EDITORIAL

Dear readers,

you have just opened the pilot issue of new international legal journal published by the Faculty of Law of the Comenius University in Bratislava, Slovakia. This new legal journal stands as the expression of the international openness and global perspective of our faculty. It follows the excellence strategy of our law school and seeks to support legal discourse and research and promote the critical legal thinking in the global extent. The journal offers a platform for fruitful scholarly discussions via various channels – be it lengthy scholarly papers, discussion papers, book reviews, annotations or conference reports.

Bratislava Law Review focuses on publishing papers not only from the area of legal theory and legal philosophy, but also other topics with international aspects (international law, EU law, regulation of the global business). Comparative papers and papers devoted to interesting trends and issues in national law that reflect various global challenges and could inspire legal knowledge and its application in other countries are also welcomed.

In addition, there are also some other specificities of this journal in comparison with other Central and East European (CEE) law journals. First of all, it is the geographical scope and focus that makes this journal special. The Bratislava Law Review namely aims to present ideas that reflect, in particular, the latest trends in legal thought in CEE countries, especially the Visegrad group countries. But of course, this does not mean that the journal will only serve as a publication medium for authors from this part of Europe. On the contrary, we believe that articles submitted by scholars from all over the Danube region, Europe, as well as from the rest of the world can enrich readers from CEE area – be it in their scholarly work or in their legal practice in various legal fields.

The Bratislava Law Review has therefore adopted multidisciplinary and interdisciplinary, but also cross-disciplinary coverage. This is also the reason why members of the Bratislava Law Review Editorial Board are experts both in legal sciences and legal practice as well as in related disciplines – to ensure cross-cutting knowledge throughout all legal sciences, branches and fields of law. The Editorial Board consisting of foreign scholars-experts in the above fields, as well as a double-blind peer review provide a guarantee of high standard of the contributions published. In this way, the Bratislava Law Review hopes to provide space for presenting a diversity of opinions and approaches to up-to-date legal issues and problems, aiming in this way to contribute to overall rise in standards of legal scholarship in the CEE region.

In the Bratislava Law Review, we are aware of the responsibility connected to issuing this type of journal. Therefore, before we publish any article, we take two things into consideration. First of all, respect for ethical rules of the Bratislava Law Review is required, making sure that only original and novel legal studies, articles, reviews, and annotations will get published. Closely connected thereto, the second important requirement is that any potential publication meets the standards of the highest scholarly quality. Therefore, a double-blind peer review process was introduced within the BLR publication process. More details are available at the BLR website.

Finally, allow us to express our sincere hopes that the journal fulfils its mission of publishing only papers of the highest quality, while finding a considerable number of regular readers.

Tomáš Gábriš – Matej Horvat – Ondrej Hamuľák

LIST OF CONTRIBUTORS

Peter-Christian Müller-Graff is a professor at the Juristische Fakultät, Ruprecht-Karls-Universität Heidelberg, Germany

Gracia Mª Luchena Mozo is a professor at the International Centre for Financial Studies, University of Castilla-La Mancha, Spain

Nellie Munin is an independent researcher and former associate professor at the Law School, Zefat Academic College, Israel

Hamed Alavi is a a lecturer at the Tallinn Law School, TTU, Estonia and PhD. candidate at Faculty of Law, Autonomous University of Barcelona, Spain.

Erzsébet Csatlós is a senior lecturer at the Faculty of Law and Political Sciences, Uiversity of Szeged, Hungary

Balazs Horvathy is a research fellow at the Institute for Legal Studies, HAS Centre for Social Sciences, Hungary

Michal Mrva is an assistant professor at the Faculty of Law, Comenius University in Bratislava, Slovakia

Michal Krajčovič is a PhD candidate at the Faculty of Law, Comenius University in Bratislava, Slovakia

Judit Siket is an assistant lecturer at the Faculty of Law and Political Sciences, University of Szeged, Hungary

Jan Mazur is a PhD candidate at the Faculty of Law, Comenius University in Bratislava, Slovakia

Ondrej Blažo is an assistant professor at the Faculty of Law, Comenius University in Bratislava, Slovakia

Kristína Považanová is an assistant professor at the Faculty of Law, Comenius University in Bratislava, Slovakia

Hana Kováčiková is an assistant professor at the Faculty of Law, Comenius University in Bratislava, Slovakia

Katarína Burdová is an assistant professor at the Faculty of Law, Comenius University in Bratislava, Slovakia

Daniela Lukáčová is a legal expert from Antimonopoly Office of the Slovak Republic

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LEGAL EUROPEANIZATION OUTSIDE THE EUROPEAN UNION

Peter-Christian Müller-Graff
Ruprecht-Karls-Universität Heidelberg, Juristische Fakultät

Abstract: Legal Europeanization outside the European Union is an epochal multifaceted phenomenon. The text distinguishes three types: the autonomous Europeanization, the preparatory Europeanization and the contracted Europeanization. All three types are illustrated by prominent examples. The article discusses differences and commonalities between them in regard to their substantive scope of subject matters covered, their reasons and their public and societal ramifications as well as the perspectives of this development.

Keywords: Europeanization, European Union

1 INTRODUCTION

Legal Europeanization *outside* the European Union is an *epochal multi-faceted phenomenon* and a great topic. Until now it is *not adequately explored*. Despite a multitude of publications on the legal europeanization of individual third states or groups of third states (e.g.: O. Blažo; P. Forstmoser; H. P. Graves; N. A. Guney; H.-H. Herrnfeld; Chr. Hillion; V. Kunová; M. Maresceau; P.-CHr. Muller-Graff; R. Petrov; J. Piskulinski; N. Šišková; L. Tichý; D. Tzouganatos; L. Vékás; J. Zemánek; F. Zoll) the phenomenon still deserves a comprehensive comparative investigation of its types, its substantive scope and its reasons. This contribution can only serve as a rather short outline. Legal Europeanization can be understood, in its *core*, as *any adaptation* of the law of *non-EU member States* to legal rules and principles of the European Union. An *early example* was the adoption of the Greek competition Act of 1977,[1] which entered into force three years before Greece became a member of the European Economic Community (EEC). It shaped the Greek competition law in accordance with the substantive provisions of the cartel law of the EEC,[2] in particular with the prohibitions of cartel agreements and abuses of a dominant market position as contained in (today) Articles 101 and 102 TFEU[3] and created the challenging tasks of establishing an adequate national infrastructure for the interpretation and application of this imported set of rules and its judicial review.[4] *Since then* this phenomenon of non-EU-members which adapt their legal order to the law of the European Union *has increasingly occurred*. The following observations focus on *four* of its aspects: on its typology, on its substantive scope, on its reasons, on its public and societal ramifications and on its perspectives.

The submitted understanding of legal Europeanization draws a distinguishing line in relation to the regularly expected phenomenon of *compliance of undertakings* from abroad with EU law.

1 Gesetz 703/1977; PAPADELLI A.: Beweislastverteilung bei der privaten Durchsetzung des Kartellrechts. Münster: LIT Verlag, 2010, p. 248ff.

2 PAPATHOMA-BAETGE, A.: Die Neuregelung des Kartellrechts in Griechenland, in: Recht der internationalen Wirtschaft, 1996, p. 1013.

3 PAPADELLI, A.: Beweislastverteilung bei der privaten Durchsetzung des Kartellrechts, p. 249.

4 See as an analysis of the transplantation of foreign antitrust devices TZOUGANATOS, D.: Zur Rezeption fremden Rechtsguts im Bereich des Wirtschaftsrechts: dargestellt am Beispiel der Problematik einer Fusionskontrolle nach dem griechischen Kartellgesetz. Bonn: Stollfuss, 1983.

Complying with the legal standards is a normal worldwide requirement for any undertaking which pursues economic activities within a specific jurisdiction. E.g., should the result of the British referendum of June 23, 2016 lead to the withdrawal of Britain from the European Union, then the enterprises located in Britain which aim at dealing within the internal market of the Union would nevertheless have to comply with the applicable European regulatory law. This would imply for banks located in Britain to open a registered office in a Member State of the Union in order to obtain a "European passport" for rendering services to customers within the internal market.

2 THE TYPES OF LEGAL EUROPEANIZATION OUTSIDE THE EUROPEAN UNION

For the purpose of systematizing the types of legal Europeanization outside the European Union I propose to differentiate between three basic forms: the autonomous Europeanization, the preparatory Europeanization and the contractual Europeanization.

2.1 Autonomous Legal Europeanization

The *autonomous* legal Europeanization can be described as Europeanization *without any obligation* towards the Union or *any current desire* for membership in the Union. This is the situation of *Switzerland* as far as the Swiss adaptation to *secondary* Union law is concerned. It is true that Switzerland has concluded a multitude of bilateral agreements with the European Union. They range from the Free Trade Agreement (1972) to the Agreement on the Free Movement of Persons (1999). However, these agreements do not provide, in principle, for the permanent adaptation of the Swiss legal order to new acts of the legislation of the Union,[5] in particular to directives which aim at harmonizing national laws in order to facilitate the free movement of goods or services. This secondary law deals with market-relevant standards of, e.g., health protection, consumer protection, environmental protection. Since non-compliance of Swiss goods or services with the protection standards of secondary Union law would bar their marketing within the internal market (as far as the bilateral agreements do not yet address these issues), Switzerland has developed a technique which is called "autonomer Nachvollzug"[6] (autonomous adaptation to relevant secondary Union law). This technique is marked by the tendency to revise national Swiss law in order to facilitate exports of enterprises which are located in Switzerland into the internal market. As a matter of course Switzerland, being a non-member of the European Union, can have no right to partake in the decision on adopting secondary Union law. In the future this might well become the situation of Britain after its withdrawal from the Union, if it desires to facilitate exports of enterprises which are located in Britain into the internal market. It would be an ironic punchline of *Boris Johnson´s* selling point of Brexit as Britain´s "independence day".[7]

[5] See for the Agreement on the Free Movement of Persons GROSSEN, D. W. – COULON, C. de: Bilaterales Abkommen über die Freizügigkeit zwischen der Schweiz und der Europäischen Gemeinschaft und ihren Mitgliedstaaten. In: THÜRER, D. – WEBER, R. H. – PORTMANN, W. – KELLERHALS, A. (Hrsg.): Bilaterale Verträge I und II Schweiz – EU. Zürich: Schulthess, 2007, p.135, 139.

[6] See FORSTMOSER, P.: Der autonome Nach-, Mit- und Vorvollzug europäischen Rechts: das Beispiel der Anlagefondsgesetzgebung. In: Festschrift für Roger Zäch. Zürich: Schulthess, 1999, p. 523ff.

[7] See http://www.theguardian.com/politics/2016/jun/22/brexit-independence-day-claim-nonsense-says-david-cameron (22.6.2016).

2.2 Preparatory Legal Europeanization

A second type of legal Europeanization can be identified as *preparatory* Europeanization. Similar to the autonomous Europeanization it occurs without any obligation towards the European Union and is in this respect autonomous. However, at the same time this type of legal Europeanization is motivated and driven by the endeavour of the respective state to prepare itself for future membership in the European Union.

The epochal historical examples were the adaptations of the national legal orders of *East Central European States* to the legal order of the European Union on their path to accession to the Union in the nineties of last century.[8] While it is true that the so called Europe Agreements between the EC and its Member States on the one side and the respective East Central European State on the other side addressed the issue of approximation of laws, they did not contain a precise obligation in this respect. E.g., Article 68 of the respective Agreement with *Poland* read: "The Contracting Parties recognize that the major precondition for Poland´s economic integration into the Community is the approximation of that country´s existing and future legislation to that of the Community. Poland shall use its best endeavours to ensure that future legislation is compatible with Community legislation". Article 60 of that Agreement designated as substantive areas in particular "customs law, company law, banking law, company accounts and taxes, intellectual property, protection of workers at the working place, financial services, rules on competition, protection of health and life of humans, animals and plants, consumer protection, indirect taxation, technical rules and standards, transport and the environment". In short, this provision comprised the whole scope of the internal market law. However, this wording did not impose obligations on the respective East Central European State to implement secondary Community law. Also this situation did not change after the Copenhagen summit in 1993 when the European Communities and its Member States paved the way for a potential enlargement.[9] It is well known that the main part of Community legislation was gradually implemented by the candidate states before accession on May 1st, 2004 in an epochal "road-mapped"-process which developed in connection with and parallel to the accession negotiations on the 31 so called chapters of subject matters.[10]

This pattern of preparatory legal Europeanization is, in principle, also provided for in the *Stabilisation and Association Agreements* between the Union and its Member States with the Balcans. Article 72 par. 1 of the Agreement with Serbia, which can serve as an example, is nearly identically worded to the Europe Agreement with Poland: "The Parties recognize the importance of the approximation of the existing legislation on Serbia to that of the Community and of its effective legislation. Serbia shall endeavour to ensure that its existing laws and future legislation will be gradually made compatible with the Community acquis." However, different from the former Agreement with Poland, the Agreement with Serbia already leaps into a *procedural form* of *obliging* Serbia to approximate its law, since the quoted provision contains three further paragraphs concerning the road to be

8 See ANDERSON, M. – GAUTRON, J. C. – ESTRIN, S. – HESSE, J. J. – MORAN, M. – MÜLLER-GRAFF, P. Ch.: The Legal, Economic and Administrative Adaptations of Central European Countries to the European Community. Baden-Baden: Nomos, 1992; MÜLLER-GRAFF, P.-Ch. (ed.): East Central European States and the European Communities: Legal Adaptation to the Market Economy. Baden-Baden: Nomos, 1993; MÜLLER-GRAFF, P.-Ch. (ed.): East Central Europe and the European Union: From Europe Agreements to a Member Status. Baden-Baden: Nomos, 1997.

9 Bulletin EC 6/1993, I 13; MÜLLER-GRAFF, P.-Ch. (ed.): East Central Europe and the European Union: From Europe Agreements to a Member Status, p. 9, 17.

10 See HEUSEL, W. (Hrsg.): Die Osterweiterung der Europäischen Union. Köln, 2002, p. 21, 27.

taken: namely the starting date of the approximation (viz the signing of the Agreement), the target date of the implementation of all elements of the Community acquis referred to in the Agreement (viz the end of the transitional period) and the sequence of the steps of approximation (viz fundamental elements of the internal market acquis, the matters of justice, freedom and security as well as other trade-related areas ranking as first priority). In addition, Article 72 of the Agreement with Serbia provides for the implementation of Union law on the basis of a programme to be agreed upon between the Union and Serbia and for the definition of detailed arrangements for the monitoring of the implementation of the approximation of legislation and for law enforcement actions which have to be taken. In other words, a certain "road-mapping" is already included in this Agreement.

2.3 Contractual Legal Europeanization

A *third type* of legal Europeanization can be described as *contractual* Europeanization. This form occurs in all agreements of the Union with third states in which the Union succeeds in inserting standards of Union law into them, although it has to be kept in mind that an agreement on rules is not identical with the actual implementation of them. The Union has been *very successful* in *extending the contracted radius* of its own legal standards in many geographic directions by means of *international treaties* (see *infra*.). Several reasons contribute to this achievement. A *first* element can be seen in the consequence of the internal *principle of conferral* (Art. 5 par. 2 TEU) which limits the Union in its competences and tasks and hence guides it to primarily focus on enhanced commercial agreements. These are partially inspired by topics of its internal market standards and the experience of their ramifications into all market-relevant areas of legal issues such as the protection of health, consumers, workers and the environment. This reason is, secondly, connected to the *obligation* of the Union as laid down in Article 21 TEU that its action on the international scene "shall be guided by the principles which have inspired its *own* creation, development and enlargement", among them the rule of law, and which it should seek "to advance in the wider world." A *third* reason for the Union´s successful emphasis on furthering its legal standards in international treaties can be seen in its deeply rooted self-understanding of its basic character as "Rechtsgemeinschaft", as the first President of the EEC, *Walter Hallstein*, named it[11] – a Community of law mirrored by the establishment and the task of the European Court of Justice to ensure that in the interpretation and application of the Treaties the law is observed (Article 19 TEU) and accentuated by the "rule of law" as one of the values on which the European Union is founded (Article 2 TEU). Last, but not least, the presumably most important reason for the radiation of Union law is due to the attractiveness of the Union and, in particular, its internal market (with all its consequences for the legal order). The *results* of this development are *many* international agreements which attempt to "*export*" principles and even rules of primary and secondary *Union law*. This applies, e.g., to the already mentioned Agreements with *Switzerland* and the *Balcans* and also to the Ankara Agreement with *Turkey*,[12] the *EEA*-Agreement with Norway, Iceland and Liechtenstein[13] and the Association Agreements with now independent,

11 HALLSTEIN, W.: Die Europäische Gemeinschaft. 5.Aufl. Düsseldorf, Wien: Econ Verlag, 1979, p. 51ff.

12 GÜNEY, N. A.: Abkommen Europäische Union – Türkei. In: HATJE, A. – MÜLLER-GRAFF, P.-Ch. (Hrsg.): Europäisches Organisations- und Verfassungsrecht (Enzyklopädie Europarecht Band 1). Baden-Baden: Nomos, 2014, § 23 (p. 1029ff.).

13 GRAVER, H. P.: Der Europäische Wirtschaftsraum. In: HATJE, A. – MÜLLER-GRAFF, P.-Ch. (Hrsg.): Europäisches Organisations- und Verfassungsrecht (Enzyklopädie Europarecht Band 1), § 19 (S. 921ff.); MÜLLER-GRAFF, P.-Ch. – SELVIG, E. (Hrsg.): The European Economic Area – Norway´s Basic Status in the Legal Construction of Europe. Berlin: Verlag Arno Spitz, 1997.

former Soviet Republics such as Ukraine,[14] Moldovia[15] or Georgia.[16] They all mirror more or less some of the topics of the Union´s internal market law and include subject matters connected to it. Traces of this approach can even be found in Agreements of the Union with *Canada*,[17] *Mexico*[18] *Central American states,*[19] *South American states* (Chile,[20] Colombia and Peru[21]) and *East Asian* States (Singapur,[22] Vietnam[23]).

By far the closest and most intensive legal Europeanization in this respect is the European Economic Area (EEA-Agreement) which contains the four basic freedoms and the competition rules of the Treaty on the Functioning of the European Union (TFEU) in nearly identical terms[24] and provides for a functioning system of ensuring as uniform an interpretation as possible of this Agreement.[25] In addition, it provides for a simple mechanism to incorporate into EEA-law any new secondary law which is relevant for establishing homogenous rules in the common economic area.[26] A remarkable range of the topics of secondary law of the Union is part of the new generation of the (voluminous) Association Agreements with East European states such as the Ukraine. The meanwhile suspended negotiations of a TTIP ignited an intensive public debate whether it would be harmful to the Union if the contractual Europeanization could not be pursued. All in all it seems that the Union can offer a much deeper legal experience than any other actor on the globe for a conceptually coherent legally governed, functioning transnational commercial exchange.[27]

3 THE SUBSTANTIVE SCOPE OF SUBJECT MATTERS OF LEGAL EUROPEANIZATION OUTSIDE THE EUROPEAN UNION

The substantive scope of legal Europeanization can not be neatly linked to the outlined different types of this epochal development. However, a cautious assessment can be attempted. As already analyzed, all types have *in common* that their topics mirror the center of gravity of the Union´s main

14 ABl. 2014 L 161/3.
15 ABl. 1998 L 181/1.
16 ABl. 2014 L 261/4.
17 See: European Commission - Press Release 30 October 2016 (EU-Canada summit: newly signed trade agreement sets high standards for global trade); COM(2016) 444 final.
18 See Free Trade Agreement EU-Mexico 1997/1999.
19 See: EU startet Freihandel mit Zentralamerika, http://www.handelsblatt.com (19.5.2010).
20 See: EUR-Lex: EC-Chile Association Agreement (22.3.2005); OJ 2002 L 352.
21 See: Trade Agreement between the EU and its Member States, of the one part, and Colombia and Peru, of the other part, OJ 2012 L 354.
22 See: EU-Singapore Free Trade Agreement, http://trade.ec.europa.eu (29.6.2015).
23 See: EU-Vietnam Free Trade Agreement, http://trade.ec.europa.eu (1.2.2016).
24 See Articles 8 et seq. And 28 et seq. EEA-Agreement.
25 See Article 106 EEA-Agreement.
26 See Article 98, 102 EEA-Agreement. Article 102 EEA-Agreement provides: „In order to guarantee the legal security and the homogeneity of the EEA, the EEA Joint Committee shall take a decision concerning the amendment of an Annex to this Agreement as closely as possible to the adoption by the Community of the corresponding new Community legislation with a view to permitting a simultaneous application of the latter as well as of the amendments of the Annexes to the Agreement".
27 See for a comparison of German, European and US-American approaches to the rule of law in the relation of state and market MÜLLER-GRAFF, P.-Ch. – JACKSON, J. H. (eds.): Transatlantic Perspectives on International Economic Law. Baden-Baden: Nomos, 2009, p. 79ff.

objectives, as laid down in Article 3 TEU,[28] and its competences and its law. In short, they reflect elements of its transnational market law with all its ramifications into other areas of law which are relevant for the functioning of a market with free and undistorted competition and guard mandatory public interests. On this common ground *slight differences* in the substantive scope of legal Europeanization may be identified when comparing the three types described above.

