to the type of banking activity and the type of customer. The Court further suggested that the requirement of a banking license apparently was more inspired by the protection of the depositors with banks, who should be confident in dealing with a solvent and reliable institution, than with the protection of borrowers.

In its Interpretative Communication, the Commission also relies on the degree of vulnerability of the recipients of banking services in deciding whether the host state acts in the interest of the general good when applying its own rules to foreign financial institutions on grounds of consumer protection. In general, the Commission finds in the Deposit Guarantee Directive[71] an appropriate criterion to assess whether a recipient is to be regarded as circumspect: financial institutions, institutional investors and larger enterprises which can be excluded form coverage by a deposit protection scheme, should in general be expected not to need any protection with respect to banking services, as they are in a position to properly assess the risks they are running when acquiring banking and investment products. It might be doubted whether this proposition holds true for all banking services: several recent examples illustrate that even larger enterprises are often unaware of the risks inherent to sophisticated (derivative) financial products. This could lead to the conclusion that the financial intermediary might have limited professional duties towards 'professional clients' for highly sophisticated products.[72] Moreover, the rationale for prudential supervision is partly to be found in the prevention of systemic risk, i.e. maintaining the overall confidence in the banking system (cf. *infra*), and cannot therefore be reduced to the sole protection of the 'weak' consumer.

2. Fairness of the commercial transactions

The need to ensure the fairness in commercial transactions as general good motive will to a large extent be related to the protection of the financial consumer: the risks involved with and complexity of many financial products may justify restrictive rules on advertising, selling methods, transparency of the prices etc. for the financial services. As for consumer protection in the narrow sense, the extent to which such protective measures may result in restrictions on cross-border free movement will primarily depend of the nature of the financial product and the type of customer.

3. Financial market integrity

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69 ECJ, 4 December 1986, case 205/84 *(Commission v Germany)*, E.C.R., 1586, 3755.

70 ECJ, 9 July 1997, case C-222/95 *(Parodi)*, E.C.R., 1997, I-3899.

71 Directive 94/19/EC of 30 May 1994, OJ L 135/5 of 31 May 1994.

72 Compare the duty for the Member States to elaborate conduct of business rules for investment firms, which should take account of the professional nature of the person for whom the service is provided: Art. 11 Investment Services Directive.

Although the need to ensure financial market integrity only recently received explicit backing as general good motive by the Court, it goes without saying that this motive underpins much of the legislative efforts at Community level in the fields of banking and investment services.

The relevant case-law shows that the integrity motive in reality has a double dimension. At the micro-level, it refers to the vulnerability of financial markets for the confidence of the consumers in the quality of the products offered on the market and of the intermediaries active in it. This will usually call for rules with respect to specific market practices by financial intermediaries towards financial consumers, such as a prohibition on «cold calling» for highly speculative products. In this sense, financial market integrity is closely related to consumer protection as general good motive. This was clearly illustrated in *Alpine Investments*, where the Court in part justified the ban on «cold calling» with reference to the complexity and high risk level of the financial products involved. The scope of the protective measures allowed under the integrity motive nevertheless seems broader than under the classical consumer protection motive: first, as the protected interest is related to the market itself, the member state of the market may also assume the protection of the financial consumer in other member states, although this protection would normally be best ensured by their countries of residence. Furthermore, it is not excluded that market participants other than 'consumers' in its traditional understanding[73] could enjoy protection under the banner of financial market integrity.

At macro-level, the integrity of the financial markets refers to the particular functions of financial intermediaries in the economic process. Excessive risk-taking by credit institutions may provoke a confidence crisis from the part of depositors resulting in a run on deposits, and a contagion effect on the financial soundness of other banks. Equally, the capital markets may suffer high damage from investment firm failures, due to the loss of client money and the loss of open positions on the failed firm by other investment firms. The confidence risks involved at the macro-level therefore mainly call for prudential rules preventing excessive risk-taking by the financial intermediaries and guaranteeing their financial strength.

The macro-dimension of financial market integrity, referring to the overall financial stability, in part underpinned the decision in *Alpine Investments*, where the Court referred to the importance of financial markets in the financing of economic subjects. Equally important in this respect is the view of the Court in *Panagis Pafitis*.[74] Although unrelated with the freedom to provide services as such — the questions raised before the Court concerned the Greek law which had allowed to raise capital in ailing banks without intervention of the general meeting of shareholders — the Court in general held that prudential requirements could constitute a valid general good motive. It is surprising that the Court did not seize the opportunity to confirm the prudential dimension of financial regulation as autonomous general good motive in subsequent cases: neither in the *SIM*-case[75], involving the requirement under Italian law for foreign securities brokers to have an establishment in Italy, nor in *Parodi* did the Court at any time refer to the systemic dimension of prudential regulation. Reducing the rationale of banking regulation to a matter of consumer protection, as the Court did in *Parodi*, might however impair on the outcome of such cases: it could be difficult to demonstrate the objective necessity of prudential regulations to the extent that the *individual* banking customer, as recipient of services, is protected through the application of its domestic consumer laws.

In conclusion, some of the Court's recent case law demonstrates that the integrity and stability of the financial system constitute autonomous justification grounds for measures restricting the free movement. Given the present state of Community harmonisation with respect

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73 See ECJ, 3 July 1997, case C-269/95, (*Benincasa)*, E.C.R., I-3767, where the Court adopted a fairly restrictive approach on the notion of 'consumer' for the application of the 1968 Brussels Convention.

74 ECJ, 12 March 1996, case C-441/93 *(Panagis Pafitis)*, E.C.R., 1996, I-1347.

75 ECJ, 6 June 1996, Case C-101/94 *(Commission v. Italy)*, E.C.R., I-2691.

to prudential standards for financial institutions, the practical importance of this general good motive will however be limited to those financial institutions not covered by the internal market directives (e.g. financial institutions attracting deposits from the public without granting credit[76] or *vice versa*).

4. Coherence of the fiscal system

The Court's case-law accepting the coherence of the fiscal system as a general good motive to justify trade-restrictive measures is to be regarded in the perspective of the difficult relationship between the member states' regulatory powers in the field of direct taxation on the one hand, and the overall scope of the free movement principles on the other.[77] The only case in which the Court accepted the tax coherence motive, is precisely to be found in the area of financial services: in *Bachmann* and *Commission v. Belgium*[78] the Court upheld the Belgian tax regime for deduction of life insurance premiums, which was granted only for contracts offered by insurers established in Belgium: the deductibility of the premiums paid by the insured being closely linked with the taxation as income of the capital paid at the end of the contract, the tax deduction could logically be refused in cases where no taxes could be levied on the capital, *in casu* when the insurer has no fiscal establishment in Belgium.

The Court's positive attitude towards the possibility of maintaining discriminatory tax provisions has been highly criticised by many authors, as it had potentially far-reaching effects for the liberalisation of cross-border financial services in a non-unified tax environment: member states could, by maintaining fiscal provisions of the kind, raise barriers to the free provision of services which the internal market directives precisely intended to eliminate.[79] However, in subsequent cases the Court seems to have significantly narrowed the concept of fiscal coherence: in *Wielockx*[80], the Court clarified that the coherence between direct benefits and future costs should exist with respect to the situation of one and the same person. Furthermore, the coherence should, when applied in an international tax context, take account of its potential neutralisation by double taxation treaties[81], an aspect of the problem apparently left open by the Court in *Bachmann*.[82]

The Court's judgment in *Svensson*[83] further narrows the fiscal coherence movement: the case concerned interest rate subsidies granted under Luxembourg law for the financing of the acquisition of housing by Luxembourg residents. For this regime to apply, the mortgage loan had to be concluded with a credit institution licensed in Luxembourg. The applicants claimed the

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76 See in this respect Art. 3 Second Banking Directive: in the cases expressly covered by national legislation the deposit-taking business by non-banks is still permitted, provided that these activities are subject to regulation and controls intended to protect depositors and investors.

77 The Court's practice over the last few years amply demonstrates this difficult symbiosis, and the Court's determination, in particular in the area of establishment, to reject all discriminatory regimes in direct taxation. See for an overview of the issues: WOUTERS, J., "Fiscal Barriers to Companies' Cross-Border Establishment in the Case-Law of the EC Court of Justice", *YEL*, vol. 14, 1994, 73-109.

78 Both cited *supra* note 59.

79 See, *inter alia*, DASSESSE, M., "Tax Obstacles to the free Provision of Financial services: The New Frontier?", *JIBFL*, 1993, 12-16.

80 ECJ, 11 August 1995, Case C-80/94, E.C.R., I-2493.

81 Compare DE WEERDT, J., "EG-Recht und Direkte Steuern", *RIW*, 1995, (928), at 930.

82 See also DASSESSE, M., "Examen de jurisprudence. Les services financiers: banques et assurances", *Journal des Tribunaux Droit européen*, 1996, (15), at p. 19. Others have indicated that the double taxation treaty between Belgium and Germany did not apply to insurance premiums, so that the Court in *Bachmann* did not have to rule on the impact of double taxation treaties on assessing the fiscal coherence as general good motive: DEVROE, W., "Samenhang van nationale fiscale stelsels en algemeen belang: de rechtspraak na Bachmann", *Tijdschrift voor Rechtspersoon en Vennootschappen* 1996, (310), at p. 316, no. 15.

83 ECJ, 14 November 1995, case C-484/93 *(Svensson and Gustavsson)*, E.C.R., 1995, I-3955.

benefit of the subsidy for a loan obtained with a Belgian credit institution, and invoked the incompatibility of the Luxembourg regime with the free movement of capital and services. The Court rejected the argument based on the coherence of the fiscal system for the justification of the restriction put forward by the Luxembourg government, as there was no direct relationship between the cost of the subsidy regime for the public authorities and the expected benefits stemming from the general income taxes raised solely on the income of Luxembourg credit institutions. The need to demonstrate a direct and necessary interrelationship between fiscal costs and benefits for the same person was further more recently stressed in *Asscher*.[84]

In view of the recent developments in the Court's case law, one may therefore conclude that the Court reduced the coherence motive to more or less reasonable proportions. Even if it can be deplored that the Court ever walked that road in *Bachmann*, there seems at present to remain little scope for a multitude of applications of the *Bachmann* jurisprudence with respect to taxation of financial products by the member states.

5. The effectiveness of fiscal supervision

Already in *Cassis de Dijon* did the Court include among the non-exhaustive set of general good motives the 'effectiveness of fiscal supervision'. Even if this motive has not given rise to extensive case-law from the Court of Justice[85], one might wonder whether it could be used in the area of (direct) taxation of financial services. The combination of capital movement liberalisation and the absence of common European rules with respect to direct taxation of income on financial products (withdrawal tax) indeed creates a large potential of fiscal evasion through the use for the Treaty freedoms.

