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Territoriality in EU (taxation) law: A sacred principle, or dépassé?

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“[T]he first and foremost restriction imposed by international law upon a State is that – failing the existence of a permissive rule to the contrary – it may not exercise its power in any form in the territory of another State.”


“The European Union must respect international law in the exercise of its powers...” Case C-286/90 Poulsen and Diva Navigation, paragraph 9

1. Introduction

Since the Peace Treaties of Osnabrück and Münster, of May and October 1648 respectively, the Westphalian notion that each State is sovereign over its own territory, with interaction between sovereign states to be determined by law, has been fundamental to the international legal order. Thus, the UN is, as its Charter proclaims, based on the principle of “sovereign equality” of all its Member States (Article 2(1), UN Charter).

The concepts of sovereignty, jurisdiction and territoriality are closely linked. One of the key features of the (traditional) concept of sovereignty is that it entails the right of the State to prescribe the laws in force, and to enforce those laws, on its own territory.¹ As Lord Macmillan famously expressed it in the UK House of Lords some 75 years ago,

“It is an essential attribute of the sovereignty of this realm, as of all sovereign independent States, that it should possess jurisdiction over all persons and things within its territorial limits and in all causes civil and criminal arising within these limits.”²

This positive concept of territoriality (power to make laws for one’s territory) has the logical negative corollary as expressed in the excerpt from the Lotus above, i.e., in principle and in the absence of a permissive rule to the contrary, a State ought not to exercise jurisdiction in another State’s territory. Exercise of extra-territorial jurisdiction has, therefore, typically been treated with suspicion under international law doctrine.

At the same time, however, States and regions have increasingly been faced with global problems which do not respect traditional State boundaries, and for which effective regulation may require (legal) solutions that transcend the State geographies we have become used to. Daniel Bethlehem

has rather provocatively termed this the “end of geography”: denoting the array of trans-border, geography-defying challenges which will, he argues, force us to move beyond our traditional notions of Westphalian States and international law, and with them our traditional concepts of sovereignty, jurisdiction and territoriality.\(^3\) These challenges include the globalisation of the economic system, trade and financial flows; the globalisation of security risks; as well as global warming and other environmental problems of a global scale.

Viewed in this light, it is perhaps unsurprising that an increasing number of States and entities that might normally (claim to) respect international law are being criticised for alleged extraterritorial exercise of jurisdiction. Among them is the EU, although it is by no means the only culprit in this regard.\(^4\) This contribution considers the relevance of territoriality as a restricting factor on the legislative jurisdiction of EU Member States, and the EU itself, with particular regard to EU tax law. Section 2 considers jurisdictional bases and conceptions of territoriality in international law. Section 3 switches to an EU law perspective, considering the status of customary international law in EU law. Section 4 considers the CJEU’s approach to territoriality as a justification for Member State action. Section 5 considers the CJEU’s approach to territoriality as a limitation on EU action, focusing on three examples of alleged extraterritorial exercise of jurisdiction by the EU in the past – in the fields of competition law, environmental law, data protection law, and financial markets law - and considers the legal and political responses to such exercise. Section 6 considers the case of the proposed Financial Transaction Tax (FTT), and the objections linked to territoriality concerns. Section 7 concludes with a discussion.

2. Jurisdictional bases and conceptions of territoriality in international law

   a. Jurisdictional bases in international law, and their legal status

As Lord MacMillan’s statement suggests, a distinction must be made between the types of jurisdiction of the State under international law, namely, prescriptive jurisdiction (i.e., the jurisdiction to legislate), adjudicative jurisdiction and enforcement jurisdiction. This chapter is concerned with the limits of the EU’s prescriptive jurisdiction, so neither adjudicative nor enforcement jurisdiction will be treated (although, as discussed below, one of the challenges posed by extraterritorial exercise of prescriptive jurisdiction may well be enforcement).

In terms of prescriptive jurisdiction, Lord Macmillan’s statement remains largely correct in modern international law. Thus, territoriality, or the “territorial principle” as it is often known in

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\(^3\) D. Bethlehem, “The end of geography: the changing nature of the international system and the challenge to international law” (2014) *EJIL* 9. See similarly, G. Handl, “Extra-territoriality and transnational legal authority” in G. Handl, J. Zekoll and P. Zumbansen (eds.), *Beyond Territoriality: Transnational Legal Authority in an Age of Globalisation* (Leiden, Martinus Nijhoff, 2012), noting that globalisation brings with it a “fundamental change in time and space dimensions of human existence” which “brings into sharp relief a growing discrepancy between the transnational, indeed, non-territorial nature of the problems and challenges posed by interconnectedness in a globalised world and traditional state-based, i.e., territorially focused, legal tools, structures and processes to manage interdependence” (at p. 3).

\(^4\) In the economic sphere see, for instance, the example of the US’s Dodd-Frank rules on derivatives and clearing, discussed below. See E. Greene and I. Potiha, “Issues in the extraterritorial application of Dodd-Frank’s derivatives and clearing rules, the impact on global markets and the inevitability of cross-border and US domestic coordination” (2013) *Capital Markets Law Journal* (8) 4, 338. For examples of the trend towards the EU’s using legislative techniques to regulate conduct that occurs outside the EU’s own borders, and a suggested categorisation of such techniques, see J. Scott, “The New EU “Extraterritoriality”” (2014) 51 *Common Market Law Review* 1343.
international law, remains one of the fundamental legal bases of jurisdiction. Before turning to its meaning, it should be noted that territoriality is not, of course, the only basis of jurisdiction recognised by international law doctrine. Rather, it is now broadly accepted that State (prescriptive) jurisdiction may also arise under three other bases. First, States have a jurisdiction over their nationals, wherever they may be (the “nationality” or “personality” principle). Second, States have jurisdiction to act to protect their essential interests (the “protective” principle) – but this principle is narrowly interpreted to cover only the most serious threats to vital State interests. Third, States have jurisdiction to act in the face of a small category of particularly heinous crimes, such as genocide (the “universal” principle). States may also have additional rights to exercise jurisdiction derived from, for instance, specific Treaty provisions.

The golden principle running through these jurisdictional bases, or principles, has been summarised as follows: there must be some clear connecting factor, or linking point, between the legislating State and the regulated conduct.

The key question in determining the legal status of a particular jurisdictional principle in international law is whether it has become sufficiently accepted as a matter of State practice to constitute customary international law. As is well-known, in order to constitute a binding rule of customary international law, the act must not only be settled State practice, but must also be

“such, or be carried out in such a way, as to be evidence of a belief that this practice is rendered obligatory by the existence of a rule of law requiring it”.

This second requirement, opinio juris sive necessitatis or subjective element, distinguishes customary international law from mere practices that, while not formally objected to, are not considered to constitute a rule of law. As regards the first requirement or objective element – settled State practice – it should be noted that it unnecessary for this purpose for all States to conform to the practice at issue. Rather, it is sufficient that,

“the conduct of States should, in general, be consistent with such rules, and that instances of State conduct inconsistent with a given rule should generally have been treated as breaches of that rule, not as indications of recognition of a new rule”.


Pursuant to the “passive personality” principle, this jurisdiction can also extend to assertions of prescriptive jurisdiction where the victim of an offence is a national of the State.

See for instance, in the US context, the Alien Tort Claims Act 1789, which provides that “district courts shall have original jurisdiction of any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States”. See recently, *Kiobel v Royal Dutch Petroleum* 621 F. 3d 111 (2010) 2d Cir (US).


*North Sea Continental Shelf*, Judgment, ICJ Reports 1969, p. 3, paragraph 77. See Article 38.1.b , Statute of the International Court of Justice.

These requirements are of relevance in considering the extent to which new or alternative (interpretations of) jurisdictional bases have gained the status of customary international law.

b. The territoriality principle

By far the most common basis for assertion of prescriptive jurisdiction is, however, the territorial principle. While the essence of the principle is clear – States have the right to pass laws within their own territorial limits – international law doctrine generally distinguishes between two variants of the principle, developed in recognition of the fact that not all elements of a given act may take place within a single territory.\(^{11}\)

The first variant, subjective territoriality, indicates prescriptive jurisdiction where a State applies its law to an incident initiated within its territory, but completed outside the territory (as with, for instance, the prosecution within a State where a bomb was loaded upon an aircraft, where the bomb exploded within another State’s airspace).

The second variant, objective territoriality, indicates jurisdiction exercised where an act is completed within the State, but was initiated in another State. An example is the famous *Lotus* case, decided by the PCIJ in 1927, where the *Lotus* – a French steamer - collided with a Turkish ship within Turkish territory.\(^{12}\) The PCIJ held that Turkey had validly exercised jurisdiction, reasoning on the basis of the objective territoriality principle.