The *autonomous* Europeanization pursued by Switzerland – and in the future probably by Britain – will usually comprise *detailed rules* in order to facilitate exports of enterprises located in its territory into the internal market. The *preparatory* Europeanization will comprise also the adaptation to general *principles* in the sense of the values of the Union as contained in Article 2 TEU. This is demonstrated by the (already contractually Europeanizing) texts of the Stabilisation and Association Agreements with the Balcans. E.g., Article 2 of the Agreement with *Serbia* contains the proclamation, that "Respect for democratic principles and human rights as proclaimed in the Universal Declaration of Human Rights and as defined in the Convention for the Protection of Human Rights and Fundamental Freedoms … and the rule of law as well as the principles of market economy … shall form the basis of the domestic and external policies of the Parties and constitute essential elements of this Agreement." This wording resembles Articles 2 and 21 TEU. In the cases of *contractual* Europeanization the relation between detailed rules and principles varies. While the *EEA*-Agreement and the bilateral Agreements with Switzerland are businesslike orientated to a plentitude of detailed rules which grant the access to the internal market, the Agreement with the *Ukraine* which draws its extensive volume from the bulk of detailed rules also contains a starting article on general principles equivalent to the respective article in the Agreement with Serbia.

4 REASONS FOR THE LEGAL EUROPEANIZATION OUTSIDE THE EUROPEAN UNION

From the aforesaid it can easily be deduced that the reasons for legal Europeanization outside the European Union *differ* according to its types.

The *autonomous* Europeanization is obviously rooted in the interest of the respective states to facilitate the access of undertakings located in their territory to successfully manoeuvre within the legal order of the internal market. As a consequence of the Europeanization of the market relevant rules in their home country they are getting trained in and accustomed to internal market law standards, as exemplified in the case of Switzerland.

Different from the reason of autonomous Europeanization, the basic motivation for the *preparatory* Europeanization, while also comprising this aspect, reaches further than alleviating the business of enterprises, since the adaptation of the domestic legal order to Union law serves as a precursor for the intended full membership with all its components, e.g. in the areas of internal security and crime prevention, as seen in the case of the Balcans. Here, on the *other side*, also the interests of the Union promote this approximation in the rather soft way of conditionalities for support programs as seen during the course to the Eastern enlargement of the Union. This allowed also the support for the costly adaptation to the high environmental law standards of the Union (also in order to avoid

[28] See for Art. 3 TEU MÜLLER-GRAFF, P-Ch.: Verfassungsziele der Europäischen Union. In: DAUSES, M. (Hrsg.): Handbuch des EU-Wirtschaftsrechts. München: C. H. Beck, 2012, A I.

distorted competition). Even and in particular if a future membership in the Union is politically not yet decided upon from its side, the Union is bound by Article 8 TEU to develop a special relationship with neighbouring countries, founded on the values of the Union and, according to Article 21 TEU, guided by the principles which have inspired its own creation, development and enlargement. This leads to a central conclusion. Taking into account that the Union is based on law and hence is, in its genetic code, a "Rechtsgemeinschaft"[29] and, in particular, pursues all its activities on the basis of transnational commercial and market relations and corresponding transnational law, its approach to external relations is inherently driven to offer its internal legal standards to its neighbours.

Eventually the reasons for *contractual* legal Europeanization are marked by the same set of normative guidelines on the side of the Union, while the reasons of the third country depend upon its specific motivation for closer relation with the Union as exemplified in the case of the three EFTA members in their EEA-relation with the Union and its member states.

5 PUBLIC AND SOCIETAL RAMIFICATIONS OF THE LEGAL EUROPEANIZATION OUTSIDE THE EUROPEAN UNION

The political and societal ramifications of legal Europeanization outside the European Union affect, above all, the legal system of the *third country* on all of its public and societal levels. The *legislation* is challenged to adapt the statutory order to the respective principles and rules of European Union law. The *administration* is challenged to apply the implemented new rules in the sense which the national legislator has given them. The *judiciary* is challenged to interpret them. The *societies* of third countries encounter in their Europeanized domestic legal order concrete pieces of the consequences of the normative point of orientation of the European Union as laid down in Article 2 TEU, namely, in the words of this provision, of a polity based on the values of respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights, and of a society in which pluralism, non-discrimination, tolerance, justice, solidarity and equality between women and men prevail.

The *EEA-Agreement*, which most closely resembles Union law for the common economic area based on homogenous rules, even provides for the objective of the Contracting Parties to arrive at as uniform an interpretation as possible of the provisions of this Agreement and those provisions of Union legislation which are substantially reproduced in the Agreement.[30] To these ends the EEA Joint Committee is charged to act so as to preserve the homogenous interpretation of the Agreement and to realise, in full deference to the independence of courts, a system of exchange of information concerning judgments by the EFTA Court, the European Court of Justice (ECJ) and the Courts of last instance of the EFTA states.[31] In fact, both the ECJ and the EFTA Court observe the respective jurisprudence of the other court.[32] In the absence of a mechanism as in the EEA national law may expressly or implicitly, even in the form of an assumption, oblige the domestic administration and judiciary to interpret the respective amended domestic law in conformity with the interpretation of parallel provisions or principles of Union law.

[29] See above.

[30] See Article 105 EEA-Agreement.

[31] See Article 106 EEA-Agreement.

[32] See, e.g., BAUDENBACHER, C.: The EFTA Court and the European Court. In: MÜLLER-GRAFF, P.-Ch. – SELVIG, E. (Hrsg.): EU-EEA Relations. Berlin: Berlin Verlag, 1999, p. 65ff.

The mutual observation of the respective jurisprudence can even impact on the jurisprudence in *Union law*. The incumbent President of the EFTA Court, *Carl Baudenbacher*, has listed several cases in which the ECJ followed the EFTA Court in the interpretation of EEA-law.[33] This can also influence the interpretation of parallel provisions in Union law. In this way, legal Europeanization outside the Union can *conversely* impact on the development of Union law, if the latter draws inspiration from its export.

6 SUMMARY: PERSPECTIVES OF LEGAL EUROPEANIZATION OUTSIDE THE EUROPEAN UNION

The perspectives of this epochal process of legal Europeanization depend upon the attractiveness, the radiation and the aura of the European Union and its transnational legal order and, in particular, its internal market law with all its ramifications in the traditional areas of law. As long as a third country will perceive the Union as an appealing polity and society, the Europeanization of its domestic legal order will progress to the degree considered beneficial for its own aspirations. This again should motivate the Union to assume responsibility for developing its legal order in the most convincing way possible.

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[33] See above.

MÜLLER-GRAFF, P-Ch.: Verfassungsziele der Europäischen Union. In: DAUSES, M. (Hrsg.): Handbuch des EU-Wirtschaftsrechts. München: C.H.Beck, 2012.

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Contact information:

Professor Dr.iur.habil.Dr.h.c.mult.Peter-Christian Müller-Graff, Ph.D.h.c., MAE
p.mueller-graff@igw.uni-heidelberg.de
Ruprecht-Karls-Universität Heidelberg
Friedrich-Ebert-Platz 2
D-69117 Heidelberg
Germany

ANALYSIS OF ECJ CASE LAW ON DISCRIMINATORY TREATMENT OF CROSS-BORDER INHERITANCE TAX

Gracia Mª Luchena Mozo
University of Castilla-La Mancha,
International Centre for Financial Studies

Abstract: Recently, the European Commission has launched a package which deals with issues of double taxation and discriminatory tax treatment in the area of inheritance and estate tax. In the paper the Commission discusses ten cases in which the European Court of Justice examined the inheritance tax rules of Member States. In eight out of the ten cases it concluded that the Member States in question breached EU rules on the free movement of capital and/or freedom of establishment. For example, on the 3rd of September 2014, the ECJ entered/made a judgment resolving that the Spanish Inheritance Tax should impose restrictions on the free movement of capital, one of the fundamental principles of the EU's Single Market. Taking into consideration the merits of the case the Court of Justice finally concluded that the situations between resident and non-resident taxpayers or between goods located in Spain or abroad are comparable and that therefore the applicable tax treatment should be the same**.**

Keywords: Inheritance and gift tax, Direct Taxation, Non-Residents, No Discrimination

1 INTRODUCTION

Judgements by the Court of Justice of the European Union (CJEU) on inheritance tax are relatively new. In fact, the EU until recently had no standard regulations on direct taxation and much less so on Inheritance and Gift Tax (IGT). In the absence of such regulations, IGT is a responsibility of individual EU Member States. All Member States shall, however, ensure to exercise the fundamental freedoms laid down by the EU legislation. This means that all Member States shall not draw a distinction between taxpayers on the basis of their nationality and should not restrict the fundamental freedoms arbitrarily. The CJEU confirmed that taxation on gifts and inheritances is subject to these freedoms. Nevertheless, the CJEU also declared that EU Member States are not liable to eliminate double taxation occurring as a result of their tax sovereignty.

The few number of Double Taxation Agreements on IGT makes the problem even more evident.

2 INHERITANCE AND GIFT TAX IN JUDGEMENTS OF THE COURT OF JUSTICE OF THE EUROPEAN UNION

As can be concluded from the analysis of the judgements of the CJEU in terms of inheritance taxation, the fundamental freedom set out by the Court judgements of 11 December 2003, Barbier (C-364/01, ECLI:EU:C:2003:665); in the Jäger Case (C-256/06, EU:C:2008:20); in the Halley

case (C-132/10, ECLI:EU:C:2011:586) or in the Welte case (C-181/12, EU:C:2013:662) is the free movement of capital[1]. Nevertheless, judgements of 25 October 2007, *Geurts and Vogten* (C-464/05, ECLI:EU:C:2007:631) and of 9 July 2012, *Scheunemann* (C-31/11, ECLI:EU:C:2012:481), conclude that the type of freedom that is restricted is freedom of establishment, which concerns Member States themselves restrictively. The dividing line between the two types of freedom is delineated by the subject of the legislation under analysis, as the Court has provided in a number of judgements[2]. These circumstances make the freedom of establishment and the free movement of capital *lex specialis* to the general principle of non-discrimination stated in Article 18 TFEU.

As shown by previous studies[3], the principle of non-discrimination is regarded as the negative formulation of the principle of equality[4]. Equality, as a universal fundamental principle, dignifies international relations[5]. Within the European Union framework, the principle of equality is set out in Article 18 TFEU — formerly Article 12 EC Treaty —, which establishes a specific formulation of equality[6] for each type of freedom securing the proper functioning of the common market[7], ultimately guaranteed by the CJEU. The internal market has been taken as a reference by the CJEU as part of its harmonisation policy with a view to attaining the four Community freedoms, based on

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1 Commission Staff Working Paper, Non-discriminatory inheritance tax system: principles drawn from EU case-law. SEC(2011) 1488 final, 3.

2 Judgements of 12 September 2006, *Cadbury Schweppes and Cadbury Schweppes Overseas* (C-196/04), ECLI:EU:C:2006:544, paragraphs 31 to 33; of 3 October 2006, *Fidium Finanz* (C-452/04), ECLI:EU:C:2006:631, paragraphs 34 and 44 to 49; of 12 December 2006, *Test Claimants in Class IV of the ACT Group Litigation* (C-374/04), ECLI:EU:C:2006:773, paragraphs 37 to 38; *Test Claimants in the FII Group Litigation* (C-446/04), ECLI:EU:C:2006:774, paragraph 36; and of 13 March 2007, *Test Claimants in the Thin Cap Group Litigation* (C-524/04), ECLI:EU:C:2007:161, paragraphs 26 to 34.

3 LUCHENA MOZO, G. M.: La justicia tributaria en la imposición directa española a la luz del derecho comunitario: algunas reflexiones. In: Revista Peruana de Derecho Tributario, Universidad de San Martín de Porres Tax Law Review, Year 3, Issue 13, 2009; LUCHENA MOZO, G. M.: El principio de no discriminación en la jurisprudencia del TJUE: incidencia en la imposición directa española. In: Rivista Italiana Di Diritto Pubblico Comunitario, Issues 3-4, 2010, pp. 945-998.

4 This view is also supported by GOGA, G.L.: The General Principle of non Discrimination and Equal Treatment in the Legislation and Jurisprudence of the Court of Justice of the European Union. In: Acta Universitatis Danubius, vol. 5, num. 1/2013, 138.

5 As a fundamental principle of International Law, equality entails equal treatment as set out by Article 24 OECD Model Agreement, yet subject to a reciprocity clause. To this matter, see MARTÍN JIMÉNEZ, A.J., CALDERÓN CARRERO, J.M.: Imposición directa y no discriminación comunitaria. Madrid: Edersa, p. 15 and ff.; MIRANDA PÉREZ, A.: La no discriminación fiscal en los ámbitos internacional y comunitario. Barcelona: Bosch, p. 91 and ff.; MARTÍN JIMÉNEZ, A.J.: No discriminación. AA.VV. In: Convenios Fiscales Internacionales y Fiscalidad de la Unión Europea. CISS, Valencia, 2008, p. 523 ff.

The principle of non-discrimination in terms of tax legislation was promptly acknowledged by the European Court of Human Rights in *Darby* v *Sweden*, (June 2016) DOI= http://hudoc.echr.coe.int/sites/eng/pages/search.aspx?i=001-57642#{"itemid":["001-57642"].

See BARDINI, C.: The Ability to Pay in the European Market: An Impossible Sudoku for the ECJ. In: Intertax, 2010, issue 1, 38, 2; ATTARD, R.: The European Convention on Human Rights (ECHR), tax controversy and tax policy. In: EU direct tax news, 2011, Issue 41 January/February, 2; ERGEC, R.. Taxation and Property Rights under the European Convention on Human Rights. In: Intertax, issue 1, 39, 2011, p. 10.

6 As highlighted by GARCÍA PRATS (1998), the principle of non-discrimination should be interpreted in consideration of each type of freedom: "with regard to the free movement of services, goods and capital, it is a regulatory or administrative obstacle restricting services or goods from other Member States that is considered as discriminatory. By contrast, when it comes to free movement of workers, discrimination occurs by placing obstacles — be it positive or negative —, such as more restrictive or rigorous measures and denial of the advantages granted to nationals themselves, to workers from other Member States or migrant workers" (Cf. Imposición directa, no discriminación y derecho comunitario. Madrid: Tecnos, 1998, p. 42).

7 MABBETT, D.: A Rights Revolution in Europe?. Regulatory and judicial approaches to nondiscrimination in insurance. In: *LEQS* Paper 38/2011. DOI= http://www.lse.ac.uk/europeanInstitute/LEQS/LEQSPaper38.pdf

the equality of treatment between nationals and non-nationals, and thus, on the principle of non-discrimination on the grounds of nationality. The latter principle thus constitutes a fundamental value and right[8].

This new legal and political scenario has provided all European citizens with a number of rights that constitute their set of legal assets, granting them the status of Citizens of the European Union[9]. This status "constitutes the guarantee of belonging to a political community under the rule of law"[10]. This guarantee is in turn grounded in the values of freedom, democracy, and equality shared by all Member States with a pluralistic society and based on non-discrimination, tolerance, justice, solidarity and equality[11], as stated in the current Charter of Fundamental Rights of the European Union of March 2010[12].

However, "the Community notion of discrimination poses a problem to the general taxation system, which distinguishes between residents and non-residents, because this notion is alien to international tax law. From a general perspective, Member States discriminate between resident and non-resident taxpayers and place the two types in different schemes in order to meet a minimum tax revenue threshold, promote national savings, and attract foreign investors"[13]. In addition, it should not be forgotten that Double Taxation Agreements (DTAs) between Member States — which the former Article 220 of the EC Treaty encouraged to conclude — are based on the mutual granting of advantages between two States, advantages that, by definition, are only applicable to residents in the States concerned. As a consequence, the Court "has no other choice but to try to strike a happy medium, being aware that the elimination of DTAs is not possible and preventing tax discrimination from being detrimental to the proper functioning of the internal market"[14].

Undoubtedly, direct tax harmonisation in the European Union is, to say the least, difficult to achieve, given the lack of consensus as to which is the most adequate regulation system[15] that would

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8 IGLESIAS CASAIS, J.M.: No discriminación fiscal y derecho de establecimiento en la Unión Europea. Navarra: Aranzadi, 2007, p. 37.

This view is also held by the European Union Agency for Fundamental Rights: Handbook on European non-discrimination law. Publications Office of the European Union, 2010.

9 Cf. JACOBS, F.G.: Citizenship of the European Union—A Legal Analysis. In: European Law Journal, 2007, Vol. 13, No. 5, 597; TRYFONIDOU, A.: Purely Internal Situations and Reverse Discrimination in a Citizens Europe: Time to "Reverse" Reverse Discrimination. DOI= http://www.um.edu.mt/europeanstudies/books/CD_MESA09/pdf/atryfonidou.pdf.

10 Second Report from the Commission on Citizenship of the Union (COM (97) 230 final.

11 The Boukhalfa judgement of 30 April 1996, (C-214/94), ECLI:EU:C:1996:174, lays the ground for the CJEU to determine the scope, *ratione territori*, of Community provisions on the free movement of persons, more specifically, on the prohibition of discrimination between nationals within the European Union. Contrary to the view that the scope of application of such provisions would be limited to territories of the Member States, the CJEU would extend the scope beyond these territories, addressing situations and circumstances outside the European Union. This way, the CJEU is underscoring the strictly imperative nature of the principle of non-discrimination on grounds of nationality. This principle will be applicable to all situations holding a connection with the Union, whether in- or outside the Community. See GARDEÑES SANTIAGO, M.: La imperatividad internacional del principio comunitario de no discriminación por razón de la nacionalidad. In: Revista de Instituciones Europeas, issue 3, 1996, p. 863 ff.

12 OJEC C 83 of 30 March 2010.

13 HINOJOSA MARTÍNEZ, L. M.: Reflexiones en torno al concepto de discriminación: los obstáculos fiscales a la libre circulación de personas en la CE. In: Revista de Derecho Comunitario Europeo vol. 1, issue 2, 1997, p. 514.