As a rule, Member states should, in the exercise of their fiscal competencies, comply with the fundamental freedoms of the EC Treaty[86], which implies the obligation to maintain only these fiscal supervision measures which, if they produce restrictive effects on free movement, are objectively necessary to ensure the effectiveness of fiscal supervision.[87] However, the Court's attitude in *Bachmann* apparently does not seem to leave ample room for the member states in restricting the free movement of financial services for the sake of effective fiscal supervision: in the Court's view, Directive 77/799/EEC on the mutual assistance between member states in the field of direct taxation[88] provides an adequate framework for co-operation between member states. Moreover, member states are not automatically entitled to impose restrictions on free movement for tax supervisory reasons outside the (limited) scope of the mutual assistance imposed by the directive when other alternatives are available which do not restrict free movement to the same extent: in *Bachmann* it was held that the tax authorities had a valuable alternative for the restriction by asking the insured person to give proof of the payment of insurance premiums to the foreign insurance company as a condition for obtaining the tax benefit, without having to take recourse to measures restricting the free provision of services by foreign insurance companies.

However, it may be doubted whether this line of reasoning may be extrapolated to the taxation of financial services in general. It should be borne in mind that in *Bachmann* the information provided by the individual could be considered as a satisfactory alternative for the co-operation between tax authorities: the insured had a proper interest in providing the

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84 ECJ, 27 June 1996, case C-107/94 *(Asscher)*, E.C.R., I-3089; see on this case also BINON, J.-M., "Avantages fiscaux en assurance de personnes et droit européen", *Revue du Marché Unique européen*, 1996/2, (129), at p. 138, no. 14.

85 See for an overview OLIVER, P., *Free Movement of Goods in the E.E.C.*, London, European Law Centre, 1988, at p. 205-208.

86 ECJ, 6 July 1988, *Ledoux*, case C-127/86, E.C.R., p. 3741.

87 ECJ, 15 May 1997, *Futura Participations and Singer*, case C-250/95, E.C.R., p. I-2471, para 31.

88 *OJ*, L 336, 27 December 1977, p. 15.

information, as it led to a tax benefit (deductibility of premium payments). The same motives underpinned the judgment in *Futura Participations*[89], where the Court held that the requirement for a EU based undertaking to hold separate accounts for its Luxembourg branch in compliance with the Luxembourg accounting rules in order to be allowed tax deduction of losses incurred by the branch under the Luxembourg corporate tax law, was not necessary to ensure the effectiveness of fiscal supervision. As the undertaking had a specific interest in proving the losses for obtaining the tax benefit, a valuable alternative could consist of allowing the undertaking to use other reliable means.

On the contrary, a voluntarist alternative allowing the tax payer to prove his fiscal situation may not be sufficient when it comes to raising taxes on the income of a resident with respect to financial services obtained with a bank licensed in another member state, and active under the regime of free movement of services. The customer will have no interest at all in declaring his income in his state of (fiscal) residence, especially when the income is not taxed abroad, while on the other hand, the collection of information in the home state of the credit institution via the mutual assistance procedure may be obstructed by banking secrecy laws.

It appears therefore that the need to ensure the effectiveness of fiscal supervision might lead to specific measures by a member state towards foreign credit institutions, with a view to properly supervising the tax obligations of resident bank customers. The proportionality requirement will however act as an important filter on the member states' discretion. This would in first instance rule out measures which generally impede the free provision of services through measures barring the access to the domestic market. For instance, it seems excluded for the host member state to subject the right to provide services by foreign credit institutions in general to the obligation for the latter to provide the tax authorities with all data on the income perceived by all its customers resident in the host member state. Moreover, the tax authorities should in any case have regard to the right to passive freedom of services: a member state may not unduly restrict the right for its residents to have services provided on their own initiative by financial institutions in other member states. Therefore, imposing tax supervisory obligations on these credit institutions by the residents' member state could easily constitute a disproportionate restriction on the free flow of services.[90]

6. Conclusions on the general good motives in the context of financial services

The analysis of the Court's case law on the general good as applied in the area of financial services, shows that the concept intrinsically is surrounded by uncertainties: first, the general good in its very essence is an evolutionary concept, and hence new motives might in the future be validated by the Court of Justice as legitimate restrictions to free movement. Furthermore, although the conditions attached to the general good-exception might at present be firmly established in the Court's case law, they nevertheless are often difficult to apply in specific situations. It goes without saying that the legal uncertainty thus created imposes important impediments on the financial institutions which want to enjoy the benefit of the freedoms of movement. It is therefore essential to find effective means to reduce the cost of this legal uncertainty. An important step in this direction appeared to be made in the context of the financial market directives, by requiring the member states to notify to foreign financial institutions wishing to enter the market, which rules apply in the general good. However, member states have managed to largely reduce the practical importance of the relevant provisions in the financial services directives to the extent that they do not impose any obligation upon the member

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89 ECJ, 15 May 1997, *Futura Participations and Singer*, cited *supra* note 87, para 38-40.

90 In this respect, it should be noted that in Belgium a draft bill was submitted a few years ago for advice to the *Conseil d'Etat*, which would impose specific tax obligations on foreign financial institutions as regards their Belgian resident customers, *inter alia* the obligation to block all accounts upon decease of the client until the Belgian tax administration has been informed on the existence and the state of the account. The bill was however never introduced in Parliament.

states (cf. *infra*).

Part III — The general good in the directives on banking and investment services

A. The function of the general good in the 'new approach' to harmonisation

It cannot be denied that the 'new approach' to harmonisation which the Commission proposed in its 1985 White Book on the Completion of the Internal Market gave a significant boost to the market unification efforts, at least as concerns its legal framework: harmonisation was to be limited to those elements which were necessary but sufficient to ensure member states' mutual confidence in each other's regulatory and supervisory standards, and hence to come to a mandatory application of the mutual recognition principle. In effect, this approach could be considered as an application of the subsidiarity principle *avant la lettre*: Community legislation is only required to the strict extent necessary for enabling the unification of the national markets in a single market.[91]

A comparison between the mutual recognition as deriving from primary EC law, *i.e.* the Treaty freedoms, and the same principle in the internal market directives, reveals the complementary nature of the latter to the former. Under the Treaty freedoms, the mutual recognition could be qualified as 'imperfect': the host member state is entitled to put aside the mutual recognition principle when the application of its own laws to the cross-border situation, which by assumption produces a restrictive effect on free movement, is justified by the general good. By contrast, the mutual recognition principle as formulated by the internal market directives is absolute or 'perfect': the minimum harmonisation directives having introduced equivalent regulatory standards in all member states, the host member state is no longer entitled to invoke the general good to justify the application of its own laws to the foreign service provider. In other words, the minimum harmonisation constitutes, in the view of the Community legislator, the codification of what in the absence of harmonisation would fall under the general good exception.

However, the 'new approach' based on minimum harmonisation does not entirely paralyse the member states' regulatory powers. In the field covered by the 'minimum' harmonisation, member states are enabled to maintain or introduce stricter standards than the minimum level imposed by Community law, provided the stricter standards apply solely to the domestic enterprises.[92] The risk of reverse discriminations and competitive disadvantages for the domestic industry are likely to highly reduce the use of these powers. In effect, one can observe a *de facto* convergence of prudential standards to the 'minimum' imposed by the directives.[93]

Outside the fields covered by the minimum harmonisation and 'perfect' mutual recognition, member states also retain full regulatory powers. The use of these powers will,

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91 Compare PADOA-SCHIOPPA a.o., *Efficacité, stabilité, equité*, Paris, Economica, 1987, p. 14; BOYE JACOBSON, C., "Rapport communautaire", in *Rapports au XV° congrès de la FIDE*, Vol. I: *Les prestations de services au sein de la CEE et avec les pays tiers*, Lisbonn, 1992, at p. 30-31.

92 To the extent that the use by a member state of these powers restricts the 'outward' free provision of services by a credit institution, the restriction should also satisfy the general good-test: compare in the context of cross-border television broadcasting ECJ, 28 October 1999, *ARD and PRO Sieben*, case C-6/98, *not yet reported*, para 49-52.

93 It should be noted however that the banking and investment services directives in general led to higher prudential standards than those previously contained in the law of the member states. This conclusion should to a certain extent mitigate the classical argument against the 'new approach' as provoking excessive regulatory competition between member states to the detriment of sufficiently high regulatory standards.

however, in line with the case-law on the Treaty freedoms, have to conform to the general good exception when it leads to restrictions on free movement.

B. References to the general good in the banking and investment services directives

It is well known that several provisions in both the Second Banking Directive (SBD) and the Investment Services Directive (ISD) refer to the general good. These may be summarised as follows:

- In general, the preamble to both the SBD and the ISD impose upon the member states the duty to ensure that there are no obstacles to carrying on banking and investment activities receiving mutual recognition in the same manner as in the home member state, as long as the latter do not conflict with legal provisions protecting the general good in the host member state;[94]
- Host member states are entitled to take appropriate measures to prevent or to punish irregularities committed within their territories which are contrary to the legal rules they have adopted in the interest of the general good;[95]
- Credit institutions and investment firms can advertise their services in other member states through all available means of communication in the host member state, subject to any rules governing the form and the content of such advertising adopted in the interest of the general good;[96]
- At a procedural level, the host state's competent authority will 'if necessary' notify to the credit institution or investment firm wishing to open a branch in the host member state the conditions under which, in the interest of the general good, those activities must be carried on in the host member state;[97] for investment firms, the procedure also applies in the context of the first cross-border provision of services.[98]

The community legislator has deliberately refrained from giving a general definition of the 'general good' in the directives on banking and investment services. It is commonly accepted that the general good in these provisions has to be understood as referring to the same concept in the Court's case law on the justification of restrictions to free movement, and the conditions attached to the use of the general good exception.[99] However, it has been indicated above that the general good exception no longer applies in the fields where the directives consecrate the 'perfect' mutual recognition principle. In order to assess the practical meaning of the general good clauses in the banking and investment services directives, it is therefore important to carefully delimit the proper scope of the 'perfect' mutual recognition principle, in contrast to the situations in which the member states still are entitled to apply their laws which satisfy the general good test.

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94 16th recital of the preamble to the Second Banking Directive; 33th recital of the preamble to the ISD.

95 Art. 21(5) SBD; Art. 19(6) ISD

96 Art. 21(11) SBD; Art. 13 ISD.

97 Art. 18(4) SBD; Art. 17(4) ISD.

98 Art. 18(2) ISD.

99 See the answer by Sir Leon BRITTAN on behalf of the Commission to written question no. 916/89, *OJ*, C 139, 7 June 1990, p. 14; VAN GERVEN, W., "La deuxième directive bancaire et la jurisprudence de la Cour de Justice", *Revue de la Banque*, 1992, (39), at p. 43 (also published as "The Second Banking Directive and the Case-law of the Court of Justice", *YEL*, 1990, 57; KATZ, S., "The Second Banking Directive", *YEL*, 1993, (249), at p. 261; DASSESSE, M., ISAACS, S., PENN, G., *EC Banking Law*, 2nd ed., London, LLP, 1994, para 4.39, p. 43; ROTH, W.-H., "General Introduction to the Second Banking Directive and the Proposal for a Directive on Investment Services", in *Financial and Monetary Integration in the European Community*, J. STUYCK (ed.), Deventer, Kluwer, 1993, 77; SOUSI-ROUBI, B., *Droit bancaire européen*, Paris, Dalloz, 1995, no. 285, p. 145.

C. Material scope of the general good in the banking and investment services directives

In determining the material scope of the general good as exception to the mutual recognition in the context of the banking and investment services directives, a further distinction can be drawn between (1) rules on market access and prudential regulation; (2) rules on market behaviour, including advertising, and (3) private law regulation of financial products. In Part I, we demonstrated that the 'imperfect' mutual recognition as formulated by the Treaty freedoms is likely to apply, with varying intensity, in all of these areas.

