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DIRECTIVE ON SERVICES IN THE INTERNAL MARKET

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INTRODUCTION

Freedom to provide services (the freedom) is at this moment one of the most intensely discussed issues in the European Union. Especially the proposal of the EC Directive on the services in the Internal Market (the Directive) has been a 'hot topic' ever since it was first presented by the Commission in 2004.

Arguments of politicians and lobbying groups (especially labour unions), mostly opposing the project, are the loudest and most vehement. Consequently, it is not surprising that they get most publicity, while not many people are aware of the legal aspects of the proposal. Meanwhile, also within the circle of scholars and lawyers a lively discussion on the potential interrelations of the Directive with the national law and *acquis communaitre* takes place. Numerous symposiums are organised, articles and reports are written, in the effort to predict the legal and economic consequences it might produce. As usually, views differ significantly not only in relation to details such as the 'proper' wording of each article, but also in general attitude (in favour or against) towards the project.

At the same time, countless bureaucrats in every Member State and in the EU institutions examine and negotiate every single word of the project in a seemingly hopeless effort to satisfy everyone without actually giving up the idea of liberalisation.

In this paper, I undertake to analyse the legal side of the current discussion, giving special attention to the case law of the European Court of Justice (the ECJ or the Court), upon which the Commission construed the first draft. I will attempt to establish whether the Directive, as it stands now, has any liberalising capacity or whether it is in fact a step backward in relation to what has been already achieved by the Court.

Since only the freedom to provide services is of the interest to the author of this paper, the provisions of the Directive which regulate freedom of establishment are not discussed. Also the rules on administrative cooperation are mentioned only to the extent that they influence the scope of the freedom. Furthermore, the problems relating to the private international law and conflict of rules[1] also fall outside the scope of this paper. Although

[1] For the discussion of possible conflicts between the country of origin principle and the rules on law applicable to contractual and non-contractual obligations see the Opinion of the Committee on Civil Law Matters (General Questions) of 24 9 2004, 12655/04 together with annexed Technical analysis of the provisions of the Rome I Convention and the Rome II Draft Regulation in the light of the Draft Services Directive of 25 6 2004, 10542/04 See also the response to these papers prepared by the Legal Service of the Council, according to which there is no conflict and eventual adoption of the country of origin principle

the adoption of the country of origin principle (the COP) may influence the choice of law applicable to the contractual and non-contractual obligations of the provider, this matter is only indirectly related to the scope of the freedom.

The First Chapter of this paper contains general information on the freedom to provide services. The EC Treaty provisions and their development through jurisprudence and secondary law are described in order to show the background from which the idea of a horizontal directive originated.

In the Second Chapter steps leading to adoption of the first project of the Directive in 2004 are presented. Contents of the draft, reasons given by the Commission for particular solutions and the relevant case law are also discussed

In the Third Chapter the debate about the project and opinions of various bodies are analysed with particular attention given to the most problematic issues and reasons of the disagreements between the Member States and EC institutions. Changes recommended by the European Parliament in the first reading of the project are also described.

The Fourth Chapter presents a compromise version of the Directive prepared by the Commission in April 2006. On the basis of conclusions derived from preceding Chapters an attempt is made to answer the question whether this final draft offers any improvement of the situation of service providers and recipients as compared with the present state of affairs.

Finally, in the concluding Fifth Chapter it is discussed whether the Commission's initiative can be regarded as a failure. Also some ideas for the prospects of the future liberalisation of the freedom to provide services are offered.

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depends on the political choice, 13858/04, 22.10.2004.

CHAPTER ONE

FREEDOM TO PROVIDE SERVICES

1. Introduction

Freedom to provide services is one of the four fundamental freedoms on which the Internal Market is based.[2] Provisions on the liberalisation of services have been a part of Community's legal order since its very beginning in 1957 when the Rome Treaty has been adopted[3] and have not been changed much since then. Nevertheless, their importance grows together with the development of the Member State's economies, as services' share in the national GDP and creation of new jobs constantly increases.

Presently, the freedom is regulated in Title III, Chapter three of the EC Treaty,[4] but also some of the provisions (articles 45 to 48) of the preceding Chapter on the right of establishment apply to it. After the expiry of the transitional period, the Court declared article 49 EC, prohibiting restrictions of the freedom to provide services, to be sufficiently clear and precise for direct application, irrespective of lack of harmonisation or coordination between Member States.[5] Since then, individuals may rely directly on this Treaty provision before national courts which significantly increases its effectiveness.

2. Material scope

According to article 55 EC services *"are normally provided for remuneration, in so far as they are not governed by the provisions relating to freedom of movement for goods, capital and persons"*. This rather vague definition relying mainly on the default rule has been supplemented by an open list of economic activities which may constitute services: industrial, commercial, craft or professional. Because this catalogue provides only possible examples, an enormous variety of activities is in practice included in the

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[2] For the legal analysis of the creation and operation of the Internal Market see K. Mortelmans "The Common Market, the Internal Market and the Single Market, what is in a market?" C.M.L. Rev. 35(1998), p. 101-136.

[3] Treaty establishing the European Economic Community adopted in Rome on 25.3.1957. Freedom to provide services was regulated in articles 59 to 66.

[4] Articles 49 to 55 of the Treaty establishing the European Community (consolidated version), OJ C325 of 24.12.2002.

[5] See Case 33/74 *Van Binsbergen* [1974] ECR 1299, par. 24; Case C-279/80 *Webb* [1981] ECR 3305, par. 13; Case 205/84 *Commission v Germany* [1986] ECR 3755, par. 25. For an elaborate analysis of the functioning of direct effect see J.H. Jans and J.M. Prinssen "Direct Effect: Convergence or Divergence? A Comparative Perspective" in J.M. Prinssen and A. Schrauwen (eds) "Direct Effect; Rethinking a Classic of EC Legal Doctrine" Groningen: Europa Law Publishing 2002, p. 105-126.

definition of services.[6] Only transport, banking and insurance services have been expressly excluded and made subject to provisions regulating respectively transport and the free movement of capital.[7] At this point the problem with the distinction of the freedom arises because all of the abovementioned activities can be also exercised through the freedom of establishment.[8] In result, the distinction solely on the basis of the type of economic activity is not feasible. Many criteria of differentiation have been proposed[9] but only the one based on the temporary nature of services has been finally accepted and consequently applied by the Court:

"where the provider of services moves to another Member State (...) he is to pursue his activity there on a temporary basis

(...) the temporary nature of the activities in question has to be determined in the light, not only of the duration of the provision of the service, but also of its regularity, periodicity or continuity. The fact that the provision of services is temporary does not mean that the provider of services within the meaning of the Treaty may not equip himself with some form of infrastructure in the host Member State (including an office, chambers or consulting rooms) in so far as such infrastructure is necessary for the purposes of performing the services in question "[10]

In contrast, freedom of establishments presupposes stable and continuous participation in the economic life of the host Member State.[11]

The requirement of remuneration does not mean that every single service has to be paid for (that is why the word 'normally' has been used). It rather serves to exclude from the scope of the freedom activities which do not have economic character, for example when the service is financed by the State acting in fulfilment of its duties towards the citizens.[12] Similarly, a musician performing on a public highway does not receive remuneration within the meaning of article 50 EC, because the money donated to him by the passers-by

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[6] For a more detailed analysis of the concept of 'services' see L. Woods "Free movement of goods and services within the European Community" Ashgate 2004, p. 159-184.

[7] See article 51 EC.

[8] For the elaborate explanation of the scope of freedom of establishment, also with regard to distinguishing it from freedom to provide services, see D. Schnichels "Reichwete der Niederlassungsfreiheit" Nomos Verlagsgesellschaft, Baden Baden 1995. On the differences between both freedoms see also J.L. Hansen "Full circle: Is there a Difference Between the Freedom of Establishment and the Freedom to Provide Services?" European Business Law Rev. 11(2000), p. 83-90.

[9] For example, the one based on the establishment of an infrastructure at the place the service is provided.

[10] Case C-55/94 *Gebhard* [1995] ECR I-4165, par. 26 and 27.

[11] Ibid. par. 25.

[12] See Case C-109/92 *Wirth* [1993] ECR I-6447, par. 15.

are given voluntarily without earlier agreement or obligation on either side.[13] However, the situation would be different if the musician were hired by a third party. According to the ECJ the fact that the consideration for the service is paid by somebody else than the recipient, is of no relevance.[14]

Another obligatory element for the service to fall within the scope of the Treaty is its cross-border character. This requirement is a consequence of a general rule that Community law does not apply to purely internal situations.[15] Article 49 EC expressly requires that the service provider shall be established in a different Member State than the recipient. Accordingly, three forms of service provision seem to be covered:

- when the service itself moves (e.g. a legal advice is sent through internet);
- when the provider goes to the recipient in order to provide service there (e.g. to build a house);
- when the recipient travels to the provider (e.g. in order to receive medical treatment).[16]

However, in late eighties, the Court added a fourth possibility, declaring that the freedom applies to all situations when the provider provides service in a Member State different from that in which he is established, irrespective of the place of establishment of the recipient.[17] It follows that the provider and recipient may be established in the same Member State as long as the provision of services takes place in a different EU country.

3. Personal scope

Both natural and legal persons can benefit from the Treaty provisions on the freedom to provide services, the only requirement being the nationality of one of the Member States. In relation to individuals, the possession of EU citizenship is essential, while legal entities must be "*formed in accordance with the law of a Member State and having their*

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[13] See Case C-16/93 *Tolsma* [1994] ECR I-743, par. 15-20

[14] See Case 352/85 *Bond van Adverteerders* [1988] ECR 2085, par. 16.

[15] See Case 115/78 *Knoors* [1779] ECR 399, par. 24; Case C-52/79 *Debauve* [1980] ECR 833, par. 9; Case C-17/94 *Gervais* [1995] ECR I-4353, par. 24. For the opinion that this principle has been eroded by the ECJ, see C. Barnard "The Substantive Law of EU; The Four Freedoms" Oxford University Press 2004, First edition, p. 332. See also N.N. Shuibhne "Free Movement of Persons and the Wholly Internal Rule: Time to move on?" C.M.L. Rev. 39(2002), p. 731-771.

[16] For the opinion that the recipient can relay on the freedom only if he does not reside permanently in the place where service is provided, see T. Oppermann "Europarecht" CH Beck München 1991, p. 579.

[17] See so called tourist guides cases: C-145/89 *Commission v France* [1991] ECR I-659, par. 9-10; Case C-180/89 *Commission v Italy* [1991] ECR I-709, par. 8-9; Case C-198/89 *Commission v Greece* [1991] ECR I-727, par. 10-11.

registered office, central administration or principal place of business within the Community".[18] It should be noted that initially this condition bound only the provider, while the recipient could be a third country national. The situation changed after the personal scope of the freedom was extended to cover also the recipients. Even though rights of the recipients are not expressly mentioned in the Treaty, first the Council[19] and subsequently the Court decided that also they should also be able to rely on the freedom.[20] In order to do so, they must however fulfil the nationality condition. The personal scope of the freedom was further broadened in *Rush Portuguesa* where the ECJ ruled that a provider can move to the host country together with his own labour force, irrespective of its nationality.[21]

4. Rights granted

Although article 49 EC expressly prohibits restrictions on freedom to provide services within the Community, initially only the national treatment rule was applied. Basically, it meant that nationals from other Member States could not be discriminated as compared with own citizens.[22] Soon it turned out that the prohibition of discrimination on the grounds of nationality (so called direct discrimination) is not sufficient because also other criteria of differentiation are used. Such requirements as knowledge of local language or permanent residence allowed the Member States to favour their own citizens, without violating the prohibition of direct discrimination. The ECJ responded firmly by extending the prohibition also to indirect discrimination covering restrictions which, although not based on the nationality criterion, lead to the same result.[23] Despite this broad interpretation of the national treatment rule, many restrictions of the freedom still escaped the prohibition from article 49 EC and hindered the establishment of the Internal Market.