Objective territoriality is uncontroversial in cases where there are distinct physical elements of an offence which have occurred within State territory. Difficulties have, however, arisen where certain elements of an offence involve not physical acts, but economic consequences or potential consequences. The classic example is the development of the “effects” doctrine, as initially developed in US antitrust law, discussed in detail below. The effects doctrine was usefully summarised by the Third Restatement of the Foreign Relations Law of the United States (1986), section 402 of which provides that a State has prescriptive jurisdiction over:

- conduct that, wholly or in substantial part, takes place within its territory; and
- conduct that takes place outside its territory, which has or is intended to have substantial effect within its territory.

Section 403(1), however, notes the existence of a reasonableness requirement in international (as opposed to US) law\(^{13}\) in relation to exercise of jurisdiction:

> “Even when one of the bases for jurisdiction under section 402 is present, a state may not exercise jurisdiction to prescribe law with respect to a person or activity having connections with another state when the exercise of such jurisdiction is unreasonable”.

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\(^{11}\) See generally, Crawford, *op. cit*. The international law doctrine of territoriality is, of course, far more complex and varied than can be reflected here. Our aim is the modest one of summarising the key features of international law doctrine of relevance to the present topic.

\(^{12}\) In fact, the collision took place within the high seas, but the PCIJ held that this could be assimilated to Turkish territory because the flag of the vessel hit was Turkish.

\(^{13}\) Importantly, the comment to section 403(1) states that this reasonableness requirement is a requirement of international law (rather than US domestic law).
Section 403(2) provides that reasonableness, in this sense, is to be evaluated by considering all relevant factors. While not exhaustive, the list of factors indicated is instructive for present purposes. It includes:

- the activity’s link to the regulating State’s territory,
- the connections between the regulating State and the person principally responsible for the activity to be regulated or between that State and those whom the regulation is designed to protect,
- the character of the activity to be regulated, the importance of regulation to the regulating state, the extent to which other states regulate such activities,
- the existence of justified expectations that might be protected or hurt by the regulation,
- the importance of the regulation to the international political, legal or economic system, and
- the likelihood of a conflict with regulation by another state.

While the “reasonableness” requirement has subsequently been rejected as a matter of US law by a number of US courts, the notion of a sufficient connecting factor is, as noted above, generally accepted to be key to the modern international law doctrine of jurisdiction, 14 and the factors listed in section 403(2) remain a useful summary of factors relevant to sufficiency in this context.

As regards the final factor, likelihood of a conflict with another State’s regulation, it should be added that, while concurrent and overlapping jurisdiction is of course accepted as a matter of international law, it is also broadly accepted that a proportionate approach should be adopted, such that nationals resident abroad should not be constrained to violate the law of the place of residence. 15

In light of this (necessarily brief) overview of the question of territoriality in international law, we turn now to consider the status and meaning of territoriality in EU law.

3. The status of customary international law in EU law

As the citation from Poulsen and Diva at the opening of this contribution indicates, the CJEU has held that the EU is bound by international law, including customary international law. In AATA, the CJEU used Article 3(5) TEU (inserted by the Treaty of Lisbon) to confirm this, holding that,

“when it adopts an act, [the EU] is bound to observe international law in its entirety, including customary international law, which is binding upon the institutions of the European Union”. 16

As a result, customary international law binds the EU and must be complied with in all EU actions. This is not to say, of course, that individuals have the right to reply on every rule of customary international law in reviewing the validity of EU acts: for such right to exist, 17

- The rule must be capable of calling into question the competence of the EU to adopt that act; and

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14 See, e.g., Crawford, op. cit., p.311; Mann, 111 Hague Recueil (1964, I) 44-51, 126.
15 Crawford, ibid, citing Oppenheim, i. 406.
17 AATA, op. cit, paragraph 107.
The act in question must be “liable to affect rights which the individual derives from European Union law or to create obligations under European Union law in his regard”.

However, in AATA, the CJEU specified that the standard of review for compliance with rules of customary international law was less intense than, for instance, review for compliance with a (precise) rule of an international agreement,

“Since a principle of customary international law does not have the same degree of precision as a provision of an international agreement, judicial review must necessarily be limited to the question whether, in adopting the act in question, the institutions of the European Union made manifest errors of assessment concerning the conditions for applying those principles.”

As an aside, this reasoning is, on its face, rather curious given the wide variety of rules of customary international law (which may be more, or less, specific), and the equally wide variety of provisions of international agreements. What may in fact be underlying this part of the judgment is not really some necessary distinction of content between customary international rules and rules of international agreements, but perhaps a distinction in recognition of their existence and binding force, i.e., the very recognition of a rule as a binding rule of customary international law is often contested and unclear.

While this is a fair point, it does not really justify a lower standard of review for those rules of customary international law which (the CJEU accepts) are recognised as binding. As Advocate General Kokott reasoned in her Opinion in AATA, there would seem no good logical reason for a difference of approach per se to customary international law and international agreements, given that many principles of customary international law have now been codified in agreements. It is of interest, however, that the Advocate General ultimately reached the same outcome on the facts in that case by different legal means, reasoning the customary international law rules at stake could not in any event be relied upon by individual claimants, due to their “nature and broad logic” – whereas the CJEU had accepted that the rules could in principle have direct effect. In reality, therefore, on the facts of that case the CJEU’s approach gave greater effect to customary international law.

Leaving this debate aside, it is clear that the AATA manifest error standard now governs judicial review for compliance with customary international law in the EU legal order.

4. Territoriality as a justification for Member State action

Member States have frequently invoked the territoriality principle in tax cases before the CJEU, particularly in cases involving the application of the EU free movement rules to national direct tax measures. The CJEU has made frequent reference to the “fiscal” principle of territoriality, and has accepted the principle subject to certain conditions, although its approach has changed somewhat over the years.

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18 AATA, op. cit., paragraph 110.
19 AATA, Opinion, paragraphs 111-112.
In *Future Participations*, the fiscal principle of territoriality was famously relied on by the CJEU in a case concerning Luxembourg’s distinction between residents and non-residents in allowing losses to be carried over. The CJEU reasoned:

“Luxembourg Law provides that, as regards resident taxpayers, all of their income is taxable, the basis of assessment to tax not being limited to their Luxembourg activities. Consequently, although there are exemptions under which a part or event, in certain cases, all of their income earned outside Luxembourg is not subject to tax in that country, the basis for assessment for resident taxpayers at any rate includes profits and losses arising from their Luxembourg activities.

On the other hand, for the purpose of calculating the basis for assessment for non-resident taxpayers, only profits and losses arising from their Luxembourg activities are taken into account in calculating the tax payable by them in the State.

Such a system, which is in conformity with the fiscal principle of territoriality, cannot be regarded as entailing any discrimination, overt or covert, prohibited by the Treaty.”

In other words, the CJEU effectively here relies on territoriality to justify its basic acceptance of a difference in treatment of residents and non-residents, in exercise of Member State tax jurisdiction, and the distinction between world-wide and source State taxation in that context.

Since *Futura*, the CJEU has refined its use of the territoriality principle as its case-law on direct taxation has matured and developed in subtlety over the past 10 years or so (in circumstances where Member States have sought to invoke the principle to justify differences of treatment of taxpayers in virtually every case). It is clear from this case-law that territoriality may, in certain conditions and if the measure at issue is proportionate, justify *prima facie* restrictions on free movement. In particular, the CJEU’s reasoning on territoriality is often bundled with its reasoning on the notion of a “balanced allocation of taxation powers”, which has been accepted as a justification for State measures in a similar way.

Thus, in *Marks & Spencer*, in relation to group relief of cross-border losses of subsidiaries, the CJEU rejected the territoriality-based argument that the distinction between residents and non-residents could in itself justify a difference in treatment, reasoning that the question of justification depended on consideration of “each specific situation”, and whether the fact that that a tax advantage was available solely to residents was based on “relevant objective elements apt to justify the difference in treatment”.

In this context, the CJEU famously accepted the UK’s argument that symmetric treatment of profits and losses was necessary to preserve the balanced allocation of the power to impose taxes between Member States, and to reduce the risk that cross-border losses would be used twice. However, the measure at issue must be proportionate to those justifications.

It is of note that Advocate General Maduro’s Opinion considered the relevance of territoriality in some detail, rejecting the UK’s understanding of the principle of territoriality, ruling that the “precise meaning” of the principle in EU law was that the Court,

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22 Case C-446/03 Marks & Spencer ECLI:EU:C:2005:763, paragraph 38.
“thereby recognises merely the need to take account of constraints resulting from the fact that Member States are equally sovereign in tax matters. Those constraints require each Member State to reach an accommodation with States enjoying equal sovereignty in tax matters.”

The Advocate General viewed territoriality as primarily a rule of priority preventing conflicts in tax jurisdiction between the Member States, but was clear that territoriality could not “be invoked to enable the Member States to evade their obligations under Community law.”

This understanding of the meaning and function of territoriality has been present, albeit with varying emphases, in subsequent CJEU judgments. Thus, in Busley, the CJEU summarised the purpose of the fiscal territoriality principle as “to establish, in the application of Community law, the need to take into account the limits on the Member States’ powers of taxation”.