1. Market access and prudential regulation

a. Overview of the directives

Both the Second Banking Directive and the Investment Services Directive introduce, as well known, a single European passport and the principle of home country prudential supervision for the financial institutions to which they apply. On basis of the minimum harmonisation of prudential standards, the directives thus attribute, unless otherwise provided, exclusive regulatory and supervisory competence in prudential matters to the home country of the banking and investment firms. The other member states in which these institutions wish to set up a branch or to be active under the free provision of services, can no longer exercise any competence in these fields: any recourse to the general good doctrine has been eliminated by the 'minimum' harmonisation at Community level, except where the directives allow for such exceptions.

The exceptions to the home state principle in the *prudential* area are limited. In the context of the Second Banking Directive, the residual powers of the host state prudential authorities are restricted to the liquidity supervision of branches.[100] This competence should moreover be exercised in co-operation with the home state authority, which is competent for the overall liquidity supervision of the credit institution as a whole (head offices and branches altogether). The Second Banking Directive also contains a particular division of supervisory competencies with respect to open market positions resulting from the credit institutions' transactions carried out on the financial markets of other member states.[101] In view of the harmonisation effected by the Capital Adequacy Directive[102], it may be submitted that at present the supervision of these risks falls under the exclusive competence of the home country supervisor.

Outside the area of prudential supervision, the Second Banking Directive, pending further Community initiatives, attributed to the host country full competence with respect to monetary supervision.[103] With the transfer of monetary supervision to the European System of Central Banks (ESCB) since January 1st, 1999 (Stage 3 of EMU), this provision may be considered to have become obsolete, at least for the member states of the eurozone. This implies that a member state of the eurosystem is no longer entitled to invoke monetary reasons to justify the application of a restriction on the free provision of services by a EU credit institution[104], unless the restriction

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100 Art. 14(2) SBD.

101 Art. 14(3) SBD.

102 Directive 93/6/EC of 15 March 1993, *OJ*, L 141/1 of 11 June 1993.

103 Art. 14(2) SBD.

104 In recent months, a peculiar problem has arisen with the so called 'ni-ni'-principle in French law, according to which it is prohibited to offer interest-bearing current accounts in France denominated in French francs. The prohibition, which used to be motivated on grounds of monetary policy, has since the introduction of the euro been extended to accounts denominated in euro and in all other currencies of the euro-zone. Surprisingly, the French authorities do no longer refer to monetary motives as a justification — which would be no longer valid in view of the transfer of monetary powers to the ESCB — but at present invoke the general good clause as a justification, and consumer protection in particular (see also FERRY, J., "Le «ni-ni» à l'épreuve de Maastricht", *Banque & Droit*, 1999, N° 65, p. 17-21.

would flow from a decision taken in accordance with the division of powers within the ESCB.[105]

In the context of the Investment Services Directive, the home country principle with respect to prudential supervision has an absolute character: no exception applies with respect to liquidity supervision of branches, nor does the ISD provide for any explicit host state residual power for monetary reasons. However, it may be submitted that the host state could exercise competencies in this field under the overall general good clause contained in Article 19(6), as far as compatible with the transfer of monetary powers to the ESCB.[106]

b. Implications of 'perfect' mutual recognition for the general good exception

The main implication of the 'perfect' mutual recognition principle with respect to market access and prudential supervision is the impossibility for the host state to interfere in any kind in the home state's exclusive competence, not even on basis of the residual general good clause of Article 21(5) SBD or 19(6) ISD. This principle does not only apply in the specific areas of prudential regulation which were the subject of minimum harmonisation, but extends to prudential regulation in general.[107] For instance, host states may not impose any additional prudential obligation upon the credit institution or investment firm duly authorised in another member state (e.g. own funds requirements of any kind[108], fit and proper-test for managers[109]). The Interpretative Communication on the contrary suggests that the elimination of host country competence would only apply to the fields of prudential regulation which were effectively harmonised.[110] Finally, as was made clear by the Court's decision in *Ambry*[111], the extent to which the host state is empowered to take measures which impair on the access to the market by a EU based credit institution, may still give rise to interpretation problems: does the access to the market solely relate to the possibility for a credit institution to take up a banking activity in the home member state without obtaining a new authorisation, or should it be considered to include all rules of the host member state which do impose additional requirements upon EU credit institutions in order to have their banking products recognised as fully equivalent to the products offered by a domestic credit institution ? In view of the objectives of the Second Banking Directive, it may be submitted that the latter broader interpretation should prevail.

More delicate is the question whether the host state may impose upon the foreign financial

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105 See in this respect the general overview by ZILIOLI, CH., SEMAYR, M., "The European Central Bank, its System and its Law", Euredia, 1999/2, pp. 187-230 and 1999/3, pp. 307-364.

106 Compare Art. 19(1) ISD, which empowers the host state, in the discharge of its responsibilities in the conduct of monetary policy, to require from branches of foreign investment firms the same information as from domestic firms. The provision, which implicitly confirmed a proper competence of the host state in the field of monetary policy, must at present be read in conjunction with the Treaty provisions on the powers of the ESCB.

107 Indeed, the attribution of general regulatory and supervisory compentence to the home state with respect to prudential supervision forms the corollary of 'minimum' but 'sufficient' harmonization of prudential standards: cf. 4th recital, preamble SBD; 3th recital, preamble ISD.

108 Article 15(2) ISD contains however a limited exception to this rule: a member state could formulate additional own funds requirements as a condition for obtaining access to the regulated markets by investment firms. These requirements may also be applied to investment firms authorized in another member state, provided they relate to risks not covered by ISD.

109 See for instance the point of view of the Belgian Banking and Finance Commission (BFC) with respect to the fit and proper test for managers of Belgian branches of foreign credit institutions: the BFC is of the opinion that it may, under the general good, revoke a manager who has previously been convicted for certain criminal offences, mainly in the financial area (see Annex to circular letter of 19 March 1993). In view of the home country principle however, only the home country supervisor will be competent for exercising this competence.

110 Interpretative communication, p. 19.

111 ECJ, 1 December 1998, *Ambry*, case C-410/96, cited *supra* note 57.

institution a prior control on the compatibility of financial products with its mandatory contract law before taking up a banking activity in the host state with use of the single banking license. This is for instance the case in Belgian law as concerns the granting of consumer or mortgage credit: the foreign financial institution wishing to offer such credits in Belgium under the single passport regime should first notify its model contracts to the competent supervisory authority. The latter may prohibit the financial institution from offering these contracts when they are contrary to the provisions of Belgian law justified by the general good.[112] It is true that this kind of — non-prudential — supervision may be related to the residual host state powers under the general good exception, which can also include powers to *prevent* irregularities on the host state's territory. However, it is doubtful whether the exercise of these competencies could interfere with the right to market access guaranteed by the directives: the host state's procedure may not result in a disguised authorisation procedure frustrating the *effet utile* of the single passport. Therefore, it may be submitted that the contract supervision should be effected on an *ex post* basis, and cannot be incorporated in the procedures for obtaining market access in the host state.[113] This is also the solution adopted within the context of the insurance directives.[114]

The elimination of general good competencies for the host member state in the area of market access and prudential supervision will of course only apply to those financial institutions to which the Second Banking Directive or the Investment Services Directive apply, and for the banking and investment services defined in the directives for which these institutions obtained an authorisation in their home state. For other services of other financial institutions, the general Treaty principles apply: the host state will be entitled to apply its domestic laws, which, if they amount to a restriction to cross-border free movement, must satisfy the conditions attached to the general good exception.[115] This will under certain circumstances require that the host member state duly takes account of guarantees to which the service provider already satisfies on basis of the rules applicable in its home state.

Two examples will illustrate the above principles. First, when a credit institution wishes to act as insurance intermediary in another member state — an activity which is not included in the list of banking activities enjoying mutual recognition — the host member state could impose its own requirements justified by the general good (e.g. rules on specific professional skills and experience with respect to insurance products). Host state rules could also include an authorisation procedure applying specifically to the activity as insurance intermediary. However, it will be up to the home state banking supervisory authority to decide whether the activity as insurance intermediary is compatible with the banking activity, and whether it does not imply prudential risks for the latter.

Second, the home country principle will generally[116] not apply to specialised financial institutions which do not qualify as 'credit institution' (e.g. enterprise for consumer or mortgage credit) or 'investment firm' (e.g. specialised investment adviser). Their cross-border activities will be subjected to the regulations protecting the general good in the host state, which may possibly include the submission to prudential regulations and a separate authorisation in the host state. The latter should however, in view of the Court's case law on the Treaty freedoms, take due

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112 See Art. 75bis Law 12 June 1991 on consumer credit and art. 43bis Law 4 August 1992 on mortgage credit (both introduced by Law of 11 February 1994, *Mon.*, 16 March 1994.

113 It should be noted that in the Netherlands, the implementation of the Second Banking Directive has led to a modification in this sense of the Law on Consumer Credit. The prior control on contracts has been substituted by an *ex post* control: immediately after having obtained market access, the foreign credit institution should notify its model contracts to the competent supervisor, which can prohibit the further use of these models when contrary to the general good.

114 See in particular 29 Third Non-Life Insurance Directive; Art. 29(1) Third Life Insurance Directive.

115 Compare 13th and 15th recital, preamble SBD; 28th recital, preamble ISD.

116 Except when they are 80% subsidiaries of a credit institution and satisfy specific requirements imposed by Art. 18.2 Second Banking Directive.

account of the guarantees which these financial institutions already offer by virtue of the supervision regime in their home state. If for instance the financial institution is submitted in its home state to similar prudential obligations as credit institutions which satisfy the Second Banking Directive[117], it is doubtful whether the host state still could apply its own prudential regulations, and impose a separate authorisation: the prudential standards contained in the Second Banking Directive are supposed to codify the general good, and will therefore also influence the application of the general good clause to financial institutions offering banking services without qualifying as credit institution.

2. Regulation of market behaviour

a. General principles

Contrary to the areas of market access and prudential regulation, the regulation of market practices to a large extent is left untouched by the Second Banking Directive and the Investment Services Directive: except with respect to conduct of business rules (cf. *infra*), substantial harmonisation in this field has not at present been realised.[118]

In this context, proper consideration should be given to the already cited recitals in the preamble to both directives, which formulate a principle of mutual recognition with respect to the way the banking and investment business is carried on in the host member states, without prejudice to the application of the host state's rules which are justified in the general good.[119] The reference to the way the business is carried on could be interpreted as including the rules on commercial practices and unfair competition, including the regulation of advertising. In the same line, both directives explicitly allow a financial institution to advertise its services in the host member state, without prejudice to the latter's right to impose its general good rules with regard to the form and content of the advertisement.