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[18] Article 48 EC, first sentence

[19] See article 1b of Council Directive 73/149 on the abolition of the restrictions on movement and residence within Community for nationals of Member States with regard to establishment and the provision of services, OJ L172, 28.6.1973, p. 0014-0016 (repealed by Directive 2004/38).

[20] See Case 286/82 *Luisi and Carbone* [1984] ECR 377, par. 16; Case 187/86 *Cowan* [1989] ECR 195, par. 15; Case C-348/96 *Calfa* [1999] ECR I-0011, par. 16; Case C-55/98 *Vestergraad* [1999] ECR I-7641, par. 20.

[21] Case C-113/89 *Rush Portuguesa* [1990] ECR I-1417, par. 19. See also Directive 96/71 concerning the posting of workers in the framework of the provision of services, OJ L18, 21.1 1997, p. 1-6

[22] However, Community law does not prohibit reverse discrimination privileging foreigners as compared with nationals. On the problem of national discrimination see G. Davies "Nationality discrimination in the European Internal Market" European Monographs, Kluwer Law International 2003.

[23] See Joined Cases 62 and 63/81 *Seco* [1982] ECR 223, par. 8; Joined Cases C-330 and 331/90 *López Brea and Hidalgo Palacios* [1992] ECR I-323, par. 13; Case C-484/93 *Svensson and Gustavsson* [1995] ECR I-3955, par. 12

Some measures, even though non-discriminatory in form and application, restricted the freedom through the creation of 'double burden' for the nationals of other Member States.[24] With a view to counteracting such barriers, the Court broadened even further the scope of article 49 EC claiming that it included a prohibition of all restrictions which hinder the exercise of the freedom or render it less attractive.[25] Other means of fighting the double burden were provided by the Community secondary legislation on the mutual recognition of qualifications and diplomas.[26]

The ECJ interpreted extensively not only the rights granted but also the activities to which they applied. As was mentioned before, even though article 49 EC mentions only the provision of services also their receipt was declared to be protected. Additionally, so called 'accessory rights', such as the right of entry and residence, that the Court deemed necessary for (or at least influencing) the exercise of the freedom were included in the 'package' as well.[27] Judgment in *Carpenter* where the Court declared that a deportation of Filipino wife of a service provider constituted a violation of article 49 EC, because it could hinder him in exercise of the freedom as it affected his family life,[28] can serve as an excellent example of the ECJ's creative interpretation.

5. Admissible restrictions

In the recognition of national interests, the EC Treaty contains also provisions expressly allowing Member States to discriminate against foreign service providers (recipients). Nevertheless, these derogations are interpreted restrictively by the Court.

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[24] For example, if every person who wants to practice the profession of an architect in a given Member State is obliged to pass an exam before a national body, architects who have already acquired qualifications and experience abroad are disadvantaged because they are forced to fulfil the same (or similar) conditions more than once. See also Case C-288/89 *Gouda* [1991] ECR I-4007, par. 12-13.

[25] So called market access approach. See Case C-76/90 *Säger* [1991] ECR I-4221, par. 12; Case C-424/97 *Haim* [2000] ECR I-5123, par. 57.

[26] See Directive 89/48 on general system for the recognition of higher education diplomas awarded on completion of professional education and training of at least three year's duration, OJ L19, 24.1.1989, p. 16-23; Directive 92/51 on a second general system for the recognition of professional education and training to supplement Directive 89/48, OJ L017, 25.1.1995, p. 0020. See also sectoral regulations such as Directive 77/249 to facilitate the effective exercise by lawyers of freedom to provide services, OJ L78, 26.3.1977, p. 17-18.

[27] Because matters relating to movement of persons are deemed especially sensitive, the accessory rights were soon and heavily regulated in secondary law. Presently, see especially: Directive 2004/38 on the right of citizens of the Union and their family members to move and reside freely within the territory of the Member States, OJ L158, 30.4.2004, p. 77-123.

[28] Case C-60/00 *Carpenter* [2002] ECR I-6279, par. 39.

Article 45 EC envisages derogation in relation to activities connected with the exercise of official authority. However, the Court requires this connection to be direct and specific.[29] Consequently, it is possible that the justification will be accepted only in relation to certain functions but the exclusion of whole profession will not be possible.[30]

Furthermore, article 46.1 EC allows special treatment of foreigners on grounds of public policy, public security or public health. Despite the lack of Community definitions of these notions, Member States can invoke this provision only in exceptional circumstances and their reasoning is thoroughly examined by the Court.[31] Discretion of national authorities is additionally limited by rules set in secondary law[32] building upon the jurisprudence of the ECJ.

In addition to express Treaty derogations the Court, initially in relation to the free movement of goods and subsequently also other freedoms, developed a rule of reason doctrine.[33] It was a necessary consequence of the introduction of market access approach. Were it to remain unlimited, practically every regulation of economic activity could be struck down as hindering one the freedoms. To prevent such situation, the ECJ accepted possible justification of non-discriminatory measures by overriding reasons relating to the public interest (imperative/mandatory requirements), such as protection of workers, environment, consumers or intellectual property.[34] However, the reasoning based solely on administrative or economic grounds is not admissible.[35] Measures taken by the Member States not only have to be properly justified but also proportional. The proportionality test has to establish that the interest which a Member State claims to protect is not sufficiently protected by the country of origin; the measure is suitable for securing attainment of the objective it pursues and it does not go beyond what is necessary

[29] See Case C-114/97 *Commission v Spain* [1998] ECR I-6717, par. 35; Case C-355/98 *Commission v Belgium* [2000] ECR I-1221, par. 25;
[30] See Case 2/74 *Reyners* [1974] ECR 631, par. 46-47.
[31] See for example Case C-158/96 *Kohll* [1998] ECR I-1931; Case C-348/96 *Calfa* [1999] ECR I-0011.
[32] See Chapter VI of Directive 2004/38 on the right of citizens of the Union and their family members to move and reside freely within the territory of the Member States, OJ L158, 30.4 2004, p. 77-123
[33] For an extensive analysis of the application of the rule of reason by the Court, especially to the sensitive issues of moral and ethical nature, see S. O'Leary and J.M. Fernández-Martín "Judicially-created Exceptions to the Free Provision of Services" European Business Law Rev. 11(2000), p. 347-362
[34] The catalogue is open and subject to continuous development by the Court
[35] See Case C-158/96 *Kohll* [1998] ECR I-1931, par. 41; Joined Cases C-369 and 376/96 *Arblade* [1999] ECR I-8453, par. 37.

to attain this objective.[36] The Court applied the rule of reasons also in relation to national measures which could be perceived as indirectly discriminatory, even though they may be in principle justified only by one of the express Treaty derogations.[37]

6. Conclusions

In this Chapter the evolution of the freedom to provide services has been described. It is apparent that even without substantial changes in the wording of the EC Treaty provisions, the European Court of Justice managed to extend the scope of the freedom through creative interpretation. Meanwhile, secondary law addressed particular problems, concentrating mainly on the regulation of access to and exercise of specific sectors (e.g. telecommunications).[38] However, these combined efforts of the Court and EC institutions proved to be insufficient to remove all barriers to the freedom. Up to now, no Member State has adopted a comprehensive act that would regulate cross-border provision of services, there are only sectoral regulations issued in order to implement directives. In result, providers are often treated on the same terms as entrepreneurs permanently established in a given country. Infringement procedures initiated by the Commission and preliminary rulings of the ECJ are not capable of solving that problem. They are too slow, costly and their results bind in principle only the parties to the proceedings. Additionally, the abolition of some barriers requires prior establishment of minimum standards, especially in relation to the protection of consumers' interests. Consequently, the Commission has come up with the project of horizontal harmonisation as a tool best suited for the achievement of true Internal Market in services.[39]

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[36] See Case C-272/94 *Guiot* [1996] ECR I-1905, par. 13; Case C-6/98 *ARD* [1999] ECR I-7599, par. 51. See also J. Snell "True proportionality and free movement of goods and services" European Business Law Rev. 11(2000), p. 50-57; where the application of proportionality test by the Court is analysed in relation to both: the Treaty derogations and the rule of reason.

[37] See Case C-288/89 *Gouda* [1991] ECR I-4007, par. 11; Case C-224/97 *Ciola* [1999] ECR I-2517, par. 17. For an opinion that the Court has eliminated discrimination from most used language, except in most obvious cases, see G. Davies "Nationality discrimination in the European Internal Market" European Monographs, Kluwer Law International 2003, p. 58

[38] See M. Brealey and C. Quingley "Completing the Internal Market of the European Community; 1992 Handbook" Graham and Trotman; London/Dordrecht/Boston 1991; second edition.

[39] For an elaborate opinion on the role of harmonisation in the process of liberalisation of service trade see P. Nicolaides "Liberalizing service trade; Strategies for services" Chatham House Papers, The Royal Institute for International Affairs, Routledge London 1989

CHAPTER TWO

THE FIRST DRAFT

1. Introduction

In order to counteract the slow removal of barriers to the free movement of services and to meet the goals set out by the Lisbon European Council,[40] in December 2000 the Commission presented the Internal Market Strategy for Services (the Strategy).[41] Stressing the role of services as drivers of the European economy, the Commission devised a two-stage plan aiming at the creation of efficient Internal Market for services. First of all, initiatives targeted at specific problem areas (such as commercial communications) and the analyses of remaining barriers were to be undertaken. The following step consisted of removal of the identified barriers through direct application of the Treaty, non-legislative measures and targeted harmonisation.

Less than two years later, under the first stage of the Strategy, the Commission produced a Report on the State of Internal Market for Services[42] specifying the barriers and their impact on the European market. The report concluded that a decade after the envisaged completion of the Internal Market, there are still huge disparities between planned results and the reality. In 2003 the Commission proceeded with the second stage of the Strategy launching initiatives to remedy the situation. Preparation of a Directive on services in the Internal Market was one of the priorities.[43] During the examination of remaining national barriers it turned out that many legal obstacles are common to different kinds of activities, therefore a horizontal act would be most efficient. As for the harmonisation itself, it is necessary to remove restrictions to freedom resulting from diverging national provisions or from unlawful measures introduced by the Member States (it would be impractical and ineffective to fight them with the infringement procedure). The First draft was presented

[40] The European Council (23 and 24.3.2000) launched the Lisbon strategy aiming at making the EU the most competitive and dynamic knowledge-based economy in the world by 2010. In point 17 of the Presidency Conclusions the Council asked the Commission to set out the strategy for removal, till the end of the year, of barriers to services.

[41] Commission Communication "The Internal Market Strategy for Services", COM(2000) 888 final, 29.12.2000.

[42] Report from the Commission to the Council and the European Parliament on the State of the Internal Market for Services, COM(2002) 441 final, Brussels 30.7.2002.

[43] See Commission Communication "Internal Market Strategy – Priorities 2003-2006", COM(2003) 238, 7.5.2003, p. 11.

to the Council and the European Parliament at the beginning of 2004.[44] As the legal basis, the Commission pointed to articles 47.2, 55, 71 and 80.2 EC. The proposal consists of seven chapters: 1) general provisions; 2) freedom of establishment for service providers; 3) free movement of services; 4) Quality of services; 5) Supervision; 6) Convergence programme and 7) Final provisions.