14 Ibid., p. 515.

15 This claim is also made by DAHLBERG (2007). Dahlberg writes that "what is special with the area of direct taxation in relation to the European Union is that there have so far been few acts of law decided upon by the Member States. There are a few directives, but they affect only fragments of the tax law of the Member States, albeit important fragments. Such 'positive integration' has proved difficult for the Member States to agree upon. In stark contrast, there are well over one hundred cases decided by or pending at the Court where measures of direct taxation are questioned in relation to the

harmonise Member States' domestic tax legislations — with a special focus on the principles of tax equity— with the EU's fundamental principles. We are referring to the principle of non-discrimination in matters of income taxes[16], provided by the CJEU at the judgement *Commission* v *France - Avoir Fiscal* on 28 January 1986[17]. This judgement gave rise to a long series of ensuing judgements on the prohibition of tax discrimination in matters of direct taxation and on limited tax obligation. The effects of this principle affect other tax regulations, such as Corporation Tax (CT) — more specifically, undercapitalisation (Article 20 of the Consolidated Version of the Spanish Law on Corporation Tax)[18] and R+D deduction (Article 35 of the Consolidated Version of the Spanish Law on Corporation Tax[19]) —, and recently, Inheritance and Gift Tax (IGT). IGT is affected by the overused equality of treatment (based on the principle of non-discrimination), resulting in decreased tax power of Member States[20].

It should be noted that although direct taxation falls within the competence of individual Member States, the latter should also respect Community Law[21], and particularly, the principle of non-discrimination. This said, the rules regarding equal treatment forbid not only overt discrimination by reason of nationality but also all covert forms of discrimination which, by the application of other criteria of differentiation, lead in fact to the same result[22].

Consequently, discrimination can arise only through the application of different rules to comparable situations or the application of the same rule to different situations[23]. To this rule we should add a fun-

fundamental freedoms of the EC Treaty. In the large majority of the decided cases the outcome has been that national tax laws have been found to be in breach of fundamental freedoms. This has been labelled "negative integration". Such integration is problematic. The complex solutions needed for the facilitation of cross-border movement also in the area of direct taxation require general Community measures like directives. The Court can only respond to the isolated questions put before it." (Cf. The European Court of Justice and direct taxation: a recent change of direction, in National Tax Policy in Europe. München: Springer Gmbh & Co, 2007, p. 167).

16 According to GONZÁLEZ GARCÍA (2004), the role of the principle of non-discrimination has changed over time in the jurisprudence of the CJEU to the point of becoming "the main limit to the exclusive competence that Member States rely on in terms of national taxation […] [Consequently] the effects of this principle may cause the foundations of Member States' taxation systems to fall apart" (Cf. Una aproximación al contenido de los conceptos de no discriminación y restricción en el Derecho Comunitario. In: Documentos, issue 8, 2004, p. 10).

For a similar view, see HERRERA MOLINA, P.: Los Convenios de Doble Imposición ante las libertades comunitarias (Análisis de la Jurisprudencia del TJCE). In: Fiscalidad internacional. CEF, Madrid, 2005, p. 1079-1080.

According to the Directive of the Committee of the Regions on Frontier workers: Assessment of the situation after 20 years of the internal market: problems and perspectives – the development of Community-wide social law should not be left mainly to the European Court of Justice, but should itself actively contribute to solving frontier worker problems (OECD C 43, of 18 Februar 2005).

17 Judgement of 28 January 1986, *Commission* v *France Avoir Fiscal*, (C-270/83), ECLI:EU:C:1986:37.

18 Judgements of 12 December 2002, *Lankhorst-Hohorst*, (C-324/00), ECLI:EU:C:2002:749; of 13 March 2007, *Test Claimants in the Thin Cap Group Litigation*, (C-524/04), ECLI:EU:C:2007:161.

19 Judgement of 13 March 2008, (C-248/06), ECLI:EU:C:2008:161, which orders Spain to modify its regulation by virtue of Law 4/2008 of 23 December, so that deduction of costs relating to research and development is equally favourable in respect of costs incurred in Spain, in any Member State of the EU or the EEA.

20 See, to that matter, the cited Judgement *Manninen* (C-319/02), paragraph 19.

Cf. also MASON, R.: Flunking the ECJ's Tax Discrimination Test. In: Columbia Journal of Transnational Law, vol. 46, 2007. DOI= http://ssrn.com/abstract=1025522.

21 See judgements of 11 August 1995, *Wielockx*, (C-80/94), ECLI:EU:C:1995:271, paragraph 16; of 16 July 1998 ICI, (C-264/96), ECLI:EU:C:1998:370, paragraph 19; of 29 April 1999, *Royal Bank of Scotland*, (C-311/97), ECLI:EU:C:1999:216, paragraph 19; *Manninen*, (C-319/02), cited above, paragraph 19; of 6 March 2007, *Meilicke* and Others, (C-292/04), ECLI:EU:C:2007:132, paragraph 19; and of 24 May 2007, *Holböck*, (C-157/05), ECLI:EU:C:2007:297, paragraph 21.

22 Judgement of 14 February 1995, *Schumacker*, (C-279/93), ECLI:EU:C:1995:31, paragraph 26.

23 Cited-above judgements, *Schumacker*, (C-279/93), paragraph 30; of 29 April 1999, *Royal Bank of Scotland*, (C-311/97), paragraph 26; of 14 September 1999, *Geschwind*, (C-391/97), ECLI:EU:C:1999:409, paragraph 21; of 27 March 2007, *Talotta*, (C-383/05), ECLI:EU:C:2007:181, paragraph 18.

damental provision set out by the Court in relation to Personal Income Tax. According to this provision, the situations of residents and of non-residents are not, as a rule, comparable since they are objectively different in terms of where the major part of their income is normally concentrated, their personal ability to pay tax as well as their personal and family circumstances[24]. Nevertheless, tax benefits granted only to residents of a Member State may constitute discrimination in the spirit of the Treaty if there is no objective difference between the situations of a non-resident and a resident that justifies different treatment in this regard[25]. The CJEU has not conducted a test of comparability in the Judgement under analysis, as it did not in the Judgement handed down on the Spain case (C-127/12). This means that the CJEU is implicitly dismissing any justification for a difference between the two types of taxpayer.

Until recently, there were no measures for harmonisation of EU legislation in direct taxation[26], and even less so in IGT. In the absence of regulations, IGT falls within the competence of individual Member States. However, Member States should respect the fundamental freedoms enshrined in the EU Law, and thus, they may not discriminate by reason of nationality or restrict these freedoms arbitrarily. The terms *discrimination* and *restriction on Community freedoms* have co-occurred and been used interchangeably in CJEU Judgements[27]. This may be the reason why no test of comparability was conducted. The opposite argument would involve a need for the Court to set a criterion when to use a test of comparability in order to objectively deliver judgements. To our view, although the Schumacker test seems to be implicitly overridden in Welte[28], it would be better off relying on a specific criterion in cross-border situations[29].

The Court also holds that Member States are not obliged to eliminate double taxation arising from the exercise in parallel of their fiscal sovereignty[30]. The few number of DTAs on IGT[31] makes

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24 Cited-above judgements, *Schumacker*, (C-279/93), paragraphs 31 to 34; *Wielockx*, (C-80/94), paragraph 18; of 27 June 1996, *Asscher*, (C-107/94), ECLI:EU:C:1996:251, paragraph 41; and Talotta, (C-383/05), paragraph 19.

25 Cited-above judgements, *Schumacker*, (C-279/93), paragraphs 36 to 38, *Asscher*, (C-107/94), paragraph 42; *Talotta*, (C-383/05), paragraph 19; of 18 June 2007, *Lakebrink and Peters-Lakebrinkde*, (C-182/06), ECLI:EU:C:2007:452, paragraph 29; and of 16 October 2008, *Renneberg*, (C-527/06), ECLI:EU:C:2008:566, paragraph 60.

26 The OECD began to work on inheritance matters in 1963, producing a Draft Convention to address the issue of double taxation on inheritances. On 31 May 1966, the first Model Double Taxation Convention on Inheritance Tax came to light. It was back in 1982 that the current DTA (Double Taxation Agreement) was drafted. This DTA extends its scope of application to *inter vivos* gifts, which were not provided for in the 1966 Model (Article 2.1 OCDE 1982).

27 See DAFNOMILIS, V.: A Comprehensive Analysis of ECJ Case Law on Discriminatory Treatment of Cross-Border Inheritances – Part 1. In: European Taxation, vol. 55, issue 11, 2015, p. 506.

28 (C-181/12), EU:C:2013:662, paragraph 46.

29 In this line of argumentation, see DAFNOMILIS, V.: A Comprehensive Analysis of ECJ Case Law on Discriminatory Treatment of Cross-Border Inheritances – Part 2. In: European Taxation, vol. 55, issue 12, 2015, pp. 575-577.

30 Judgement of 12 February 2009, *Block*, (C-67/08), ECLI:EU:C:2009:92, paragraph 30.

31 This type of agreement is particularly uncommon, particularly when compared to agreements on income and wealth tax. In fact, Spain has so far signed only three DTAs on IGT, namely: Greece (6 March 1919), France (Official State Gazette of 7 January 1964), and Sweden (Official State Gazette of 16 January 1964). Moreover, these agreements are so old that the only settled case-law that they include in this regard is but a ruling settled by the Directorate General for Taxation (12 February 1990). For further details, see LUCHENA MOZO, G. M.: Las PYMES familiares en Europa: notas sobre su tratamiento fiscal. In: Noticias de la Unión Europea, issue 303, 2010, p. 138; and TRINXET LLORCA, S.: European Union Direct Taxes. UK: Asset Protection Publishing, 2010, p. 121-122.

DTAs on IGT signed by Italy are also very few. Moreover, Italy's domestic law sets out a provision for unilateral elimination of double taxation, provided for by Article 26(1)b from the Decree Law 346/1990. See ALTANA, E. – SILVESTRI, L.: L'imposta sulle successioni e donazioni nel Testo Milano: Unico, 1963, p. 14.

For DTAs on IGT signed by Member States, see Commission Recommendation regarding relief for double taxation of inheritances, COM (2011) 8819 final. Annex II, 12; and European Union 2015. Ways to tackle inheritance cross-border tax obstacles facing individuals within the EU. Luxembourg, p. 14.

the problem even more evident[32]. This problem would be solved by developing a multilateral instrument, which was suggested for the first time at a symposium on transferring businesses organised by the European Union and held in Brussels on 29–30 January 1994. Considering the Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (90/436/EEC), the implementation of a multilateral instrument would not be totally unfamiliar to the EU. Moreover, a multilateral instrument would also be in line with the provisions laid down in Action 15 of the OECD Base Erosion and Profit Shifting (BEPS) Plan. In any case, the effectiveness of the instrument would be yet to be determined.

Given the significance of IGT and its impact on the effectiveness of Community freedoms, the Commission Staff[33] paid special attention to IGT in cross-border situations in the *Commission Recommendation regarding relief for double taxation of inheritances*[34]. Added to this is the Opinion of the European Economic and Social Committee on the 'Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee — Tackling cross-border inheritance tax obstacles within the EU'[35].

The Commission and the Economic and Social Committee argue that cross-border inheritance tax obstacles could be tackled without adopting an instrument that would harmonise Member States' regulations on cross-border inheritance tax [36]. This instrument would then also be subject to tax-related strategies of each Member State. An apparently more effective way to tackle obstacles involves interfacing Member States' national tax systems, thus reducing chances of double or multiple inheritance taxation[37]. By the same token, the Commission requires, by virtue of fundamental freedoms enshrined by Community Treaties, that Member States should refrain from levying IGT that discriminates against cross-border situations[38].

See RUST, A.: The concept of residence in inheritance tax law. In: Residence of individuals under tax treaties and EC law. Amsterdam: IBFD, p. 85-103.

32 This claim is also made in CUESTA DOMÍNGUEZ, J. – CARMONA MENDOZA, P.: La eliminación de la doble imposición internacional en materia de sucesiones: un camino aún por recorrer. In: Revista Aranzadi, issue 11, BIB 2012, p. 361. DOI= www.westlaw.es.

See also MAISTO, G.: The pursuit of harmonization regarding taxes on death and the international implications. In: Bulletin of International Taxation, 2011, vol. 65, issues 4-5, p. 253 ff.

33 SEC(2011) 1488 final, SEC(2011) 1489 final, and SEC(2011) 1490.

See COM(2010) 769 and Commission Staff working paper SEC(2010) 1576.

34 COM (2011) 8819 final.

35 Opinion of the European Economic and Social Committee on the 'Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee — Tackling cross-border inheritance tax obstacles within the EU', COM(2011) 864 final] (2012/C 351/09).

36 This opinion does not seem to be expressed in the Report of the European Union Expert Group. 2015. Ways to tackle inheritance cross-border tax obstacles facing individuals within the EU, p. 23, where one of the conclusions read: "By far the better solution to the problems we have identified would be the adoption of an instrument of EU law. The recommendation which the Commission has already made could be made legally binding".

37 The Opinion of the European Economic and Social Committee on the 'Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee — Tackling cross-border inheritance tax obstacles within the EU' specifically comments that "the approach of merely providing recommendations for implementation by individual Members States may be viewed to be not sufficiently effective in practice – it is recognised that it is also desirable, as the Commission is proposing, for individual Member States to be encouraged, in an expeditious manner, to operate multiple taxation relief mechanisms in a more effective and flexible manner, while the Commission would observe developments over the next three years with a view of adopting a stronger stance through a Directive if so required".

38 See O'SHEA, T.: Belgian Inheritance Tax Rules Breach EU Law. In: Tax Notes International, issue 18, 2011, p. 217 and ff.

Some CJEU Judgements addressing situations contrary to inheritance taxation systems pursuant to Community Law[39] are the following:

a) Judgement of 11 December 2003, *Barbier* (C-364/01, ECLI:EU:C:2003:665), is one of the first to prosecute a case involving a Netherlands' provision, where certain assets of a deceased's estate situated in the Netherlands and liable to transfer duty are levied differently according to whether the deceased resided in the Netherlands or abroad at the time of death. The Court finds that, within the meaning of Directive 88/361, national provisions that determine the value of immovable property for assessment of inheritance tax liability based on the criterion of residence are a restriction to the free movement of capital.
b) In the Geurts and Vogten Case (C-464/05, ECLI:EU:C:2007:631), the CJEU found, as far as freedom of establishment is concerned, that discrimination arises when family companies are not allowed to deduct inheritance tax liabilities because the companies do not employ workers from the Member State at issue.
c) In the Jäger Case (C-256/06, EU:C:2008:20), the Court found that free movement of capital prohibits Member States to implement legislation that advantages assets situated in the Member State at issue with a particularly favourable assessment and partial exemption over assets situated in other Member States, which would be assessed on the basis of regulations following fair market value. The calculation of the tax is directly linked to the value of the assets included in the estate, with the result that there is objectively no difference in situation such as to justify unequal tax treatment so far as concerns the level of inheritance tax payable in relation to, respectively, an asset situated in Germany and an asset situated in another Member State. A situation such as that of Mr Jäger is therefore comparable to that of any other heir whose inheritance consists only of agricultural land and forestry situated in Germany bequeathed by a person domiciled in that State[40].
d) In the Eckelkamp case (C-11/07, ECLI:EU:C:2008:489), 2008, free movement of capital is also taken as the fundamental criterion to lay down that the situation of a non-resident heir who acquires immovable property located in Belgium and the situation of a resident heir are comparable in relation with the rules governing the taxable amount of the inheritance tax[41].
e) In the same vein, in the Judgement of 11 September 2008, Arens-Sikken case (C-43/07, ECLI:EU:C:2008:490), the Court held that the rules of a Member State are contrary to EU Law if an heir is allowed to deduct debts by reason of inheritance solely when the heir is residing in the Member State where the property is situated[42].

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39 This was not the case for the cited-above Judgement, *Van Hilten-Van der Heijden*, (C-513/03), of 18 December 2014, Q, (C-133/13), ECLI:EU:C:2014:2460.

In this Sentence, the CJEU "holds, in relation to inheritance tax, that the fact that the grant of tax advantages is made subject to the condition that the asset transferred be situated in the national territory constitutes a restriction on the free movement of capital prohibited, in principle, by Article 63(1) TFEU (paragraph 20)". This decision applies save "the difference in treatment relates to situations which are not objectively comparable, such comparability being required to be assessed on the basis of the object and content of the national provisions at issue in the main proceedings" (paragraph 22). Precisely, this is mentioned in the main proceedings, given that "the object of the exemption from gift tax provided for by the Netherlands rules at issue in the main proceedings is to protect the integrity of the estates that are typical of the traditional Netherlands landscape" (paragraph 24).

See BROEK, J.J. VAN DEN – WILDEBOER, M.R.: European Court of Justice permits inheritance tax based on nationality in Van Hilten-Van der Heijden. In: Bulletin for International Taxation, vol. 61, issue 5, 2007, pp. 214-219.

40 Paragraph 44.

41 Paragraphs 61 and 63.

42 Paragraph 46.

f) The Court also held that a provision on inheritance and gift tax in the Mattner case (C-510/08, EU:C:2010:216), where the allowance to be set against the taxable value in the case of a gift of immovable property in the State at issue is smaller where the donor and the donee are resident in another Member State than the deduction which would have applied if at least one of them had been resident in the Member State at issue, is incompatible with the free movement of capital[43].

g) In the Halley case (C-132/10, ECLI:EU:C:2011:586), the Court found it discriminatory that in matters of inheritance tax, a Member State provides for a limitation period for the valuation of registered shares which differs according to whether or not the centre of effective management of the company in which the deceased was a shareholder is situated in the Member State at issue. The Court held that a restriction on the exercise of free movement of capital cannot be justified[44], on the grounds that the application of a limitation period of 10 years is not based on the time needed by the tax authorities of the Member State to have effective recourse to mechanisms of mutual assistance between Member States or other alternative means of investigating the value of the shares in question.

h) In the Scheunemann case (C-31/11, ECLI:EU:C:2012:481), the Court held that legislation of a Member State which, for the purposes of the calculation of inheritance tax, excludes the application of certain tax advantages to an estate in the form of a shareholding in a capital company established in a third country, while conferring those advantages in the event of the inheritance of such a shareholding when the registered office of the company is in a Member State, primarily affects the exercise of the freedom of establishment for the purposes of Article 49 TFEU et seq., since that holding enables the shareholder to exert a definite influence over the decisions of that company and to determine its activities. Those Treaty provisions are not intended to apply to a situation concerning a shareholding held in a company which has its registered office in a third country[45].

i) The Court's Judgement in Welte (C-181/12, EU:C:2013:662) holds that "as regards inheritances, the measures which Article 56(1) EC prohibits as being restrictions on the movement of capital include those whose effect is to reduce the value of the inheritance of a resident of a State other than the State in which the assets concerned are situated and which taxes the inheritance of those assets[46]. In other words, and most importantly, "the situations of those subject to inheritance tax, be resident or non-resident, are wholly comparable, although a resident heir is taxed on all of the assets acquired, whereas a non-resident heir is only taxed on the assets situated in the Member State levying tax[47].

j) Judgement of 4 September 2014 (C-211/13, EU:C:2014:2148) was delivered following the infringement proceedings against Germany because of derogation of the Inheritance and Gift Tax Scheme (*Erbschaftsteuer-und Schenkungsteuergesetz* – ErbStG-), which provides that tax is solely

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43 See O'SHEA, T.: News Analysis: No Excuses for German Gift Tax Rule. In: Tax Notes International, issue 28, 2010, pp. 1021 ff.; VICENTE-ARCHE COLOMA, P.: El Impuesto sobre Donaciones y la libre circulación de capitales a la luz de la Sentencia Mattner, de 22 de abril de 2010 (C-510/08). In: Noticias de la Unión Europea, issue 330, 2012, p. 139.