The practical significance of the cited recitals and provisions on advertising should not be overestimated. Both the wording of the recital and its evolution in the drafting process of the Second Banking Directive[120] suggest that the directive did not intend to formulate the mutual recognition in the same absolute sense as with respect to market access and prudential supervision. Merely should these recitals be regarded as mainly declaratory in comparison with the Court's case law on the free movement of services: this freedom entitles a credit institution to rely on the market behaviour rules of its home state as being equivalent to those in the host state with respect to the offer of its financial products; the host state may apply its rules which constitute a restriction to this freedom only in so far as justified by the general good. The mutual recognition of the home state rules, and the general good as correction to the rule, are therefore directly rooted in the EC Treaty, and cannot be restricted in any way by the internal market

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117 This will in particular be the case for financial institutions in Germany and France which qualify as credit institution under their home laws, but not under the Second Banking Directive, and therefore, do not enjoy the benefit of the single passport provided by the Second Banking Directive.

118 See however the amended draft directive on distance selling of financial services (COM(1999)385 def. of 23 July 1999), which, contrary to the initial Commission proposal, is not based on the paradigm of minimum harmonisation and mutual recognition, but instead would apply the principle of maximum harmonisation: the preamble considers that allowing Member states to enact or maintain divergent or stricter rules would produce adverse effects on the functioning of the internal market and on competition.

119 *Supra*, note 94.

120 It should be reminded that the initial draft of the Second Banking Directive laid down a principle of mutual recognition of 'financial techniques', a notion which subsequently disappeared, due to fierce criticism from the part of some member states. See for an overview of the drafting process in this respect DASSESSE, M., ISAACS, S., PENN, G., *EC Banking Law*, cited *supra* note 99, at p. 37-40.

directives. In this approach, the mutual recognition principle as enshrined in the recitals to the directive is to be considered 'imperfect', and merely refers to the present state of the Court's case law on the free provision of services (Article 49 EC).

b. Extension of the mutual recognition principle to branches ?

An additional difficulty in the interpretation of the mutual recognition principle for market behaviour rules, as written down in the preamble of both the SBD and the ISD, stems from its general wording, which operates no distinction between the activities undertaken through free provision of services or through a branch located in the host member state. This would imply that the out-of-state branch of a credit institution may invoke in the host state the mutual recognition of the home state rules on e.g. distance selling or tied product offers, against the application of the host state's rules, unless the latter satisfy the general good test. In this respect, the directive would in our view[121] effectively innovate compared to the current interpretation of the Treaty provisions on freedom of establishment: it has been advocated above that the general prohibition of non-discriminatory restrictions in the freedom of establishment did not apply to those rules in the host member state which are unrelated to the cross-border mobility of enterprises, in particular the product-related rules on market behaviour. Consequently, under Article 43 EC the host state could apply these rules to the branch on the sole condition of being non-discriminatory.

This point of view, previously expressed by former advocate-general VAN GERVEN[122], was initially backed by the Commission in its Draft Interpretative Communication.[123] Others have rejected this point of view, arguing that the — quite vaguely formulated — mutual recognition principle in the preamble to the directives could not express the intention to add new elements to the interpretation of the Treaty freedoms by the Court of Justice.[124] However, it should be noted that the extension of the mutual recognition principle to the activities of branches can not only be deducted from the preamble of the directive, which in any case may act as element in the interpretation of the provisions of a directive.[125] This interpretation is also corroborated by the substantive provisions of the directive: indeed, the principle of notification of general good provisions by the host state's authorities to the branch of a foreign credit institution or investment firms[126], cannot be given a reasonable significance, unless one accepts this extension of the mutual recognition principle to the activities of branches. If not, the application of host state's rules to branches outside the fields of market access and prudential regulation — which are covered by the 'perfect' mutual recognition — would be limited by the non-discrimination principle only, and there would be no reason for notifying any 'general good' provisions.

In its final Interpretative Communication, the European Commission defends a more advanced interpretation of the Treaty freedom of establishment: the mutual recognition of home state rules relating to the way banking and investment services are conducted in the host country through a branch, would now be directly rooted in Article 43 EC, as would appear from the Court's ruling in *Gebhard*.[127] Host states could consequently apply their own restrictive rules to a

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121 See *supra*, part I, B, 2 with respect to the material scope of the restriction based concept of the freedom of establishment and the distinction between 'enterprise related' and 'product related' rules.

122 See VAN GERVEN, W., "La deuxième directive bancaire…", cited *supra* note 99, at p. 42 ; ROTH, W.-H., "General Introduction…", cited *supra* note 99, p. 78; TISON, M., "Europese bankintegratie…", *supra* note 67, p. 219, no. 24.

123 Draft communication, *OJ*, C 291 of 4 November 1995, at p. 17.

124 In this sense ROEGES, L., "L'exercice de l'activité bancaire par la voie d'une succursale après la deuxième directive bancaire", *Revue de Droit bancaire et de la Bourse*, 1994, at p. 115.

125 See for a recent example in which the Court extensively relied on the preamble of a Directive in interpreting its substantive provisions: Decision of 10 september 1996, case C-222/94 *(Commission and France vs. United Kingdom)*, E.C.R., I-4025.

126 See Art. 19(4) SBD; Art. 17(4) and 18(2) ISD.

127 Interpretative Communication, p. 16.

branch only when the general good test is satisfied. Hence, the preamble of the SBD and ISD would even in the context of establishment be merely declaratory compared to the interpretation of the EC Treaty.

We may conclude from above that the preambles to ISD and SBD, in conjunction with specific provisions of the directives, effectively have a significance compared to the situation under primary EC law, by extending the paradigm of mutual recognition-general good to 'product-related' rules in the context of cross-border branching by credit institutions and investment firms.

Although clear in principle, the practical implementation of this extension raises new questions as how to apply the general good test. In the Commission's view, the assessment of the proportionality requirement might give different results depending on the mode of operation — free provision of services or branch — of the foreign financial institution: a restriction in the host state's law could more easily be regarded as proportionate towards a branch, which is permanently integrated within the economy of the host member state, than towards a non-established service provider. Consequently, a single host state measure could constitute a restriction on the free provision of services, but at the same time be justified towards the branch.[128]

The Commission's point of view cannot be shared. It is true that the Court's case law in the past often stressed the objective difference between services and establishment, in order to demonstrate that a service provider should not be submitted to the same rules as the person established in the host country and integrated in its social order. However, this case-law precisely developed in the context of the evolution of the freedom to provide services from a discrimination to a restriction based freedom, at a time when the freedom of establishment still was interpreted as prohibiting only discriminatory measures. Since the beginning of the '90s, the dichotomy services-establishment, at least with respect to enterprise-related rules, has been largely abolished in the Court's case law. Furthermore, it should be stressed that the SBD and the ISD precisely aim at placing the activity through direct provision of services and establishment of a branch on an equal footing. It might therefore be doubted whether reintroducing a distinction between services and branch activities *via* the proportionality requirement does not counter the objective of both directives. Finally, it is totally unclear along which criteria a distinction should be drawn between the provision of services and the establishment of a branch when addressing the proportionality of a restriction to free movement. It is difficult to understand the relevance of the more or less permanent integration in the host state's economy as a valid distinctive criterion in the context of market behaviour rules.

In its final Interpretative Communication, the Commission partially reviewed its position: in the field of consumer protection rules, the proportionality test should now give identical results independently from the mode of operation of the foreign financial institution: it would indeed be unacceptable for a consumer to be less protected when receiving the service from a non established undertaking, than from a branch in the host country.[129]

We can conclude that, by extending the mutual recognition principle applicable within the area of services to the activities of branches, the Community legislator aimed at extending the general good test to branches in an identical way as it applies to the provision of services. Consequently, there is no reason to further differentiate in the assessment of the proportionality requirement when doing the general good test. It is nevertheless debatable whether this extension should be welcomed. On the one hand, this would substantially enhance the intensity of regulatory competition between member states: the risk of reverse discrimination not only exists

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128 Interpretative Communication, p. 22-23; see also Draft Interpretative Communication, p. 22-23.

129 Interpretative Communication, p. 23.

in the field of prudential standards, but also in the areas of market behaviour and private law rules, where the branch could evade the application of restrictive rules in the host member state. It is also true that the risk of excessive regulatory competition to the detriment of consumer protection would be limited by the continuing validity of the general good clause as an exception to the mutual recognition in the fields of market behaviour and financial contract regulation. On the other hand, the above analysis has shown that the concept of general good itself is surrounded by many uncertainties. Extending the mutual recognition-general good paradigm to the activities of branches, which are fully integrated in the economy of the host member state, would only enhance this uncertainty, as consumers generally will not make the distinction between domestic institutions and branches of foreign institutions. In the absence of minimum harmonisation of market behaviour and product related rules at Community level, as is the case with prudential rules, it may be feared that the cost of legal uncertainty for all market participants — both financial institutions and consumers — will outweigh the potential benefits stemming from the extended mutual recognition. The extension of the mutual recognition-general good paradigm to the activities undertaken through a branch in another member state therefore only seems feasible when two additional conditions are met: (a) a sufficient flow of information between member states and the market participants on the actual use and implementation of the general good clause in each member state; and (b) a strict monitoring by the Commission of the use by the member states of the general good clause.

c. Conduct of business rules

Within the context of the Investment Services Directive, the interaction between the conduct of business rules and the general good exception raises specific difficulties. It is well known that Article 11(1) of the ISD lays down a number of general principles with which the member states should at least comply in the elaboration of conduct of business rules to be satisfied by investment firms and credit institutions in the exercise of their activities. The main problem stems from the fact that Article 11(2) ISD attributes the competence to lay down and supervise the conduct of business rules to the member state in which the service is provided, without further specifying how to determine the competent member state. In reality, several member states could simultaneously claim competence as member state in which the service is provided. For instance, when an investment firm, authorised in member state A, receives an order from a customer resident in member state B, and executes it on a regulated market in member state C, it is unclear which member state should apply its conduct of business rules: member state A could claim application as state of reception of the order; member state B could invoke that the service has been provided in the member state of the customer; member state C could apply its conduct rules as law of execution of the service. Consequently, the attribution of powers in Article 11(2) ISD may be considered non-exclusive, which could lead to burdensome, and sometimes conflicting obligations to be met by the investment firm in conducting his cross-border business.

The general obligation to interpret national and Community law in conformity with the Treaty, *viz.* the free movement principle, leads to the introduction of the general good test in the application of the conduct of business rules: an investment firm which in one member state is subjected to conduct of business rules, will have to comply with the conduct rules of other member states in which he offers investment products only as far as the application of these rules, assuming that they lead to a restriction to free movement, satisfies the general good test.[130]

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130 In the same sense CRUICKSHANK, CH., "The Investment Services Directive", in *Further Perspectives in Financial Integration in Europe*, E. WYMEERSCH (ed.), Berlin, De Gruyter, 1994, p. 73; WOUTERS, J., "Rules of conduct, foreign investment firms and the ECJ's case-law on services", *Comp. Lawy.*, vol. 14, 1993, (194), 195; LASTENOUSE, P., "Les règles de conduite et la reconnaissance mutuelle dans la directive sur les services d'investissement", *Revue du Marché Unique européen*, 1995/4, (79), 101-102; THEIL, L.R., "The EC Investment services Directive: A Critical Time for Investment Firms", *JIBFL*,

How should the general good test in practice be applied within the context of the conduct of business rules ?

First, it goes without saying that the conduct of business rules may be related to a general good motive, either the protection of financial market integrity, or more generally consumer protection.