2. Scope and general provisions

The aim of the Directive is to create a general legal framework applicable to the cross-border provision of services (also through establishment), in compliance with Treaty provisions and without interfering with other Community instruments. Proposed definition of a 'service' refers to article 50 EC and encompasses every self-employed economic activity consisting of the provision of services for consideration.[45] Consequently, no new elements have been added to the definition already functioning and it will still be necessary to refer to the jurisprudence of the ECJ in order to categorize given activity as a service.[46] Areas, such as finances, transport, communication services and networks; which are already covered by comprehensive Community policies, have been excluded from the scope of the Directive.[47] Additionally, in the field of taxation, the country of origin principle shall apply only to the extent not covered by other Community instruments.[48] In this respect it should be noted that the Court has consistently held that national tax measures are capable of restricting the freedom, and can therefore be examined under article 49 EC.[49] Even in the area of direct taxation which belongs to the

[44] Proposal for a Directive of the European Parliament and of the Council on services in the internal market, COM (2004)0002 final, 13.1.2004. For a critical analysis of the First draft see W. Gekiere "The Proposal of the European Commission for a directive on services in the internal market: an overview of its main features and critical reflections" in R. Blanpein (ed.) "Freedom of services in the European Union; Labour and Social Security Law: the Bolkenstein Initiative" Bulletin of Comparative Labour Relations, Kluwer Law International 2006, p. 3-18. See also J.M. Schlichting and W. Spelten "Die Dienstleistungsrechtlinie" Europäische Zeitschrift für Wirtschaftsrecht 8/2005, p. 238-240 where the contents of the proposal are described.

[45] Article 4.1.

[46] For an opinion that reliance on the definition established on a case-by-case basis by the Court is questionable, and that the distribution of goods – mentioned by the Commission in an explanatory recital 14 - should not be included (as it has not been recognised by the ECJ) see the Research Report of W. Gekiere Institute for European Law "Towards a European Directive on services in the Internal Market: Analysing the Legal Repercussions of the Draft Services Directive and its Impact on National Services Regulations" Catholic University of Leuven, 24.9.2004, point II A.

[47] Article 2.2.

[48] Article 2.3.

[49] See Case C-204/90 *Bachmann* [1992] ECR I-249, par. 31-33; Case C-300/90 *Commission v Belgium* [1992] ECR I-305, par. 22-23; Case C-17/00 *De Coster* [2001] ECR I-9445, par. 26.

exclusive competences of Member States, the ECJ ruled that their authority has to be exercised consistently with the Community law.[50]

3. The country of origin principle

According to the COP expressed in article 16 of the First draft, the country where a service provider is established, is responsible for regulation and supervision of his (her) activities in relation to the access to and the exercise of service activity, the quality and contents of the service, advertising, contracts and liability. The host Member State cannot restrict the freedom by requirements applicable to access to or exercise of service activities. Paragraph four of article 16 contains an open list of prohibited requirements.

The COP as defined above has not been clearly established in the case law of the Court. Admittedly, the ECJ has repeatedly stated that all restrictions liable to prohibit or otherwise impede the exercise of freedom to provide services should be eliminated.[51] Also the catalogue of prohibited restrictions from article 16.4 of the First draft reflects the Court's jurisprudence.[52] However, it is not only the host state but also the home country that should refrain from obstructing the exercise of the freedom.[53] Moreover, even though the Court has often ruled that article 49 EC precludes the application of specific restrictions; these decisions were always preceded by the examination of possible justifications and proportionality of the measure at issue. In the absence of Community harmonization, the freedom can be limited by measures justified by Treaty derogations or overriding requirements relating to the public interest.[54] The host Member State can also take measures necessary to ensure that its rules on establishment are not circumvented

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[50] See Case C-331/97 *Gschwind* [1999] ECR I-05451, par. 20

[51] See Case C-76/90 *Säger* [1991] ECR I-4221, par. 12; Case C-58/98 *Corsten* [2000] ECR I-7919, par. 33.

[52] An obligation to have an establishment within the host state's territory: Case 205/84 *Commission v Germany* [1986] ECR 3755, par. 52. A prohibition of setting up an infrastructure in host state: Case C-55/94 *Gebhard* [1995] ECR I-4165, par. 27. A requirement to be entered into register: Case C-131/01 *Commission v Italy* [2003] ECR I-1659, par. 27. An obligation to possess an identity document issued by authorities: Case C-355/98 *Commission v Belgium* [2000] ECR I-1221, par. 39 and 40. Obligatory application of specific contractual arrangements: Case C-398/95 *SETTG* [1997] ECR I-3091, par. 19. Requirements affecting use of necessary equipment: Case C-17/00 *De Coster* [2001] ECR I-9445, par. 35. Application of host state's requirements relating to provision of services: Case C-288/89 *Gouda* [1991] ECR I-4007, par. 12.

[53] See Case C-18/93 *Corsica Ferries* [1994] ECR I-1783, par. 30; Case C-379/92 *Peralta* [1994] ECR I-3453, par. 40; Case C-381/93 *Commission v France* [1994] ECR I-5145, par. 14; Case C-70/95 *Sodemare* [1997] ECR I-3395, par. 37; and Case C-405/98 *Gourmet* [2001] ECR I-1795, par. 37. For an opinion that in relation to the country of origin, only the measures discriminating against the interstate transactions should be regarded as impinging on the freedom to provide services, see P. Oliver and W.H. Roth "The Internal Market and the Four Freedoms" C.M.L. Rev. 41(2004), p. 419.

[54] See Case C-262/02 *Commission v France* [2004] ECR I-6569, par. 23

through the abuse of EC law.[55] In no case did the Court establish a general rule that it is the law of the country of origin that should apply to the service provider, or that this country should be responsible for the supervision.[56] On the contrary, the ECJ has acknowledged that the home state control principle is not laid down in the Treaty;[57] consequently it cannot be relied upon unless it expressly follows from the secondary law.[58] Otherwise, it is established on the case-by-case basis which country is better equipped to supervise and regulate the situation of the provider.[59] In *Arblade* the Court stated that: "*overriding reasons relating to the public interest which justify the substantive provisions of a set of rules may also justify the control measures needed to ensure compliance with them*".[60] Consequently, supervision and power to regulate given situation are often linked.

On the other hand, according to the Court, Member States cannot apply to foreign service providers all the requirements that the national entrepreneurs have to fulfil,[61] especially if it would result in the imposition of a double burden. Additionally, freedom to provide services may be restricted only in so far as the interest protected is not equally safeguarded by the rules to which the provider of the service is subject in the Member State of establishment.[62] If the fact, that practically any national requirement may be

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[55] See Case C-148/91 *Veronica* [1993] ECR I-487, par. 12. However the case law in this respect is somehow confusing because, at the same time, Member States cannot subject service providers to all laws applicable to permanent establishments and even if the service provider offers no services in the country of establishment it does not automatically mean that the freedom is abused. See V.G. Hatzopoulos "Recent developments of the case law of the ECJ in the field of services" C.M.L.Rev. 37(2000), p. 62-64.

[56] For an opinion that Court's approach cannot be explained by the allocation of regulatory competences but is based on the concept of market access see J. Snell and M. Andenas "Explaining the outer limits: restrictions on the free movement of goods and services" in M. Andenas and W.H. Roth "Services and Free Movement in EU Law" The British Institute of International and Comparative Law, Oxford University Press 2002, p. 115. The authors also argue that production rules should be subject to home state control, while the host state would control the rules on market circumstances (p. 93). Similar view was expressed by H. Muir Watt in "Experiences from Europe: Legal Divrsity and the Internal Market" Texas International Law Journal 39(2004), p. 448 and 452-454.

[57] See Case C-233/94 *Germany v Parliament and Council* [1997] ECR I-2405, par. 64.

[58] See for example Directive 2000/31 on certain legal aspects of information society services, in particular electronic commerce, in the internal market, OJ L178, p. 1. See also Case C-14/96 *Criminal proceedings against P. Denuit* [1997] ECR I-02785, par. 32 and 33. On the application of the COP to financial services see E. Lomnicka "The Home Country Control Principle in the Financial Services Directives and the Case Law" European Business Law Rev. 11(2000), p. 324-336. According to D. Kugelmann the introduction of the COP in secondary law is hardly revolutionary and it would greatly improve the free movement of services, "Die Dienstleistungs-Richtlinie der EG zwischen der Liberalisierung von Wachstumsmärkten und europäischen Socialmodell" Europäische Zeitschrift für Wirtschaftsrecht 11/2005, p. 327-331.

[59] See Case C-384/93 *Alpine Investments* [1995] ECR I-1141, par. 48.

[60] Joined Cases 369 and 376/96 *Arblade* [1999] ECR I-8453, par. 36.

[61] Case C-279/80 *Webb* [1981] ECR 3305, par. 16.

[62] Case C-3/98 *Reisebüro Broede* [1996] ECR I-6511, par. 28.

perceived as a restriction of a freedom, is taken into account, it is not surprising that the practical outcome of Court's reasoning can be often equalled to the application of the COP. However, according to S. Weatherill, there is no absolute rule of home state control in the Treaty; rather a non-absolute principle of mutual recognition is judicially applied in absence of sufficiently justified basis for host state control.[63]

The First draft envisages three different kinds of derogations from the COP. First of all, article 17 contains a list of twenty three general derogations. Some of them, for example these referring to postal services, gas distribution and recognition of professional qualifications, cover areas already regulated by Community instruments which confer some powers to host state. Others are granted in recognition of Members States' right to regulate in specific situations. For example, the COP does not apply to services covered by total prohibition in host state if it is justified by reasons relating to public policy, public security or public health[64] or to registration of vehicles leased in another Member State.[65]

Second, article 18 lists three transitional derogations relating to cash-in transit, judicial recovery of debts and gambling, that would apply until the adoption of specific harmonization instruments (but in case of the first two – no longer than until 2010). These areas were deemed too sensitive to be made subject to the COP without prior determination of common minimum standards. As regards cash-in transit it technically falls under the transport provisions which constitute *lex specialis* in relation to the freedom to provide services. The Commission has included this activity in the draft because of the large number of complaints it has received from entrepreneurs. As regards the other two derogations, the case law confirms their sensitive nature and resulting discretion of Member States. Regulation of the activity of judicial recovery of debts was examined by the Court in *Reisebüro Broede*. The ECJ ruled that German rules allowing undertakings to carry it out only through the intermediary of a lawyer constitute a restriction to the freedom. However, in the present state of Community law, Member

[63] S. Weatherill "Pre-emption, Harmonisation and the Distribution of Competence to Regulate the Internal Market" in C. Barnard nad J. Scott (eds) "The Law of the Single European Market; Unpackaging the premises" Hart Publishing 2002, p. 41-73. The author also notices that such principle may cause a race to the bottom in relation to enforcement.

[64] In this respect see Case C-275/92 *Schindler* [1994]ECR I-1039, par. 58-59, where the Court ruled that the prohibition of large scale lotteries may be justified by the need to protect consumers.

[65] See Case C-451/99 *Cura Anlagen* [2002] ECR I-3193, where the Court allowed the requirement of registration of vehicles leased in another Member State (par. 42), however it also ruled that short time limit and additional conditions of registration violate article 49 EC (par. 71).

States can assess on their own whether it is necessary to place restrictions on the professional recovery of debts by way of judicial proceedings.[66] There is also a rich case law concerning gambling,[67] where the Court generally gave Member States wide discretion in relation to the adoption of national measures justified by the protection of consumers, even though the freedom was restricted. This approach is a consequence of specific nature of gambling activities which are prone to fraud and may produce negative social effects. The fact that many Member States have strict regulations in this area was also taken into account. Nevertheless, the Court put its foot down when it came to downright discrimination. In *Lindman* it ruled that "*Article 49 EC prohibits a Member State's legislation under which winnings from games of chance organized in other Member States are treated as income of the winner chargeable to income tax, whereas winnings from games of chance conducted in the Member State in question are not taxable*".[68]

At last, in exceptional circumstances, Member States may derogate from the COP on the case-by-case basis, taking measures relating to the safety of services, exercise of health profession or protection of public policy (article 19). This list of admissible justifications is much narrower than the rule of reason catalogue established by the Court,[69] especially if we take into account the fact that it is still under development. Additionally, the measures taken by Member States according to article 19 not only have to pass the proportionality test[70] but should be also preceded by the mutual assistance procedure in which the Commission and country of origin are involved.

4. Rights of recipients

As was mentioned in the First Chapter, EC Treaty provisions on the freedom to provide services offer protection also to recipients. Consequently, the prohibition of

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[66] Case C-3/95 *Reisebüro Broede* [1996] ECR I-6511, par. 27 and 41.