44 See O'SHEA, T.: Belgian Inheritance Tax Rules Successfully Challenged Before the ECJ. In: Tax Analysts, issue 5, 2011, p. 721 ff.

45 O'SHEA, T.: German Inheritance Tax Rules Upheld by the ECJ. In: Tax Notes International, issue 15, 2012, p. 289 ff.

46 Welte Judgement, (C-181/12), cited above, paragraph 23.

47 WATTEL, P. J.: Progressive Taxation of Non-Residents and Intra-EC Allocation of Personal Tax Allowances: Why Schumacker, Gilly and Gschwind do not suce. In: European Taxation, Volume 40, issue 6, 2000, pp. 227-228; HERRERA MOLINA, P.M.: STJUE WELTE: ¿El fin de las reducciones y beneficios fiscales autonómicos en el Impuesto sobre Sucesiones? In: ECJ leading cases, Tributos, gasto público y la crisis del Estado de Derecho, 2015. https://ecjleadingcases.wordpress.com/?s=+WELTE.

levied on immovable property situated in Germany. Under this scheme, a significantly lower allowance is applicable if the donor or deceased person and the recipient of the inheritance or gift are non-residents at the time of the succession or donation, in contrast to a situation where at least one of them resides in Germany. This applies despite the legislative amendment made to the Inheritance and Gift Tax Scheme in 2011 following the judgment in Mattner (C-510/08, EU:C:2010:216), where non-residents are granted the possibility to be treated, upon request, in Germany as tax residents for the purposes of gift and inheritance tax. However, this option does not, in view of the Commission, eliminate the infringement[48].

k) Judgement of 4 September 2014 was delivered following the infringement proceedings against Spain (C-127/12, EU:C:2014:2130)[49]. The Court finds that Spain does not comply with the obligations laid down by TFUE in permitting different succession and donation tax treatments between resident and non-resident successors and donees in Spain, between deceased persons residing and not residing in Spain and between donations and similar arrangements of immovable property located inside and outside Spain.

l) Judgment of the Court of 16 July 2015 (C-485/14, ECLI:EU:C:2015:506). According to the Commission, the Court declares that, French legislation, as interpreted by the tax authorities, exempts from droits de mutation à titre gratuit gifts and legacies to public bodies or to charitable bodies only where such bodies are established in France, in a Member State or in a State which is party to the Agreement on the European Economic Area which has concluded a bilateral agreement with France. The Commission considers that that constitutes a restriction on free movement of capital, contrary to Article 56 EC and Article 40 of the EEA Agreement.

Based on the abovementioned rulings, TFEU holds that free movement of capital is restricted in the following cases:

- If the value of an inheritance or gift is reduced as a result of a higher tax burden on the acquirer who resides in a Member State other than that of the deceased or donor[50];
- If non-residents are treated more favourably[51];
- In case of restriction on deductibility of liabilities linked to inheritance assets[52];
- If resident taxpayers are granted higher personal allowances than non-resident taxpayers[53].

48 IP/12/1018, http://europa.eu/rapid/press-release_IP-12-1018_de.htm.
It could not be otherwise after Judgement of 18 March 2010, Gielen, (C-440/08), ECLI: EU:C:2010:148, where the Court holds that the possibility granted to non-residents does not eliminate the infringement.

49 LUCHENA MOZO, G. M.: La definitiva configuración del estatuto del no residente comunitario en la imposición directa tras la sentencia de 3 de septiembre de 2014, Comisión/España, (C-127/12). In: Rivista di Diritto Tributario Internazionale, 3/2013; ROVIRA FERRER, I.: The taxation of gratuitous transfers between immediate family members: an analysis of the Spanish perspective. In: European Taxation, vol. 55, issue 8, 2015, p. 385.

50 See abovementioned Judgements Jäger, (C-256/06), paragraph 31, and Mattner, (C-510/08), paragraph 25.
See also GARCÍA DE PABLOS, J. F.: Impuesto sobre Sucesiones y Donaciones en España: la necesaria reforma a la luz de la jurisprudencia del TJUE. In: Quincena Fiscal, issue 17, BIB 2010, 1975. DOI= www.westlaw.es; LUCAS DURÁN, M.: Fiscalidad y libre circulación de capitales y pagos en el Derecho de la Unión Europea: análisis jurisprudencial. In: Documentos de Trabajo UC-CIFF-IELAT, issue 8, 2012. DOI= http://www.ciff.net/attachments/publicaciondtc8.pdf; CALVO VÉRGEZ, J.: La aplicación del Impuesto sobre Sucesiones y Donaciones a los no residentes a la luz de los últimos pronunciamientos de la Comisión Europea. In: Quincena Fiscal, issue 11, BIB 2013, p. 1177. DOI= www.westlaw.es.

51 As found in the abovementioned Judgement Van Hilten-Van der Heijden, (C-513/03), paragraph 41.

52 See COPENHAGEN ECONOMICS. Study on Inheritance Taxes in EU Member States and Possible Mechanisms to Resolve Problems of Double Inheritance Taxation in the EU, August 2010, p. 7.

53 See, to that matter, Judgements of 4 September 2014, Commission/Germany (C-211/13) and Commission/Spain (C-127/12), cited above.

This all applies in the understanding that the existence of an option which would possibly render a situation compatible with EU law does not, in itself, correct the unlawful nature of a system which still includes a mechanism of taxation that is not compatible with that law[54]. This is referred to by the CJEU in Judgement of 8 June 2016, Hünnebeck, (C-479/14, ECLI:EU:C:2016:412), paragraph 42.

As a result of the above, many Member States still have great difficulty making their domestic tax regimes entirely compatible with rules on free movement of capital laid down by the Treaty[55]. Evidence can be found in the number of procedures undertaken by the Commission in relation to a variety of inheritance tax regulations in different Member States, as documented in this paper. It should also be noted that the majority of Member States have an inheritance tax regime, which normally takes place of residence as the criterion for inheritance tax assessment [56]. However, the CJEU does not legitimise any tax rules that establish a difference in treatment between taxpayers based on their place of residence[57], but such a difference in treatment must concern situations which are not objectively comparable or be justified by overriding reasons in the general interest[58]. In the case at issue, the Court held that "a national tax legislation which, for the purposes of calculating inheritance tax, treats residents and non-residents or assets situated inside and outside the Member State concerned on the same footing cannot, without being discriminatory, treat the two categories of taxpayer or asset unequally as far tax reduction is concerned[59]. It then follows that there is no objective difference between the two taxpayer models justifying unequal tax treatment. This general statement was also sufficient for the CJEU to find a breach of the Treaty Law in its Judgement of 3 September 2014, Commission/Spain, (C-127/12). Thus no effective comparability analysis was necessary to be conducted, but it would have been highly advisable, given the singularities of the Spanish legal regime[60]. Conducting the analysis would also be positive because it would raise the question whether or not the test of comparability and the justification of the measure overlap[61].

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54 See the Court's ruling in Judgement of 18 March 2010, Gielen, (C-440/08), cited above, where the Court declares that the possibility granted to non-residents excludes any validatory effects, since it would involve opting for a discriminatory or non-discriminatory regime. Arguing otherwise would mean "validating a tax regime which, in itself, remains contrary to Article 49 TFEU by reason of its discriminatory nature" (paragraph 52). It thus follows that "the choice offered, in the dispute in the main proceedings, to non-resident taxable persons by means of the option to be treated as resident taxable persons does not serve to neutralise the discrimination established in paragraph 48 above" (paragraph 54).

55 COPENHAGEN ECONOMICS. Study on Inheritance Taxes in EU Member States and Possible Mechanisms to Resolve Problems of Double Inheritance Taxation in the EU, pp. 7 and 33.

See also MOLL, H. – RAVENTÓS CALVO, S.: Case Study: On possible double taxation and other problems affecting the Free Movement of Persons and Capital within Europe resulting from Inheritance tax, illustrated by the example Gemany/Sapin. In: European Taxation, Volume 45, 2005, issue 9/10, pp. 452-460.

56 Belgium, Czech Republic, Denmark, Finland, Germany, Hungary, Ireland, Italy, Lithuania, Luxemburg, The Netherlands, Poland, Slovenia, and Spain are the Member States in the EU that take residence as a criterion for inheritance tax assessment.

See also COPENHAGEN ECONOMICS. Study on Inheritance Taxes in EU Member States and Possible Mechanisms to Resolve Problems of Double Inheritance Taxation in the EU, p. 21.

57 See GARCÍA DE PABLOS, J. F.: La urgente reforma del Impuesto sobre Sucesiones y Donaciones en España a la luz del Derecho comunitario. In: Quincena Fiscal, issue 18, BIB 2014, p. 3507. DOI= www.westlaw.es.

58 See abovementioned Judgement Arens-Sikken, (C-43/07), paragrah 53.

59 See abovementioned Judgement of 26 May 2016, Commission/Hellenic Republic, paragraph 36.

60 GARCÍA PRATS, F.A.: El Derecho de la unión Europea ante la encrucijada del Impuesto sobre Sucesiones y Donaciones español. In: Revista Española de Derecho Financiero, issue 164, 2014, pp. 33-34.

61 See WATTEL, P.: Non-Discrimination à la Cour: The ECJ' s (Lack of) Comparability Analysis in Direct Tax Cases. In: European Taxation, vol. 55, 2015, issue 12, p. 542.

However, as highlighted above, inheritance tax obstacles do not exclusively arise from discrimination found in domestic legislation systems between cross-border and national-only situations, but also from risk of double taxation. For this reason, the Commission has opted for a flexible approach to the matter, promoting coordination between national law regimes in entire compliance with rules on tax policy[62]. However, it is yet to be determined if the Commission's initiative demonstrates effective in the tax regimes of Member States[63].

3 CONCLUSIONS

This paper calls for the need to stay informed about upcoming rulings issued by the CJEU on IGT in its process of adaptation to and regularisation in Community Law, rulings that will certainly continue to be issued in the future. Since direct taxation is still the responsibility of Member States, it is Member States that tackle problems caused by management of this taxation at Community level. However, action by the EU seems to be justified not only because of inaction of Member States themselves, but also because of the impact that this inaction has on the interior market. This impact is precisely what justifies EU action. Union action, which departs from harmonisation, shall respect the principle of proportionality (as laid down by Article 5 TEU9), but it shall have a bearing on Member States' legislation systems. The problem emerges in the way Community Law may/should have an influence on Member States' legal regulations[64]. In this regard, risk comes from finding obstacles to the normal functioning of the interior market in matters of taxation as a potential reason for the Union to consider that any national tax measures affecting national and cross-border situations are contrary to Community Law, unless the Court considers that there is justification for those measures to be taken.

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62 Opinion of the European Economic and Social Committee on "Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee – Tackling cross-border inheritance tax obstacles within the EU", COM(2011) 864 final.

63 See NAVEZ, E.J.: The Influence of EU Law on Inheritance Taxation: Is the Intensification of Negative Integration Enough to Eliminate Obstacles Preventing EU Citizens from Crossing Borders within the Single Market? In: EC Tax Review, vol. 21, issue 2, 2012, p. 93.

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64 The Report of the European Union Expert Group. Ways to tackle inheritance cross-border tax obstacles facing individuals within the EU, 2015, p. 19, reads: "although the recommendation has been ignored by Member States, it has not been met with strong expressions of hostility. It would, therefore, be reasonable for the European Commission to propose that the terms of the recommendation be turned into a regulation".

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Contact information:

Gracia M. Luchena Mozo
Full Professor Tax Law, International Centre for Financial Studies
Gracia.Luchena@uclm.es
University of Castilla-La Mancha (Spain)
Plaza de la Universidad 1, 02071, Albacete. Spain.
Telephone: 0034967599200, ext. 2317

COLLECTIVISM V. INDIVIDUALISM: CAN THE EU LEARN FROM THE HISTORY OF THE ISRAELI KIBBUTZ?[1]

Nellie Munin
LLD, Advocate, independent scholar, Former Minister of Economic Affairs in the Israeli Mission to the EU
Former Chief Legal Advisor, State Revenue Administration, the Israeli Ministry of Finance.
Former Associate Professor at the law school, Zefat Academic College, Israel.

Abstract: The EU seems to share some basic characteristics with the original model of the Israeli Kibbutz: both aim at enhancing a society based on solidarity and mutual guarantee, where members' contribution is proportional to their abilities while their benefits are determined according to their needs. Both are underlined by the perception of subsidiarity, according to which the alliance is stronger than each of its individual members and can thus enhance their welfare more efficiently. On the other hand, both the Kibbutz and the EU were or are facing similar dilemmas. This paper reviews the efforts of Israeli Kibbutzim to encounter these challenges throughout their history, assessing whether a lesson relevant to current EU dilemmas can be drawn.

Keywords: Kibbutz, European Union, Integration, Crises.

1 INTRODUCTION

The kibbutz is a unique way of community life, forming one of the symbols of the State of Israel. In Israel, there are 270 kibbutzim, encompassing less than 150,000 inhabitants.[2]

The EU is an international alliance of 28 member states, encompassing more than 500 million inhabitants.

There are some other, substantial differences between the kibbutz and the EU: first, the kibbutz was established *bottom up*, by groups of pioneers who, at first, were not directed by a supreme authority such as a government. The EU was established *top down* by a group of leaders and thinkers. The top down approach continues to characterize EU development and functioning, forming a constant source of tension between EU authorities, on the one hand, and its citizens and member states, on the other hand. Second, kibbutz founders aimed to create a new form of community, inspired by communism or socialism. EU founders were motivated by a political desire to prevent the next

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[2] This number forms about 2% of the Jewish population, encompassing 6.45 million inhabitants, and about 1.7% of the entire Israeli population, encompassing 8.63 million inhabitants at the end of 2016. The Israeli Central Bureau of Statistics, 2017 Population. Available at: http://www.cbs.gov.il/publications17/yarhon0117/pdf/b1.pdf

war and by a capitalist desire to create a strong and competitive economic alliance. Third, the kibbutz started from a collective model, based on full sharing of assets, burden and privileges. The EU started with individual member states, striving towards gradual market integration.

Despite these differences, the EU seems to share some basic characteristics with the original model of the Israeli Kibbutz: both are underlined by the principle of their members' equality; Both aim at enhancing a society based on solidarity and mutual guarantee, where members' contribution is proportional to their abilities while their benefits are determined according to their needs; both follow the notion of subsidiarity, according to which the alliance is stronger than each of its individual members and can thus enhance their welfare more efficiently, e.g. by initiating mutual projects that could not be obtained individually.

Attempting to live by their basic values, both the kibbutz and the EU were or are facing similar dilemmas.

This paper will depict the basic characteristics and perceptions of the kibbutz, reviewing the changing strategies Israeli kibbutzim chose to meet these challenges during the years. Assessing their success or failure, it will try to draw a lesson relevant to current EU dilemmas, taking into account the differences between these two models.

2 THE ISRAELI KIBBUTZ – 1909-2017

Brief History of the Kibbutz

The kibbutz – a unique social and economic unit, traditionally based on agriculture, was developed by Jewish newcomers to Palestine long before the State of Israel was established. The first kibbutz, established in 1909, was Degania, situated in the North of Israel, near the Sea of Galilee.[3] Kibbutzim's founders faced a tough surrounding: most of the land was either rocky, swampy or a desert. The sanitary conditions were poor. Diseases such as malaria, typhus and cholera were common. Arab and Bedouin threats were constant. The Ottoman authorities, who ruled Palestine until 1918, had made Jewish immigration to Palestine difficult and restricted land purchases by Jews. The British regime that replaced the Ottoman regime following World War I, encouraged Jewish immigration, mainly from eastern Europe and Russia, to Palestine during the 1920's. At that time, Jewish youth movements flourished, being active both in Palestine and abroad, facilitating immigration to Israel and the development of new kibbutzim. Kibbutzim established during this period enjoyed many more members than the first ones.[4] Most of them were enthusiastic, ideologically motivated youngsters. Some kibbutzim movements were developed, representing different ideological, political and religious orientations. Each kibbutz became associated with one of these movements.[5] Gradually, the kibbutzim assumed a military role, actively participating in the protection of the 'Yishuv' – the pre-state, and the resistance to the British regime that later begun to restrict Jewish immigration

[3] See Degania Group. Available at: www.Degania.org.il.

[4] For example, while Degania started with 12 members, Ein Harod, situated in the North near Mount Gilboa, had 239 members when it moved to its permanent location in 1930.

[5] For the different ideological narratives of the different movements see: STERNHELL, Z.: The Founding Myths of Israel: Nationalism, Socialism and the Making of the Jewish State. Princeton: Princeton University Press, 1998.

and the establishment of new Jewish settlements, due to Arab pressure.[6] Some kibbutzim were established in outlying areas to ensure that the land would be incorporated into the future Jewish state.

When Israel was established, in 1948, the kibbutz was already a well-developed, leading model of settlement, practiced by 6.5% of the Jewish population of Israel.[7]

In the coming years, the kibbutzim continued to assume important defense functions. Their relative contribution to the new state's defense, politics and economy was larger than their relative share in its population.[8] They took an active part in the challenges faced by the new state. Their flourishing and strong position in the Israeli society continued until mid-1980's.

Despite their success, internal social cracks begun to occur and grow in the kibbutzim during these years. A severe financial crisis that took place from end 1970's, reinforcing a social crisis, forced the kibbutzim into a process of privatization that had substantially changed their original nature, from collective to more individual, privatized settlements. Nowadays these 'renewed kibbutzim', encompassing the majority of the 270 kibbutzim existing in Israel,[9] enjoy a new blossom, attracting many Israelis to choose them as their homes. Some of them present very impressive economic achievements.[10]

The original collectivist model

The kibbutzim begun as utopian communities, a combination of Zionism and socialism.[11] Many of the Kibbutzim's founders, originating in Eastern Europe and pre-revolution Russia, were inspired by the socialist vision. Others were educated in youth movements, according to the same principles. They shaped the original kibbutz accordingly.

The original model of the kibbutz was very idealistic, thus very strict. Its original founders, many of whom originated in middle or high class families abroad and deserted their convenient life style out of idealism, were ready to suffer very tough standards of living to avoid any compromise on their model. Thus, for example, members of the original kibbutzim did not enjoy any private ownership: all assets were shared by all members. This rule, illustrating a high level of *material equality*, applied

6 LIEBLICH, A.:.Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, pp. 29-30, 73-85.

7 While the *percentage* of kibbutz members compared to other Israeli citizens gradually descended, the *number* of kibbutz members constantly augmented. In 1948, there were 46,940 kibbutz members in Israel. In 2005, 117,685 kibbutz members formed only 2.2% of the Israeli Jewish population. The Israeli Central Bureau of Statstics. The Kibbutzim and Their Population: Demographic Changes During the Years 1961-2005, 2008. Available at: http://www.cbs.gov.il/publications/kib05/pdf/h_print.pdf

8 For example, in the Independence War (1948) Israel lost 5,800 soldiers. 850 (12%) were kibbutz members. In the Six Day War (1967) Israel lost 800 soldiers. 200 (25%) of them were kibbutz members; In the 1960's, when kibbutz members formed 4% of the Israeli population, 15% of the Israeli parliament (Knesset) members were kibbutz members: BETTELHEIM, B.: The Children of the Dream. New York: Simon & Schuster, 2001, p. 15. During these years, the kibbutzim's standard of living was higher than that of the rest of Israel. One of the signs for that was the establishment of swimming pools in many kibbutzim.