The requirement of non-harmonisation could be more problematic, as Article 11(1) already contains a harmonised catalogue of conduct of business rules, although limited to the formulation of general principles. It could be argued that the member states' conduct of business rules which aim at achieving the objectives of Article 11(1) are to be considered as equivalent. Consequently, the host state's conduct of business rules could never satisfy the general good test as these have made the object of harmonisation. In reality, this would come down to considering that the catalogue of conduct of business rules in Article 11(1) ISD constitutes a 'minimum' but sufficient harmonisation excluding the application of host state rules.[131] However, neither the legislative history of the ISD nor its provisions can support this conclusion. In reality, Article 11(1) intended to give member states actual autonomy in elaborating their conduct of business rules, taking account of the proper characteristics of their markets and the policy choices in the protection of the consumers of investment services. Henceforth, the catalogue of objectives in Article 11(1) ISD cannot be considered to constitute a 'sufficient' harmonisation of conduct of business rules excluding all recourse to the general good. The only useful function of Article 11(1) in the general good test may be to create a refutable presumption of equivalence between the member states' conduct of business rules worked out within these objectives.[132] This equivalence will mainly appear in the context of the conduct rules relating to market integrity, while member states usually will enjoy greater discretion in the elaboration of the conduct of business rules related to the protection of the consumer.[133]

Finally, as the catalogue of objectives in article 11(1) only constitutes a minimum, member states are free to set other general principles with corresponding conduct of business rules. When theses rules are to be regarded as restricting cross-border investment business, they should also satisfy the general good test.

The European Commission's Interpretative Communication on the Second Banking Directive does not give any guidance on the relationship between the conduct of business rules and the general good. Although credit institutions should also observe these rules when supplying investment services, the Commission formally restricted the scope of its interpretation to the SBD.[134]

3. Private law regulation of financial products

As for the rules on market behaviour, the private law regulation with respect to the

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1994, (61), at p. 64; ALCOCK, A., "UK implementation of European Investment Services Directives", *Comp. Lawy.*, vol. 15, 1994, (291), at p. 299; WYMEERSCH, E., "Les règles de conduite relatives aux opérations sur instruments financiers", *Revue de la Banque*, 1995/10, (574), at p. 591; O'NEILL, N., "The Investment Services Directive", in *The Single Market and the Law of Banking*, 2nd ed., London, LLP, 1995, (189), at p. 201-202; DAX, D., "L'impact de la communication interprétative pour le secteur des services d'investissement", *Bulletin Droit & Banque*, 1999, No 28, p. 11, para 36.

131 See CARBONE, S.M., MUNARI, F., "The Enforcement of the European Regime for Investment Services in the Member States and Its Impact on National Conflict of Laws", in *European Securities Markets. The Investment Services Directive and beyond*, G. FERRARINI (ed.), London, Kluwer, 1998, p. 342-343

132 Compare WYMEERSCH, E., "Les règles de conduite…", *supra* note 130, p. 592, no. 45.

133 See HERTIG, G., "Imperfect Mutual Recognition for EU Financial Services", in *European Economic and Business Law*, R.M. BUXBAUM, G. HERTIG, A. HIRSCH, K.J. HOPT (eds.), Berlin, Walter de Gruyter, 1996, (218), 225.

134 Interpretative Communication, p. 3.

financial products offered by credit institutions and investment firms is not covered by the 'absolute' mutual recognition applicable to market access and prudential rules. However, the preamble to the SBD and the ISD may also be regarded as laying down a principle of mutual recognition in the area of private law regulation, and thus mainly confirming the current state of the Court's case-law with respect to the free provision of services: a financial institution may offer its financial products in the host member state under the same conditions as in its home member state. The financial institution will have to satisfy the mandatory contract rules of the host member state which constitute a restriction to free movement only as far as these rules also satisfy the general good test.

Equally, the 16th recital of the preamble of the SBD and the corresponding 33rd recital to the ISD may be interpreted as extending the mutual recognition-general good paradigm to the financial products offered through a branch in the host member state. The principles developed with respect to market behaviour regulation will apply by analogy.

D. Elaboration of host state powers in the interest of the general good

The powers of the host states to impose their general good rules within the general good exception are further, and in identical terms, clarified in the SBD and the ISD: the directives enable the host member state to take appropriate measures to prevent or to punish irregularities which are contrary to the general good rules. This competence shall include the possibility of preventing institutions from initiating any further transaction within their territories.[135]

The aformentioned provision calls for several remarks. First, it is clear that the general good clause of Art. 21.5 SBD and Art. 19.6 ISD should take account of the material scope of 'perfect' mutual recognition under both directives, as analysed above. This means that the clause cannot possibly be invoked in the fields of market access and prudential supervision by a EU financial institution, which have made the object of sufficient harmonisation.[136]

Second, the host state general good competence is not attributed specifically to the prudential authority, but to the member state in general. It is up to the member state to decide which authorities are competent to control or enforce the general good rules. This might be an administrative body (e.g. the authority competent for supervision of mortgage contracts) or a judicial entity (e.g. an injunction imposed by a court in a matter of unfair competition). On the contrary, host member states may not use this provision to declare the host state prudential authority competent for supervising compliance by a EU financial institution with the — non-prudential — general good rules.[137] Such attribution could only be valid under condition of non-

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135 Art. 21(5) Second Banking Directive; Art. 19(6) Investment Services Directive.

136 The exercise by the host state prudential authority of its residual powers with respect to liquidity supervision of foreign credit institutions is covered by the procedure of Art. 21(2) to (4) and (7) Second Banking Directive. In summary, the host state must first ask for intervention by the home state; only when this leads to insatisfactory results will the host state have authority to intervene istself; however, in case of emergency, the host state authority is entitled to take the necessary precautionary measures without prior consultation of the home state authority. It should be stressed that the latter host state powers apply exclusively within the scope of the competencies attributed to it by the directive, *i.e.*, essentially the liquidity supervision over branches. It may not be used to intervene in matters which fall under the exclusive prudential competence of the home state supervisor, for instance in roder to remedy to alleged deficient prudential supervision by the home state authorities.

137 See however BALATE, E., "L'intérêt général en droit communautaire: observations critiques au regard de la loi du 22 mars 1993 relative au statut et au contrôle des établissements de crédit", in *Liber amicorum Paul De Vroede*, Antwerp; Kluwer, 1994, (41), p. 56 and 62-63; DASSESSE, M., ISAACS, S., PENN, G., *EC Banking Law*, cited *supra* note 99, § 13.11, p. 124-125. See also in Belgian law Article 11

discrimination, the domestic financial institutions in the host state being subjected to the same kind of supervision.

Finally, the host state intervention for reasons of general good may be both repressive and preventive, although in the latter case the intervention may not interfere with the very principle of the single passport and restrict the right to market access for financial institutions in general. The host state power should furthermore be limited to taking 'appropriate' action, *i.e.* the nature and gravity of the sanction should be proportionate to the gravity of the violation of the general good rules.[138] The general non-discrimination principle finally will fully apply to the nature of sanctions to be applied in case of non-compliance with host state general good rules: foreign credit institutions may not suffer more severe sanctions than domestic institutions.

By way of conclusion, it can be stated that the provisions in the SBD and the ISD on host state's powers under the general good are mainly of declaratory nature: the provisions should be read as a mere confirmation of normal host state powers under the EC Treaty. The nature of the intervention by the host member state should however be in accordance with the proportionality requirement, and may in no case frustrate the *effet utile* of the single passport.

E. Procedural aspects of the general good powers — notification of general good rules by the host state authorities

With a view to facilitating the use of the single passport by financial institutions and reducing information costs related with the identification of the rules in the host state which the financial institution should comply with, the SBD and the ISD both introduced a notification procedure with respect to general good rules: prior to the granting of the single passport to a foreign financial institution, the host state authority should notify 'if necessary' the rules under which, in the interest of the general good, the activities enjoying mutual recognition must be exercised in the host state. Both directives apply the notification procedure for the setting up of a branch in the host member state; the ISD also extends the notification to the first cross-border provision of services.

The legal significance of the notification of general good rules is controversial with respect to both its nature (mandatory or optional) and the legal consequences of non-notification. The Commission seems to have been sensitive to the arguments advanced by several Member States, as the Interpretative Communication favours the approach of a non-mandatory notification.

1. Mandatory or optional notification ?

At the time of adoption of the Second Banking Directive, there seemed to be no controversy as to the nature of the notification: most authors, including Commission officials, and several member states considered the general good notification by host state authorities as mandatory[139], and some member states indeed prescribed the notification of general good as an

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of the Royal decree of 20 December 1995 on foreign investment firms, which initially attributed competence to the Belgian Banking and Finance Commission (B.F.C.) for the supervision of compliance by the foreign investment firms with the (non-prudential) general good rules which apply to them. The provision was subsequently redrafted in order to limit its scope to the power for the B.F.C. to take appropriate sanctions at the request of other authorities in charge of the supervision of general good provisions in the host state (Art. 1, R.D. of 27 January 1997, *Mon.*, 15 February 1997).

138 Compare the Court's judgment in *Skanavi*, applying the proportionality criterion to the sanctions imposed under German law for the failure by an non-national to exchange a driving permit obtained abroad: ECJ, 29 February 1996, case C-193/94 (*Skanavi*), E.C.R., 1996, I-1307.

139 VAN GERVEN, W., "La deuxième directive bancaire…", cited *supra* note 99, at p. 46; BALATE, E.,

obligation into their national implementation laws.[140] However, only few member states went on in drafting lists of general good rules.[141] The existing lists moreover witness a very extensive view on the general good rules to be complied with by foreign financial institutions. Meanwhile, several member states lobbied in favour of interpreting the relevant provisions as constituting no obligation for the host state authorities. This viewpoint was recently supported by several authors[142] and, maybe surprisingly, by the European Commission.[143] The Commission nevertheless deplored the state of affairs and announced that it would 'make every attempt to remedy this situation', however without further specifying possible action.[144] More recently, the Commission even seems to favour the complete abolishment of the notification procedure prior to first cross-border provision of services — which would imply the abolishment of the notification of general good rules by the host state.[145]

The main interpretation issue concerned the words 'if necessary' in the relevant provisions on notification: those who support the optional nature of the notification consider that it is up to the member states to decide whether there is a need for notifying these general good rules; the proponents of a mandatory notification on the contrary consider that the necessity does not refer to an option for the member states, but to the very existence of general good rules: as soon as

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"L'intérêt général en droit communautaire…", cited *supra* note 137, p. 45; DASSESSE, M., "1992: An EEC Update", *JIBFL*, 1991, (384), at p. 385; SMITS, R., "Freedom of Establishment and Freedom to Provide Services under the Second Banking Directive", in *Banking And EC Law Commentary*, Amsterdam Financial Series, Kluwer, looseleaf (March 1992), p. 34; sub 6.3.4; TISON, M., "Europese bankintegratie…", cited *supra* note 67, p. 225, para 42; WILMS, W., *De Europese regelgeving inzake banktoezicht*, Ghent, Mys & Breesch, 1996, no. 194-195, p. 130-131; compare with respect to insurance: VAN SCHOUBROECK, C., "The Concept of the general Good", cited *supra* note 48, at p. 154.