In Oy, the CJEU expanded on Marks & Spencer on this issue, in a case concerning restrictions on deductibility of transfers from a resident subsidiary to a non-resident parent company. In response to territoriality arguments, the CJEU emphasised its consistent case-law that, in the absence of harmonising EU measures, “Member States retain the power to define, by treaty or unilaterally the criteria for allocating their powers of taxation”. Applying its previous case-law, the CJEU held that the justification of safeguarding a balanced allocation of taxation powers may be allowed where the “system in question is designed to prevent conduct capable of jeopardising the right of the Member States to exercise their taxing powers in relation to activities carried on in their territory”. In that case, as with Marks & Spencer, the justification applied in principle because there was a risk that groups could exercise their discretion organise themselves “by means of purely artificial arrangements” to avoid tax by choosing freely the Member State in which their profits would be taxed.

Further, the Finnish rule was proportionate to that justification, as there was no less restrictive means of achieving the same aim.

The CJEU’s approach in Marks & Spencer may be contrasted with its outright rejection of territoriality as a valid justification in cases like Manninen, in the case of Finland’s failure to grant a tax credit to a resident taxpayer in respect of dividends paid by non-resident companies. In that case, the CJEU chose to base its substantive reasoning on the Bachmann/cohesion justification put forward by Finland, developing the requirement of a direct link between the tax advantage and the offsetting of the advantage.

Territoriality has also featured prominently in the CJEU’s judgments on exit taxes. In N, which concerned an exit tax on unrealised capital gains in individuals’ shareholdings, and followed Marks & Spencer, the CJEU relied on territoriality and the balanced allocation of powers between Member States in finding that the restriction resulting from the exit tax pursued an objective in the public

24 Case C-446/03 Marks & Spencer, op. cit., paragraph 60.
25 Case C-35/08 Busley ECLI:EU:C:2009:625, paragraph 30. Contrast, for instance, Case C-250/08 Commission v Belgium ECLI:EU:C:2011:793 (registration duties on purchase of principal residence), where Belgium used a slightly different meaning of territoriality, namely, the notion that independent tax systems “coexist without a hierarchy between them” (i.e., the idea of parallel exercise of taxation powers, as accepted in e.g., Case C-374/04 Test Claims in Class IV of the ACT Group Litigation ECLI:EU:C:2006:773), although the CJEU considered it effectively as a cohesion argument.
26 Case C-231/05 Oy ECLI:EU:C:2007:439, paragraphs 58-60.
27 Case C-319/02 Manninen ECLI:EU:C:2004:484, paragraphs 38-39.
interest and was appropriate for ensuring the attainment of that objective.\footnote{28 Case C-470/04 N ECLI:EU:C:2006:525, paragraph 47.} However, the final element of proportionality – whether a measure goes beyond what is necessary to attain the objective pursued – was not satisfied in circumstances where certain features of the tax (e.g., the obligation to provide guarantees) went beyond the requirements of territoriality,\footnote{29 \textit{Ibid}, paragraph 51.} especially given the existence of relevant mutual assistance Directives.

Similarly, in \textit{National Grid Indus}, which concerned the Dutch rules taxing unrealised capital gains upon transfer of the place of effective management of a company to the UK, the CJEU was clear that, as per \textit{N}, exit taxes as such were justified by the principle of fiscal territoriality “\textit{linked to a temporal component, namely the taxpayer’s residence for tax purposes within national territory during the period in which the capital gains arise}”, such that a Member State is entitled to charge tax on those gains at the time when the taxpayer leaves the country. The fact that the capital gains being taxed were unrealised did not affect the fact that they had arisen in the Netherlands. However, as to proportionality, a requirement of immediate recovery went beyond what was necessary in that context.\footnote{30 Case C-371/10 \textit{National Grid Indus} ECLI:EU:C:2011:785, esp. paragraphs 45-48. See similarly, Case C-269/09 \textit{Commission v Spain} ECLI:EU:C:2012:439; Case C-380/11 \textit{Dl. VI. Finanziaria} ECLI:EU:C:2012:552 (territoriality considered and rejected by the CJEU reformulated as balanced allocation of powers and cohesion arguments).}

Overall, therefore, the principle of “fiscal” territoriality is clearly accepted by the CJEU as relevant and even as binding the EU in these tax cases, but it has not given Member States a free pass to avoid the application of the free movement provisions. Broadly speaking, the CJEU tends to use the principle to indicate a basic acceptance that Member States’ taxation powers are limited, and that Member States’ tax systems co-exist side-by-side and apply in parallel, subject to bilateral agreements. As such, the fiscal territoriality principle as applied by the CJEU is essentially a specialised form of the wider territoriality principle in international law.

Nonetheless, the way in which the CJEU refers to fiscal territoriality has changed considerably in recent years. In \textit{Futura Participations}, the CJEU used the principle almost as a proxy for the fundamental difference between home State and source State taxation, and the principle’s justificatory potential for difference of treatment between residents and non-residents appeared to be immense. In later cases such as \textit{Marks & Spencer, Oy} and \textit{National Grid Indus}, however, the CJEU made it very clear that, in the free movement context, the territoriality principle is effectively translated into the specific justifications developed by the CJEU, namely, the balanced allocation of taxation powers, the cohesion of the tax system, and even the need to counter tax avoidance. (Indeed, the distinction between these justifications has at times been difficult to discern, although to some extent this may simply reflect the way in which the case was argued by the Member State at issue, rather than any principled difference in scope of application of the justifications.\footnote{31 Contrast, for instance, Case C-42/10 \textit{Commission v Finland} ECLI:EU:C:2011:253 (Finland used territoriality arguments in a basic \textit{Futura Participations} manner, \textit{i.e.}, to justify a difference of treatment of non-resident and resident pension funds as regards taxation of dividends; argument was reformulated by the CJEU as a cohesion argument); Case C-350/11 \textit{Argenta Spaarbank} ECLI:EU:C:2013:447 (Belgium’s territoriality argument dealt with cohesion and preservation of balanced allocation of powers issues); Case C-164/12 \textit{DMC} ECLI:EU:C:2014:20 (German territoriality argument dealt with as issue of balanced allocation of powers alone).})
In other words, Member States have won and lost their arguments not on the basis of recourse to the principle of territoriality as such, but by reference to the detail of the CJEU’s conditions of applicability of the justification at issue. In this way, the CJEU has repackaged Member State (international law) territoriality arguments into its own (EU law) formulas, which instantly gives the CJEU greater freedom to define the boundaries of these formulas in a way that is (more) consistent with the rest of its internal market case-law. This illustrates the open-textured nature of the territoriality principle – it can mean different things to different actors, at different points in time, and it has certainly not been a silver bullet for Member States seeking to justify differential tax rules.

5. Territoriality as a limiting factor for EU action

a. The case of competition law

Competition law is of course one of the oldest examples of successful assertion of what was effectively extraterritorial jurisdiction of State economic laws, beginning in the US in the 1940s and reciprocated, albeit in different terms, in the EU some 40 years later. As detailed below, the US and EU effectively developed new versions of the territoriality principle to deal with the problem of the need to protect their markets from global cartels. However, this has not prevented widespread objection from other States, in political but also legal form.

i. The effects doctrine in the US, and international responses

The notion of extra-territorial jurisdiction in competition law was first developed judicially in the US in 1945. In Alcoa, the US asserted jurisdiction over a cartel of European and Canadian aluminium producers, on the basis that the cartel was intended to, and did, affect imports and exports to the US. In a controversial ruling, Justice Hand held that,

> “it is settled law (...) that any state may impose liabilities, even on persons not within its allegiance, for conduct outside its borders that has consequences within its borders which the state reprehends; and these liabilities other states will ordinarily recognize.”

Despite the fact that Alcoa was widely perceived internationally as the extra-territorial application of US antitrust law – in circumstances where virtually no other States had anything resembling an antitrust law at the time – the US courts subsequently extended the doctrine even further, dispensing with a requirement that effects within the US should be intended in cases such as Incandescent Lamp and Swiss Watchmakers. The high point was the Uranium Antitrust litigation, where uranium producers in a number of non-US States (including the UK, Australia and France) formed a cartel, with the knowledge or encouragement of their national governments, to maintain the global market price of uranium. In private litigation brought by Westinghouse, which alleged it had been damaged by the cartel, the US Court of Appeals accepted jurisdiction despite the fact that

32 United States v Aluminium Company of America, 148 F. 2d 416 (2nd Cir. 1945), at 443.
the only link with the US was the cartel’s effect in the US, and despite the fact that there had been no intraterritorial conduct at all.\textsuperscript{34}

This controversial extension of jurisdiction to extraterritorial conduct (albeit with intraterritorial effects) led to the enactment, by a large number of States, of legislation specifically blocking the enforcement of foreign antitrust laws. These blocking statutes ranged from preventing access by foreign antitrust authorities to domestic records, to declaring foreign antitrust judgments/decisions to be unenforceable, to allowing the recovery of damages paid. For instance, the UK’s Protection of Trading Interests Act 1980, gives the UK Secretary of State discretion to prohibit compliance with foreign discovery orders; the French Law No. 8-538 of 16 July 1980 prohibits compliance with foreign discovery orders, subject to the requirements of international agreements.