9 This number has remained fairly stable since the 1970's.

10 One of the richest kibbutzim in Israel is Sasa (a traditional kibbutz), situated in the Galilee, owning 'Plasan', a factory developing and producing special custom-built vehicle armor, exporting 95% of its production to the US armed forces. Another Northern kibbutz, Hanita (a 'renewed kibbutz' including 175 full members, 55 economically independent members, and about 200 inhabitants) recently sold its firm: 'Hanita coating (Kotlav)', producing engineered polyester films and laminates, to American Avery Dennison for 75 million dollars. ZURIEL HARARI, K.: The Basketball Player, the Lebanese and Kibbutz Elders: Behind the Huge Exit of Hanita. In: Calcalist, 2017. Available at: http://www.calcalist.co.il/local/articles/0,7340,L-3706492,00.html

11 GOLDENBERG, S. – WEKERLE, G.: From utopia to total institution in a single generation: the kibbutz and Bruderhof. In: International Review of Modern Sociology, 1972, vol. 2, no. 2, pp. 224–232.

to the land,[12] the machines, the tents, huts and later houses, to the animals and plants. However, it also applied to personal belongings such as clothes, furniture, electric appliances etc.[13]

A hundred years ago, a kibbutznik somewhere wanted to bring a kettle home… He was told he had to drink his tea in the dining room like everyone else.[14]

Any belongings owned by new kibbutz members, or accepted by kibbutz members, were immediately confiscated to the general benefit. Thus, for example, there is documentation of a female kibbutz member who worked in the cowshed wearing an elegant fur coat that was confiscated from another, newly arrived immigrant kibbutz member.[15] However, such luxuries were rare and in general, all kibbutzim were very poor and their members suffered hunger on daily bases.

Those who had families in Israel, attempting to stay with their families for a while, to rest from the hard work or even to recover sickness, were immediately condemned by the group, perceived as undermining equality.[16]

The value of *self-labour* was enshrined. It meant that the kibbutz must rely solely on its members to do all the necessary work. The kibbutz would not employ external labour. Each of the members was apt to work for the kibbutz, doing his or her best to meet the demands of the job assigned to them, based on the kibbutz's needs, sometimes irrespective of their education, personal qualifications or aspirations.

Substantial equality was further enhanced by a basic principle, inspired by communism: 'From each according to his/her ability, to each according to his/her need.'

The responsibility to raise the kibbutz children, feed them, and educate them was perceived as collective. They were sleeping in 'children's houses', separate from their families, both to nurture the value of their equal treatment by their educators, and to free their parents from most of their parental responsibilities, to let them dedicate more time to the collective needs of the kibbutz. The family used to meet for short intervals every afternoon and during weekends.[17]

Personal matters such as the desire to get married, to have children or to acquire professional or personal skills or training were subject to a decision of the kibbutz's general assembly, assuming that all such matters had potentially borne financial and social implications for the entire community and thus should be decided by it.[18]

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12 The land was state-owned and the kibbutz only leased it. Leasing was originally limited to agricultural use. Nevertheless, in 1992, following a huge wave of immigrants from the former USSR, the Israeli government allowed the kibbutzim, in collaboration with entrepreneurs, to build neighborhoods on this land and sell the apartments built in the free market, for considerable profits, as if they've owned this land. Some kibbutzim, such as Ramat Rachel near Jerusalem, and Glil Yam near Tel Aviv, managed to make huge profits of this venture. These deals drew severe public criticism, on grounds that giving the right to build on state land and gain profits to the kibbutzim discriminates against other Israeli citizens who did not accept such a ‚present' from the State. Eventually, seven Israeli Court of Justice judges deleted this government decision in consensus, in 2002. BOSSO, N.: When Farmers Found Gold in the Land. In: TheMarker, 2014. Available at: http://www.themarker.com/magazine/1.2456648; *HCJ 244/00* The New Discourse Association for Democratic Discourse v. The National Infrastructure Minister, judgement of 29.8.02.

13 LIEBLICH, A.: Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, pp. 35, 44, 259; INBARI, A.: Habayta. Tel Aviv: Yediot Sfarim, 2009.

14 SHOR, Ze'ev, head of the Kibbutz Movement. In: RIFKIN, L.: Adult Children of the Dream. In: The Jerusalem Post, 2010. Available at: http://www.jpost.com/Jerusalem-Report/Adult-Children-of-the-Dream.

15 LIEBLICH, A.: Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, p. 91 .

16 Ibid., pp. 43, 92.

17 Ibid., pp. 52, 99, 104,109, 111-115.

18 BAR ON, M. – MELTZER, A.: The Kibbutz. Documentary (4 chapters), 2013, chapter 3. Available at: https://www.youtube.com/watch?v=pVbgxd7Z3mQ

As economic units, all the kibbutzim relied on agriculture. Nevertheless, many of them also developed industries. A minority of kibbutz members were assigned by the kibbutz to work outside the kibbutz, as politicians, army officers, professionals etc. Their remuneration was paid to the kibbutz, rather than to them. The kibbutz could have decided to stop their work outside the kibbutz at any time. Originally, the kibbutz supplied its members food, clothes and shelter. As the economic situation of the kibbutzim improved, their members were also entitled to a small personal 'budget' at the kibbutz's store, or to a small personal allowance.

From Collectivism to individualism

During time, the kibbutz members' sense of identification with the kibbutz and its goals decreased. The second and third generations of kibbutz members were less devoted to the ideals that led kibbutz founders, less ready for self-sacrifice, more pragmatic and more frustrated by the limits of this model: the limited personal property (and the implied financial inability of parents to help grown up children who wanted to leave), the limited options of work, study, career development or chances to experience other forms of self-realization outside the kibbutz, according to the personal interest, rather than serve the interests of the kibbutz. Some envied the relatively few kibbutz members who managed to establish professional careers outside the kibbutz, accumulating power, privileges and prestige.[19] Others desired a higher standard of living. When the kibbutz 'surrendered' members' pressure, allowing them to have television sets or telephones in their rooms or to travel abroad, their awareness and appetite for 'capitalist' pleasures grew. Questions of personal and group identity and the limits of solidarity were raised.

These doubts were reinforced by a growing conflict between the rural nature of the kibbutzim and the urban pattern of settlement, adopted by most Israelis. This conflict had some dimensions. One aspect was the necessity to subsidize agriculture and provide for a safety net in cases of natural disasters, criticized by urban Israelis, particularly citizens of border towns and development towns, as an unnecessary or rather exaggerated burden on the state's budget. The growing resentment among the Sephardic community in Israel for the kibbutzim, perceived as ivory towers of the Ashkenazi elite, underlined this conflict.[20]

By end 1970's many kibbutzim experienced a severe financial crisis. In 1977 the Likud party was first elected for government, replacing the Avoda party which ruled since the establishment of Israel. While the latter represented left wing, social ideas and was highly supportive of the kibbutzim, the former represented a right-wing, capitalist vision, and was mainly supported by kibbutz opponents, capitalists and urban inhabitants, mostly of Sephardic origin. This government was less attentive to the growing financial needs of the kibbutzim and substantially decreased their financial support.[21]

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19 SHAPIRA, R.: Academic Capital or Scientific Progress? A Critique of Studies of Kibbutz Stratification. In: Journal of Anthropological Research, 2005, vol. 61, no. 3, pp. 357-380; SHAPIRA, R.: Communal Decline: The Vanishing of High-Moral Leaders and the Decay of Democratic, High-Trust Kibbutz Cultures. In: Sociological Inquiry, 2001, vol. 71, no. 1, pp. 13-38.

20 In one of his pre-elections speeches, in 1981, Menachem Begin, head of the Likud party, who was elected as Prime Minister in 1977 and served in this office until 1983, incited potential voters from border and development towns against kibbutz members, describing them as millionaires with private swimming pools. A recent research shows that these hard feelings still persist: ASHKENAZI, E.: Mutual Prejudice of Kibbutz Members and Development Towns' Citizens. In: Haaretz, 2007. Available at: http://www.haaretz.co.il/misc/1.1467375

21 NAVON, T.: The Kibbutzim's Crisis and the Israeli Economic Policy (1977-1989). Haifa: Haifa University, 2010, pp. 11-20. Available at: https://observpost.files.wordpress.com/2012/04/d79ed7a9d791d7a8-d794d7a7d799d791d795d7a6d-799d79d-d795d794d79ed793d799d7a0d799d795d7aa-d794d79bd79cd79bd79cd799d7aa-d791d799d7a9d7a8.pdf

At that time, the entire Israeli economy suffered growing financial instability, that gradually developed into stagflation. Many kibbutzim invested their savings in misfortunate financial investments. Other kibbutzim took huge loans from the banks (or in the grey market) to finance both the enlargement of their economic activities, aiming to raise their incomes in the medium and long run, and the immediate desires of their members for a higher standard of living. As inflation augmented to two and then three digits, the kibbutzim could not repay their debts and many of them slid into insolvency. By 1989, strict arrangements were finally worked out, involving the kibbutzim, the banks and the Israeli government, to pull the kibbutzim out of the crisis. Some of the debts were written off,[22] an act that drew even more resentment to the kibbutzim. Implying substantial lowering of the standard of living, austerity measures taken motivated many kibbutz members, frustrated anyhow due to the reasons mentioned, to leave the kibbutz. In many kibbutzim, the majority of members who chose to stay were the elders. There was insufficient young labour to produce incomes, to finance the growing expenses and pay the debts. The standard of living declined, encouraging more leavings.

This immense crisis forced the kibbutzim's leaders to capitalist thinking, to enable payment of kibbutzim's debts to the banks and restructure their economy: empty houses were rented to non-members; services that the kibbutz used to offer for free to its members, such as education, laundry, health and feeding were offered for payment to non-members, to create income and enjoy the economies of scale's advantages, despite the shrinking number of kibbutz members. Gradually, many kibbutzim privatized more and more services, even for their own members, realizing that this move implied a solid income to the kibbutz, and a more economic use of these services by the users.[23] Many kibbutzim privatized even the ownership of certain properties, such as members' houses and a sort of a 'stock' in the manufacturing component of the kibbutz. Consequently, the kibbutzim became attractive again, both to their original members and to new settlers, some opting for full membership while others opt to live in the kibbutz, enjoying its atmosphere and services for payment, without becoming members.

Despite all these changes, legally until 2005 (to be recognized as [a kibbutz] by the government, it had to be an entity based on collective and equal ownership, as well as on common production, consumption and education).[24]

Nowadays, most of the 270 existing kibbutzim are wholly or mostly privatized, thus considered as 'renewed kibbutzim', perceived by traditional thinkers not to be reflecting the original values of the kibbutz. The kibbutzim continuing under the original kibbutz scheme are associated with the 'collaborative model.'[25]

Since 2005 the legal definition of the kibbutz recognizes, in addition to the traditional model, the 'renewed kibbutzim', defined as based on shared property, independent labour, equality and sharing of production, consumption and education, and mutual guarantee. The protocol of these kibbutzim has to provide for allocation of the kibbutz's production means (except for land and water), apartments and/or budgets to its members, in proportion to their contribution, position and seniority.[26]

22 Ibid., pp. 46-59.

23 For example, see a description of this process in kibbutz Hulda, in: RIFKIN, L.: Adult Children of the Dream. In: The Jerusalem Post, 2010. Available at: http://www.jpost.com/Jerusalem-Report/Adult-Children-of-the-Dream.

24 Dr. Getz Shlomo, cited ibidem.

25 In 2011 there were 193 'renewed kibbutzim' and 62 'collaborative kibbutzim'. GILBOA, N.: Kibbutzim's Status: 73% Renewed Kibbutzim, 2011. Available at: http://www.kibbutz.org.il/itonut/2011/dafyarok/110203_mithadshim.htm

26 The full version of the relevant regulation (in Hebrew) is available at: http://www.kibbutz.org.il/tnua/sivug/051218_takanot_sivug.pdf

3 THE KIBBUTZ AND THE EU

Basic Perceptions

Full integration

The original kibbutz model was based on 'full integration' of members' powers and property. As this model failed, the majority of kibbutzim backed towards a more flexible model of operation, acceptable by their members, involving a lower level of integration to allow for the continuation of the kibbutz.

While EU leaders encourage quick enhancement towards more intensified integration,[27] regarding it as inevitable to pull the EU out of current crises, this opinion does not seem to reflect the will of most EU citizens. Similarly to the kibbutz, at least from the political point of view, backing towards a more flexible model of cooperation[28] may better ensure the continuity of the EU in the long run, whereas insistence on intensifying integration at this point may have an adverse effect.

Equality

The original kibbutz model was underlined by the notion of its members' equality. Consequently, each member had one voice in the kibbutz's 'general assembly'. Each member was entitled to an equal share of the benefits offered by the kibbutz: food, clothes, housing, education, health etc. Equality was implemented on pragmatic bases, namely: 'from each according to his/her ability, to each according to his/her need.'

In cases where it was impossible to provide a benefit to all interested members simultaneously (e.g. private telephones in the members' rooms, travels abroad, higher education), the kibbutz's authorities decided priorities.

Equality of members is a basic value of the EU as well,[29] subject to acknowledgment and respect of the differences between the member states and their national contexts.[30] The application of this value at the EU seems to share many similarities with its application at the kibbutz:

– Each member state has one vote in the highest EU authority, deciding its policy and vision: the European Council, and one Commissioner in the EU Commission.[31]

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27 See JUNCKER, J. C.: Completing Europe's Economic and Monetary Union. 2015. Available at http://ec.europa.eu/priorities/economic-monetary-union/docs/5-presidents-report_en.pdf

28 For example, one new flexible model recently discussed by experts and in the press is the creation of a geo-economic German core that would include countries associated with the German supply chain, such as the Netherlands, Poland, the Czech Republic, Slovakia, and certain Scandinavian countries: CARACCIOLO, L. – BRUNELLO, R.: Europe in the Brexit and Trump Era: Disintegration and Regrouping. In: MacroGeo, 2017. Available at: https://www.macrogeo.global/nexus/europe-in-the-brexit-and-trump-era-dis-integration/. BARBER, T.: Europe Starts to Think the Unthinkable: Breaking Up. In: Financial Times, 2017. Available at: https://www.ft.com/content/0b7b1616-ff3d-11e6-8d8e-a5e3738f9ae4. Five possible scenarios for the potential state of the European Union have been recently presented by the European Commission. White Paper on the Future of Europe, 2017. Available at: http://europa.eu/rapid/press-release_IP-17-385_en.htm

29 See the Preamble and Article 2 of the Treaty on the European Union (TEU), available at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:115:0013:0045:en:PDF

30 Article 4 (2) TEU.

31 The sophistication and largeness of the EU system dictates that in other institutions material equality would be obtained by other formulae, by which voting power reflects the number of each member's citizens (e.g. Council of the EU, EU Parliament), or the size of its economy (e.g. the rotation system at the ECB's Governing Council).

- The contribution of each member state to EU's budget is determined by its GDP ('from each according to its ability').
- Financial (and other) assistance to the member states is decided according to their needs. Consequently, weak economies, or economies suffering a temporary crisis, may enjoy more EU financing than strong economies ('to each according to its need'). [32]
- Priorities, where necessary, are determined by relevant EU authorities.

Formal versus Material Equality

The kibbutz paid tribute to formal equality. However, many members were frustrated, feeling that in fact they had no influence over decision making, despite their equal right to vote, either because of their non-influential personality, because they identified with a minority opinion or because of their belonging to a group with a relatively low social status in the kibbutz.[33]

In the EU, certain – mainly relatively weak or small member states – feel frustrated that despite their allegedly equal status, strong countries like France and Germany practically dictate priorities. Recently, this frustration is particularly associated with regard to the financial crisis.[34]

Solidarity

Solidarity is defined as 'unity or agreement of feeling or action, especially among individuals with a common interest; mutual support within a group.'[35] The kibbutz – and the EU[36] – are underlined by both these dimensions of solidarity: their members created them out of unity of feeling, values and action, being ready to provide mutual economic, political and defense support within the group. During their history, both these alliances provided the promised mutual guarantee to their members. The kibbutz offered weak members, sick members, old members, disabled members, or members suffering personal crises economic and social support. The EU offers its members political support in external relations, economic support, e.g. through the Common Agricultural Policy (CAP),[37] cohesion funds, facilities such as the European Stability Mechanism (ESM) developed to pull member states out of the financial crisis, etc.

Abuse of Equality and Solidarity by Free riders

In the kibbutz, a major source of frustration was the abuse of equality and solidarity by 'free rider' members, who enjoyed all the benefits offered by the kibbutz for minimum labour contribution un-

[32] See, for example, PING CHAN, S.: EU Budget: What You Need to Know. In: The Telegraph, 2017. Available at: http://www.telegraph.co.uk/finance/financialcrisis/11221427/EU-budget-what-you-need-to-know.html

[33] One such group included women, who felt that they were expected to function mainly as service providers in fields such as education, laundry and cooking, while men as a group were offered more challenging jobs: LIEBLICH, A. Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, pp. 105, 112, 205, 264.

[34] See, for example: MUNIN, N.: The 'Five Presidents Report': Dogs Bark but the Caravan Moves on? In: European Politics and the Society, 2016, vol. 17, no. 3, pp. 401-420, 404, 415; MUNIN, N.: European Monetary Union's Single Banking Supervision Mechanism: Another Brick in the Wall? In: IUP Journal of International Relations, 2016, vol. X, no. 4, pp. 7-31, 14; MUNIN, N.: Democracy and Financial Crisis Between the Five Presidents Report and the Brexit: In Search for a New Way? In: International and Comparative Law Review, 2016, vol. 16, no. 2, pp. 7-28.

[35] Oxford Dictionary. Available at: https://en.oxforddictionaries.com/definition/solidarity.

[36] See TEU the Preamble, Article 2, 3, 31, 32; Treaty on the functioning of the EU (TFEU) Articles 67, 80, 122, 194, 222, first paragraph of Protocol no. 28 on economic, social and territorial cohesion. Available at: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A12012E%2FTXT

[37] RAMIRO TROITINO, D. – CHOCHIA, A.: The Common Agricultural Policy, its Role in European Integration and Influence on the Enlargements of the Organization. In: International and Comparative Law Review, 2013, vol. 13, no. 1, pp. 39-60.

justified on grounds of real inability, or abused the common property.[38] Due to the original kibbutz rules such members, considered 'parasites', could not be expelled from the kibbutz.

In the context of the current financial crisis, similar claims were invoked towards certain assisted countries by frustrated citizens and politicians of the assisting countries. These assisted countries were blamed, among other things, for conducting irresponsible spending policies, for maintaining a huge and inefficient public sector or corrupted governments and for not striving hard enough to raise productivity.[39] Accusers were frustrated that according to EU law, these reasons did not suffice to expel a member state from the Union, and that allegedly they had to bear the costs of this behaviour.[40]

In the kibbutz, privatization of work solved the problem of parasites: everyone is now paid for their actual contribution, and may be fired if they do not perform satisfactorily. They can only enjoy services they can afford paying for.[41]

In the EU, questions such as: to what extent strong members have a moral obligation to support weak (or 'parasite') members? How to treat members acting irresponsibly, thus endangering the entire alliance?, still remain open. In the meantime, solidarity prevailed, associated with the requirement that assisted countries adopt stricter discipline and recovering measures.

Yet another controversy among EU member states refers to the treatment of current huge waves of refugees flooding Europe. To a certain extent, member states refusing to participate in this effort are perceived as 'parasites' by other member states, bearing this entire economic and social burden.

The UK is the second net contributor to EU budget.[42] The Brexit implies the end of UK's financial contribution to the assisted countries and to further immigration into the EU.[43]

In both contexts, potentially followed by other member states, initiatives like the Brexit may lead to an equivalent by-product as kibbutz privatization: breaking up solidarity (and the support of alleged 'parasites') by withdrawing the alliance.

Subsidiarity

The original kibbutz was underlined by subsidiarity: it offered individuals desiring to live in an unwelcoming land mutual economic, social and security guarantee. Being a capital-and-labour-intensive project, it could be only obtained collectively.