[67] See Case C-275/92 *Schindler* [1994] ECR I-1039; Case C-124/97 *Läärä* [1999] ECR I-6067; Case C-67/98 *Zenatti* [1999] ECR I-7289; Case C-6/01 *Anomar* [2003] ECR I-8621; Case C-243/01 *Gambelli* [2003] ECR I-13031.

[68] Case C-42/02 *Lindman* [2003] ECR I-13519, par. 27.

[69] Which contains, among others: the conservation of the national historic and artistic heritage (Case C-180/89 *Commission v Italy* [1991] ECR I-709, par. 20) and the cohesion of tax system (Case C-204/90 *Bachmann* [1992] ECR I-248, par. 28)?

[70] Requirements relating to lack of harmonisation (art. 19.2 a), higher level of protection of recipients (art. 19(2) b) and insufficient action taken by the Member State of origin (art. 19.2 c), can be all subsumed under the proportionality test

discrimination contained in article 21 of the First draft is by no means revolutionary.[71] Similarly, elimination of restrictions on the use of service supplied by the provider established in another Member State (article 20), is consistent with the Court's jurisprudence.[72]

Further assistance for the recipients is provided in article 22, which renders Member States responsible for ensuring that recipients can obtain information about services, providers and bodies offering practical help. Thus, the general system of administrative cooperation and exchange of information established by the First draft is complemented.

The only truly controversial provision in this Section is article 23 concerning the assumption of health care costs.[73] This article should be read in the light of the Report on the application of Internal Market rules to health services, in which the Commission concluded that the Internal Market in health services is not functioning satisfactorily and that "*the Commission services will endeavour to ensure that European citizens benefit, irrespective of their country of origin, from the reimbursement of medical costs incurred in another Member State under the conditions laid down by the Court*".[74] In accordance with the case law, two different sets of rules are established: for non-hospital and hospital care respectively.[75] Assumption of costs of non-hospital care in another Member State cannot be made subject to prior authorization if these costs would have been assumed by the social security system in relation to care provided within the country.[76] Only

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[71] See Case C-45/93 *Commission v Spain* [1994] ECR I-911, par. 9-10.

[72] Especially cases concerning the fiscal restrictions are often examined by the ECJ. For example, in Case C-294/97 *Eurowings Luftverkehr* [1999] ECR I-7447, it was ruled that national legislation on trade tax conferring fiscal advantage to recipients of services provided by national undertakings is contrary to the freedom (par. 33-46)

[73] For a critical assessment of the influence of the Services Directive on the health care services see the Research Report of W. Gekiere Institute for European Law "Towards a European Directive on services in the Internal Market: Analysing the Legal repercussions of the Draft Services Directive and its Impact on National Services Regulations" Catholic University of Leuven, 24.9.2004, point III.

[74] Commission Staff Working Paper "Report on the application of Internal Market rules to health services. Implementation by the Member States of the Court's jurisprudence" 28.7.2003, SEC(2003) 900

[75] Hospital care is defined in article 4 point 10 as *"medical care which can be provided only within a medical infrastructure and which normally requires the accommodation therein of the person receiving the care"* This definition is partially based on the case law; the Court however has not delivered a clear cut distinction but limited itself to providing guidelines. See Case C-157/99 *Geraets-Smits and Peerbooms* [2001] ECR I-5473, par. 76. For an analysis of the case law in this respect see E. Steyger "National health care systems under fire (but not so heavily); European Court of Justice, 12 July 2001, Case C-157/99, Geraets-Smits v. Stichting CZ Groep Zorgverzekeringen, not yet published" Legal Issues of Economic Integration 29(2002), p. 97-107.

[76] In this respect see Case C-158/96 *Kohll* [1998] ECR I-01931, par. 52-53; Case C-385/99 Müller-Fauré [2003] ECR I-4509, par. 108-109

conditions and formalities which the recipient would be obliged to fulfil regardless of the place, the service is received, can be set up.

On the other hand, assumption of costs of hospital care can be subject to authorization.[77] However, it should not be refused "*where the treatment in question is among the benefits provided for by the legislation of the Member State of affiliation and where such treatment cannot be given to the patient within a time frame which is medically acceptable in the light of the patient's current state of health and the probable course of the illness*".[78] Additionally, whenever Member States reimburse costs of medical care provided abroad, they should do so at the same level that would be provided if the treatment took place within their borders.[79] These rules build upon the Court's jurisprudence on the interpretation of article 22 of Regulation 1408/71[80] The ECJ treats the rights derived from this provision as a starting point and broadens their scope through the application of Treaty rules.[81]

5. Posting of workers

Articles 24 and 25 of the First draft are devoted to the problem of posting of workers.[82] Although matters covered by Directive 96/71 (the Posting Directive)[83] are excluded from the application of the COP (article 17 point 5 of the First draft), in view of problems encountered by the entrepreneurs who want to take their staff to the host country, the Commission did not completely give up the idea of regulating this area. In order to secure the protection of workers, article 24.1 leaves intact the host state's power to conduct on its territory checks, inspections and investigations necessary to ensure the compliance with

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[77] See Case C-157/99 *Geraets-Smits and Peerbooms* [2001] ECR I-5473, par. 80-82, Case C-385/99 *Müller-Fauré* [2003] ECR I-4509, par. 81.

[78] Article 23.2 of the First draft. See also Case C-157/99 *Geraets-Smits and Peerbooms* [2001] ECR I-5473, par. 103; Case C-56/01 *Inizan* [2003] ECR I-12403, par. 59.

[79] See Case C-368/98 *Vanbraekel* [2001] ECR I-5363, par. 45 and 53.

[80] Regulation 1408/71 on the application of social security schemes to employed persons and their families moving within the Community, OJ L149, 5.7.1971, p. 2–50.

[81] See V.G. Hatzopoulos "Killing national health and insurance systems but healing patients? The European market for health care services after the judgments of the ECJ in Vanbraekel and Peerbooms" C.M.L. Rev. 39(2002), p. 683-729, point 3.1. See also Case C-372/02 *Watts* (not published yet).

[82] For a critical opinion on the provisions on posting see F. Hendrickx "Monitoring of labour standards in case of posting: some troublesome issues under the proposed services directive" in R. Blanpein (ed.) "Freedom of services in the European Union; Labour and Social Security Law: the Bolkenstein Initiative" Bulletin of Comparative Labour Relations, Kluwer Law International 2006, p. 105-114; who argues that there is insufficient harmonization and inadequate monitoring so the introduction of articles 24 and 25 may result in social dumping. For a more optimistic view see M. Colucci "Surveillance and control of labour standards at EU level" Ibid. p. 115-126; who however also points to the weak control in the host state.

[83] Directive 96/71 concerning the posting of workers in the framework of the provision of services, OJ L18, 21.1.1997, p. 1–6.

the employment and working conditions applicable under the Posting Directive,[84] as well as to take, in accordance with the Community law, measures in respect of a service provider who fails to comply with these conditions. However, paragraph two of the same provision, lists a number of obligations to which neither the service provider, nor the worker can be made subject. This catalogue reflects more closely the practical problems of entrepreneurs than the case law of the ECJ.[85] The approach adopted by the Commission suggests that protection given under the Posting Directive is sufficient and Member States should not be allowed to introduce further protectionist measures, such as for example the requirement of additional declarations (article 24.1 b of the First draft).

Meanwhile, the Court does not strike down automatically the national requirements involving administrative or economic burden, even though it regards them as restrictions to the freedom.[86] Instead, it always examines whether the measure at issue can be justified by mandatory requirements and is appropriate for their achievement. The best example is the *Arblade* case, where an obligation to keep the additional documents in the host state was considered.[87] The ECJ ruled that it could be justified if it was necessary for effective monitoring of compliance with legislation safeguarding social protection of workers, especially in the absence of an organised system of cooperation and exchange of information between the Member States.[88] Furthermore, the Court allowed the host Member State to conduct checks in order to establish whether the provider does not take advantage of the freedom for reasons other than the accomplishment of a service.[89] It appears that the Commission regards the system established by the First draft as sufficient to prohibit such requirement (article 24.1 d of the First draft). Especially, after making the Member State of origin responsible for ensuring that providers will make essential information available to the authorities of the host country within two years of the end of posting (article 24.2 of the First draft).

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[84] Additionally, the Member State of origin is obliged to assist it in this task, see art. 14.3 of the First draft.
[85] See the Explanatory note from the Commission Services on the provisions relating to the posting of workers with a particular emphasis on Article 24; Brussels, 5.7.2004; 11153/04, p. 8.
[86] For an analysis of the case law see R. Giesen "Posting: Social Protection of Workers vs Fundamental Freedoms?" C.M.L. Rev. 40(2003), p. 143-158.
[87] See Joined Cases C-369 and 376/96 *Arblade* [1999] ECR I-8453, par. 58-80.
[88] However, due to the system established by Directive 96/71, this requirement cannot continue after the employer has ceased to employ workers in the territory of host Member State.
[89] See Case C-113/89 *Rush Portuguesa* [1990] ECR I-1417, par. 17; Case C-445/03 *Commission v Luxembourg* [2004] ECR I-10191, par. 39.

On the other hand, the Commission did not refer to the case law concerning obligatory social security contributions imposed on a provider by the host state. The Court has consistently held that whenever the employer is already subject to such obligation which is essentially comparable as regards the protection of employees' interests, imposition of additional requirements is precluded by article 49 EC.[90]

Article 25 of the First draft is worded more carefully than the preceding provision, probably because it concerns the sensitive matter of posting of third country nationals. To appease doubts of Member States, consistency with the Schengen agreement is confirmed and country of origin is obliged to supervise the lawfulness of employment of posted workers.[91] However, the article in principle prohibits host state to require an entry, residence or work permit. The jurisprudence seems to confirm such approach. The burden and difficulties involved with obtaining of work permits were deemed disproportionate as compared with the aim of avoiding disturbances on the national labour market.[92] It can be assumed that after the establishment of the mutual assistance system envisaged in the First draft, Member States would have even smaller chances of justifying similar requirements.

6. Quality of services

Chapter four of the First draft obliges Member States to ensure proper quality of services, thus complementing the country of origin principle. In the absence of specific sectoral harmonization, requirements listed in these provisions aim at safeguarding the minimum level of protection of recipients. Although the articles are addressed to Member States, the burden of compliance lays mainly on providers. Foremost, they will have to make specified information available to the recipients.[93]

As long as requirements relating to the quality of services imposed by the Member State of origin are applied equally to all providers (both providing cross-border services and active only within one country) and are not questioned by other Member States, there

[90] See Case C-272/94 *Guiot* [1996] ECR I-1905, par. 14-21; Joined Cases C-49, 50, 52 to 54, 68 to 71/98 *Finalarte* [2001] ECR I-7831, par. 53; Case C-60/03 *Wolf and Müller* [2004] ECR I-9553, par. 45.

[91] Thus relieving the provider of the obligation to provide such verification to local authorities, imposition of which was implicitly allowed by the Court in Case C-445/03 *Commission v Luxembourg* [2004] ECR I-10191, par. 46

[92] See Case C-43/93 *Vander Elst* [1994] ECR I-3803, par. 26; Case C-445/03 *Commission v Luxembourg* [2004] ECR I-10191, par. 30.

[93] See articles 26, 27.2, 28, 30.3, 32.1 and 32.5 of the First draft.

should be no restriction of the freedom.[94] However, there are some additional limits to the discretion of national authorities. Article 29.1 forbids total prohibition on commercial communications by regulated professions[95] and article 30 allows for prohibition of multidisciplinary activities only in specified circumstances. These reservations are partially based on the case law of the Court.