From the company’s perspective, such legislation raises the obvious problem of deciding which law to comply with if faced, for instance, with a discovery order of a US court. In cases of non-compliance, such companies may plead by way of defence that they were obliged by foreign law not to comply with discovery orders of US courts, subject to the parameters of the foreign state compulsion defence in US law.\textsuperscript{35} Nonetheless, this undoubtedly gave rise to uncertainty, compounded by the fact that certain US courts rejected a strict effects-based test, in favour of a jurisdictional rule of reason whereby foreign State interests must be balanced with the interest in US antitrust enforcement on a case-by-case basis (see the judgment of Judge Choy in \textit{Timberlane}, and the judgment of Judge Adams in \textit{Mannington}, for instance).\textsuperscript{36}

In practice, the blocking statutes have never been frequently invoked in discrete cases, but have not been repealed and remain good law in most jurisdictions. Perhaps their more important function has been at the political level, in signalling that extra-territorial enforcement of US antitrust laws in this manner is widely regarded as unacceptable by the international community. Specifically, they led to the passing of the US Foreign Trade Antitrust Improvements Act of 1982 (FTAIA) provides that the Sherman Act “shall not apply to conduct involving trade or commerce … with foreign nations,” but contains exceptions for conduct that significantly harms imports, domestic commerce, or American exporters.\textsuperscript{37} This was subsequently broadly reflected in the 1986 Foreign Relations Law Restatement, discussed above, which stated that, as a matter of international law, a reasonableness requirement applied in the context of effects-based claims to jurisdiction.

A reasonableness approach has been applied by the US courts in cases such as \textit{Hartford Fire Insurance}, albeit confined to situations where there is an express jurisdictional clash obliging parties to act in a contradictory manner (a “true conflict”).\textsuperscript{38} In \textit{Empagran}, the US Supreme Court limited the effects doctrine in US law somewhat in holding that, where price-fixing conduct significantly and adversely affected both customers outside and within the United States, but the adverse foreign

\begin{itemize}
\item \textsuperscript{34} \textit{In re Uranium Antitrust Litigation}, 617 F. 2d 1248, 1250-1251 (7\textsuperscript{th} Cir. 1980).
\item \textsuperscript{35} See Restatement of the Law (Third): Foreign Relations Law of the United States, para 442.
\item \textsuperscript{36} \textit{Timberlane Lumber Co. v. Bank of America} N.T. & S.A 549 F.2D 597 (9th Cir. 1976); \textit{Mannington Mills, Inc. v Congoleum Corp.}, 595 F.2d 1287 (3rd Cir. 1979).
\item \textsuperscript{38} \textit{Hartford Fire Insurance v California}, 509 U.S. 764 (1993).
\end{itemize}
effect was independent of any adverse domestic effect, the FTAIA exception did not apply, and thus, neither did the Sherman Act, to a claim based solely on the foreign effect.

As the number of States with competition laws has increased dramatically in the past years, so too has the number of States using the effects doctrine as a jurisdictional base for these laws. China’s competition law, for instance, applies to “the conducts outside the territory of the People’s Republic of China if they eliminate or have restrictive effect on competition on the domestic market of the PRC.” Ultimately, however, the international community has generally recognised the problems with responding to jurisdictional conflicts in antitrust by means of blocking statutes. The response has been a greater level of harmonisation in antitrust laws globally, combined with the development of a network of bilateral and multilateral agreements promoting comity between antitrust enforcers, and the development of networks aimed at achieving similar goals. At international level, the largest of these networks is the International Competition Network, which aims inter alia to formulate proposals for procedural and substantive convergence in competition laws globally. 39

ii. The EU’s implementation and qualified effects doctrines

In Woodpulp I, the CJEU established what remains the key test of jurisdictional basis of EU competition law, namely, that EU competition law applies if an anti-competitive practice is implemented within the EU. That case concerned a cartel between non-EU wood pulp producers, in circumstances where the supply of wood pulp was a global market. In holding that EU competition law applied, the CJEU rejected the applicants’ argument that this was contrary to international law on the grounds that jurisdiction was founded solely on the economic effects within the EU of conduct that took place outside the EU, reasoning that an infringement of (what is now) Article 101 TFEU, “consists of conduct made up of two elements, the formation of the agreement, decision or concerted practice and the implementation thereof. If the applicability of prohibitions laid down under competition law were made to depend on the place where the agreement, decision or concerted practice was formed, the result would obviously be to give undertakings an easy means of evading those prohibitions. The decisive factor is therefore the place where it is implemented.

The producers in this case implemented their pricing agreement within the common market. It is immaterial in that respect whether or not they had recourse to subsidiaries, agents, sub-agents, or branches within the Community in order to make their contacts with purchasers within the Community.

Accordingly the Community’s jurisdiction to apply its competition rules to such conduct is covered by the territoriality principle as universally recognized in public international law. 40

It was, therefore, decisive to the Court’s reasoning that implementation of the conduct was a necessary constituent element of a breach of Article 101 TFEU. The CJEU also expressly rejected the

39 See generally, I. Maher, “Transnational Legal Authority in Competition Law and Governance: Territoriality, Commonality and Networks” in Handl, Zekoll and Zumbansen (eds), op. cit.
applicability of any principle of non-interference in international law, as US law (in that case, the Webb Pomerene Act) permitted export cartels (i.e., cartels which took effect solely outside the US), but did not require companies to form them. Further, the CJEU rejected arguments that such a result breached international comity requirements, on the basis that this would call into question the EU’s jurisdiction to apply its competition rules.\footnote{Paragraphs 19 – 22.}

In \textit{Gencor}, the General Court developed an alternative basis of jurisdiction in the merger context by ruling that application of the EU merger control rules was justified under international law when it was foreseeable that a proposed concentration would have an immediate and substantial effect in the EU (the “qualified effects” doctrine).\footnote{Case T-102/96 \textit{Gencor} ECLI:EU:T:1999:65.} In that case, this criterion was satisfied by mere sale within the EU of the product which was the subject of the agreement, irrespective of the local of the sources of supply and the production plant (which were located in South Africa).\footnote{Paragraph 87.} As has since been clarified in \textit{InnoLux},\footnote{Case T-91/11 \textit{Innolux} ECLI:EU:T:2014:92.} \textit{Gencor} does not cast doubt on \textit{Wood Pulp I}, and it is sufficient if cartelised products are sold within the EEA in order for EU competition rules to apply. Further, implementation of a cartel does not require actual impact on prices, or proof that cartel participants adhered to pricing decisions.\footnote{Paragraph 66.}

In \textit{Intel}, the General Court further considered the matter in the context of alleged abuse of a dominant position contrary to Article 102 TFEU in the form of, inter alia, rebates, clarifying that the implementation (\textit{Woodpulp I}) and qualified effects (\textit{Gencor}) tests were alternatives (and not cumulative).\footnote{Case T-286/09 \textit{Intel} ECLI:EU:T:2014:547 paragraphs 231-233, 244.} Further, the General Court clarified that the qualified effects test did not require actual effects, but required only that it be,

\begin{quote}
“sufficiently probable that the agreement at issue is capable of having a more than insignificant influence [in the EU].”\footnote{Paragraph 257.}
\end{quote}

Further, the General Court rejected the argument that direct sales into the EU were necessary in order to fulfil the implementation test (see similarly, its judgment in \textit{InnoLux}).\footnote{The General Court also considered whether the EU’s own jurisdictional test for the applicability of EU competition law, namely effect on inter-State trade, had been met. This is distinct from the question of the jurisdictional requirements of international law, and is not discussed here.}

For these reasons, the General Court rejected Intel’s argument that the Commission was obliged to establish a direct causal connection with the EU’s territory, by showing actual implementation of the conduct leading to a substantial effect on competition within the EU.

Finally, in \textit{Nexans}, the General Court rejected the argument that the Commission was prevented by the principle of territoriality from examining documents in a dawn raid relating to non-EU markets. The Court reasoned that jurisdiction was sufficiently established if the investigation was carried out
in order to detect conduct liable to affect trade between Member States and which has as its object or effect the prevention, restriction or distortion of competition within the internal market.\(^{49}\)

In sum, therefore, it is clear that the CJEU’s doctrines of implementation and qualified effects in competition law are far-reaching, particularly given the clarification in \textit{Intel} of the meaning of qualified effects, such that no actual substantial effects in the EU territory need be shown for the EU to have territorial jurisdiction.