140 The Belgian law considers the notification as mandatory, however without any liability for the Banking and Finance Commission with respect to the content of the notification: see Art. 70 Law of 22 March 1993 (credit institutions) and Art. 8 Royal Decree of 20 December 1995 (investment firms). Likewise, notification of the general good rules is mandatory for the French authorities in relation to incoming financial institutions: see *La libre prestation de services en matière de services d'investissement. Rapport au CECEI*, Paris, 1998, p. 33 (document available at URL: http://www.banque-france.fr/fr/telechar/lps2.pdf).

141 In Belgium, the Banking and Finance Commission issued a circular letter enumerating which provisions were to be considered, in its view, as falling under the general good; in France, a list of general good rules has been adopted by way of *règlement* issued by the *Comité de la Réglementation bancaire et financière*; In Germany, the banking law itself contains a limited catalogue of general good rules to be complied with by foreign credit institutions.

142 See SOUSI-ROUBI, B., *Droit bancaire européen*, Paris, Dalloz, 1994, no. 284, p. 145; STUYCK, J., STRAETMANS, G., *Financiële diensten en de consument*, Antwerp, Kluwer, 1993, no. 673, p. 218. Implicitly: USHER, J.A., *The Law of Money…*, cited *supra* note 16, p. 78; EGAN, M., RUSHBROOKE, J., LOCKETT, N., *EC Financial Services Regulation*, London, Chancery Law, 1994, no. 3.20, p. 3-9; compare with respect to the insurance directives: DUBUISSON, B., "L'intérêt général en droit communautaire de l'assurance", *R.G.A.T.*, 1995/4, (809), 815, para 6. The same opinion is now of course defended by the Commission officials: CLAROTTI, P., "The Implementation of the Second Banking Directive and its Aftermath", in *Further Perspectives in Financial Integration in Europe*, E. WYMEERSCH (ed.), Berlin, De Gruyter, 1994, , p. 55.

143 Interpretative Communication, p. 15.

144 Interpretative Communication, p. 15. In an interim report drafted after consultations on the Draft Communication (document XV/1104/96 of 16 July 1996), the Commission considered to propose amendments to the Second Banking Directive, which would make the notification of general good rules mandatory towards credit institutions passporting in through either a branch or free provision of services. Moreover, all member states would be required to communicate these lists, and draft legislation purporting to the general good to the European Commission.

145 See the viewpoint of the European Commission in the context of the SLIM working party on the simplification of European banking legislation: see EUROPEAN COMMISSION (DG XV), *Single Market News*, No 10, December 1997, p. 4-5.

such rules exist will there be a necessity for member states to notify them to the incoming financial institution.[146]

Even if the wording of the relevant provisions cannot lead to a conclusive interpretation, it does nevertheless appear more in line with the proper aims of the directives to interpret them as imposing an obligation upon the host state authorities. It is true that, as the Commission states[147], the principle that anybody should know the law equally applies to financial institutions wishing to deploy activities in another member state. However, it should be borne in mind that the general good concept is uncertain by its very nature. Consequently, it seems inappropriate to shift the information costs with respect to the application of the general good test in the member states' laws from the host state to the financial institutions. It would be advisable to create a more balanced situation between the principle that the financial institution should know the law, and the information duty upon the host state with respect to the general good. Thus, without prejudice to the obligation for the financial institution to enquire about the application of the host state's laws, the primary task of informing the financial institution would rest on the host state. This is also more in line with the general obligation of member states to co-operate in order to achieve the *effet utile* of Community law (article 10 EC). Finally, it should be stressed that a mandatory notification of general good rules is likely to create a more dynamic application of the general good clause: the publication of a general good list could provoke discussions at Community level on the application of the general good test by the member states. The Commission could exercise its moral authority (and, possibly, the threat to bring cases before the Court), to discipline member states in the use of the general good clause. Bearing in mind the risk of a 'nationalistic' approach towards the own general good by member states, as was recently illustrated by the *Parodi* case and its aftermath in the French courts, it is imperative to strengthen the monitoring by the Community institutions on the use by the Member States of the general good clauses.

2. Consequences of deficient notification of general good rules by the host state

The interpretation of the notification of general good rules as optional or mandatory also bears consequences on the legal effects to be attached to deficient notification by the host member state, *i.e.* notification of a rule as falling under the general good while it does not, or *vice versa*, non-notification of a host state rule while it does qualify as falling under the general good.

It seems normal to accept that, if notification is optional, the host member state should not suffer any liability from errors in the notification. However, the Commission is of the opinion that, if the host state voluntarily accepts to notify the general good rules on a financial institution's request, it will be bound by an obligation as to means.[148] Implicitly, the Commission therefore does not totally exclude the possible liability of the host state authority under national law for shortcomings in the notification.

The issue becomes more delicate when the notification is to be regarded as mandatory. Should the negligence of the host member state in notifying a rule lead to non-applicability of this rule towards the foreign credit institution? In other words, would the applicability of a host state's rule in the interest of the general good depend upon its notification to the foreign financial institution ? This sanction would seriously disrupt the balance between the financial institution's obligation to enquire about the application of the host state law, and the duty of the host state authorities to properly inform the financial institution. The question as to the application of host state law in the interest of the general good should better primarily depend on a substantive

146 See also the opinion of the Economic and Social Committee on the Draft Commission Communication, *OJ*, C 204, 15 July 1996, p. 72.

147 Draft Interpretative Communication, p. 14.

148 Interpretative Communication, p. 15.

compatibility test, and not on a purely formalistic element.

Therefore, it may be submitted that the non-notification of a general good rule will usually not prevent the host state from effectively applying it to the foreign financial institution.[149] A more appropriate sanction probably is to be found in liability rules: the host state authority may be held liable for the damages suffered by the financial institution due to the latter's reasonable expectation that the non-notified rule would not apply. This liability could find a legal basis not only in national law, but possibly also directly in Community law, on basis of the *Francovich* jurisprudence: the notification being imposed by the internal market directives, the negligence of the host state authority in assessing which rules could fall under the general good, could constitute a breach of the obligations under the directives which engages the member state's liability.[150]

Part IV — The general good and conflict of laws in private law

A. Mutual recognition and conflict of laws

The ever widening scope of the principles of free movement in the Court's case law, in particular in the private law area, increasingly raises questions with respect to the relationship between the Treaty freedoms and the member states' conflict rules in private international law. More specifically, how do the principles of mutual recognition as resulting from the Treaty freedoms, and the general good as exception to the principle, affect or influence the traditional techniques for the solution of conflicts of law in the private law area ? This issue will be the more important in the area of cross-border services, the substance of which are determined mainly by contract law.

In general, one can consider that the free movement principle and the conflict of law rules are closely related to each other. Both the principle of free movement and the conflict of law rules apply in a legal situation with a transnational dimension. With respect to services, the cross-border element needed for the application of Article 49 EC will usually also contain an element of internationality involving a possible conflict of laws.[151] Moreover, both sets of rules proceed to a kind of arbitrage between several legal provisions which may come into play as applying to the cross-border situation. A traditional conflict of laws rule will indicate which law should govern the cross-border situation, on basis of objective connecting factors to the one or the other member state. On the other hand, the principle of free movement of services will result in the non-application of the rules of the home state — or, as the case may be, of the host state — which are regarded as unduly restricting cross-border trade. This example also points to a fundamental difference between both sets of rules: while the conflict of law rule will lead to indication of a law applicable to the transaction, the free movement principle merely produces a negative effect, by disapplying those rules which are considered restrictive to free movement.

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149 See in the same sense VAN GERVEN, W., "La deuxième directive…", cited *supra* note 99, at p. 46; BRUYNEEL, A., FYON, M., "La loi du 2 mars 1993 relative au statut et au contrôle des établissements de crédit", *Journal des Tribunaux*, 1993, (565), at p. 569, no. 22 and footnote 84; DASSESSE, M., "1992: An EEC Update", cited *supra* note 139, at p. 385; SMITS, R., "Freedom of establishment…", cited *supra* note 139, at p. 39, sub 6.3.4; WILMS, W., *De Europese regelgeving…*, cited *supra* note 139, no. 194, p. 131. Compare in the field of insurance: VAN SCHOUBROECK, C., "The Concept of the general Good", cited *supra* note 48, at p. 154.

150 See on the conditions of Member state's liability for breach of Community law: ECJ, 5 March 1996 (*Brasserie du Pêcheur/Factortame III)*, cases C-46 and 48/93, E.C.R., I-1023.

151 The most common example will be the cross-border service relationship, where provider and customer are established in different member states.

B. Does the free movement principle result in a conflict rule ?

In legal writing[152], several authors have echoed the point of view that the mutual recognition principle resulting from the free movement under primary EC law results in formulating a conflict of law rule: with respect to cross-border transactions in goods or services, this would usually result in the application of the home state law.[153] As an exception to this 'home state rule' *("Herkunftlandsprinzip")*, the application of host state rules could prevail on grounds of general good. In conflict of law terms, the general good exception would thus qualify as *ordre public* rules.[154] More recently, another author further refined this approach: the free movement principle would result in a conflict rule opting for the law which is most favourable for the service provider *(Gunstigkeitsprinzip)*: home state law when host state rules are more restrictive and *vice versa*.[155]

The conception of the free movement as formulating a conflict of law rule must be rejected, as it does not reflect the actual effects of the Treaty freedoms on national law. As already indicated, the Treaty freedoms have a purely negative impact on national law: when a measure in the law of a host member state is considered contrary to the free movement of services, it will be disapplied by virtue of the precedence of EC law. The measure thus ruled out is however not substituted by the law of the member state of origin of the service or the service provider. The host state measure continues to apply in internal situations, but is merely declared non-applicable in cross-border situations.

In reality, the free movement does not interfere in the process of *formulating* the conflict of law rules in trans-border transactions.[156] The free movement principle only intervenes at a later stage, namely in the *actual application* of the substantive law declared applicable by the conflict of law rules. This view is corroborated by the Court's case law: in all cases where it has to decide on the compatibility of national law with the free movement of goods or services, the Court assumes that the said rules apply to the cross-border transaction at stake by virtue of the normal conflict of law rules in national law.[157] The Court will then analyse whether the substantive law thus

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152 See for a general overview of the doctrinal debate in general and with respect to financial services: TISON, M., *De interne markt voor bank- en beleggingsdiensten*, cited *supra* note 31, paras 777-803; WOUTERS, J., "Europees en nationaal conflictenrecht en de interne markt voor financiële diensten", Metro Working Paper, Mastricht, 1996, p. 54-61

153 WOLF, M., "Privates Bankvertragsrecht im EG-Binnenmarkt", *Wertpapier-Mitteilungen*, 1990, 1945; JAYME, E., KOHLER, CH., "Das Internationale Privat- und Verfahrensrecht der EG 1991…", *IPRax*, 1991, p. 369; compare KREUZER, K.F., "Die Europäisierung des Internationalen Privatrechts — Vorgaben des Gemeinschaftsrechts", in *Gemeinsames Privatrecht in der Europäischen Gemeinschaft*, P.-CH. MÜLLER-GRAFF, Baden-Baden, Nomos, 1993, (373), p. 420-421.