38 LIEBLICH, A. Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, pp. 53-4.

39 In extreme cases, this frustration turned into an incitement campaign. See, for example: BICKES, H. – OTTEN, T. – WEYMANN, L. C.: The Financial Crisis in the German and English Press: Metaphorical Structures in the Media Coverage on Greece, Spain and Italy. In: Discourse and Society, 2014, vol. 25, no. 4, pp. 424-445.

40 MUNIN, N.: The 'Five Presidents Report': Dogs Bark but the Caravan Moves on? In: European Politics and the Society, 2016, vol. 17, no. 3, p. 404. MUNIN, N.: European Monetary Union's Single Banking Supervision Mechanism: Another Brick in the Wall? In: IUP Journal of International Relations, 2016, vol. X, no. 4, p. 11. See also the counter-arguments made by the assisted countries and scholars specified in these articles.

41 Nowadays, certain kibbutz members perceive other members, fulfilling senior positions in the kibbutz, now involving considerable remuneration, as parasites. See: SHAPIRA, E.: Who is a Parasite? Shavim website, 2010. Available at: http://www.kibbutz.org.il/shavim/articles/yomyom/100630_e_shapira.htm

42 PING CHAN, S.: EU Budget: What You Need to Know. In: The Telegraph, 2017. Available at: http://www.telegraph.co.uk/finance/financialcrisis/11221427/EU-budget-what-you-need-to-know.html

43 One third (33%) of leave voters in the Brexit referendum said the main reason was that leaving 'offered the best chance for the UK to regain control over immigration and its own borders'. How the United Kingdom voted on Thursday…and Why. In: Lord Ashcroft's Polls, 2016. Available at: http://lordashcroftpolls.com/2016/06/how-the-united-kingdom-voted-and-why/

The notion of subsidiarity underlines the EU as well:[44] it enabled its members to become the largest trade block in the world, thus to profit from a better bargaining power than each of them would have had individually. It enabled the issuing of a mutual currency: the Euro, the second most attractive investment currency in the world, after the US Dollar. It facilitated the restructuring of Europe after World War II and the obtainment of peace in Europe ever since. It facilitated the stabilization and upgrading of Central and Eastern European economies after their release from communist regime. It facilitates cross-border projects that cannot be pursued by individual member states, in fields such as international transportation and the environment.

With privatization, kibbutzim lost much of the advantages offered by their original model in terms of subsidiarity. They can still perform as a group to obtain mutual external advantages or exercise a collective bargaining power. Nevertheless, the ideological variety and different motivations characterizing the members (and other citizens) of current kibbutzim, the weakening status of the kibbutzim in the Israeli society and the lack of their economic consolidation as a group decrease their subsidiary power to a great extent. This is an interesting point to bear in mind for Eurosceptics.

External Labour

The original kibbutz model was based solely on internal labour. In ideological terms, this was explained by the communist/socialist perception that hiring other people to work for them would turn kibbutz members into capitalists, exploiting the working class.[45] As the economic needs of the kibbutzim grew, due to the growth in the number of their members and their growing expectations for a higher standard of leaving, this ideology became more and more controversial. In certain cases, kibbutz members argued that even if all of them worked as hard as they could, it was still impossible to meet all the needs of the kibbutz. This distress grew as the second and third generations of kibbutz members had to support a constantly growing group of retired elders, a challenge that the kibbutz founders did not face. In other cases, frustration emanated from the necessity to perform jobs that no kibbutz member fancied. Kibbutz leaders forced members to perform them using a mix of carrots and sticks. Yet a third justification to hire external workers occurred where the kibbutz needed a professional service that no member could provide, e.g. physicians, social workers or other experts.[46] During the years, as the ideological foundations of the kibbutz became shaky and the needs grew, more and more kibbutzim surrendered to members' pressure to some extent.[47] In the 1970s kibbutzim frequently hired Arab labourers. Due to the political escalation and growing threat of terror, since the 1990s local Arab workers were replaced by teams of foreign workers, many from Thailand and China.

The growing share of elder population in the entire population, combined with the average low birth ratio, the preference of EU citizens not to perform certain, particularly labour-intensive jobs and the necessity for external experts in certain cases led the EU to a similar dilemma.[48] Nevertheless, while the kibbutz could afford abstaining from turning most of external workers into kibbutz members, in the EU's reality this is more difficult. Experts, for example, can stay at the EU for short

44 Article 5 TEU, Article 3 TFEU, Protocol (No. 2) on the principles of subsidiarity and proportionality.

45 LIEBLICH, A. Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, pp. 35, 37, 106-7, 131, 200.

46 Ibid., pp. 260.

47 See, for example, INBARI, A.: Habayta. Tel Aviv: Yediot Sfarim, 2009.

48 Eurostat. Europe 2020 Indicators – Employment. 2016. Available at: http://ec.europa.eu/eurostat/statistics-explained/index.php/Europe_2020_indicators_-_employment

intervals. In border areas, workers can cross the border daily to work in the EU and return to their homes, outside the EU, after work. But most of the foreign workers immigrate to the EU, in many cases with their families. This reality imposes EU leaders and citizens to the dilemma: how to deal with social side-effects of foreign labour's employment? To what extent do foreign workers affect the homogeneity of the local/national/EU social tissue? To what extent social homogeneity is important to the success of the alliance?

Labour immigration in the EU encompasses internal immigration, i.e. between member states, and external immigration, i.e. from third countries.[49] While more tolerance could have been anticipated towards the former, unfortunately this is not the case. Some argue that in fact, intensified labour immigration into the UK and the feeling of many UK citizens that their communities were 'captured' by foreign cultures, as well as the feeling that intensive immigration lowers wages and overburdens health and education systems formed major triggers to the Brexit vote.[50]

Foreign immigrants, particularly those of Muslim origin, invoke even stronger resistance, due to more extreme cultural differences, combined with their different religion and their association with a potential security threat, following terrorist incidents associated with extreme Muslim movements, occurring in recent years all over Europe. These fears are further reinforced by the refusal of many of these foreign immigrants to assimilate into the hosting countries' societies by learning their language, adopting their manner of dressing and to a certain extent – their culture. Some even refuse to engage in productive work, taking advantage of social security schemes to support them financially.[51] Member states refusing to allow the access of immigrants justify this position not only on grounds of potential security threats that such immigration may involve, but also on grounds of the potential damage such immigration implies to their social tissue, referring to the experience of countries such as France, Germany, Belgium and Sweden.[52]

When the state of Israel was established, the kibbutzim participated in the general national efforts to handle the huge waves of Jewish refugees or immigrants who came to Israel. To that extent, the kibbutz offered some schemes:

Short term scheme: in times of Ottoman and British regimes, part of the refugees stayed at the

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49 According to Eurostat, foreign citizens made up 7.4 % of persons in employment in the EU in 2015. The split between intra- and extra-EU migrants was almost even, with 3.6 % having their citizenship from another EU country, and 3.8 % coming from outside the EU. Eurostat. Labor Market and Labor Force Survey (LFS) Statistics, 2016. Available at: http://ec.europa.eu/eurostat/statistics-explained/index.php/Labour_market_and_Labour_force_survey_(LFS)_statistics

50 TILFORD, S.: Britain, Immigration and Brexit. In: CER Bulletin, 2016. Available at: https://www.cer.org.uk/sites/default/files/bulletin_105_st_article1.pdf See also: The Migration Observatory. Migration and Brexit. 2017. Available at: http://www.migrationobservatory.ox.ac.uk/projects/migration-and-brexit/

51 YEHEZKELI, Z. – DERYI, D.: Allah Islam – Documentary on the Muslims in Europe. 2012. Available at: https://www.youtube.com/watch?v=hR7REARFFpQ; For more details on the link between unemployment and national social policies in the EU see: HUNGLER, S.: The Poor, The Unemployed and the Public Worker – A Comparative Essay on National Unemployment Policies Contribution to Deepening Poverty. In: International and Comparative Law Review, 2012, vol. 12, no. 1, pp. 123-140.

52 See, for example, MORTIMER, C.: Hungary Set to Reject EU Refugee Quotas in Referendum in Victory for Ruling Anti-Immigration Party. In: Independent, 2016. Available at: http://www.independent.co.uk/news/world/europe/hungary-eu-referendum-refugee-quota-migrant-crisis-xenophobia-border-control-racism-a7341276.html; FREJ, W.: Here Are the European Countries that Want to Refuse Refugees. In: Worldpost, 2017. Available at: http://www.huffingtonpost.com/entry/europe-refugees-not-welcome_us_55ef3dabe4b093be51bc8824. A recent poll by the UK's Royal Institute of International Affairs reflects that an average of 55% across 10 EU member states support stopping Muslim immigration to the EU: GOODWIN, M. – RAINES, T. – CUTTS, D.: What do Europeans Think about Muslim Immigration? In: Chatham House, 2017. Available at: https://www.chathamhouse.org/expert/comment/what-do-europeans-think-about-muslim-immigration

kibbutzim temporarily, for short periods after their illegal arrival, pretending to be kibbutz members to hide from authorities until a permanent arrangement would have been found for them. In these cases, the kibbutzim did not bear the long term burden of refugees' treatment.

Medium term scheme: Other refugees stayed in the kibbutzim as 'external children', an arrangement that was meant to provide a home for children who immigrated without their families (particularly after World War II), until they have reached the age of eighteen. Thereafter, their potential long term kibbutz membership was mutually considered, according to their individual circumstances and desires.

Long term scheme: Certain refugees aimed immediately upon arrival at becoming full members. In addition, after Israel's establishment, immigrants joined kibbutzim as individuals, out of their own considerations.

In all cases, immigrants were expected to contribute to the overall labour effort from day one. Except for the short term scheme (that may be seen as equivalent to temporary stay of immigrants in EU countries, crossed on the way to the final destination) they were expected to learn Hebrew and to assimilate culturally and socially as soon as possible. In the long run, this approach ensured a process of natural filtering of the individuals who could not meet this challenge, and the maintenance of the unique character and social tissue of the kibbutz.

Moreover, in most cases the kibbutz made sure that an immigrant would become a full kibbutz member (with voting rights) only after a long process of assimilation. Any such membership application had to be decided in the 'general assembly', after the majority of kibbutz members were satisfied that the candidate performs satisfactorily both in social terms and in terms of labour.[53]

By analogy, the EU might have profited from applying a similar, stricter policy towards immigrants desiring to stay in EU member states as residents or citizens.

In the 1970's, due to a growing national criticism on the kibbutz for not contributing enough to the national effort of assimilating immigrants into the Israeli society during the 1950's,[54] some of the kibbutzim sent their youth to work outside the kibbutz, as social guides of street gangs and population of low socio-economic status in development towns, consisting mainly of former immigrants. This project offered an opportunity for mutual cultural acquaintance and contributed to some gap-bridging and resentment reduction between these groups.[55] A similar approach could have enhanced social consolidation in the EU.

Massive immigration invokes the question whether, and to what extent, religious and cultural homogeneity is essential to the success of a collective such as the kibbutz or the EU.

Historically, the majority of kibbutz founders were Ashkenazi Jews. Jewish individuals of Sephardic origin found it difficult to assimilate in this society, that did not welcome them.[56] During the years, cultural awareness in the kibbutzim (and in Israel as a whole) grew, reinforced by mixed marriages that produced offsprings of mixed origins. The reality of the Israeli society as a melting

53 LIEBLICH, A. Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, pp. 54-65, 69-72, 216-230.

54 In the 1950's huge immigration waves included many elders, families, sick and wounded newcomers. Most of them did not settle in the kibbutzim. The kibbutzim were blamed for deliberately refraining to assimilate them. Consequently, the national image and status of the kibbutzim dropped. Such newcomers who desired agricultural life preferred the Moshavim, agricultural settlements where families form independent economic units. Many others settled in development or border towns.

55 LIEBLICH, A. Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, p. 316.

56 Ibid., pp. 59-65, 69-72.

pot further blurred these differences, so that nowadays this issue seems to be of less interest and importance, albeit the image of kibbutz is still broadly associated with Ashkenazim.

Moreover, following some appeals by Israeli citizens of Arab origin to the Israeli Court of Justice, arguing that their requests to become kibbutz or community town members were refused on grounds of their origin, the court provided that such practices are unconstitutional, rejecting claims that such practices would substantially change the unique, homogeneous social tissue of the settlement at stake.[57] These decisions opened the way to Arab membership in the kibbutzim, although in the meantime such practice is very rare.

The EU is mainly a Christian society.[58] Some argue that part of its identity is based on the exclusion and fear of the Other.[59] Although the TFEU provides for non-discrimination, among other things on grounds of religion,[60] deterrence from a substantial change of its generally homogeneous social tissue seems to be, for example, one of the motives for EU's ongoing avoidance to accept Turkey, a huge Muslim country, as a member state, as well as for the recent broad outcry against the huge waves of Muslim refugees, added to the large Muslim population already living in the EU.

Despite the shared, desired image of cultural melting-pots, it seems that both the kibbutz and the EU find it difficult to live by this image or goal.

4 RECENT EU DILEMMAS AND THEIR PARALLEL IN THE HISTORY OF THE KIBBUTZ

Little and selective or big and less selective alliances?

The first kibbutzim were very small and intimate, encompassing only a few members. This framework had some advantages: the group could have been selective; to a great extent, the group was culturally and religiously homogeneous; all group members shared similar ideas and were devoted to their fulfilment. They were established by young and elitist members of European origin. On the other hand, this format had many disadvantages: the small groups were poor and could not handle large scale projects that would have yielded more income. They could barely handle daily security threats and the hard terms of living. Consequently, they strove to enlarge the kibbutzim.

Kibbutzim grew to include hundreds of members. In many cases, some were strangers to others. Aside advantages such as economies of scale, this reality implied disadvantages such as less selectivity, that could adversely affect the personal quality of the members, in some cases encouraging a lower sense of members' responsibility. The 'general assembly' – superior decision making forum of the kibbutz, where all members had speaking and voting rights, became greatly ineffective. Moreover, this relatively huge format consumed a great administrative effort.[61]

The EU started its way with six member states, gradually growing to 28 members. While the founding members were relatively economically strong, many members that joined later were eco-

57 E.g. HCJ 8036/07 Fatina Ebriq Zubeidat et al. v. The Israel Land Administration, et al (re community town Rakefet); HCJ 6698/95 Aadel Ka'adan, et al. v. The Israel Land Administration, et al. (re community town Katzir).

58 WEILER, J.: L'Europe Chrétienne: une Excursion. Paris: Éditions du Cerf, 2007.

59 KONOPACKI, S.: Europe and its Problem with Identity in the Globalized World. In: European Studies, 2014, vol. 1, pp. 56-69.

60 Articles 10, 19, TFEU.

61 LIEBLICH, A. Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, pp. 32, 183-214.

nomically weaker, necessitating financial assistance. Members previously under communist regime further needed support in establishing market economies as well as features that would turn them into solid democracies, e.g. the rule of law, anti-corruption systems, and strong enforcement mechanisms. While this large alliance offers advantages such as economies of scale and political stability, the different economic and political profile of the different EU member states forms a source of constant challenges and disagreements.[62] Similarly to the kibbutz, decision making processes in the EU became more elaborated and less efficient, despite the adaptations made by the Treaties, and handling this huge framework necessitates a great administrative effort. In December 2016, a report by Guy Verhofstadt, suggesting a substantial reform in the roles of major EU institutions in the decision-making process, was approved in the EU Parliament's AFCO Committee by a large majority.[63]

Conflicts of powers

In the EU, there is a constant conflict of power between the supranational and national regimes, underlying the 'democratic deficit' frustration. While EU authorities seem to aim at enhancing market integration, towards a federation,[64] the national regimes, acting under the pressure of their voters, try to maintain their powers to the extent possible.[65] This conflict fills a decisive role in the current political crisis that evolved on grounds of what is perceived by many EU citizens as unacceptable dictations by EU authorities regarding the solutions to the current financial, political and refugees' crises.

When the state of Israel was established, the kibbutzim, that already existed and were used to a relatively high level of independence, were frustrated by the acts of David Ben Gurion, the first Israeli prime-minister, who tried to impose the power of the state on them, to prevent anarchy. Ben Gurion dismantled the Palmach (defense forces established by the kibbutzim before the state of Israel was established), replacing it by the IDF, managed by the government, and transferred all the powers to prepare Jewish youth abroad for immigration to Israel and kibbutz life from the kibbutzim to the new government. Many kibbutz members experienced these attempts as a conflict of powers, refusing to obey. However, they mainly resisted the *timing* of establishing the Jewish state, which they considered to be too early, not the very necessity for a Jewish state as a final goal. Thus, it did not take Ben Gurion a long time to bring all the kibbutzim under the umbrella of the new state: as the new state found itself immediately after its formal establishment under an existential military threat, everybody realized that the chances to maintain the state depend upon unifying forces to meet immediate challenges.[66]

62 Which appears regularly and orbits mainly around the topical questions of sovereignty and division of powers, like in the current dispute on so called OMT programme, see HAMUĽÁK, O. – KOPAL, D. – KERIKMÄE, T.: Walking a Tightrope - Looking Back on Risky Position of German Federal Constitutional Court in OMT Preliminary Question. In: European Studies: the review of European law, economics and politics, 2016, vol. 3, pp. 115-141; or in general to the issue of sovereignty HAMUĽÁK, O.: Lessons from the "Constitutional Mythology" or How to Reconcile the Concept of State Sovereignty with European Integration. In: Danube: Law and Economics Review, 2015, vol. 6, no. 2, pp. 75-90.

63 ALDE. before: Today, Guy Verhofstadt's report on the reform of the European Union has been approved in the European Parliament's AFCO committee by a large majority. 2016. Available at: http://alde.eu/en/news/782-today-guy-verhofstadt-s-report-on-the-reform-of-the-european-union-has-been-approved-in-the-european-parliament-s-afco-committee-by-a-large-majority/

64 JUNCKER, J. C.: Completing Europe's Economic and Monetary Union. 2015. Available at http://ec.europa.eu/priorities/economic-monetary-union/docs/5-presidents-report_en.pdf

65 For discussion on major theories trying to analyse the relationships between national and supranational regime at the EU see: KOPAL, D.: Is Constitutional Pluralism Really Pluralist? In: European Studies, 2015, vol.2, pp. 186-196.

66 LIEBLICH, A. Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, pp. 128. Kibbutz members objecting the *timing* of Israel's establishment believed that without the formality of a state it would have been easier to continue the

The case of the EU is more elaborated in this sense, since there does not seem to be a broad consensus over the final goal of this alliance. Moreover, at this stage even the level of integration already obtained seems to be doubted by certain member states, considering to withdraw it wholly or partly. This reality inflames the conflict of powers. To solve it, broad decision on the final destination of this alliance should be obtained. It seems that the current threats the EU faces are insufficient to trigger such unification of forces.

Citizens' passivity leads to detachment and indifference

The kibbutz founders were both ideologically and pragmatically active, fuelled by the challenge of creating a globally new form of community, as well as by the daily economic, social and security challenges. They succeeded to transfer part of this enthusiasm and commitment to the kibbutz project to the second generation, mainly through education. However, by the time the third generation turned adolescents, these strong feelings of ideological and pragmatic enthusiasm were watered down by the experience of growing in a strong, smoothly managed system that seemed to function perfectly. This generation felt that everything is ready, in some cases taking the kibbutz reality for granted, thinking that there is nothing more to change or improve and thus – there is no challenge, no opportunity for trial and error, no meaning. The sense that the functioning of the kibbutz is indifferent to whatever they choose to do or not do led to passivity of the young generation, followed by their deep frustration and lack of clear personal direction.[67] In the long term, these counterproductive feelings, encouraging kibbutz members to avoid responsibility, weakened the kibbutz, harming its daily functioning. When the crises hit many of these passive members were unwilling to stay and struggle for kibbutz recovery.