**b. The case of environmental law**

While pollution is a classically transfrontier problem, as a matter of public law\(^{50}\) the task of regulating pollution is typically left to the polluting State in environmental law, rather than the “victim” State suffering damage, applying a strict territoriality principle.\(^{51}\) A major reason for this in practice is the difficult of proving causation in the case of much transboundary pollution. However, the occurrence of a number of major and disastrous transboundary pollution events since the 1980s within Europe have changed the position somewhat – in particular, the 1986 nuclear accident in Chernobyl; the 1986 chemical fire at the Sandoz factory that polluted the river Rhine and, more recently, the 2010 Ajka alumina plant accident, causing a red mud slide in Hungary that seeped into the Danube. This has led, amongst other things, to the conclusion of a number of agreements imposing varieties of duties to protect other territories, such as the UNECE Convention on the Protection and Use of Transboundary Watercourses and International Lakes of 1992. Further, a principle of public participation and consultation in potentially pollutant transboundary projects has been established in, for instance, the EU’s Environmental Impact Assessment Directive and the UNECE Espoo Convention on Environmental Impact Assessment, as well as in the Environmental Liability Directive (Article 15).\(^{52}\)

Aside from these initiatives, in its 2008 judgment in \textit{Commune de Mesquer v Total France}, the Grand Chamber of the CJEU went further, taking not the place of the polluting event, but rather the place of the damage to the environment, as the relevant place of discharge in analysing whether the EU’s Waste Directive applied \textit{ratione loci}.\(^{53}\) In that case, which concerned compensation for the damage caused by the waste spread on the territory of the municipality of Mesquer following the sinking of the oil tanker Erika, the CJEU held that the place where the ship sank (not Member State territory, but rather its exclusive economic zone) was not determinative:

\begin{quote}
“Without there being any need to rule on the applicability of the directive at the place where the ship sank, it suffices to observe that the hydrocarbons thus accidentally spilled drifted
\end{quote}


\(^{50}\) As distinct from private international law, where Regulation 44/2001 provides that, by way of exception from the general rule that the defendant’s State courts have jurisdiction, the courts of the State in which the harmful event occurred have jurisdiction. This can mean either the place of the tortious conduct, or the place of damage (Case 21/76 \textit{Mines de potasse d’Alsace} ECLI:EU:C:1976:166). However, problems of proof of causation are, evidently, common.

\(^{51}\) See generally, E. Rehbinder, “Extra-territoriality of Pollution Control Laws” in Handl, Zekoll and Zumbansen (eds), \textit{op. cit.}.

\(^{52}\) [ ]

\(^{53}\) [ [Waste Directive]]
This approach formed the basis of the CJEU’s more controversial ruling in AATA, which concerned a challenge by a group of US airlines to the validity of the EU’s extension of its Emissions Trading Scheme (ETS) to aviation. As is well-known, the ETS was set up by Directive of 2003, and created the world’s largest greenhouse gas allowance trading scheme, based on the “cap and trade” principle. It obliges all installations covered by the scheme to surrender sufficient allowances each year to account for their GHG emissions in that period, thus placing a price on carbon. At least in its initial incarnation, the scheme applied to major industrial installations located within the territory of the EU/EEA (some 11,000 installations), primarily power plants and energy intensive plants. In 2008, however, a Directive was passed extending the scope of the ETS to cover commercial aviation operators. Specifically, the Directive provided that all aircraft operators must surrender allowances in relation to aviation activities defined as,

“all flights which arrive at or depart from an aerodrome situated in the territory of a Member State to which the Treaty applies”.

More controversially, however, the Directive obliged the allowances to be surrendered for such flights to be calculated on the basis of the whole of the international flight to be performed (in the case of EU departures) or that had been performed (in the case of arrivals).

The High Court of England and Wales referred a variety of questions on the validity of the Directive to the CJEU, including questions as to the compatibility of the Directive with international law principles that a State has “complete and exclusive sovereignty” over its airspace.

In upholding the Directive, the Grand Chamber of the CJEU was of the clear view that, as a matter of international law, the territoriality principle applied here, in the same way as in Woodpulp I and Commune de Mesquer (each of which it specifically cited). While the EU “must respect international law in the exercise of its powers”, the fact that the ETS applied to flights arriving at or departing from an EEA Member State fulfilled this requirement and did not infringe the principles of territoriality or sovereignty of third States’ airspace, because

“those aircraft are physically in the territory of one of the Member States of the European Union and are thus subject on that basis to the unlimited jurisdiction of the European Union.”

While this statement is uncontroversial, far more so is the CJEU’s rejection of the argument that the Directive could not validly require surrender of allowances representing the whole of an international flight (as opposed to, for instance, that part taking place in EEA airspace). Here, the CJEU relied upon the EU’s own aims in the field of environmental policy, namely, the Article 191(2) TFEU aim of ensuring a high level of protection of the environment, in reasoning that,

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54 Case C-188/07 ECLI:EU:C:2008:359, paragraph 61.
55 The personal scope of the Directive was effectively equivalent to that of the EU’s Industrial Prevention Pollution and Control (IPPC) Directive.
57 Case C-366/10, ECLI:EU:C:2011:864, paragraph 125.
“the European Union legislature may in principle choose to permit a commercial activity, in this case air transport, to be carried out in the territory of the European Union only on condition that operators comply with the criteria that have been established by the European Union and are designed to fulfil the environmental protection objectives which it has set for itself, in particular where those objectives follow on from an international agreement to which the European Union is a signatory, such as the [United Nations Framework Convention on Climate Change] and the Kyoto Protocol.

Furthermore, the fact that, in the context of applying European Union environmental legislation, certain matters contributing to the pollution of the air, sea or land territory of the Member States originate in an event which occurs partly outside that territory is not such as to call into question, in the light of the principles of customary international law capable of being relied upon in the main proceedings, the full applicability of European Union law in that territory...”

This mode of reasoning deserves comment on a number of grounds.

First, the CJEU is careful to characterise the applicability of the ETS as dependent on the aircraft operator’s own choice to operate a commercial air route arriving at or departing from an EEA airport. In other words, if you want to benefit from our market, you must do it on our terms. This is forceful reasoning, and uncontroversial if one considers the multitude of ways in which the EU’s standards are imposed on non-EU businesses seeking to market their products within the EU, for instance. However, it does not in itself answer the question of compatibility with international law. On that point, the CJEU relies firmly on the territoriality principle, implicitly in its subjective (in the case of departures from the EU) and objective (in the case of arrivals into the EU) forms.

Secondly, the CJEU’s reasoning in ATAA effectively rejects what are fundamentally international law –based arguments by interpreting territoriality in the light of the principles of the EU’s own legal order – here, the EU’s environmental goals as set out in the EU Treaties. In one sense, this is unsurprising, given the CJEU’s role as the constitutional court tasked with interpreting and applying the EU Treaties. Yet, from the international law perspective, this turns on its head the traditional hierarchy of laws, interpreting the (international law) principle of territoriality in light of the EU’s (regional) aims. As I argue below, this can be seen as a type of reverse interprétation conforme, and it raises obvious risks for fragmentation and inconsistency in international law concepts along regional lines.

In the aftermath to the ATAA judgment, however, the EU has in fact been forced to suspend the application of the ETS to international aviation activities, meaning that the scheme only applies to flights within Europe until 2016 (exemptions for operators with low emissions have also been introduced). Officially, the EU’s action was in response to the agreement, in October 2013, of the International Civil Aviation Organization (ICAO) Assembly to develop a global market-based mechanism to address international aviation emissions by 2016, and to apply it by 2020. As a matter of political reality, however, the EU’s action came in the wake of a refusal by States including China

58 Paragraphs 128-129.
59 Such as, for instance, the REACH standards for chemicals, etc. See for full discussion A. Bradford, The Brussels Effect (2012) 107(1) NWU Law Review 1.
to accept the ETS extension. Subsequently, the EU amended its legislation to derogate temporarily from the original scope of the 2008 Directive, such that, until 2016, only flights within the EEA are covered by the ETS. The AATA saga, therefore, is a stark illustration of the limits to the EU’s extraterritorial excursions, imposed not by law, but by political reality.

c. Data protection

A further rather controversial extension of the EU’s prescriptive (legislative) territorial jurisdiction has been in the field of data protection. By Article 4 of the EU’s Data Protection Directive, the EU data protection rules apply wherever (a) processing is carried out “in the context of the activities of an establishment of the controller on the territory of the Member State”; (b) where the controller is established in a place where a Member State national law applies by virtue of international public law; or (c) the controller is not established on EU territory but for the purposes of processing personal data “makes use of equipment” in a Member State territory (unless this is only used for transit purposes).