154 This was also the position of the European Commission in its Draft Interpretative Communication: "the principle of mutual recognition (…) tends towards application of the substantive law of the service provider (…)"

155 See in particular BASEDOW, J., "Der Kollisionsrechtliche Gehalt der Produktfreiheiten im europäischen Binnenmarkt: favor offerentis", *RabelsZ*, 1995, (1), at p. 12 *et seq.*

156 In the same sense DUINTJER TEBBENS, H., "Les conflits de lois en matière de publicité déloyale à l'épreuve du droit communautaire", *R.C.D.I.P.*, 1994, (451), at p. 474-478; GEBAUER, M., "Internationales Privatrecht und Warenverkehrsfreiheit in Europa", *IPRax*, 1995, (152), at p. 154-155; KOHLER, CH., "La Cour de Justice des Communautés européennes et le droit international privé", *Trav. du Comité français de droit international privé*, 1993-94, (71), at p. 75-77; ROTH, W.-H., "Der Einfluß des Europäisches Gemeinschaftsrechts auf das Internationale Privatrecht", *RabelsZ*, 1991, (623), p. 668-669. The same point of view was already defended in the early '80s in reaction to the Court's decision in *Koestler*: SAMTLEBEN, J., "Das Internationale Privatrecht der Börsentermingeschäfte und der EWG-Vertrag", *RabelsZ*, 1981, (240), at p. 243.

157 The most illustrative example in this respect is the *GB-Inno-BM* case, which concerned the application of the Luxembourg law to publicity leaflets distributed in Luxembourg by a Belgian supermarket.

declared applicable constitutes a restriction, and, if so, preclude the member state from applying it in the cross-border situation.

This is not to say that the home state rules will be irrelevant in the context of the free movement principle. In particular, the circumstance that the service complies with the rules of its home member state will be important in assessing whether the host state rules constitute a restriction to free movement. This 'conformity' of the service with home state rules as precondition for the existence of a restriction to the free movement explains why the free movement principle may be translated into a principle of (imperfect) mutual recognition: a service which complies with the home state rules cannot be submitted to the host state rules (negative effect), as both laws are assumed to achieve the same interests. However, should the service not comply with its home state rules, then neither would the application of the host state rules be considered a restriction to the free movement of services: the service is not already subjected in its home state to rules which are deemed equivalent to those in the host state.

The above principles can be fully applied to the regulation of financial services: the Treaty freedoms and the mutual recognition principle resulting from it do not affect the normal conflict of law rules for cross-border financial services. In the field of contract law, the Rome Convention of 19 June 1980 constitutes the common framework for most member states with respect to conflict rules.[158] As a rule, parties to the financial service will enjoy freedom of choice as to the applicable law. The main exceptions to party autonomy in the Rome Convention with relevance for financial services concern contracts concluded with consumers (Article 5), or in general the application of mandatory rules *(lois de police)* of either the forum, or another state (Art. 7). With respect to rules of market behaviour (unfair competition, advertising etc.), the applicable law will usually be determined by a conflict rule referring to the 'market principle': the law of the market on which the behaviour produces significant effects, *i.e.* where the interests of competitors or consumers may be affected, will apply.[159] Only when the law thus declared applicable qualifies as a restriction to cross-border free movement — a question which should be considered having regard to the proper contents of the applicable substantive law — will the primacy of the free movement principle come into play.

C. Can conflict of law rules constitute a restriction to free movement ?

Once it is established that the free movement principle does not interfere with the technique of determining the applicable law by of a conflict rule, the next question arising is to what extent the conflict rule itself could be regarded as a restriction to free movement, and consequently would be subjected to the general good-test.

In this context, one should first have regard to the specificity of conflict rules in assessing whether a rule of substantive law should be regarded as constituting a restriction to free movement. In the field of contract law, it has been mentioned that the determination of the *lex contractus* in first instance is a matter of party autonomy. For the service provider, the free choice

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The Court was asked whether the provisions of Luxembourg substantive law, which were applicable by virtue of the Luxembourg conflict of law rules, did not constitute an unduly restriction to free movement of goods.

158 It should be noted that the Rome Convention does not *stricto sensu* make part of the Community legal order, as it is not based on Article 293 EC. However, the Convention is regarded as so closely related to the objectives of the Treaty that the accession treaties for new member states systematically prescribe the signature of the Rome convention as a condition for accession to the European Community. Moreover, in the post-Amsterdam era, the Rome Convention is considered to fall under Title IV (Article 65?) of the Treaty on co-operation in the field of Justice..

159 See for a comparative overview of the conflict rules in different European countries: DUINTJER TEBBENS, H., "Les conflits de lois en matière de publicité déloyale à l'épreuve du droit communautaire", *Rev. Crit. d.i.p.*, 1994, (451), p. 455 *et seq.*

of applicable law implies that he will be able to stipulate application of its home state law with respect to its community-wide provision of services, thus in effect realising the 'mutual recognition' which is also achieved by the free movement principle.[160] Consequently, it may be submitted that, as far as parties to the contract enjoy freedom of choice with respect to the applicable law, a substantive law provision cannot be regarded as constituting a restriction to free movement, as parties are able to rule out the possibly restrictive rules through the choice of another law for the service contract. This view seems also to be supported by the Court's jurisprudence.[161]

Not only when parties to the contract have made an express choice of applicable law, will the possible 'restrictive' effect of national law be neutralised. The same principles should reasonably prevail when, in absence of choice of law clause in the contract, the applicable law is determined by reference to the country with which the contract is most closely connected.[162] Indeed, in this case the applicable law may be presumed to result from an *implicit* choice of law: parties to the contract had the opportunity to disapply an alleged provision in national law through their choice of law clause, and cannot therefore invoke the 'restrictive' effect of this provision for their freedom to provide services.

It follows from the foregoing that, with respect to rules of contract law, a restriction to cross-border free movement can only be identified where the alleged provisions in national law are imposed through mandatory conflict rules which they cannot rule out. Within the context of the Rome Convention, these relate mainly to consumer contracts (Art. 5), mandatory provisions of the *lex fori* or of another law (Art. 7) and the public order of the competent judge (Art. 16).

The European Commission's position on these issues is far from clear: on the one hand the Interpretative Communication suggests, in line with the principles set out above, that provisions in national law could only qualify as a restriction when applied pursuant to mandatory conflict rules.[163] However, when the Commission comes to exemplifying this principle on banking contracts concluded by the branch of a foreign credit institution in the host state, the Commission adopts different standards: it seems to accept that, even in the absence of a mandatory conflict rule, the application of host state law when no express choice of law was made by the parties, could be overruled by the free movement principle, and consequently only be maintained under the general good exception.[164]

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160 Compare, *inter alia*, SCHNEIDER, U.H., "Europäische und internationale Harmonisierung des Bankvertragsrechts", *Neue Juristische Wochenschrift*, 1991, (1985), at p. 1992; SMULDERS, B., GLAZENER, P., "Harmonization in the field of insurance law through the introduction of community rules of conflict", *CMLR*, 1992, (775), at p. 777, footnote 4;

161 See in particular the Decision of 24 januari 1991 in case C-339/89 *(Alsthom Atlantique)*, E.C.R., 1991, I-107.

162 Art. 4 Rome-Convention contains a (refutable) presumption that a contract is most closely connected with the country where the party who is to effect the most characteristic performance of the contract has its habitual residence or central administration.

163 Interpretative Communication, p. 25: "Thus, (…) the provisions of substantive law applicable to a banking service pursuant to the choice-of-law rules laid down in the Rome Convention (*it being possible for freedom of choice to be overriden by mandatory rules, mandatory requirements and public policy*) may, if they constitute a restriction, be examined in the light of the general good." [emphasis added].

164 Interpretative Communication, p. 25: "The Convention (…) implies that, where a service is supplied by a bank branch, the law of the country where the branch is situated is presumed to prevail *in the absence of a choice by the parties concerned*. In accordance with the principle of the precedence of Community law, the Commission considers that, where the legal provisions of the country of the branch constitute a restriction, they may be put to the general good test and, if necessary, overruled". [emphasis added].
The Interpretative communication provides a second example with respect to banking contracts concluded with consumers, to which Article 5 of the Rome convention applies. Here, the Commission does only mention the possible restrictive character of the mandatory provisions of consumer protection in the country of residence of the consumer, which results from a mandatory conflict rule.

The next question is whether the conflict rule itself could be regarded as constituting a restriction to free movement. In this respect, one should have regard to the very nature of a conflict of law rule: in most cases, the sole function of the conflict rule is to determine, on basis of objective connecting factors, which law will be applicable to a transnational situation, without anticipating to the result of the application of the substantive rules thus designated. For instance, when the conflict rules of a member state indicate the market law as being applicable to trans-border advertising, they do not contain any indication as to the possible restrictive nature of the substantive law declared applicable. Consequently, these purely indicative conflict laws can not by their nature contain any restriction to the free movement of goods or services.

Some conflict rules might however contain elements which refer to the contents or the purpose of substantive law in order to determine which law should apply. A typical example in the context of the Rome-convention is to be found in Article 5 with respect to contracts concluded with consumers: the principle of party autonomy in the determination of the law applicable to the contract does not prejudice to the application of the law of the consumer's place of residence when it offers the consumer a more extensive protection than under the *lex contractus*: the possible application of provisions of the consumer's law thus depends on a comparison of its substantive provisions with the *lex causae*. In the same line, the possible mandatory application of *lois de police* to the contract will depend upon the purposes achieved by these provisions of substantive law, and which justify their unilateral application to the contract notwithstanding the *lex contractus*.

The circumstance that conflict rules take into account elements of substantive law in determining which law should apply, does not in our view modify the essentially indicative nature of the conflict rule: the restriction imposed by national law on freedom of movement is the sole consequence of the effect of the rules of substantive law applied pursuant to the conflict rule. Consequently, it may be submitted that even the conflict rules which cannot be considered as 'neutral' as to the substantive content of the conflicting laws cannot by themselves be considered contrary to EC law.

Nevertheless, it cannot be denied that some conflict rules will be 'suspect' in view of the free movement principle, and their application should therefore be watched with particular vigilance. In the field of financial services, this will in particular hold true for contracts with consumers: the prevalence of the more protective law of the consumer's residence, *i.e.* the host state law, over the law of the financial institution (the home state) pursuant to Article 5 Rome Convention, could for the latter constitute a restriction to free movement of services, as it impedes on the possibility for the financial institution to distribute a same service community-wide. However, the restrictive nature does not in itself invalidate the conflict rule as such, but only intervenes at the level of the application of the rule to the substantive law provisions. Moreover, it should be borne in mind that consumer protection is accepted as legitimate general good motive in the field of financial services.

D. Conflict of law rules and the general good

It follows from the above analysis that the principle of free movement basically does not interfere with the determination of the applicable law to cross-border services by virtue of the normal conflict of law rules. Their interference is to be situated at the level of the application of the substantive law provision applied pursuant to these conflict rules. If the substantive law provisions are considered a restriction to the free movement, the member state will be disallowed to apply them in the cross-border service relationship, unless they could be justified by the public order exception of Article 46 EC, or under the general good exception.