In the EU, equivalent frustration, emanating from a lack of clear vision about the desired EU future, shared by many of its citizens, combined with the sense of 'democratic deficit' and detachment from decision-making processes, leads many citizens to an equivalent passivity, fuelled by frustration. The misfortunate results of this passivity have been recently reflected by the poor economic situation of certain members. They were further reflected by the default of many young UK citizens to exercise their voting rights in the Brexit referendum, that could have changed the referendum's results, dominated by a great percentage of elder voters.[68]

Regulation

The original kibbutz was underlined by full commitment of its members to this framework. The second and third generations, who were less devoted to the ideology and more pragmatic, gradually started to deviate from the underlining principles of the kibbutz. To stop this erosion, the kibbutz drafted more and more regulations that the members were required to follow.[69]

The EU is a legal entity, underlined by regulation. However, irresponsible behaviour of member

'settlement enterprise' in Israel, while its establishment may imply freezing of its size BAR ON, M. – MELTZER, A.: The Kibbutz. Documentary (4 chapters), 2013, chapter 3. Available at: https://www.youtube.com/watch?v=pVbgxd7Z3mQ

67 LIEBLICH, A. Kibbutz Makom. Jerusalem and Tel Aviv. New York: Shocken, 1986, pp. 294, 301, 303, 314, 317.

68 While elders' turnout was 90%, youngsters' (18-24) turnout was only 36%. It was assessed that the majority of youngsters would have supported remaining in the EU. See, for example: SPEED B.: How Did Different Demographic Groups Vote in the Referendum? In: The Staggers, 2016. Available at: http://www.newstatesman.com/politics/staggers/2016/06/how-did-different-demographic-groups-vote-eu-referendum

69 BAR ON, M. – MELTZER, A.: The Kibbutz. Documentary (4 chapters), 2013, chapter 3. Available at: https://www.youtube.com/watch?v=pVbgxd7Z3mQ

states, such as ignoring the financial stability criteria known as the 'Maastricht Criteria' before the financial crisis, encouraged more detailed regulation, to impose stricter discipline.

In both cases, individual members find it hard to follow the constantly developing regulation and live by it. In both cases, regulation is necessary, but at the same time forms a constant source of frustration and its enactment – and enforcement – consume a great time and administrative effort. In both cases, over-regulation seems to obtain the opposite effect.

Handling of the financial crisis

Both in the kibbutz and in the EU, the financial crisis was a result of a combination of unforeseen, misfortunate external circumstances with poor, or even irresponsible, leaders' decisions. In both cases, some kibbutzim and EU member states were adversely affected more than others. In both cases, intervention by external authorities was necessary to solve the crisis: in the case of the kibbutzim it was the Israeli government. In the case of the EU – EU authorities intervened, with the help of international institutions such as the IMF and the World Bank. In both cases, the adversely affected kibbutzim/member states suffered severe austerity and were forced to engage in far-reaching reforms to recover their economies. In both cases, some of the debts were written off while others were spread into bearable payments.

Eventually, most of the kibbutzim recovered the crisis. Success of recovery programs depended, to a great extent, on their willingness to take determinant action to change their old, mal-functioning model. In many kibbutzim, a certain level of *privatization* was necessary to that extent. This practice may be advisable for – and is already followed by – some EU member states, suffering an excessively large and inefficient public sector. The kibbutzim imposed responsibility on their members, shifting their regime to include authoritative management and differential wages. In certain kibbutzim, *giving up old, unprofitable production sectors* in favour of new, yielding sectors, was necessary. Thus, for example, ZAP, an Israeli successful website comparing prices, was established by a partnership between a kibbutz member and his kibbutz (Ramat Hakovesh).[70] Kibbutz Eyal in the Sharon, in the centre of Israel, developed Eyal Microwave company, making a nice exit by selling it to the American Hereley Industries in 2008.[71] *Creative thinking* helped certain kibbutzim to turn economic disadvantages into advantages. Thus, for example, finding themselves mainly with elder members, as the majority of young kibbutz members left, in desperate need for income to support these members, who were in retirement age, two kibbutzim: Degania Aleph and Beth, both originating from the first Israeli kibbutz: Degania now offer paid services of elders' care to external consumers. Kibbutz Saar, in the Galilee, rented its old, no more used, dining room to a hi-tech company, using it as its main office. It aims to attract more hi-tech companies, to become a regional hi-tech centre, hoping that some of the hi-tech companies' employees may consider becoming kibbutz members.[72] *Charging kibbutz members for particular goods and services* raised their awareness to the costs of these services, encouraging more economic consumption. The shift to *paid work* strengthened the necessary link between financial capability and consumption, encouraging more responsible economic behaviour.

Similar strategies, adapted to their reality, may be helpful to pull EU member states out of the financial crisis. Many of them are already implemented by these states and EU authorities, e.g.

70 www.zap.co.il.

71 GRIMLAND, G.: Kibbutz Eyal's Exit. In: TheMarker, 2008. Available at: http://www.themarker.com/technation/1.1757816

72 MELTZ, J.: The New Trend: Start-ups in the Kibbutzim. In: Globes, 2002. Available at: http://www.globes.co.il/news/article.aspx?did=609054

under Europe 2020 strategy, aiming at the development of an economy based on knowledge and innovation ('smart growth'), which is more efficient, greener and more competitive ('sustainable growth'), a high-employment economy delivering economic, social and territorial cohesion ('inclusive growth') and national recovery programs.[73]

5 CONCLUSION

Despite the substantive differences between the Israeli kibbutz and the EU, both seem to share similar characteristics, perceptions, and dilemmas.

Comparison of these two attempts to build a model based on total collectivism seems to illustrate that despite theoretical advantages, such total models do not correspond to the human, individualist nature and to some extent are thus counter-productive, discouraging individual sense of responsibility and creativity. However, strong belief, persistent approach and creative thinking may produce more flexible models, encompassing a broadly agreed compromise between collectivism and individualism that would successfully function, to the benefit of its members.

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Contact information:

Prof. Nellie Munin LLD
Advocate
https://www.nelmun.com/

FRAUD IN DOCUMENTARY LETTERS OF CREDIT; A COMPARATIVE STUDY OF EXCISING INTERNATIONAL LEGAL FRAMEWORKS

Hamed Alavi
Tallinn School of Law, Tallinn University of Technology
Faculty of Law, Universitat Autònoma de Barcelona, Spain

Abstract: Documentary letters of credit are among most popular trade finance instruments used in international business. Despite the fact that main purpose derived from application of documentary letters of credit is to reduce the risk of trade, their mere documentary nature makes them vulnerable to the problem fraud. There is a huge interest among legal scholars and academicians to analyse the nature of fraud in documentary letters of credit due to its important financial effect on smooth process of international trade and also diversified approach of different legal systems to this particular problem. However, majority of conducted studies are limited to most popular legal systems including British and American law. Need for studying the LC fraud in a comprehensive comparative manner among existing international legal frameworks is well noticed for long time. Due to their international nature, LC operation is subjected to substantial number of legal frameworks which most of them are either taking a silent position towards problem of fraud or do not show uniform approach to the it. In this paper, author tries to study different sources of law in documentary letters of credit and their approach to the problem of fraud in a comparative manner. The main research question is what would be the position of fraud rule in applicable legal frameworks to the international LC operation and how do they approach the problem of fraud committed by beneficiary in documentary letters of credit? For this purpose, paper is divided into four main parts: After the introduction, second part will discuss the sources of law applicable to international LC transaction. Third section will analyse the legal nature of fraud in LC transaction. Fourth section will scrutinize the legal approach of different legal frameworks to fraud in documentary letters of credit and finally, the last section will sum up the discussion with concluding remarks.

Keywords: letters of credit, fraud

1 INTRODUCTION

Documentary letters of credit are among most popular trade finance instruments used in international trade. They are also known as "Life bold of international commerce".[1] In the simple documentary letters of credit transaction, an importer-buyer approaches a bank of good reputation to open an irrevocable letter of credit in favour of exporter to cover the cost of goods or services covered in the underlying contract between parties. In this way, risk of payment from buyer will be transferred to a bank with much stronger financial standing.[2] The credit will be advised to the

[1] Harbottle (RD) (Mercantile) Ltd v National Westminster Bank Ltd [1978] 1 QB 146.

[2] ALAVI, H.: Documentary Letters of Credit, Legal Nature and Sources of Law. In: Journal of legal studies, 2016, 17, 31, pp. 106-121.

exporter and in case of his agreement with terms and conditions of the credit, it will be issued in his favour. Exporter will ship the goods to importer and present complying documents to terms and conditions of the credit to bank. The bank will honour seller's presentation after examination of documents presented by seller and making sure about their strict compliance with the credit. As a result, it is possible to mention that three main parties are involved in operation of commercial documentary letters of credit: Importer applicant, exporter and issuing bank. However, due to long distance between buyer and seller in international commercial transaction, other parties will eventually become involved in operation of documentary letters of credit. Such parties can play the role of advising bank, confirming bank, nominated bank and reimbursing bank.[3] The development of law and practice of documentary letters of credit has been subject to customs of international trade as evolved in the course of time.[4] Despite the fact that main purpose derived from application of documentary letters of credit in practice of international trade finance is to reduce the risk of trade, their mere documentary nature makes them vulnerable to the problem of fraud.[5] This is evident from "a huge volume of case law concerning the issue of fraud has grown up. Legal writing on this topic is no less voluminous."[6] There is a huge interest among legal scholars and academicians to analyse the nature of fraud in documentary letters of credit due to its important financial effect on smooth process of international trade and also diversified approach of different legal systems to this particular problem. Fraud in documentary letters of credit is even considered as "the most controversial and confused area"[7] because it "goes to the heart" of letter of credit operation.[8] Situation will be even more complicated when it becomes clear that due to international nature of LC operation, they are subjected to substantial number of legal frameworks where most of them are either taking a silent position towards or do not show uniform approach to the same problem. United States of America is the only country which has statutory law which recognizes the fraud in documentary letters of credit. Article 5-109 of the revised Uniform Commercial Code provides a detailed legal position of LC fraud in American legal system. In England, LC fraud is subject to principles of common law system embodied in number body of case law on the subject matter. Other existing legal frameworks applicable to international operation of documentary letters of credit have more international nature and were introduced by International Chamber of Commerce or UNCITRAL. ICC has introduced Uniform Customs and Practices for Documentary Letters of Credit (UCP), Uniform Rules for Demand Guarantees (URDG), Uniform Rules for Contract Guarantees (URCG), International Standby Practices (ISP 98). UNCITRAL has introduced United Nations Convention on Independent Guarantees and Standby Letters of Credit (the Convention) on 1995.[9]

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3 ALAVI, H.: Illegality as an Exception to Principle of Autonomy in Documentary Letters of Credit; A Comparative Approach. In: Korea University Law Review, 2016, 20, pp. 3-23.

4 KOZLCHYK, B., Letters of Credit. In: Int'l Encyclopaedia of Comparative Law, 1979, 10.

5 ALAVI, H.: Autonomy Principle and Fraud Exception in Documentary Letters of Credit, a Comparative Study between United States and England. In: International and Comparative Law Review, 2015, 15, 2, p. 45.

6 BERTRAMS, R.: Bank Guarantees in International Trade. 3d. ed. The Hague: Kluwer Law International, 2004, p. 335.

7 BUCKLEY, R.P. – GAO, X.: The Development of the Fraud Rule in Letter of Credit Law: The Journey so Far and the Road Ahead. In: University of Pennsylvania Journal of Economic Law, 2002, 23, p. 663.

8 BUCKLEY, R.P. – GAO, X.: Comparative Analysis of the Standard of Fraud Required under the Fraud Rule in Letter of Credit Law. In: Duke J. Comp. & Int'l L., 2003, 13, p. 293.

9 United Nations Convention on Independent Guarantees and Stand-by Letters of Credit art. 5, Dec. 11, 1995, A/RES/50/48. Available at http://www.uncitral.org/pdf/english/texts/ payments/guarantees/guarantees.pdf [the Convention].

In this paper, author tries to study different sources of law in documentary letters of credit and their approach to the problem of fraud in a comparative manner. The main research question which current paper is trying to answer is what would be the position of fraud rule in applicable legal frameworks to the international LC operation and how do they approach the problem of documentary fraud in documentary letters of credit?

For this purpose, paper is divided into four main parts: After the introduction, second part will discuss the sources of law applicable to international LC transaction. Third section will analyse the legal nature of fraud in LC transaction. Fourth section will scrutinize the legal approach of different legal frameworks to fraud in documentary letters of credit and finally, the last section will sum up the discussion with concluding remarks.

2 SOURCES OF LETTER OF CREDIT LAW

In the course of history, development of law and regulations of the Documentary Letter of Credit was based on custom. However, in modern times International Chamber of commerce has provided the major source of law for documentary letters by assuming the responsibility for codification of relevant customs and usage under Unified Custom and Practices for Documentary Credits (UCP). Additionally, International Chamber of Commerce has introduced other regulations including eUCP, Uniform Rules of Contract Guarantees, Uniform Rules for Demand Guarantees, ISP98, which is International Standby Practices for Independent Guarantees and Standby Documentary Credits. United Nations Conference for International Trade Law also individually took the initiative to prepare universal regulations for Independent Guarantees and Standby Letters of Credits which is known as UNCITRAL Convention. Despite existence of many international frameworks for regulation of documentary credits, this issue has been addressed in few national law systems. Among Civil Law countries only Colombia, El Salvador, Greece, Guatemala, Honduras, Lebanon, Mexico, and Syria have statutory rules on the letter of credit; and, the only country in the common law system is the United States. In other Common Law Countries including England, legal issues of documentary credits are subjected to case law.

The main focus of current paper in this section will be study of different International legal sources for documentary credits, and also the answer of common law system to the question of legal framework for documentary credits.

3 PRINCIPLE OF AUTONOMY AND FRAUD RULE

3.1 Principle of Autonomy

Alongside with principle of strict compliance in operation of letters of credit and cornerstone of current article is Principle of Autonomy. Independence principle has been recognised and appreciated in national and international law.[10] The principle of autonomy of letters of credit has been consid-

[10] Article 4 UCP 600; Article 2(b) URDG; Articles 2 and 3 UNCITRAL-Convention; sections 5-10 (1)(a), 5-114 (1) and 5 5-103(d) UCC.

ered as "the engine behind the letter of credit",[11] and "cornerstone of the commercial validity of the letters of credit".[12] Principle of Independence has been clearly mentioned in article 4 of UCP 600:

«Article 4 Credits v. Contracts

a. A credit by its nature is a separate transaction from the sale or other contract on which it may be based. Banks are in no way concerned with or bound by such contract, even if any reference whatsoever to it is included in the credit. Consequently, the undertaking of a bank to honour, to negotiate or to fulfil any other obligation under the credit is not subject to claims or defences by the applicant resulting from its relationships with the issuing bank or the beneficiary."

According to Article 4 of the UCP 600 by referring to principle of independence, the beneficiary exporter receives the guarantee that he will be paid after tendering the complying presentation of documents to the issuing bank. Neither bank nor the account party will be able to withhold payment with relevant arguments to the quality of delivered goods or other issues related to performance of underlying contract. Therefore, even in cases of conflict on performance of underlying contract account party and issuing bank have no other choice rather than paying beneficiary upon presentation of complying documents and seek remedy by suing him for the breach of underlying contract. As a result, Autonomy Principle has been considered a means of promoting international trade by following the logic of "pay first, argue later".[13]

The autonomy principle also has been considered as the foundation for smooth operation of letter of credits by many scholars.[14]

In order to completely address the essence of autonomy principle, article 5 of UCP 600 specifies: "banks deal with documents and not with goods, services or performance to which the documents may relate."[15]

3.1.1 Principle of Autonomy and Common Law Position

The principle of autonomy has been recognized in many common law cases.[16] Particularly, the importance of autonomy principle has been recognized by Lord Diplock in *United City merchants (Investment) Ltd v Royal Bank of Canada*.[17]

'The whole commercial purpose for which the system of confirmed irrevocable documentary credits has been developed in international trade is to give to the seller an assured right to be paid before he parts with control of the goods that does not permit of any dispute with the buyer as to the performance of the contract of sale being used as a ground for non-payment or reduction or deferment of payment'

Trans Trust SPRL v Danubian Co Ltd[18] is another English case which raised the importance of autonomy principle when Denning LJ refers to necessity for seller to finance his own suppliers and as a result relies on provided LC by buyer for honouring his own account payables to the third party.

11 ARKINS, J.R.C.: Snow White V. Frost White: The New Cold War In Banking Law. In: Journal of International Banking Law, J.I.B.L., 2000, 15, 2, pp. 30-41.

12 Ward Petroleum Corp. v Federal Deposit Ins. Corp. (1990) 903 F.2d 1299.

13 DOLAN, J. F.: The Law of Letters of Credit: Commercial and Standby Credits. Rev. Ed. Boston: Warren, Gorham & Lamont, 1996.

14 Eakin v Continental Illinois National Bank & Trust Co. (1989) 875 F.2d 114, 116.

15 UCP600. Article 5.

16 Hamzeh Malas & Sons v. British Imex Industries Ltd [1958] 2 QB 127; [1958] 2 WLR 100; [1958] 1 All ER 262, C.A.

17 United City Merchants (Investments) Ltd v Royal Bank Of Canada [1983] 1AC 168,183.

18 Trans Trust SPRL v Danubian Co Ltd [1952] 2QB 297 at 304.

American case law also illustrates the importance of autonomy principle. For example in *Semetex Corporation v UBAF Arab American Bank,*[19] US District court granted Semtex a summary Judgement against the UBAF on the basis of autonomy principle of Irrevocable Letters of Credit despite the fact that underlying contract was not performed due to the Executive Order which blocked all Iraqi assets in USA after Iraqi invasion to Kuwait on August 2, 1990.

Power Curber International Ltd v. National Bank of Kuwait SAK[20] is another case which prohibits applicant and issuing bank from dishonouring the credit based on nonperformance of the underlying contract.

Uniform Commercial Code of USA

In United States of America, Documentary Letters of Credit are governed by Article 5 of Uniform Commerical Code. Unlike earlier version of Article 5 of UCC, which did not point at the autonomy principle,[21] revised version of UCC Article 5 clearly separates the undertaking of issuer in documentary letter of credit from existence, non-existence, performance or non-performance of underlying contract.

'the rights and obligations of an issuer to a beneficiary or a nominated person under a letter of credit are independent of the existence, performance, or non-performance of the contract or arrangement out of which the letter of credit arises or which underlie it, including contracts or arrangements between the issuer and the applicant and between the applicant and the beneficiary'[22]

'an issuer is not responsible for the performance, non-performance of the underlying contract, arrangement, or transaction'[23]

3.1.2 Exceptions to the Autonomy Principle

The autonomy principle provides beneficiary with the guarantee of the bank for payment against any issue within the terms of documentary Credits.[24] Such guarantee desires payment to the beneficiary regardless to any dispute on the underlying contract, upon tender of complying documents. Therefore, the autonomy principle creates a weaker position for account party against abusive demands of beneficiary and his fraudulent claims. On such occasions, relying on strict compliance principle and rejection of non-complying documents by bank will be the only defence of applicant. However, this defence might not work when the beneficiary is determined to obtain payment on the basis of presenting fraudulent Documents. On the other hand, the beneficiary has the upper hand against the issuing bank and account party in which regardless to any dispute on the contract of sales, he is entitled for payment upon tender of complying documents. Such upper hand can be an incentive for abusive demand for payment or presentation of fraudulent documents by beneficiary. For a long period of time the general belief was supportive towards the absolute nature of independent principle.[25] However, it became clear that exceptions are needed to deal with abusive and fraudulent demands. As result, the fraud exception has been established which is recognized by all common law and many

19 [1995] 2Bank LR 73.