Article 4(c) represents a clear extraterritorial extension of the reach of the EU’s rules, particularly as the concept of making use of equipment has been interpreted broadly, with some interpreting it to include data collection through, for instance, placing cookies on individual personal computers located within the EU. However, as the CJEU’s judgment in Google Spain illustrates, Article 4(a) can also lead to extraterritorial effects. In that case, the CJEU rejected Google’s arguments that its Spanish subsidiary fell outside the scope of Article 4(a), because the subsidiary promoted and sold advertising space offered by Google, but did not itself carry out Google’s core business, i.e., the provision of search engine services. In so holding, the CJEU interpreted the concept of “activities” of an establishment broadly to include activities that are “inextricably linked”, albeit performed outside the EU’s territory. Importantly, the CJEU justified such broad interpretation by virtue of the risk that, without that, the effectiveness of the EU’s Data Protection Directive and the EU’s fundamental rights protection would be compromised. As with AATA, therefore, Google Spain shows the CJEU rejecting claims of extraterritoriality using arguments based on the fundamental principles of the EU’s own legal order. Further to the Google Spain judgment, the independent advisory Working Party set up under Article 29 of the Data Protection Directive recommended that the delisting of search results required by the judgment should not be confined to EU/EU Member State domain names, but should be effective on “all relevant domains, including.com”. However, Google has chosen to implement the judgment only in relation to its European-directed search engines (google.de, google.fr, etc), on the basis that over 95% of queries originating in Europe are on local

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61 Directive 95/46 on the protection of individuals with regards to the processing of personal data and on the free movement of such data OJ 1995 L 281/31.


63 Case C-131/12 Google Spain ECLI:EU:C:2014:317, paragraph 56.

64 Ibid, paragraph 58.

versions of the search engine. On 6 February 2015, an Advisory Council convened by Google released its own report on the judgment, which noted a majority support for Google’s approach to the geographic scope of the judgment on the ground that “there are competing interests that outweigh the additional protection afforded to the data subject” for search engines targeted at users outside of Europe, arguing that this position is bolstered by the “principles of proportionality and extraterritoriality in the application of European law.”

It should be noted that, under the Commission’s proposal for a new EU Data Protection Regulation, currently pending before the European Parliament and Council, the territorial scope of the EU’s rules would be reduced (and clarified) such that the EU’s rules apply to processing of personal data of EU residents by a controller not established in the EU where the processing activities are related to the offering of goods/services to EU residents, or the monitoring of their behaviour. However, the equivalent provision to current Article 4(a) of the Directive (proposed Article 3(1)) retains reference to the “activities” of the establishment in similar terms to the current version.

d. Financial markets regulation

A final illustration of EU legislation with a striking extraterritorial scope can be found in the recent wave of regulation in the financial markets sector – of which the case of the financial transaction tax (FTT), considered below, forms part. It is perhaps no surprise that this legislation contains some of the most overtly extraterritorial definitions of scope of all EU legislation to date, given the inherently global nature of many financial markets, and indeed the global nature of the financial crisis to which this EU regulation seeks to respond. For instance, the EU’s 2012 Regulation on derivatives (the European Market Infrastructure Regulation, or EMIR), which subjects counterparties concluding certain derivatives contracts to inter alia clearing and risk-mitigation obligations, even if established outside the EU, if such contracts have a direct, substantial and foreseeable effect within the EU or

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67 Ibid.
68 Ibid, p. 20.
69 Commission Proposal for a Regulation on the protection of individuals with regard to the processing of personal data and on the free movement of such data COM (2012) 11, Article 3(2).
70 While competition, environment, data protection and financial markets regulation have raised the most interesting issues to date concerning territoriality as a limiting factor for EU action, the principle has also been applied in other fields. In Boukhalfa, for instance, the CJEU considered that the Treaty prohibition of non-discrimination on grounds of nationality could apply to a worker employed in an embassy of a Member State located in a third country. The test applied by the CJEU in that case was, in a similar way to the international law doctrine considered above, whether there was a “sufficiently close link” with the EU: “The geographical application of the Treaty is defined in Article 227. That article does not, however, preclude Community rules from having effects outside the territory of the Community. The Court has consistently held that provisions of Community law may apply to professional activities pursued outside Community territory as long as the employment relationship retains a sufficiently close link with the Community […] That principle must be deemed to extend also to cases in which there is a sufficiently close link between the employment relationship, on the one hand, and the law of a Member State and thus the relevant rules of Community law, on the other.” Case C-214/94, ECLI:EU:C:1996:174, paragraphs 14-15. In that case, therefore, the fact that the employment relationship was governed by German law was enough to satisfy the territoriality principle. See also, Opinion of AG Wahl in Case C-179/13 Evans ECLI:EU:C:2014:2015. The territoriality principle has also been used in other contexts by the CJEU – see, for instance, Case C-388/11 Le Crédit Lyonnais ECLI:EU:C:2013:541(VAT); Case C-419/10 Hofmann ECLI:EU:C:2012:240 (mutual recognition of driving licences); Case C-387/12 Hi Hotel ECLI:EU:C:2014:215 (judicial cooperation in civil matters).
where such obligation is “necessary or appropriate to prevent the evasion” of that Regulation.\footnote{Regulation 648/2012 on OTC derivatives, central counterparties and trade repositories OJ 2012 L 201/1, Articles 4(1)(v) and 11(12). On this see Scott, op. cit. See similarly, Regulation 600/2014 on markets in financial instruments OJ 2014 L 173/84, Article 28(2), imposing the obligation to trade (non-cash) derivatives on regulated markets, MTFs or OTFs also on “third country entities that would be subject to the clearing obligation if they were established in the Union, which enter into derivatives transactions pertaining to a class of derivatives that has been declared subject to the trading obligation, provided that the contract has a direct, substantial and foreseeable effect within the Union or where such obligation is necessary or appropriate to prevent the evasion of any provision of this Regulation.”} Further, the European Securities and Markets Authority (ESMA) is obliged to “regularly monitor” derivatives activity falling outside the scope of the Regulation, to identify cases where a “particular class of derivatives may pose systemic risk and to prevent regulatory arbitrage between cleared and non-cleared derivative transactions.”\footnote{Ibid, Article 11(13). See also, for non-cash derivatives, Article 28(2), Regulation 600/2014: obligation for ESMA to monitor and identify cases where contracts falling outside the scope of the obligation “may pose systemic risk” or where there is a need to avoid “regulatory arbitrage” between classes of contracts.}

The EU’s 2014 Market Abuse Regulation’s obligations concerning insider dealing, the unlawful disclosure of inside information and market manipulation, also have an extraterritorial scope, applying not only to financial instruments admitted to trading on a regulated market or for which a request for admission to trading on a regulated market has been made, but also to financial instruments traded on a multilateral trading facility (MTF) or organised trading facility (OTF) in the EU (even if they are primarily traded and listed outside of the EU), as well as to financial instruments “the price or value of which depends on or has an effect on the price or value of” EU-traded instruments.\footnote{Regulation 596/2014 on market abuse OJ 2014 L173/1, Article 2(1).} This is a significant broadening of the jurisdictional scope of the 2014 Regulation’s 2003 predecessor.

In *UK v Parliament and Council (Bankers’ Bonuses)*, the CJEU was offered its first chance to rule on the compatibility with the territoriality principle of one element of the EU’s response to the global financial crisis: namely, the EU’s imposition, in the 2013 Capital Requirements Directive (CRD IV), of a fixed ratio for bankers’ bonuses in relation to their basic salary (Article 94(1)(g) of the Directive).\footnote{Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms OJ 2013 L 176/338, Article 94(1)(g).} Article 92(1) of the CRD IV Directive provides that the competent authority must ensure the application of inter alia the bankers’ bonus limit “for institutions at group, parent company and subsidiary levels, including those established in offshore financial centres.” Article 109(2) of the CRD IV Directive states that competent authorities shall ensure that parent undertakings subsidiaries subject to the Directive implement the “arrangements, processes and mechanisms” referred to in Section II of Chapter II of the Directive (which includes the bankers’ bonus limit) in their “subsidiaries not subject to the directive” (save where it is established that this is contrary to the law of the State of establishment of the subsidiary: Article 109(3)). In November 2014, Advocate General Jääskinen delivered an Opinion rejecting the UK’s arguments (on this and other matters)\footnote{The UK also argued, for instance, that the provisions challenged breached data protection law and the principle of legal certainty.} in unequivocal and rather stinging terms. Aside from the fact that, in his view, the UK had argued the case incorrectly (challenging only the substantive provision of Article 94(1)(g) itself, and not the provisions defining
the scope of application of that provision, Articles 92(1) and 109(2)),76 the Advocate General strongly rejected the argument that assertion of EU jurisdiction solely on grounds of effects rendered the EU legislation invalid:

“...in my opinion an EU legislative measures cannot be invalid simply because it has effects on conduct in territory located outside of the EU...it has long been established that conduct taking place outside the EU that impacts internally on it can be regulated by EU law.”77

Citing Woodpulp I in support of this proposition, the Advocate General also relied on the PCIJ’s judgment in Lotus, considered above, observing that, in his view, the Lotus judgment established a,

“kind of burden of proof rule, entailing that the link invoked by a State to justify its legislative jurisdiction will be sufficient, absent a rule of international law to the contrary.”