According to the ECJ, total prohibition of advertisement or even of a specific form of it, may constitute an obstacle to the free movement of services.[96] However, as long as they are proportionate, such prohibitions may be justified, for example on the grounds of public health. It seems that article 29.1 of the First draft constitutes the development of Commission's initiatives in the area of regulated professions rather than a codification of the jurisprudence. In Report on Competition in Professional Services, the Commission noted that a large number of professions is subject to sector-specific advertising regulation and that such restrictions may have a potentially negative effect on competition.[97] This conclusion was supported in the follow-up to the Report which encouraged Member States to review their policies in this respect.[98]

In relation to multidisciplinary activities, in *Wouters*[99] the ECJ considered decisions of the Supervisory Boards of the Amsterdam and Rotterdam Bars prohibiting members of thse Bars to practice in full partnership with accountants. As the Court concentrated on the possible infringement of competition rules, the compatibility with free movement provisions was somehow neglected. It was simply stated, that even if it were assumed that decision of the Supervisory Board constituted restriction of the freedom to provide services and freedom of establishment, it would be justified by the objectives of the

[94] See for example article 27.3 of the First draft which (in relation to secondary freedom of establishment) prohibits Member States to demand additional professional insurance from the provider who is already covered by an equivalent one

[95] It should be noted that this provision will not prevent the application of specific advertisement prohibitions envisaged in other EC acts, such as prohibition of TV advertisement of medical treatment available only on prescription contained in article 14 of Directive 89/552 on the coordination of certain provisions laid down by law, regulation or administrative action in Member States concerning the pursuit of television broadcasting activities, OJ L298 of 17.10.1989, p. 23-30.

[96] See Case C-384/93 *Alpine Investments* [1995] ECR I-1141, par. 28 and 38; Case C-405/98 *Gourmet* [2001] ECR I-1795, par. 39, Case C-294/00 *Gräbner* [2002] ECR I-6515, par. 68 and 69.

[97] Commission Communication "Report on Competition in Professional Services" of 9.2.2004, COM(2004) 83 final, par. 42 and 45.

[98] Commission Communication "Professional Services - Scope for more reform" of 5.9.2005, COM(2005) 405 final, par. 29.

[99] Case C-309/99 *Wouters* [2002] ECR I-1577.

measure, namely the protection of consumers.[100] Consequently, it can be said that the Commission took the decision of the Court as a basis and, on its own initiative, described circumstances in which such restriction is acceptable and justified.

7. Administrative cooperation

The First draft establishes elaborate cooperation procedures with a view to supporting the liberalization provisions and securing the proper supervision of service providers. On the other hand, measures taken by the Member States are also monitored to prevent the introduction of unnecessary restrictions and to detect infringements of the freedom.

Through close cooperation, mutual trust between the Member States should be developed that would strengthen the functioning of the country of origin principle. Together with common initiatives such as codes of conduct, it will not only improve the flow of information about providers, recipients and national restrictions, but also facilitate the removal of barriers. The obligation to notify and properly justify the intent to make use of a case-by-case derogation from the COP (article 37 of the First draft) will also contribute to the reduction of the number of obstacles set up by the states. It could seriously hamper the imposition of restrictions by an obligation of prior consultations with the country of establishment and the Commission.

8. Impact assessment

The essential role of services in the generation of employment and the GDP was stressed in the Extended Impact Assessment presented by the Commission in January 2004.[101] However, it was also pointed out that their potential is not fully used. The Commission noticed that:

"The barriers affecting the freedom to provide services require mainly that Member States refrain from applying their own rules and regulations to incoming services from other Member States and from supervising and controlling them. Instead they should rely on control by the authorities in the country of origin of the service provider. This would remove the legal uncertainty and costs resulting from the application of a multitude of

[100] Ibid. par. 119-123. More elaborate examination was conducted by the Advocate General Léger in par. 242-257 of his opinion in this case (delivered on 10.7.2001), where he argued that the measure at issue constitutes an obstacle to the freedom to provide services but it could be justified by an overriding reason relating to the public interest – assurance of independence and professional secrecy.

[101] Commission Staff Working Paper "Extended Impact Assessment of a Proposal for the Directive on Services in the Internal Market", 13.1.2004, COM(2004) 2 final.

different rules and control measures to which cross-border service providers are currently subject. However, this means that Member States must have trust and confidence in each other's legal systems and control measures."[102]

The examination of possible policy options: no change of policy; voluntary self-removal of barriers by Member States; infringement procedures launched by the Commission; sectoral options; horizontal options; resulted in the conclusion that a horizontal directive would constitute the most effective instrument for the elimination of remaining barriers to the free movement of services.[103]

According to the Report delivered by Copenhagen Economics in January 2005,[104] adoption of the Directive would result in reduction of barriers to the free movement of services by approximately 50%. Additionally, the authors predicted that around 600 000 new jobs would be created and EU Gross Added Value would increase by 0,8%. Countries, such as France and Germany, which presently maintain the largest number of barriers, would profit most from the Directive. However, the scale of effects depends upon the degree of liberalisation that will be finally agreed upon. It is estimated that elimination of country of origin principle from the draft will reduce the positive impact by around 10%.[105]

9. Conclusions

As is apparent from the description of the First draft, the Commission did not simply codify the case law of the ECJ. Even though the project in big part reflects the jurisprudence, it also departs from it in some matters. Especially the country of origin principle constitutes a significant step forward in relation to the EC Treaty rules as developed by the Court. However, it has to be remembered that a legislative act cannot blindly copy the judicature. The form of the directive and the prospect of its implementation into national legal orders require a more complex approach than adopted in the decisions of the ECJ which are given in a specific factual background on a case-by-

[102] Ibid. p. 23-24.
[103] Ibid. p. 28 and 40.
[104] Independent study by Copenhagen Economics "Economic Assessment of the Barriers to the Internal Market for Services", Final Report
[105] See Copenhagen Economics "The Economic Importance of the Country of Origin Principle in the Proposed Services Directive", Final Report of 7.11.2005. See also R. de Bruijn, H. Kox, A. Lejour "The trade-induced effects of the Services Directive and the country of origin principle" CBP Netherlands Bureau for Economic Policy Analysis, February 2006; where it is argued that after the COP is deleted the intra-EU service trade will increase by 19 to 38% instead of 30 to 62%.

case basis. First, the Commission had a difficult task of creating a general framework for the functioning of services market. Second, it had to fill the gaps left by the Treaty provisions and specify in more detailed manner the rights of the providers and recipients and the obligations of the Member States providing a sufficient basis for the introduction of the country of origin principle.

CHAPTER THREE

THE DEBATE

1. Introduction

Shortly after the Commission presented the First draft, negotiations over the final shape of the Directive begun in various bodies. In accordance with the codecision procedure from article 251 EC, the Council and the European Parliament are working simultaneously at the project. Their endeavours are supported by several consultative bodies which provide opinions and suggestions of improvements of the draft.[106] The views presented show the clash between the interests of particular groups such as the labour unions[107] and further liberalisation of services market and explain why adoption of the Directive is such a long and difficult process.

2. The Working Party on Competitiveness and Growth (Services)

A Working Party composed of the representatives from all Member States was established in order to discuss the project. Its meetings are chaired by current Presidency which sets the pace of work and strives to reach a compromise. A representative from the Commission is also present to explain and support the approach adopted by this institution.

During the regularly held meetings consecutive provisions of the First draft are discussed. Delegations present the positions of their Member States as regards detailed matters such as the choice of words used, and general issues like the scope of the Directive.[108] In this Chapter the most problematic and controversial matters are presented.

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[106] See especially opinion of the European Economic and Social Committee (OJ C221, 8.9.2005, p. 113) and opinion of the Committee of the Regions (OJ C43, 18.2.2005, p. 18).

[107] As was showed in the previous Chapter, economies of Member States and EU as a whole would generally profit from the liberalisation. However, adoption of the Directive in the shape proposed by the Commission would limit the power of states to protect the national companies and workers against the competition from other Member States. Also the possibility of introducing protectionist barriers and exercising control over the foreign providers would be restricted.

[108] Information about the positions presented by the representatives of Member States come from the explanations included in proposal of the directive of 6.12.2005 (15310/05) and from the reports of Polish delegation to the meetings of the Working Party.

2.1 Scope of the Directive

Even though at the beginning it seemed that all Member States present a favourable approach towards the project of harmonisation,[109] it soon turned out that there is no agreement as to its scope and the degree of liberalisation. First of all, the definition of 'service' provided in article 4 point 1 of the First draft, was questioned. Despite the fact that it reflects the wording of article 50 EC and the case law of the Court, it was deemed too general for a legislative act.[110] Demands that the maximum duration of the provision of service is established and clear distinction between the provision of services and permanent establishment is drawn were repeatedly raised.[111] On the one hand, it is understandable that Member States did not want to introduce laws which would require an evaluation of each case separately in order to check whether it falls under the scope of the Directive. On the other, according to the ECJ, there is no definite border that would set limit to the duration and frequency of the service provision.[112]

Furthermore, many countries wanted to extend the list of activities excluded from the scope of the Directive arguing that without prior harmonisation in these areas, consumers would not be sufficiently protected.[113]

There was also strong resistance against the inclusion of taxation in the scope of the Directive, also in relation to rights of recipients (prohibition of discriminatory or disproportionate taxes, limits on tax deductibility – article 20 of the First draft).[114] Even though it is a settled case law that Member States should exercise their discretion consistently with the Community law,[115] national authorities do not want to allow an express and clear reminder of that rule in the Directive. This approach could be explained

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[109] Note from the Presidency addressed to the Council (Competitiveness) on 25/26.11.2004 (14558/04; 17.11.2004) states that discussion in the Working Party has so far confirmed that all Member States support the necessity and the general objective of the proposal.

[110] For an opinion that definitions of services can themselves account to restrictions see. J. Snell and M. Andenas "Explaining the outer limits: restrictions on the free movement of goods and services" in M. Andenas and W.-H. Roth "Services and Free Movement in EU Law" The British Institute of International and Comparative Law, Oxford University Press 2002, p. 75

[111] For example, by Poland, Latvia, Denmark, Italy, Belgium and the UK.

[112] See Case C-215/01 *Schnitzer* [2003] ECR I-14841, par. 31

[113] Economic interests and protection of national entrepreneurs were also the reasons of Member States' objections but these arguments were used rather during national political debates than during the meetings at EC level.

[114] UK, Denmark, Italy. Especially from art. 20: the Netherlands, Belgium, Portugal, Germany, Malta, Estonia, Latvia.

[115] See Case C-80/94 *Wielockx* [1995] ECR I-2493, paragraph 16; Case C-264/96 *ICI* [1998] ECR I-4695, par.19; Case C-311/97 *Royal Bank of Scotland* [1999] ECR I-2651, par. 19; Case C-35/98 *Verkooijen* [2000] ECR I-4071, par. 32; Case C-17/00 *De Coster* [2001] ECR I-9445, par. 26; Case C-136/00 *Danner* [2002] ECR I-8147, par. 28.

by a traditional perception of (especially direct) taxation as one of state's sovereign powers, but also by the increasing tendency to use taxes as protectionist tools which create competitive advantage for national companies and products.[116]

Further opposition was raised against the liberalisation of gambling activities,[117] even though they were covered by transitional derogation from the COP. In this case, also financial interests are at issue – in many Member States the organisation of (at least some) gambling activities is reserved for the State or bodies having a licence issued by the State, and creates significant income for the budget. Even though the Directive does not require the abolition of national monopolies, fiscal authorities are afraid that those profits would decrease, if only in the result of the competition with providers established in other EU countries. Moreover, in some states hazard is heavily regulated in order to protect the consumers from fraud and negative social consequences such as addiction. Entrepreneurs could avoid these rules by establishing in states with most lenient laws and relying on the COP in order to provide services in other Member States. The lenient approach of the Court in the gambling cases (see Chapter Two, point three) partially supports the arguments of the Member States.

Anxious about the possible damage that the liberalisation might cause to services (partially) financed from their budgets, many Member States wanted to exclude from the scope of the Directive the services of general economic interest (the SGEI),[118] education services,[119] health services[120] and social services.[121] Such approach is in clear opposition to the case law of the Court, which states that the system of financing of services is of no importance as long as there is a consideration and the services have an economic

[116] See for example W. Schön "Taxation and state aid law in the European Union", C.M.L. Rev. 36(1999), p. 911-936

[117] Hungary, Portugal, Poland, Slovenia, the Czech Republic, Denmark, Greece, Spain, Austria, Germany, France.