It has therefore been rightly pointed out that the relationship between free movement,

conflict of law rules and the general good could be regarded as a 'mariage à trois'[165]: the freedom of choice with regard to the determination of the *lex contractus* to a cross-border (financial) service may be ruled out in whole or in part by a mandatory conflict rule; the application of the substantive law provisions pursuant to this mandatory conflict rule should in its turn, when constituting a restriction to free movement, satisfy the general good test. If this test fails, the substantive provisions may not be applied to the cross-border service, which in practice comes down in the continuing application of the normal *lex contractus*. Thus, the general good test must be incorporated in the application of the conflict rules, in order for these conflict rules to produce their plain effects.

The former may be illustrated by an example: a French credit institution wishes to grant mortgage credit to Belgian residents under the regime of free provision of services. The contracts stipulate application of French law. However, by virtue of Article 5 Rome Convention[166], this choice may not prejudice to the application of the provisions of Belgian law which protect consumers more than the *lex contractus*. Therefore, the French credit institution will have to comply with the Belgian law concerning *inter alia* the variability of interest rates, which is more favourable for the consumer than French law. For the French credit institution, this obligation may be regarded as a restriction of his freedom to provide services: the credit institution has to tailor its product to the Belgian market, which implies additional costs and might possibly influence its financing techniques. Consequently, the rules of Belgian law can only be maintained under the general good exception, in particular the need to protect the consumer. It is in this respect not sufficient for the Belgian law to be justified by the need to protect the consumer. The restriction imposed by the Belgian law should under the general good-test also satisfy the proportionality requirement, which is absent in the context of Article 5 of the Rome Convention. If the general good test fails, the more protective provision of Belgian law will be inapplicable, and consequently the *lex contractus* will again produce its full effects.

A similar additional general good test should be applied when the application of restrictive substantive law results from other mandatory conflict rules. Thus, the *loi de police* applied to the contract must be disapplied when it does not satisfy the general good test. Equally, the judge of the forum must, in applying its *ordre public* to reject the result of the application of the *lex contractus* (Article 16 Rome Convention), check whether this intervention may be related to a justification in the general good or the community public order (Art. 46 EC). In the context of regulation of advertising, the mandatory application of the host state rules by virtue of the 'market' principle should also be submitted to the general good test when a restriction to free movement results from it.

Concluding remarks: monitoring mutual recognition and the use of the general good clause

The analysis of the general good in the Court's case law and in the directives on banking

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165 VAN GERVEN, W., "Convention de Rome, Traité de Rome et prestations de services dans le secteur financier", in *La Convention de Rome*, *Banque & Droit*, 1993, special issue, (23), at p. 30, no. 32; see also BIANCARELLI, J., "L'intérêt général et le droit applicable aux contrats financiers", *Banque*, 1992, (1090), at p. 1098; CARREAU, D., "Banques", in *Juris-Classeurs Traité de Droit européen.*, fasc. 1023 (9,1994), no. 79, at p. 16; SOUSI-ROUBI, B., "La Convention de Rome et la loi applicable aux contrats bancaires", *Recueil Dalloz*, 1993, Chron., (183), at p. 189.

166 It is assumed here that the specific conflict rule of Article 5 of the Rome-convention does apply to mortgage credits granted to consumers. The issue is, however, the subject of debate among scholars (see, for instance, DEVROE, W. and BODSON, E., "Tweespraak. Internationaal privaatrechtelijke aspecten van de nieuwe wet op het hypothecair krediet", *Tijdschrift voor rechtspersoon en vennootschap* 1993, p. 320-323), and for a general overview of the controversy: TISON, M., *De interne markt voor bank- en beleggingsdiensten*, cited *supra* note 31, para 707-711. In the hypothesis tha the law of the consumer's residence would not apply by virtue of Article 5 of the Convention, the protective rules of the *lex fori* could nevertheless come into play .

and investment services reveals that there is much scope for the application of the general good exception in the context of financial services. However, although the concept itself does not give rise to difficulties, many uncertainties surround the actual application of it to the member states' laws. The implementation of the banking and investment services directives in the member states also demonstrates the risks of abuse of the general good clause by the member states. Not only have different member states used the general good clause as alibi for attributing specific residual powers to their prudential authorities towards foreign financial institutions. The lists of general good rules established by some member states moreover are illustrative of the sometimes very extensive conception of the general good by the host countries

The initiative of the Commission to clarify the issue of the general good in the context of the Second Banking Directive — and in the future for the Investment Services Directive — should be welcomed. However, the Interpretative Communication does not always bring the clarification which market participants need: the Communication does not modify in any respect the fundamental problem underlying the general good-concept: in the absence of Community harmonisation of financial product regulation, financial institutions cannot be expected to rely on a vague and exclusively case law built construction. It goes without saying that the uncertainties surrounding the general good present a major impediment for financial institutions to effectively make use of the single passport. In practice, it would seem that the financial institutions do not take the risk of clashing with host state authorities, and simply obey to the rules of the host state. As a consequence, one can hardly speak of the existence of an actual 'internal' market without frontiers. More should one admit that, apart from supervisory aspects, the market remains largely fragmented along national borders. The competition between financial institutions does not take place at the product-level, but is mainly limited to price competition.

Which alternatives are available for improving the use of the single passport at the level of financial products ? A first step could be to improve the flow of information and discussion about the use by the member states of the general good clause. In this respect, it seems essential that the notification of the general good rules by host member states be made clearly mandatory, thus provoking a more dynamic interaction between the financial institutions and the host states even before the start of the activity in the host state. In this respect, it may be deplored that the final Interpretative Communication did not contain the suggestions made by the Commission during the consultation process on the draft Communication[167] to amend the Second Banking Directive in order to take away its current ambiguity and to consider the notification requirement as mandatory.

A further step could be to improve the communication between the European Commission and the member states on the general good issue, in order for the former to effectively exercise its monitoring function under Article 211 EC. A recent communication by the European Commission to the European Parliament and the Council on the problems surrounding the application of the mutual recognition principle in the internal market provides some interesting indications on the Commission's policy intentions with respect to the effective monitoring of the principle of mutual recognition in the area of both goods and (financial) services.[168] While stressing the landmark importance of the mutual recognition principle in the operation of the internal market, as it provides a pragmatic and powerful tool for economic integration, the Commission acknowledges the difficulties arising from the use by the Member states of the general good exception.[169] Specifically in the field of financial services, the Commission intends to improve transparency as to the legitimate motives of consumer protection which might justify an exception to (imperfect)

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167 Document XV/1104/96 of 16 July 1996.

168 EUROPEAN COMMISSION, *Mutual recognition in the context of the follow-up to the Action Plan for the Single Market.* s.l., s.d., 15 p. (URL: http://europa.eu.int/comm/dg15/en/update/general/mutualen.pdf).

169 EUROPEAN COMMISSION, *Mutual Recognition*, cited *supra* note 168, p. 4 and 6.

mutual recognition of home state rules in the cross-border provision of financial services. To this end, the Commission will draw up, in co-operation with the Member States, an inventory of obstacles to cross-border transactions, and analyse the conditions under which the host state rules should apply their rules of consumer protection in the interest of the general good.[170] It goes without saying that this exercise should not be limited to repeating the abstract criteria of the general good test, as was done in the Interpretative Communication, but should effectively apply the test to the concrete rules under scrutiny. Of course, the viewpoints thus expressed by the Commission and the member states will not prejudice the point of view of the Court of Justice, which might subsequently be asked to rule on a similar issue in a preliminary proceeding.

In addition, the Commission is considering the creation of a Community network for dealing with complaints by consumers in retail financial services, in order to promote co-operation between the national bodies (ombudsmen etc.) entrusted with the amicable settlement of disputes between consumers and financial institutions.[171] Such a network could also produce valuable information on the way the Member states apply and impose on financial institutions the general good clause. It could therefore constitute, together with the other information means described above, an additional tool to monitor the mutual recognition in cross-border financial services.

Another important recent evolution can be found in the judgment of the Court of Justice in the so-called *foie gras* case: the European Commission brought an action before the Court of Justice against the French Republic, which had adopted a decree which imposed minimum quality standards for foie gras products. The effect of the decree was to prohibit the distribution in France of foie gras products under certain denominations which did not satisfy the French product standards. Interestingly, the Court of Justice followed the argument of the European Commission, which considered the French decree to be contrary to Article 28 EC to the extent that it did not contain a mutual recognition clause which allowed the distribution in France of imported foie gras products, which were legally manufactured and distributed in their Member State of origin.[172] The Court's judgment could have farreaching implications, as their is no reason not to transpose it to the other Treaty freedoms, in particular the free provision of (financial) services. It would imply that a Member State, when enacting national rules on financial products (e.g. mandatory contract clauses) the effect of which is to prohibit the offering of financial services by EU based financial institutions which are legally offered in their home countries, should include in its legislation a mutual recognition clause. Such a clause would not eliminate the possibility that the host state rules prevail under the general good clause. It would nevertheless provide an important signal to foreign service providers that cross-border distribution of financial services is allowed under a mutual recognition regime.

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170 In its Financial Services Action Plan, the European Commission indicated that work could be undertaken to establish possible equivalence between clearly similar rules in different Member States, hence ruling out the possibility for the member states to invoke the general good clause (see EUROPEAN COMMISSION, *Financial Services: Implementing the framework for financial markets: Action Plan*, COM(1999) 232 of 11 May 1999, p. 11). It is however debatable whether such a 'negative' approach towards the general good-clause will produce significant results. Given the diversity of regulation in many member states in the area of retail financial services, it may be submitted that the cases where clearly equivalent rules of different member states can be identified, will be of marginal importance. Apparently, the European Commission is not considering any concrete initiative in this respect in the near future. As a matter of fact, the first Progress report on the Financial Services Action Plan does not mention this initiative as a possible policy priority (cf. EUROPEAN COMMISSION, *Financial Services Action Plan. Progress Report*, s.d., 16 p; see URL: http://europa.eu.int/comm/dg15/en/finances/actionplan/progress1en.pdf).

171 See EUROPEAN COMMISSION, *Mutual Recognition*, cited *supra* note 168, p. 10-11; see also EUROPEAN COMMISSION, *Financial Services Action Plan*, cited *supra* note 170, p. 10-11.

172 ECJ, 22 October 1998, case C-184/96 (*Commission v. France*), E.C.R., 1998, p. I-6197, para 28.

In connection with the former consideration, it should be examined whether inspiration for future action could for instance be found in Directive 98/34/EC of 22 June 1998[173] which, in the field of free movement of goods, imposes upon member states the obligation to notify its technical rules to the Commission as a precondition to their application. As was illustrated by the *foie gras* case, such a notification requirement could, even before adoption of new legislation in a member state, provoke an exchange of views with the European Commission, and possibly with other member states, on the international application of the draft rules and the possibility to invoke the general good in this context. Introducing a similar notificaton requirement for, for instance, all national regulation relating specifically to banking and financial services, would already constitute an important step in that direction. Not only could the dialogue provoked by the notification requirement in the end lead to more clarification for the participants in the markets. It could moreover constitute the point of departure for new harmonisation initiatives in the field of financial product regulation, which eventually would foster the cross-border mobility of financial products in a genuine internal market.

173 Directive 98/37/EC of the European Parliament and the Council of 22 June 1998, laying down a procedure for provision of information in the field of technical standards and regulations , OJ, L 204, 21 July 1998, p. 37, which repealed directive 83/189/EEC.