The only exception to this, he argued, arose in the based on a claim of universal jurisdiction, which must be based on a positive rule of international law, but which was not at issue here given that the CRD IV Directive only subjected foreign group companies of EU financial institutions to the EU regulatory framework.78

As a result of the Opinion, the UK’s Chancellor, George Osborne, decided to withdraw the UK’s challenge to the bankers’ bonus provisions, which he stated was because he now considered that the challenge was “unlikely to succeed”.79 Such decision to withdraw the action also, however, avoided the possibility that the CJEU could have delivered a ruling of such force to have negative implications from the UK’s perspective going beyond the facts of the Bankers’ bonus case itself. This would have been the case, for instance, had the CJEU accepted the approach to the territoriality principle adopted by its Advocate General, which sets out a very broad view of the implications of the principle for EU law, and leaves a great deal of discretion to the EU to decide what kind of connecting factors it wishes to rely on in exercising its legislative powers.

6. The case of the proposed FTT: jurisdictionally sound?

As is well-known, in February 2013 the Commission presented a proposal for a FTT on the basis of the enhanced cooperation procedure, pursuant to Council Decision 2013/52/EU authorising enhanced cooperation in this area. This followed a failure to agree with the requisite unanimity following its original September 2011 proposal. 11 Member States are currently envisaged to participate in the FTT under the enhanced cooperation arrangement,80 although pursuant to the Treaty’s enhanced cooperation provisions, it will be possible for additional Member States to join subsequently upon submission of a request to the Commission. The Commission’s proposal originally envisaged for the tax to apply from 1 January 2014, but the start date for implementation is now envisaged by the Council as 1 January 2016 (“at the latest”).81 The Proposal was reinvigorated at the January 2015 meeting of participating State, at the behest of France and

76 Opinion in Case C-507/13, ECLI:EU:C:2014:2394, paragraph 33.
77 Ibid, paragraph 36.
78 Ibid, paragraph 39.
79 A. Barker, “Osborne gives up on challenge to bank bonus cap” Financial Times 20 November 2014.
80 Namely, Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia.
81 Council Conclusions of 6 May 2014, 9273/14, p. 9.
Austria, with France indicating its preference that the proceeds of the tax would go to fighting climate change.82

The aims of the proposal are threefold, namely:

- harmonising indirect taxation on financial transactions, in the interests of achieving the internal market and avoiding competitive distortions;
- ensuring that the financial sector makes a “fair and substantial” contribution to public finances and covering the cost of the financial crisis, and creating a level playing field with other sectors; and
- creating disincentives for financial transactions which do “do not enhance the efficiency of financial markets” and thus helping to avoid future crises.83

The tax is envisaged to bring in €31 billion annually.84

Article 3 of the Proposal defines the scope of application of the FTT, which is to apply to,

“all financial transactions, on the condition that at least one party to the transaction is established in the territory of a participating Member State and that a financial institution established in the territory of a participating Member State is party to the transaction, acting either for its own account or for the account of another person, or is acting in the name of a party to the transaction” (Article 3(1)).

The concept of “financial transactions” is broadly defined in Article 2(2) to cover the purchase, sale or exchange of financial instruments, concluding derivative contracts, repurchase and reverse repurchase agreement, and securities lending and borrowing agreements. In the case of derivatives, the minimum rate of tax is set at 0.01 % of nominal value; in the case of other financial transactions, this is set at 0.1%. A variety of exemptions apply, for instance, for the raising of capital by primary issuance of shares and bonds, financial transactions with the ECB and national central banks, the EFSF and ESM. The tax must be paid by each financial institution that is party to the transaction (whether acting for its own account or for another person), acting in the name of a party to the transaction, or where the transaction has been carried out on its account, with the tax to be paid to the Member State in the territory of which the financial institution is deemed to be established.85

In terms of territorial scope, therefore, for the FTT to apply, at least one party to the transaction and a financial institution party to the transaction must be established in a participating Member State. The concept of establishment is defined in Article 4 in a manner that is unusual for its broadness. Specifically, establishment of financial institutions is defined to include not only the State of regulatory authorisation, registered seat, place of branch (Articles 4(1)(a)-(e)) (the “residence principle”). It also includes situations where (Article 4(1)(f)) a party to a financial transaction with another financial institution established in the Member State pursuant to Articles 4(1)(a)-(e) (the “counterparty principle”).

85 Article 10(1).
In addition, Article 4(1)(g) extends establishment to cover a party to a financial transaction in a structured product or financial instrument issued within the territory of that Member State (subject to certain exceptions) (the “issuance principle”). The issuance principle is a jurisdictional criterion of last resort, with the other criteria to prevail where applicable.66 The upshot is that there are now four possible territorial connecting factors under the Proposal:

- the seller’s residence,
- the buyer’s residence,
- the place of the transaction and
- the place of issue of the product traded.87

As a practical matter, the extended concept of establishment gives rise to rather complex questions of application, as can be seen from the lengthy Commission document attempting to explain how the jurisdictional criteria will operate in practice.88 For instance, in the case where the parties are a financial institution established in a non-participating State and an institution established in a participating State, the participating State will be due two payments of FTT, one from each institution. Where each party is established in a participating State, that State receives only one payment, but this will be shared between the two participating Member States concerned.89

The issuance principle is new to the 2013 Proposal by comparison with the 2011 Proposal, and together with the counterparty principle has given rise to some controversy insofar as these principles have been viewed in some quarters as breaching the territoriality principle of international law.90 As is well-known, the UK has already unsuccessfully tried to have the Council Decision 2013/52/EU authorising enhanced cooperation declared invalid on grounds that it authorises the adoption of an FTT with extraterritorial effects which the UK alleged failed to respect the competences, rights and obligations of non-participating States, for which there was no justification under customary international law, and the implementation of which would inevitably cause costs for non-participating States because of the obligations of mutual assistance and administrative cooperation linked to the application of Directives 2010/24 and 2011/16 to that tax. While this was dismissed by the CJEU on grounds that the action had been brought too early,91 the issue will undoubtedly return at a later date before the Court.

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66 Article 4(4) provides that, where more than one of the conditions in Articles 4(1) and (2) is fulfilled, the “first condition fulfilled from the start of the list in descending order shall be relevant for determining the participating Member State of establishment”.
71 Case C-209/13 ECLI:EU:C:2014:283.
For its part, the Commission has come out fighting in response to criticisms of on territorality grounds. It has emphasised that the purpose of adding the issuance principle was mainly to strengthen anti-relocation risks, i.e., so that it covers situations where parties are trading in financial instruments issued in the Member State, including shared, bonds and equivalent securities, money-market instruments, structured products, units and shares in collective investment undertakings and derivatives traded on organised trade venues or platforms. The Explanation to the Proposal relies on Article 4(3) (the “economic substance” clause) in further justifying this jurisdictional basis, which provides that, notwithstanding Articles 4(1) and (2),

“a financial institution or a person which is not a financial institution shall not be deemed to be established within the meaning of those paragraphs, where the person liable for payment of FTT proves that there is no link between the economic substance of the transaction and the territory of any participating Member State”.

In the Commission’s view, this is enough to ensure that taxation “can only take place in the presence of a sufficient link between the transaction and the territory of the FTT jurisdiction” and therefore respects the principle of territorality. Similarly, in its view, the counterparty principle is justified as the fact that one party is established within a participating Member State is a sufficient nexus to the jurisdiction.

As to the risk of double taxation that may arise insofar as more than one Member State may be competent to tax where different financial institutions are established in different participating States, the Commission has responded that this in itself is not contrary to international law, which does not provide for a rule of priority of taxation or prohibit double taxation, and that this can be dealt with by bilateral agreements in the normal way. Further, the Commission has argued that the risk of juridical double taxation only arises where non-participating States also have their own FTTs, which is a normal feature of non-harmonised parallel exercise of tax competence.

A further issue has been whether the Proposal respects the requirements of enhanced cooperation set out in Articles 32326 and 327 TFEU, insofar as the tax will apply to financial institutions based in non-participating States where, for instance, the other party to the transaction is based in a participating State, or where the instrument being traded is issued in a participating State. This argument is similar to the territoriality argument in some respects, as Article 327 TFEU provides that enhanced cooperation,

“shall respect the competences, rights and obligations of those Member States which do not participate in it.”

92 Explanation to the Proposal, op. cit., p. 11.
93 Explanation to the Proposal, op. cit., p. 11.
95 M. Bergman, op. cit.
Article 326 TFEU further provides that enhanced cooperation must respect the Treaties and EU law, and

“shall not undermine the internal market or economic, social and territorial cohesion. It shall not constitute a barrier to or discrimination in trade between Member States, nor shall it distort competition between them.”