[118] Austria, Cyprus, France, Malta, and Belgium are of the opinion that the Directive must not apply to public services which are guaranteed and financed by public authorities for social, educational or cultural objectives.

[119] Malta; Denmark, Germany, Austria - state education or educational institutions primarily financed by the state; Portugal – exclusion of higher education.

[120] Slovakia, Slovenia, Malta, Hungary, Greece; Poland, the United Kingdom, Italy – exclusion of publicly funded health services.

[121] Austria, Cyprus, Greece, France, Denmark, Slovenia, Germany, Hungary; Estonia - only in relation to publicly funded social services.

character.[122] Nevertheless, wealthier Member States fear that foreigners would take advantage of their social security systems undermining their financing. Also poorer countries worry that their systems might collapse if nationals were allowed to travel freely and to choose the provider without any restrictions.[123] Medical services pose a particular problem, especially in the light of article 23 of the First draft which concerns the assumption of health care costs. Member States find it difficult to agree with the broad interpretation of the remuneration requirement provided by the Court in its judgments. Some delegations argued, that publicly financed medical services lack the economic character and thus fall outside the scope of the freedom and proposed Directive.[124] They also insisted that if any harmonisation were to take place, it should be done through the modification of Regulation 1408/71 (which, contrary to the services directive, requires unanimity).[125]

However, according to the explanatory note from the Commission, the fears of patients' exodus and serious financial problems are unfounded because the patient mobility is currently negligible and there are not many requests for authorisation of treatment in another Member State.[126] Furthermore, the ECJ in many situations questioned the claim of national authorities that reimbursement would jeopardise the maintenance of medical care systems.[127]

As regards the SGEI, the Directive was meant to cover only those services which are performed for an economic consideration which - according to the Commission - is fully

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[122] See Case C-157/99 *Geraets-Smits and Peerbooms* [2001] ECR I-5473, par. 55-58. For an analysis of economic character of the national welfare systems see G. Davies "Welfare as a Service" Legal Issues of Economic Integration 29(2002), p. 27-40.

[123] In this regard the Court has held that the fact that there are waiting lists for hospital treatment on national territory cannot in itself justify a restriction to the patients' mobility; see Case C-385/99 *Müller-Fauré* [2003] ECR I-4509, par. 92.

[124] For an opinion that medical care provided in a framework of benefits in kind system or financed directly through tax revenues should not be qualified as a service within the meaning of EC Treaty, see P. Cabral "The internal market and the right to cross-border medical care" E.L. Rev. 29(2004), p. 676-678.

[125] Meanwhile, Article 20 of Regulation 883/2004 of 29.4.2004 on the coordination of social security systems (OJ 2004 L.166, p. 1), which is intended to replace Article 22 of Regulation 1408/71, introduces only minor modifications to the present scheme.

[126] Explanatory note from the Commission Services on the provisions of the proposed Directive on services in the Internal Market relating to the assumption of healthcare costs incurred in another Member State with a particular emphasis on the relationship with Regulation 1408/71; 16.7.2004; 11570/04, p. 7-8.

[127] See Case C-368/98 *Vanbraekel* [2001] ECR I-5363, par. 51-52; Case C-385/99 *Müller-Fauré* [2003] ECR I-4509, par. 74 and 96-97.

in line with the White Paper on Services of General Interest.[128] Furthermore, the Member States' right to define what constitutes the SGEI and determine their organization and financing, as confirmed by the Court,[129] would remain unchallenged.

Finally, numerous delegations supported the motion of exclusion of audiovisual services from the scope of the Directive.[130] Their reasoning was based mainly on the specific nature of this sector and social and cultural role of the media. In this regard, it should be noticed that the ECJ repeatedly stressed that the special nature of certain services does not remove them from the scope of the fundamental Treaty freedoms.[131] In all cases considered, the Court had no doubt that transmission and broadcasting of TV signals constitutes services within the meaning of the Treaty and that restriction to the freedom can be only justified either by express Treaty derogation or by the overriding reasons relating to the public interest.[132] Furthermore, certain aspects of broadcasting have been already harmonised by the 'TV without frontiers directive'[133] that introduces (even though in a limited degree) the country of origin principle.

2.2. The country of origin principle

The introduction and possible scope of the COP which constitutes one of the pillars of the First draft were also a subject of lively discussion.[134] Questions about the possible conflicts with other rules and EC instruments were raised.[135] Public and political debate on the 'race to the bottom' and 'social dumping' showed the lack of mutual trust and solidarity, especially in relations between old and new Member States. Arguments were raised that some Member States will lower their social standards in order to attract

[128] See the Explanatory note from the Commission on the activities covered by the proposal, 10865/04, 25.6.2004. White Paper on Services of General Interest COM(2004) 374 final. On the slow process of liberalisation of the SGEI see G. Napolitano "Towards a European Legal Order for Services of General Economic Interest" European Public Law 11(2005), p. 565-581.

[129] See Case T-106/95 *FFSA* [1997] ECR II-229, par. 192.

[130] France, Cyprus, Greece, Portugal, Malta.

[131] See Case 279/80 *Webb* [1981] ECR 3305, par. 10.

[132] See Case 155/73 *Sacchi* [1974] ECR 409; Case 52/79 *Debauve* [1980] ECR 833; Case 352/85 *Bond van Adverteerders* [1988] ECR 02085; Case C-260/89 *ERT* [1991] ECR I-2925; Case C-288/89 *Gouda* [1991] ECR I-04007; Case C-353/89 *Commission v the Netherlands* [1991] ECR I-04069; Case C-148/91 *Veronica* [1993] ECR I-00487; Case C-23/93 *TV10 SA* [1994] ECR I-04795; Joined Cases C-34 to 36/95 *De Agostini* [1997] ECR I-03843; Case C-56/96 *VT4* [1997] ECR I-03143; Case C-6/98 *ARD* [1999] ECR I-7599.

[133] Directive 89/552 on the coordination of certain provisions laid down by law, regulation or administrative action in Member States concerning the pursuit of television broadcasting activities, OJ L298, 17.10.1989, p. 23-30.

[134] Denmark, Portugal, Greece, Cyprus and France questioned the principle as such.

[135] Especially as regards possible conflicts with the private international law, see supra note 1. Austria, Germany, Denmark, Greece, Finland and the Czech Republic insisted on derogating matters covered by the Rome Convention and proposed Rome II Regulation.

business and others will have to follow their lead if they want to remain competitive. Even among lawyers and economists there is no agreement as to the possibility of the 'race to the bottom' actually taking place.[136] Nevertheless, it is a powerful argument especially among the countless workers afraid to loose their jobs

Moreover, even the countries which are generally in favour of the COP (e.g. Poland) demand the extension of the list of derogations to additional matters such as higher education services[137] or temporary employment agencies.[138] On the other hand, as the French delegation[139] rightly noted during the Working Party meeting on 24.6.2004, large number of derogations would make the practical application of the principle very difficult and would decrease legal certainty. At this point it should be noted that the COP has been already introduced by several acts of secondary law,[140] however only specific sectors were covered and only to the extent that they were harmonised. Conversely, the Services Directive has a horizontal character and does not provide the level of harmonisation that most Member States would regard as sufficient for the introduction of the COP. Additionally, general application of this principle does not follow from the case law (see Chapter One), so it would result in limitation of host state's discretion and control over the foreign providers as compared to one that it can presently exercise on the basis of Treaty provisions. It follows that the main function of the derogations from the COP is to assure that the authority of the host Member State will not be restricted.

2.3. Posting of workers

The articles regulating posting of workers resulted in a strong division line between the Member States. Countries such as Germany, Austria and France try to protect their labour

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[136] See C. Barnard "Social dumping and the race to the bottom: some lessons for the European Union from Delaware?" E.L. Rev. 25(2000), p. 57-78.

[137] Even though in Case 263/86 *Humbel* [1988] ECR 5365, par. 18-20 and Case C-109/92 *Wirth* [1993] ECR I-6447, par. 15-16; the Court has ruled that the element of remuneration is absent in the university courses provided within the national education system or courses given in an institute of higher education financed essentially from the public funds, and that consequently they do not constitute services within the meaning of the Treaty. Apparently, what the Member States truly want to exclude, are the courses provided for remuneration which, according to the Court, constitute economic activity. See Case C-153/02 *Valentina Neri* [2003] ECR I-13555, par. 39.

[138] Even though the hiring out of workers by temporary employment agencies falls within the scope of the Posting Directive. Additionally, the exclusion from the scope of the COP would not change the fact that a host state cannot impose licence requirements on these agencies if they are covered by comparable obligation and sufficient supervision in the state of origin. See Case 110/78 *Van Wesemael* [1979] ECR 35, par. 29-30 and Case 279/80 *Webb* [1981] ECR 3305, par. 19-20.

[139] France is generally opposed to the introduction of the COP.

[140] See, e.g. art. 4 of Directive 1999/93 on a Community framework for electronic signatures, OJ L13, 19.1.2000, p. 12-20.

markets from the inflow of delegated workers. Pressed by the lobbying of labour unions they demand the deletion of articles 24 and 25 from the project, or at least the derogation of the construction sector,[141] determination of the maximum period for posting, maintenance of the declaration obligations and perseverance of the role of collective agreements. On the other hand, states with low labour costs strongly support the liberalization arguing that the Posting Directive, constituting *lex specialis* in relation to the Services Directive, offers sufficient protection.[142] The Commission took the same position in its explanatory note, where it underlined that the powers granted to national authorities by the Posting Directive would not be undermined and therefore there is no risk of abuse of workers' rights (employment conditions of the host country would still be binding and national authorities would be empowered to enforce them) or employment for a wage lower than minimum.[143]

3. The European Parliament – main changes proposed

Consultation of the project took place in several Committees[144] and was accompanied by lively political and public debate. The EP adopted its position on the Services Directive at first reading on 16.2.2006.[145]

Generally, the modifications proposed by the EP reflect the anxiety that the Services Directive might negatively affect the 'European social model'.[146] Consequently, the changes were introduced to ensure that the level of protection offered by a state to its nationals would not diminish. Additionally, matters relating to sensitive activities or sectors where, either the Member States or the lobbying groups (labour unions, or even the entrepreneurs themselves) strongly opposed to the opening of national markets were

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[141] Particularly Germany and Austria.

[142] The Czech Republic, Poland, Estonia, Hungary, Latvia, Portugal, Slovakia, Lithuania, Slovenia, Ireland, but also the UK and the Netherlands opposed the deletion of articles 24 and 25 of the First draft.

[143] Explanatory note from the Commission Services on the provisions relating to the posting of workers with a particular emphasis on Article 24, 11153/04, 5.7.2004.

[144] The Committee of Petitions; the Committee on Budgetary Control, the Committee on Women's Rights and Gender Equality; the Committee on Legal Affairs, the Committee on Culture and Education; the Committee on Industry, Research and Energy; the Committee on the Environment, Public Health and Food Safety; the Committee on Economic and Monetary Affairs; the Committee on Employment and Social Affairs and the Committee on the Internal Market and Consumer Protection (the leading Committee)

[145] Position of the European Parliament adopted at first reading on 16 2 2006 with a view to the adoption of Directive 2006/.../EC of the European Parliament and Council on services in the internal market (EP-PE_IC1-COD(2004)0001). For a critical review of the EP's first reading see Editorial Comments "The services directive proposal: striking a balance between the promotion of the internal market and preserving the European social model?" C M L Rev 43(2006), p. 307-311

[146] Recital 4

excluded from the scope of the Directive. In my opinion, such approach not only limits the benefits of the liberalization[147] but also causes that the chance to lessen the burden of maintaining 'social states' is wasted.[148] Exclusions postulated by the EP include: health care services, audiovisual services, gambling, temporary work agencies, social services, port services, security services and matters relating to labour law. Accordingly, the provisions on assumption of health care costs and on posting of workers were also deleted. Furthermore, according to the Members the EP, the Directive should not apply in the field of taxation and private international law. The rule that every Member State is responsible for the supervision of providers on its territory was introduced (art. 17.3) and the COP was replaced by a provision on the 'freedom to provide services' (art.21). It imposes vague obligations to *"respect the right of providers to provide a service in a Member State other than that in which they are established"* and to *"ensure free access to and free exercise of a service activity within its territory"*. More importantly, all requirements imposed by the Member States must fulfil the conditions of non-discrimination, necessity and proportionality. The definition of 'necessity' is essential here; it provides that "*the requirement must be justified for reasons of public policy or public security or the protection of health and the environment*". Thus, the wording proposed by the EP refers to the possible justifications of a national measure. Meanwhile, according to the ECJ, the necessity requirement means that national measures cannot go beyond what is necessary to attain their objective.[149] J. Snell explains that "*the measure has to be necessary, in the sense that there may be no other measures that could achieve the same aim while being less restrictive of trade. The measure will not be regarded as necessary if the exporting or home state's legislation already protects the interest.*"[150] In result of the definition adopted, the discretion of Member States as compared with the broad list of imperative requirements recognised by the Court is severely limited.[151] The fact that this catalogue of justifications is almost identical to the one from article 46 EC (only the protection of

[147] See the Impact assessment in Chapter Two, point eight of this paper

[148] For example the Netherlands and Germany are presently facing serious problems with maintaining the level of social protection their citizens are used to and making their economies competitive at the same time.

[149] See Case C-424/97 *Haim* [2000] ECR I-5123, par. 60.

[150] J. Snell "True Proportionality and Free Movement of Goods and Services" European Business Law Rev. 11(2000), p. 50.

[151] For an opinion that such freezing of justifications is contrary to the notion of harmonisation, which presupposes the regulation of general, interests at the Community level see S.A. de Vries "Tensions within the Internal Market; The Functioning of the Internal Market and the Development of the Horizontal and Flanking Policies" Europa Law Publishing, Groningen 2006.

environment is not mentioned there), on the basis of which even discriminatory measures can be taken, seems to be a radical solution. Even more so, if the view expressed by J. Snell that the Court in principle does not review the justifications themselves (as long as they are not purely economical or administrative), but rather concentrates on the proportionality test, is followed.[152] However, it should be remembered that the concepts used have not been defined by the Community law and are in fact quite 'capacious'. Actually, practically every mandatory requirement could be subsumed under one of them.[153] Consequently, it is questionable whether the number of justifications at the disposal of the Member States would be in practice restricted as compared to the list of imperative requirements developed by the Court.

Paragraph 2 of article 21 transposes into the Directive the 'prohibition of restrictions' established by the Court, and gives an exemplary list of prohibited requirements (essentially comparable to this proposed by the Commission). The consistency of the provision is seriously disturbed by paragraph 3 which allows Member States to derogate from preceding paragraphs in order to impose requirements "*with regard to the provision of a service activity, where they are justified for reasons of public policy, public security, environmental protection and public health. Nor do they prevent Member States from applying, in conformity with Community law, their rules on employment conditions, including those laid down in collective agreements.*" While the first four justification repeat paragraph 1 b, the labour law (including employment conditions) is excluded from the scope of the Directive in article 1.8. Moreover, it is not specified that the requirements introduced should be proportional. Additionally, as there is no condition of non-discrimination, this provision creates a new derogation from the Treaty provisions on the freedom to provide services as compared with article 46.1 EC, where the environmental protection is not mentioned.[154] Similarly, the next article containing general derogations might be regarded as intending to derogate from the Treaty, which of course cannot be

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[152] J. Snell "Goods and Services in EC Law; A Study of the Relationship Between the Freedoms" Oxford University Press 2002, p. 191. See also V.G. Hatzopoulos "Recent developments of the case law of the ECJ in the field of services" C.M.L. Rev. 37(2000), p. 77-81; who however notices that the broad interpretation of what constitutes a purely administrative or economical justification; restrict the discretion of Member States.

[153] See P. Oliver and W.H. Roth "The Internal Market and the Four Freedoms" C.M.L. Rev. 41(2004), p. 435.

[154] Protection of environment may constitute an imperative requirement but it can be only invoked to justify non-discriminatory measures. As to the employment conditions, the provision says expressly that they should be applied in compliance with Community law.

done through the secondary law.[155] Activities listed in article 22, such as the SGEI, constitute services within the meaning of article 50 EC and fall within the scope of the freedom to provide services. Even though their exercise may be restricted by measures justified by the overriding reasons relating to the public interest or by express Treaty derogations, there are specific conditions that have to be met.[156] While the COP constituted a step forward (thus creating a possibility for some derogations), article 21 only repeats the well established Treaty rules. The only difference being the limitation of grounds for justification which, as mentioned before, does not necessarily have to result in actual change of present situation. Consequently, all the service activities, whether falling under article 21 or not, will be subject to similar principles.

In these circumstances, the provision on case-by-case derogations (no temporary derogations are envisaged in EP's proposal) complicates the matters even more. It introduces the possibility to take, in relation to a particular service provider, measures relating to safety of services, exercise of health profession or the protection of the public policy. Again, these justifications are very general and imprecise. Additionally, although the measures taken have to fulfil the proportionality test, the mutual assistance procedure requiring prior consultations was replaced with an optional request directed to the state of primary establishment to conduct checks, investigations or inspections

Altogether the changes proposed by the EP seem to strengthen the position of the host state rather than limit it.

4. Conclusions

This Chapter shows how much the views of Member States and various bodies differ in relation to the future of the services market. Even more importantly, the discrepancies prove that there is no agreement even as to the present state of liberalisation andthe scope of the freedom. Faced with the perspective of adoption of a horizontal act which will be much more effective than the infringement procedures initiated by the Commission, they cautiously examine every provision that will have to be incorporated into national legal orders. The discussion is often reduced to the conflict between protectionist interests and needs of modern economies, rendering the legal arguments incidental.

[155] On the relationship between the primary and secondary law see K. Mortelmans "The relationship between the Treaty rules and Community measures for the establishment and functioning of the Internal Market – towards a concordance rule" C M L Rev. 39(2002), p. 1303-1346.
[156] See Chapter One, point four of this paper.

CHAPTER FOUR

THE COMPROMISE

1. Introduction

After the European Parliament adopted its restrictive position on the Directive, the Commission faced two choices: either to withdraw the proposal altogether or to adapt the draft so that it would gain the approval of the Members of the EP. Apparently, it decided that half a loaf is better than none, because on 4 April 2006 the amended compromise version of the Directive, incorporating most of the changes postulated by the EP, was presented.[157]

2. Main changes in relation to the First draft

The first change that comes to attention is the severe limitation of the scope of the Directive. The new exclusions consist of port services, services of temporary work agencies, health care services, audiovisual services, gambling activities, social services, and private security services. All these activities constitute services within the meaning of the Treaty and the provisions on the freedom apply to them on regular basis.[158] However, it was successfully argued that if they are to be harmonised, then only through separate acts and not in a horizontal manner. Furthermore, the application of the Directive in the field of taxation and private international law is expressly excluded.

For the sake of compromise, the Commission has also consented to replacing the country of origin principle with the provision on the freedom to provide services (art. 16). At the outset, it should be noted that the use of EC Treaty nomenclature creates confusion as to the interrelation between the Treaty and proposed Directive. First of all, it suggests that the scope of the freedom as envisaged in the Treaty is identical to that expressed in the Directive. Second, the derogations from article 16 could be presumed to constitute exemptions from the article 49 EC itself.

The wording proposed by the EP is left practically unchanged, the only adjustment being that all requirements imposed by the Member States must fulfil the conditions of non-

[157] Amended Proposal for a Directive of the European Parliament and of the Council on services in the internal market, COM(2006) 160 final

[158] See previous Chapters of this paper. In relation to security services, which have not been discussed earlier, see Case C-114/97 *Commission v Spain* [1998] ECR I-06717; Case C-355/98 *Commission v Belgium* [2000] ECR I-1221; Case C-189/03 *Commission v Netherlands* [2004] ECR I-9289. As to the exclusion of port services it could be explained by their close relation to transport services, see Case C-18/93 *Corsica Ferries* [1994] ECR I-01783

discrimination, necessity and proportionality. Thus, paragraph 3 is rendered superfluous because it does no longer offer the Member States any true advantage – the same rules and grounds for justification apply as in paragraph 1.

Furthermore, serious problems may be caused by the fact that in the compromise version words 'in particular' are missing from paragraph 2,[159] turning the list of prohibited restrictions into an exhaustive catalogue. Meanwhile, as the experience and the case law of the ECJ show, there are numerous ways of obstructing the freedom and no such closed record can be devised. Even more importantly, words 'in particular' allowed to legitimately presume that all restrictions of the freedom are in principle prohibited. After their deletion, only general clauses from paragraph 1 are left to secure the rights of service providers and recipients.

In this situation, the activities to which article 16 does not apply on the basis of the next provision,[160] may be in result subject to more liberal rules, as according to the Court articles 49 and 50 EC: "*require not only the elimination of all discrimination on grounds of nationality against providers of services who are established in another Member State but also the abolition of any restriction, even if it applies without distinction to national providers of services and to those of other Member States, which is liable to prohibit, impede or render less advantageous the activities of a provider of services established in another Member State where he lawfully provides similar services*".[161]

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[159] Hopefully it is only a technical mistake

[160] Article 17 enumerates additional derogations from the freedom to provide services: Services of General Economic Interest which are provided in another Member State; matters covered by the Posting Directive; matters covered by Directive 95/46 on the protection of individuals with regard to the processing of personal data and on the free movement of such data; matters covered by Directive 77/249 to facilitate the effective exercise by lawyers of freedom to provide services; the activity of judicial recovery of debts; matters covered by title II of Directive 2005/36 on the recognition of professional qualifications, as well as requirements in the Member State where the service is provided which reserve an activity to a particular profession; matters covered by Regulation 1408/71; as regards administrative formalities concerning the free movement of persons and their residence, matters covered by the provisions of Directive 2004/38; as regards third country nationals who move to another Member State in the context of the provision of a service the possibility for Member States to require visa or residence permits for third country nationals who are not covered by the mutual recognition regime provided for in Article 21 of the Convention implementing the Schengen Agreement or the possibility to oblige third country nationals to report to the competent authorities of the Member State in which the service is provided on or after their entry; the authorisation regime provided for in Articles 3 and 4 of Regulation 259/93 on the supervision and control of shipments of waste within, into and out of the European Community; copyright, neighbouring rights, rights covered by Directive 87/54 and by Directive 96/9 as well as industrial property rights; acts requiring by law the involvement of a notary; matters covered by Directive . /... on statutory audit of annual accounts and consolidated accounts and amending Directives 78/660 and 83/349; the registration of vehicles leased in another Member State; provisions regarding contractual and non-contractual obligations, including the form of contracts, determined pursuant to the rules of private international law.

[161] Case C-222/95 *Parodi* [1997] ECR I-3899, par. 18.

Conversely, in relation to the case-by-case derogations from article 19,[162] the number of justifications at the disposal of Member States is in fact limited. The only ground for restrictions is the safety of services. Even though rather vague, this term must have been intended as restrictive; otherwise why the notion of 'overriding reasons relating to the public interest' is not deployed, even though it is defined in article 4.7a and afterwards used in other provisions? Additionally, the Commission did not agree to give up the mutual assistance procedure and, in result, the introduction of national measures on the basis of article 19 is conditional on the prior consultations with the Member State of establishment and notification to the Commission. On the other hand, this provision requires only that the measures introduced are proportional, but it does not specify that they should also be non-discriminatory. Without this condition, the case-by-case derogations aspire to the role of new exemptions from article 49 EC.