The Commission has defended itself on this issue essentially, on the basis that all differences between tax systems affecting cross-border activities give rise to certain distortions of competition, which can only be eliminated by harmonisation.

7. Conclusions

The EU has consistently liked to consider respect for, and compliance with, international law as a fundamental part of its identity and basic principles. While this had already been clear from the CJEU’s jurisprudence holding that the Union is bound by international law, it was driven home once again by the Treaty of Lisbon’s inclusion of the “strict observance and the development of international law” within the EU’s key aims (Article 3(5) TEU). From the CJEU’s part, it has generally speaking demonstrated serious commitment in its case-law to achieving this aim. Generally speaking, it has attributed far-reaching effects to international law in practice within the EU’s legal order, which effects have traditionally been considered to go well beyond those attributed in the case of many other Supreme Courts (including the US Supreme Court, and those of many EU Member States). While the CJEU’s adoption of a manifest error standard of review for compatibility with customary international law in AATA has been characterised as a lack of commitment to international law, in the wider context it is probably best seen as consistent with this, i.e., as an attempt to give customary international law teeth in a manner compatible with the EU legal order. The Advocate General’s approach, while ostensibly more open to customary international law, would in fact have excluded review in that case.

Having said that, when faced with a conflict, or apparent conflict, between binding rules of international law and fundamental principles of its own legal order, the CJEU has consistently given priority to the latter. As noted above, this in itself is unremarkable, given the CJEU’s role as ultimate constitutional court for the EU. What is particularly interesting about the CJEU’s approach, however, is that it likes to avoid direct confrontation by interpreting the relevant rule of international law in a way that is consistent with EU law – in one sense, a kind of “reverse” interprétation conforme, or consistent interpretation. The open-textured nature of many international law norms, as discussed above, undoubtedly facilitates this method. Of course, the approach goes far beyond territoriality and customary international law cases: it is also evident in, for instance, the famous Kadi jurisprudence where the CJEU, faced with a conflict between a binding UN Security Council Resolution and (EU) human rights norms, gave priority to the human rights norms on the reasoning that, in fact, these norms were also a priority in international law. The CJEU’s case-law to territoriality in taxation cases discussed above, where it has effectively interpreted the principle in a

way that fit with its own vision of the interaction between the free movement rules and national tax rules, is also consistent with this. In these cases, while the CJEU certainly demonstrates a desire to show respect for territoriality, ultimately it has become subsumed in the specific doctrines on justification which, in turn, seek to establish a logical system, within the scheme of EU law, demarcating the boundaries of national tax competence — and using the language of EU law, rather than that of international law. In this way, the CJEU’s approach to territoriality discussed above may be viewed as a specific illustration of the CJEU’s ultimate commitment to what many commentators have termed the “autonomy” of the EU’s legal order.

The ambiguities of the territorial principle as a matter of international law, discussed above, mean that the scope for the CJEU to adopt its own interpretation of the principle, and still (arguably) conform with international law, is considerable (compared, for instance, to other more precise rules of international law). This is perhaps most evident in the example of competition law, where the CJEU’s implementation and qualified effects doctrines are, according to its own case-law, compliant with territoriality, but most would consider them to go considerably further than traditional notions of territoriality in international law. As discussed above, however, it was highly relevant that the US had already, forty years previously, developed an effects doctrine for its own antitrust law, meaning that extraterritorial effects had already been accepted by some States as a legitimate connecting factor in this field of law. Significantly, the development of the effects doctrine by the US courts led to political retaliation via blocking statutes and, subsequently, bilateral and multilateral political efforts to smooth over the problem of extraterritoriality, via comity agreements and network-based cooperation. This process of global convergence in competition law has meant that the issue of extraterritoriality makes less practical difference, and has become less of a problem than it used to be.

The example of environmental policy stands in stark contrast to this. Here, the CJEU has similarly interpreted territoriality in a broad manner to support the EU’s view of what is a sufficient connecting factor to satisfy that principle (Commune de Mesquer, AATA). Yet the AATA example shows that, where international consensus is lacking, the CJEU’s case-law will not be sufficient to persuade third States to accept what they may perceive as the extraterritorial application of EU law. As it did in the competition example in the early 1980s, at that point law meets political reality, and the EU has been forced to suspend application of a law that it considers to be valid. In the case of data protection, the politico-economic ramifications of Google Spain are still playing out, with Google seeking to limit the extraterritorial application of the judgment by confining it to searches carried out on versions of its search engine targeting European users. This interpretation is, however, by no means obvious from the terms of the judgment itself.

From this case-law, therefore, it is clear that the CJEU adopts a relatively relaxed approach to the EU’s extraterritorial extensions of its legislative competence, and engages in a non-intensive standard of review for compliance with the territoriality principle. All of this is, of course, highly relevant to the question whether the proposed FTT is compatible with the territoriality principle of

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100 See generally, R. Wessel and S. Blockmans, Between Autonomy and Dependence: The EU Legal Order under the Influence of International Organisations (The Hague, TMC Asser Press, 2013).

101 See the Guidance of the Article 29 Working Group, op. cit.
international law. It is certainly true that the counterparty principle and the issuance principle of Article 4 of the Proposal, which have given rise to most outcry, go far beyond what we would normally class as “establishment” in EU law. Indeed, part of the problem with the proposal on this point may be precisely because it uses the term establishment, which is by now a well-established term of art in other areas of EU law, in a greatly extended fashion and in a way that bears little resemblance to its usage in, for instance, internal market law. This terminological confusion aside, however, it seems clear that both the counterparty and issuance principles demand some form of link to the participating States’ territory. In the case of the counterparty principle, it is the place of establishment of the other party to the transaction; in the case of the issuance principle, it is the place of issuance of the structured product or instrument.

Is this enough as a matter of international law? Probably yes: insofar as the aim of the FTT is to harmonised indirect taxation on financial transactions, the two principles can reasonably be viewed as capturing transactions that have a genuine link to a participating Member State (even if the place of establishment of the financial institution liable to pay the tax may be outside the FTT zone). Is this enough as a matter of EU law? Again, very probably. In the case of financial markets regulation, while we do not (yet) have any formal response of the CJEU to the remarkable express extraterritoriality contained in the EU’s legislative response to the global financial crisis, the Advocate General’s Opinion in Bankers’ Bonus strongly suggests that the CJEU’s relaxed approach would apply in much the same way here. For these reasons, it is in my view unlikely that the CJEU will strike down the proposal on territoriality grounds when, as seems inevitable, the UK brings a further challenge down the line. As the ATAA/ETS example illustrates, this would not rule out the possibility of political retaliation (and an EU political response) in the event of a CJEU judgment upholding the tax. It is, however, important to note that, in contrast to States like China in the ETS example, the UK is – at least while it remains a member of the EU - as a matter of EU law bound by the Article 4(3) TEU duty of loyal cooperation to respect CJEU judgments. Clearly, this severely limits the scope for the UK (or other like-minded Member States who have opted out of the FTT) to act in a manner that disregards the authority of the CJEU.

This last point illustrates a central difficulty that is likely to arise again in future cases. Tax has long been an obvious candidate for enhanced cooperation because of the close links to the internal market (more harmonised EU tax rules lead to a better functioning internal market), and the great resistance on the part of many Member States to tax harmonisation. At the same time, it is difficult to see how enhanced cooperation between some EU States in tax could fail to have effects on non-participating Member States, who after all still participate in the single market. The loosening of the requirements for enhanced cooperation with the Lisbon Treaty, together with the political opposition by certain Member States to greater integration, make it likely that we will see much greater use of enhanced cooperation in future. The CJEU’s approach to date to policing the limits of enhanced cooperation, as evidenced in its judgment in Spain and Italy v Council, suggest that the

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102 See, for an example of a recent political response to complaints of extraterritoriality in the economic sphere on the part of the US, the example of the US’s Dodd-Frank rules on derivatives and clearing, where the Commodity Futures Trading Commission and the Securities and Exchange Commission introduced a concept of substituted compliance in response to criticism of extraterritoriality, whereby it can exempt compliance with certain US rules if it deems host country rules sufficiently equivalent to the US rules. The CFTC also delayed requirements to comply with some cross-border rules, through the means of no-action letters. See Green and Potiha, op. cit.
CJEU will not quickly accept complaints from non-participating States that, due to alleged potential distortions within the single market, the conditions for enhanced cooperation have not been met.\textsuperscript{103}

\textsuperscript{103} Joined Cases C-274/11 and C-295 /11, ECLI:EU:C:2013:240. See the Opinion of Advocate General Bot of November 2014 rejecting a follow-on action by Spain to Regulation 1257/2012 implementing enhanced cooperation in the creation of unitary patent protection OJ 2012 L361/1: Case C-146/13 ECLI:EU:C:2014:2380, and the challenge to the sister Regulation, Case C-147/13, ECLI:EU:C:2014:2381.