After the COP has been abandoned, the national powers of supervision do not seem to be much affected by the Directive. Although article 34 lays the main burden of supervising the provider on the country of establishment; according to article 35, the host Member State retains the authority to control the observance of requirements imposed pursuant to articles 16 or 17 (derogations from the "freedom to provide services"). It seems that, as the competence to monitor is a logical consequence of the authority to apply national law to the provider, article 19 (case-by-case derogations) should be included there as well. The obligation to carry out checks and inspections at the request of the Member State of establishment constitutes a natural element of the system of mutual assistance created by the Directive. When the provider travels abroad, the country of origin cannot effectively conduct the supervision on the territory of another state. The consistency of the system of supervision is somewhat disturbed by article 35.4 which allows the host country to "*conduct checks, inspections and investigations on the spot, provided that those checks, inspections or investigations are not discriminatory, are not motivated by the fact that the provider is established in another Member State and are proportionate*". On one hand, it is not clear to which requirements this provision refers - imposed by the Member State of origin, case-by-case derogations, subscription to professional liability insurance, or others? On the other, it would be difficult to prove that the checks are not, at least partially, based on the fact that the provider is established abroad.

[162] The elimination of the provision listing temporary derogations was upheld

As regards the rights of recipients, the prohibition of discrimination (article 20) and of the restrictions on the use of services of foreign providers (article 21) remain in the compromise version of the proposal as well as various provisions obliging Member States to ensure that recipients will receive a variety of information. However, the article regulating the assumption of health care costs has been removed, leaving the present situation unchanged (the combined application of article 22 of the Regulation 1408/71 and article 49 EC). Moreover, after the removal of taxation matters from the scope of the Directive, the Chapter on recipients' rights no longer mentions the prohibition of discriminatory taxes and limits on the tax deductibility.

Under the pressure of the EP and numerous Member States, the Commission has also abandoned the idea of regulating in the Directive the issue of posting of workers. Instead, the proposal repeatedly stresses that the national labour law,[163] conditions of employment and the provisions of the Posting Directive are not affected by the Services Directive.[164]

Conversely, the Chapter on the Quality of services remained in principle untouched, including the provisions which oblige the Member States to abolish the total prohibitions of commercial communications and multidisciplinary activities[165] and prohibit the duplication of the requirements concerning the professional liability insurance.

Also the provisions on administrative cooperation, though simplified and conferring more powers to the host state than it was envisaged in the First draft, continue to form one of the main parts of the Directive.

Furthermore, following the proposal of the EP, the Commission removed the provisions on administrative simplification from the Chapter on the freedom of establishment and composed a separate Chapter which applies to the freedom to provide services as well. Member States have been obliged to examine and, if necessary, simplify administrative procedures applicable to the access to and exercise of service activities. However, it is not specified what exactly the Member States should do. There is no duty to report to the

[163] For an opinion that presently, art. 49 EC does not affect the application of national labour law as long as it is non-discriminatory, see N. Brun "The proposed directive on services and labour law" in R. Blanpein (ed.) "Freedom of services in the European Union; Labour and Social Security Law: the Bolkenstein Initiative" Bulletin of Comparative Labour Relations, Kluwer Law International 2006, p. 19-35.

[164] See recitals 6, 6g, 41a, 41b and articles 1.6, 3.1.b, 16.3 and 17.

[165] With the exception of regulated professions, in so far as is justified in order to guarantee compliance with the rules governing professional ethics and conduct and it is necessary to ensure their independence and impartiality; and with the exception of the providers of certification, accreditation, technical monitoring, test or trial services in so far as is justified in order to ensure their independence and impartiality.

Commission effects of the examination or reasons for leaving specific requirements in force. In result, if asked, national authorities may simply state that their procedures do not require simplification. The Directive is more precise only in relation to two matters. First, it prohibits the imposition of an obligation to produce a document confirming the compliance with national requirements in its original form, certified copy or certified translation unless it is justified by the overriding reasons relating to the public interest or expressly permitted by another Community instruments. Second, Member States are obliged to create the points of single contact where it will be possible, also by electronic means, to complete all procedures and receive useful information.

3. Overall evaluation of the compromise version of the proposal

Summarising, the compromise proposal presented by the Commission follows the same aim as the original First draft, namely the establishment of general legal framework regulating the cross-border provision of services.

Unfortunately, the most important provisions, namely articles 16 to 19 ('freedom to provide services' and derogations thereof), are rather a source of confusion than a solid foundation of the system. The nomenclature used suggests that the freedom to provide services, as it stands at present, has been codified. Meanwhile, a simple comparison of the Directive and rules described in the First Chapter of this paper, shows that this is not the case. The seemingly 'radical' limitation of Member States' discretion in relation to acceptable justifications of national requirements hindering the exercise of the freedom, after close examination, no longer appears to be so significant. Moreover, the fact that already in the article on the freedom itself a possibility of introducing restrictive requirements is envisaged (article 16.2) results in a serious inconstancy. In effect, the derogations listed in articles 17 and 19 do not constitute an exception to the rule, but to the exception within it, as they provide different means of introducing restrictions than these envisaged in article 16 itself. Additionally, as was explained in the previous point, the actual scope and effect of application of these derogations is not clear either.

Nevertheless, there is still a chance that even in this 'mutilated' form the Directive will actually improve the situation of service providers and recipients.

First of all, the sole fact of harmonisation will force the Member States to finally adopt comprehensive legislative acts regulating the cross-border provision of services. During

the process of implementation and subsequently, due to the interpretation of the Directive delivered by the Court in preliminary rulings, a system of clear rules should emerge. They may not be as far-reaching as the ECJ's case law, but at least there will be a basis to build upon. Most importantly, the service providers will no longer be treated like permanently established entrepreneurs.[166] Also the specific prohibitions included in the Directive (e.g. of total ban on commercial communications or of the establishment requirement) will improve the enforcement of the freedom, as the Commission will insist on their clear transposition in national legal acts and the providers (recipients) will no longer be safeguarded only by general clauses.

Second, through the creation of the system of administrative cooperation,[167] the mutual trust (and mutual control) and the flow of information between the Member States will be improved. This in turn, should cause the reduction of restrictions imposed by mal-informed or arbitrary national authorities. The tighter the links between national authorities, the more difficult it will be to hide or even explain barriers to the free movement.

4. Conclusions

Altogether, this Directive targets the enforcement problems rather than further liberalises the European services market. This conclusion shows the derogations from the scope of the Directive (article 2.2 and 2.3) in a different light. While the transport and financial services have always, pursuant to article 51 EC, been subject to separate rules, there is no such simple explanation for other derogations.[168] It seems that in relation to the remaining activities the Member States strive to retain the *satus quo*, fearing the scrutiny of close cooperation. This in turn suggests that there are still many barriers that Member States are aware of and unwilling to eliminate. Nevertheless, even in this severely limited shape, the

[166] For example in Polish law, the notion of cross-border provision of services in principle does not exist. The only exceptions relate to specific professions or activities (e.g. lawyers) where sectoral harmonisation had to be transposed into national legal order.

[167] For an opinion that the provisions on administrative cooperation seem to fail the proportionality requirement see the Research Report of W. Gekiere Institute for European Law "Towards a European Directive on services in the Internal Market: Analysing the Legal repercussions of the Draft Services Directive and its Impact on National Services Regulations" Catholic University of Leuven, 24.9.2004, point II C.

[168] With the exception of electronic communication services and networks with respect to matters covered by Directives 2002/19, 2002/20, 2002/21, 2002/22 and 2002/58. It seems however, that this exclusion is unnecessary because in article 3 it is clearly stated that other Community instruments regulating specific sectors or provisions shall prevail over the Services Directive.

Directive can still contribute to the liberalisation of the services market. As long as it is treated not as a codification of the state of affairs, but as a starting point – a basis for cooperation that would facilitate the realisation of the Internal Market and enhance the mutual trust. Hopefully, in result a new harmonisation will take place. Until then, it should be remembered that the freedom cannot be limited through harmonisation; exclusion of some sectors or rights from the Directive or their restrictive codification does not influence the fact that the Treaty provisions on the freedom to provide services, as interpreted by the Court, continue to apply to them.

CHAPTER FIVE

CONCLUSIONS

Should the Commission's initiative be regarded as a failure? Surely, to some the compromise version may appear to be only a sad caricature of the bold Bolkenstein's Directive. After the elimination of the COP and deletion of articles on the posting of workers and on the assumption of health care costs, practically only a skeleton deprived of a body has remained. Furthermore, even this skeleton is not complete as there are huge gaps left by the numerous derogations and inconsistencies. This picture looks even worse when the comparison is made with the case law of the Court. The latest proposal hardly takes into account the evolution that the freedom to provide services has undergone through the creative interpretation of the ECJ. If the Directive attempted to codify the jurisprudential developments, it has clearly failed to attain this goal. Nevertheless, even in this restricted form it is capable of having an added value. As can be seen from the First Chapter the scope of the freedom is already very broad, much broader, I guess, than the drafters of the Treaty have ever planned. The Member States already find it hard to agree with the interpretation provided by the Court and it could not be expected that they would consent to going even further. The real problem lies in the enforcement of the rules already established. Surely, the easiest solution would be to write each one of them down in an act of secondary law. As the experience with the Service Directive shows, it is not possible to do so in a single horizontal act. Member States and lobbying groups may not have much saying in the outcome of ECJ's rulings, but they definitely can influence the contents of a directive. In result, only the basic and the least controversial principles of the freedom, supported by a system of administrative cooperation, have been included in the final draft. Although the scope of the freedom itself could not be limited through restrictive harmonisation, apparently it was hoped that its full application can be hindered. However, as it was argued in the previous Chapter, even in this reduced shape the Directive is capable of improving the effectiveness of the enforcement and not only in relation to matters covered. There is a good chance for a 'spill over' effect due to the system established; the Commission will be able to monitor more closely the situation in the Member States. The national authorities should keep a check on each other as well. It can be also expected that the close cooperation will be taken into account by the Court when it considers national requirements, making it more difficult in the future to justify

restrictions on the freedom.[169] It is a modest improvement in comparison with ambitious plans but the debate about the Services Directive shows that the Member States are not ready yet for more radical steps. Even though the independent studies prove that the broader the scope of liberalisation the more beneficial it would be for national economies,[170] the threat of 'social dumping' successfully counterbalances the economic arguments. It seems that neither the Member States nor their citizens could sustain the cumulated pressure of latest EU initiatives. The enlargement, Constitutional Treaty and Services Directive were simply too much to face all at once. While the enlargement has succeeded it contributed to the problems encountered by the remaining two initiatives. In the exclusive club of fifteen, the Member States already felt quite 'comfortable' with each other, the new members with their low labour costs and social standards brought in a factor of uncertainty. The purely economic arguments are no longer sufficient as the postulate of strengthening the social dimension of the European integration gains an increasing support.[171] Altogether, the Member States are not so much unable as unwilling to catch up with the progressive case law of the Court. In these circumstances it can be expected that the Commission will come back to the method of sectoral harmonisation. Thus allowing the Member States to negotiate each matter separately and to introduce safeguards they reckon suitable for a given kind of activity. Private security services, assumption of health care costs, gambling, and the SGEI are only some of the likely candidates for a legislative action at the Community level. Only when the sensitive issues are covered and enough time passes to establish mutual trust in each other's laws, enforcement and supervision, there is a chance that the Service Directive will be revised and updated. Hopefully, by the time this slow and painstaking process ends, it will not be too late to resume the 'competitiveness race' with the rest of the world.

[169] See Joined Cases 369 and 376/96 *Arblade* [1999] ECR I-8453, par. 61-62 and 79.
[170] See the Impact assessment in Chapter Two, point eight of this paper.
[171] For an opinion that with the evolution of the Community the interplay between the economic policy, social policy and politics becomes greater see M. Wise and R. Gibb "Single Market to Social Europe; The European Community in the 1990s" Insights on Contemporary Issues, Longman Scientific and Technical 1993, p. 281. For a description of historical developments in this respect see A M. Williams "The European Community; The contradictions of integration" The Institute of British Geographers, Studies in Geography, Blackwell Oxford UK and Cambridge USA 1991.

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