20 [1981]2 Lloyd's Rep 394.

21 ENONCHONG, N.: The independence principle of letters of credit and demand guarantees. Oxford: Oxford University Press, 2011.

22 UCC. Article 5- 103(d).

23 UCC. Article 5-108(f)(1).

24 ENONCHONG, N.: The independence principle of letters of credit and demand guarantees. Oxford: Oxford University Press, 2011, p. 93.

25 United City Cooperation v. Allied Arab Bank (1985) 2 Lloyds Rep. 554, 561.

civil law countries. In cases of fraud, court has the obligation to decide between respecting the principle of autonomy and grating injunction to stop payment after considering public policy, statutes, public interest and third party rights.[26] Despite the fact that Fraud rule is a recognized expectation to principle of autonomy of documentary credits, there is no standard[27] regarding time and circumstances in which it should supersede the autonomy principle.[28] Later it became clear that the public interest requires application of exceptions in case of illegal underlying contract.[29] Therefore, clear evidences show that English Legal system is ready to recognize exceptions to the principle of autonomy.

3.2 Fraud Exception

In fact, Fraud is very old and well-known phenomenon in the business world. "As long as there have been commercial systems in place there have been those who have tried to manipulate these systems."[30] Fraud has been considered as the "the most controversial and confused area"[31] as it "goes to the very heart" of the letter of credit by providing the bank to look at the facts behind complying presentation of beneficiary and stop payment in cases of fraud in transaction.[32]

4 LEGAL APPROACH TO LC FRAUD EXCEPTION

4.1 The American View

In this section, American approach to LC fraud will be reviewed. In doing so, principle case of *Sztejn v. J.Henry Schroder* is going to be studied. Sztejn case is known for laying the foundation of LC fraud exception in the United States of American and also in England. Further, Article 5-109 of Unified Commercial Code as statuary body of law regulating Fraud in LC operation in the United States and grant of injunction as a judiciary remedy to fraud will be analysed.

4.1.1 Sztejn v. J. Henry Schroder banking Corporation[33]

This is the leading case on fraud rule in the United States of America that seriously affected development of fraud exception in documentary letters of credit.[34] Another importance of Sztejn case is

26 GARCIA, R.L.F.: Autonomy principle of the letter of credit. In: Mexican Law Review, 2009, p. 69.

27 GAO, X.: The fraud rule in the law of letters of credit: a comparative study. Vol. 2. The Hague: Kluwer law international, 2002.

28 BUCKLEY, R.P. – GAO, X.: Comparative Analysis of the Standard of Fraud Required under the Fraud Rule in Letter of Credit Law. In: Duke J. Comp. & Int'l L., 2003, 13, p. 293.

29 ENONCHONG, N.: The Autonomy Principle of Letters of Credit: An Illegality Exception? In: Lloyd's Maritime and Commercial Law Quarterly, 2006, p. 404.

30 Trade Finance Fraud –Understanding the Threats and reducing the Risk. A Special Report prepared by the ICC International Maritime Bureau. Paris: ICC International Maritime Bureau, 2002, p. 9.

31 BUCKLEY, R.P. – GAO, X.: The Development of the Fraud Rule in Letter of Credit Law: The Journey so Far and the Road Ahead. In: University of Pennsylvania Journal of Economic Law, 2002, 23, p. 663.

32 BUCKLEY, R.P. – GAO, X.: Comparative Analysis of the Standard of Fraud Required under the Fraud Rule in Letter of Credit Law. In: Duke J. Comp. & Int'l L., 2003, 13, p. 293.

33 (1941) 31 N.Y. S.2d 631.

34 BUCKLEY, R.P. – GAO, X.: The Development of the Fraud Rule in Letter of Credit Law: The Journey so Far and the Road Ahead. In: University of Pennsylvania Journal of Economic Law, 2002, 23, p. 676.

being a reference in process of codification of 1962 version of UCC as well as being the principle authority for latter cases on fraud in LC operation.[35] Gao refers to Sztejn case as "it shaped the fraud rule in virtually all jurisdictions".[36]

In this case, based on the international contract of sale between Sztejn (the buyer) and Transea Traders Ltd (the Seller), documentary letter of credit issued by Schroder (the issuing bank) as the method of payment with the draft drawn by issuing bank on the Chartered bank (presenting bank). Before presentation of documents to the bank, applicant (Sztejn) demanded court for granting injunction against beneficiary based on receiving "cow hair, other worthless material and rubbish with intent to simulate genuine merchandise and defraud the plaintiff".[37] Sztejn also named Chartered bank as collecting bank not the holder in due course of the draft issued by issuing bank. Justice Sheintag of the New York Court of Appeal considered all allegations in case as truth and rejected to motion of Chartered Bank to dismiss the compliant of Sztejn on the basis of two arguments: allegation and established fact of fraud being committed within the framework of underlying contract. His statement started as following:

"It is well established that a letter of credit is independent of the primary contract of sale between the buyer and the seller. The issuing bank agrees to pay upon presentation of documents, not goods. This rule is necessary to preserve the efficiency of the letter of credit as an instrument for the financing of trade."[38]

And continued on necessity to overrule the principle of independence in case of committing fraud by beneficiary:

"Of course, the application of this doctrine [the principle of independence] presupposes that the documents accompanying the draft are genuine and conform in terms to the requirements of the letter of credit.

However, I believe that a different situation is presented in the instant actions. This is not a controversy between the buyer and seller concerning a mere breach of warranty regarding the quality of the merchandise; on the present motion, it must be assumed that the seller has intentionally failed to ship any goods ordered by the buyer. In such a situation, where the seller's fraud had been called to the bank's attention before the drafts and documents have been presented for payment, the principle of the independence of the bank's obligation tinder the letter of credit should not be extended to protect the unscrupulous seller... Although our courts have used broad language to the effect that a letter of credit is independent of the primary contract between the buyer and seller, that language was used in cases concerning alleged breaches of warranty; no case has been brought to my attention on this point involving intentional fraud on the part of the seller which was brought to the bank's notice with the request that it withhold payment of the draft on this account." [39]

Court dismissed the motion of Chartered Bank against complaint of plaintiff and granted injunction to Sztejn:

[35] In 1964 version of UUC fraud rule was under Article 5 section 5-114, but after revision of 1995 it is under Article 5, section 5-109.

[36] KELLY-LOUW, M.: Selective legal aspects of bank demand guarantees (Doctoral dissertation). Pretoria: University of South Africa, 2009, p. 179.

[37] 31 NYS 2d 631 (1941) 633.

[38] Ibid., p. 632.

[39] Ibid., p. 633.

"Transea was engaged in a scheme to defraud the plaintiff..., that the merchandise shipped by Transea is worthless rubbish and that Chartered Bank is not an innocent holder of the draft for value but is merely attempting to procure payment of the draft for Transea's account."[40]

The case of Sztejn is also important for recognizing the immunity of the holder in due course as well as bank security as a supporting reason in application of fraud exception:

"While the primary factor in the issuance of the letter of credit is the credit standing of the buyer, the security afforded by the merchandise is also taken into account. In fact, the letter of credit requires a bill of lading made out to the order of the bank and not the buyer. Although the bank is not interested in the exact detailed performance of the sales contract, it is vitally interested in assuring itself that there are some goods represented by the documents."[41]

"On this motion only the complaint is before me and I am bound by its allegation that the Chartered Bank is not a holder in due course but is a mere agent for collection for the account of the seller charged with fraud. Therefore, the Chartered Bank's motion to dismiss the complaint must be denied, if it had appeared from the face of the complaint that the bank presenting the draft for payment was a holder in due course, its claim against the bank issuing the letter of credit would not be defeated even though the primary transaction was tainted with fraud."[42]

4.1.2 Article 5 of the Unified Commercial Code

Article 5 of the Unified Commercial Code is governing the operation of Documentary Letters of Credits besides Case Law in the United States of America. The UCC had a permanent editorial board which published commentaries often cited by judges as an authority for explanation of different provisions.[43] Article 5 of the current version of UCC is fully allocated to Documentary Letters of Credit. Drafting committee was following the goal of finding a way for further harmonization of US law with international regulations besides flexibility in practice to meet technological changes and keep the competitive position of LC in international trade. Article 5 of the UCC also contains relevant provisions in LC fraud exception.[44]

Current Article 5-109 titled "Fraud and Forgery" covers circumstances necessary for granting interlocutory injunction, the text of article describing such circumstances as following :

"(a) If a presentation is made that appears on its face strictly to comply with the terms and conditions of the letter of credit, but a required document is forged or materially fraudulent, or honour of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant: (1) the issuer shall honour the presentation, if honour is demanded by (i) a nominated person who has given value in good faith and without notice of forgery or material fraud, (ii) a confirmer who has honoured its confirmation in good faith, (iii) a holder in due course of a draft drawn under the letter of credit which was taken after acceptance by the issuer or nominated person, or (iv) an assignee of the issuer's or nominated person's deferred obligation that was taken for value and without notice of forgery or material fraud after the obligation was incurred by the

40 Ibid.
41 Ibid., p. 634-635.
42 Ibid.
43 ZHANG, Y.: Approaches to Resolving the International Documentary Letters of Credit Fraud Issue. Doctoral Dissertation. Joensuu: University of Eastern Finland, 2011, p. 74.
44 UCC, Article 5 -109.

issuer or nominated person; and (2) the issuer, acting in good faith, may honour or dishonour the presentation in any other case.

(b) If an applicant claims that a required document is forged or materially fraudulent or that honour of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant, a court of competent jurisdiction may temporarily or permanently enjoin the issuer from honouring a presentation or grant similar relief against the issuer or other persons only if the court finds that: (1) the relief is not prohibited under the law applicable to an accepted draft or deferred obligation incurred by the issuer; (2) a beneficiary, issuer, or nominated person who may be adversely affected is adequately protected against loss that it may suffer because the relief is granted; (3) all of the conditions to entitle a person to the relief under the law of this State have been met; and (4) on the basis of the information submitted to the court, the applicant is more likely than not to succeed under its claim of forgery or material fraud and the person demanding honour does not qualify for protection under subsection (a) (1)."

Text of UCC article 5-109 follows two main directions of "fraud immunisation" and "fraud exception".[45] An important aspect of Article 5-109 (a) is clarification of the fact that fraud is applicable both to forgery in documents stipulated in the Credit and in underlying sales contract. Article also comments on necessity of fraud to be material in order to issue injunctive relief. However, it does not define what does it mean for fraud to be material? Whereby, official comment on the Article provides: "the beneficiary has no colourable (meaningful) right to expect honour and where there is no basis in fact to support such a right to honour".[46]

Neither text of article 5-109 nor its official commentary refer to intention of beneficiary to defraud. As a result, it has been argued that UCC article 5-109 has focus on seriousness of fraud in the course of transaction, not beneficiary's intention and state of mind.[47] It is clear from the official commentary that standard of proof for fraud is set high and mere allegation of fraud is not sufficient for granting injunction to applicant.[48] Injunction will be granted only after meeting high standard of proof for the purpose of preventing threats to independence principle in LC operation. Commentary also stipulates that granting similar reliefs like attachment and declaratory judgement by court should follow similar high standards.[49] Attachment is a sort of preliminary relief to secure or seize the disputed property following the objective to force compliance with court decision on pending case.[50] Declaratory Judgement refers to court judgement in determining the rights of parties under, a statute, a contract or a will, on the basis of any fact or law.

Scholars consider the US approach to fraud in documentary letters of credit as "unduly narrow approach"[51] which limits the application of LC fraud exception.[52] Different interpretations of judges

45 WUNNIKE, B. – WUNNICKE, Diane B.: Standby and Commercial Letters of Credit. 2nd ed, New York: Wiley Law Publications, 1996, pp. 165-179.

46 UCC Article 5 Letters of Credit, UCC§5-109 Forgery and Fraud, Official Comment 1.

47 BUCKLEY, R. P.: The 1993 Revision of the Uniform Customs and Practice for Documentary Credits. In: Journal of Banking & Finance Law & Practice, 1995, 77, p. 97.

48 UCC Article 5 Letters of Credit, UCC §5-109 Forgery and Fraud, Official Comment 4.

49 Ibid.

50 FLETCHER, G. P. – SHEPPARD, S.: American Law in a Global Context: The Basics. Oxford; New York: Oxford University Press, 2005, p. 511.

51 BARENS, J. G. – BYRNE, J. E.: Letters of Credit: 2000. In: Business Law, 2001, 56, 4. Reprinted in: Annual Survey of Letter of Credit Law & Practice, 2002, 13, 18.

52 BARENS, J. G. – BYRNE, J. E.: Letters of Credit. In: BYRNES, J. E. - BYRNES, Ch. S. (Eds.): Annual Survey of Letter of Credit Law and Practice. Montgomery Village, MD: The Institute of International Banking Law & Practice, Inc., 2007, pp. 39-42.

from standard of proof are also a discouraging factor.[53] This can be a disadvantage for American law to show different interpretations of judges from a single problem in presence of uniform standard of "material fraud".[54]

4.2 English Law

Under English Law, Documentary Letters of Credit are considered as the life blood of the commerce[55] while fraud is considered as "the most controversial and confused area"[56] as it affects the independence principle in international operation of LC. Historically, English courts take a restrictive approach to interfering in obligation of bank to pay unless there is a corroborate evidence of committing fraud by beneficiary. Even nullity and illegality of underlying sales contract do not affect the court decision to interrupt the regular operation of LC by issuing stop order payment to bank.[57] Unlike American law, there is no statute regulating LC fraud rules in England and this area of law has been consistently governed by case law from late 1970s until today.

English law does not have any definition for fraud and court should conclude its establishment on the case by case basis. However, according to existing authorities, there are four main types of LC fraud disputes distinguished in English Law. First, beneficiary sues the bank on the basis of bank's rejection to pay despite receiving compliant presentation. Second, Bank has payed beneficiary, however, sues beneficiary due to presentation of fraudulent documents and request for restitution of the payment. Third, paying bank sues the issuing bank in request for reimbursement after effectuating the payment, and refusal of issuing bank to reimburse on the basis of fraud. Finally, before effectuating the payment by bank, applicant requests interlocutory injunction from court to stop bank from payment on the basis of beneficiary's fraud.[58]

In similar way to American Law, it seems that under English law injunction is the most popular legal relief sought by applicant against either bank or beneficiary in cases of LC fraud. However, restrictive approach of English courts to interfere in independence principle of Documentary Letters of Credit creates doubt in usefulness of such remedy. This section explores non harmonious approach of English courts to different types of LC fraud disputes with special focus on procedural aspects of interlocutory injunction in England.

4.2.1 Bank's rejection to pay

Upon presentation of confirming documents by beneficiary, issuing bank and conforming bank have the duty to honour the presentation.[59] In case of bank's decision not to effect the payment to

53 BUCKLEY, R.P. – GAO, X.: Comparative Analysis of the Standard of Fraud Required under the Fraud Rule in Letter of Credit Law. In: Duke J. Comp. & Int'l L., 2003, 13, p. 322.

54 MOONEY, J. L. – BLODGETT, M. S.: Letters of Credit in the Global Economy: Implications for International Trade. In: Journal of International Accounting, Auditing and Taxation, 1995, 4, 2, p. 183.

55 Horbottel v. National Westminster Bank [1978] QB 146;100.

56 BUCKLEY, R.P. – GAO, X.: The Development of the Fraud Rule in Letter of Credit Law: The Journey so Far and the Road Ahead. In: University of Pennsylvania Journal of Economic Law, 2002, 23, p. 663.

57 D'ARCY, L.: Schmitthoff's Export Trade - The law and Practice of International Trade. 10th ed, London: Sweet & Maxwell, 2000, p. 166.

58 MALEK, A. – QUEST, D.: Documentary Credits - The Law and Practice of Documentary Credits Including Standby Credits and Demand Guarantees. 4th Ed. Haywards Heath, West Sussex: Tottel, 2009, para 9.2, pp. 207-208.

59 Ibid, p. 264.

beneficiary, it should prove the establishment of fraud based on existing standard of proof introduced by English Courts[60] (discussed in injunction chapter of current paper). However, it is rare that the bank refuses to honour the credit on its own initiative.[61] Banks generally do not reveal fraud and the information and instructions about fraud come from account party. After receiving allegation of fraud from account party, bank has the option to pay or not. In case it decides to effect the payment, obtaining the injunction from court will be the only solution for account party to prevent payment to beneficiary.[62] If bank decides not to pay, then either beneficiary's fraud is established and bank will be excused from payment or if happened otherwise, bank will be in breach of contract. When bank decides not to effectuate the payment, beneficiary might apply for summary judgement against the bank in order to get quick remedy without going to full trial.[63] Issuing the summary judgement by court in England is subject to the English Civil Procedural Rules (CPR). Part 24.2. reads accordingly:

"The court may give summary judgment against a claimant or defendant on the whole of a claim or on a particular issue if –

(a) it considers that: (i) that claimant has no real prospect of succeeding on the claim or issue; or (ii) that defendant has no real prospect of successfully defending the claim or issue; and

(b) there is no other compelling reason why the case or issue should be disposed of at a trial."[64]

The decision of courts in *Solo Industries v Canara Bank,*[65] *Safa Ltd v Banque du Caire*[66] and *Banque Saudi Fransi v Lear Siegler Services Inc*[67] show that in case of beneficiary's application for summary judgement, bank is subject to a higher standard than what is required in CPR 24.2 . Therefore, for court, it is not sufficient that bank can show a real prospect of successfully establishing fraud in its defence. In addition, bank is required to prove the real established fraud "which has the capability of being clearly established at the interlocutory stage".[68] In occasions that bank does not resist payment on the basis of fraud rule like refraining to pay based on invalidity of letter of credit, it would be sufficient to satisfy the normal standard[69] while trying to show the real prospect of success under CPR 24.2.

4.2.2 Bank's Entitlement for Reimbursement

General rule is that the bank which has paid against conforming presentation is entitled for reimbursement. However, in case of fraud, bank has no obligation against beneficiary or entitlement against the account party to effect the payment. In case of payment in such circumstances, bank cannot claim for reimbursement.[70] However, the bank which does not have information about the fraud of beneficiary will not be prejudiced.

60 Ibid.

61 ELLINGER, P. – NOE, D.: The Law and Practice of Documentary Letters of Credit. Oxford : Hart Publishing, 2010, p. 145.

62 Ibid.

63 Ibid.

64 Part 24.2 of the Civil Procedure Rules. Available at: athttp://www.hrothgar.co.uk/YAWS/rules/part24.htm#IDAZBHOB

65 Solo Industries UK Ltd v Canara Bank [2001] 1 WLR 1800.

66 Safa Ltd v Banque du Caire [2000] 2 Lloyd's Rep.600.

67 Banque Saudi Fransi v Lear Siegler Services Inc. [2007] 2 Lloyd's Rep 47.

68 Ibid., p. 31-32.

69 Ibid., p. 33.

70 ELLINGER, P. – NOE, D.: The Law and Practice of Documentary Letters of Credit. Oxford : Hart Publishing, 2010,

In the case of Angelica-*Whitewear Ltd v Bank of Nova Scotia*[71] which was referenced by English courts, Le Dien J. from the Supreme court of Canada argued that it case of improperly paid draft by issuing bank the standard of proof for fraud should be set in the question "Whether fraud was so established to the knowledge of issuing bank before payment of the draft as to make the fraud clear or obvious to the bank".[72] According to Le Dien J, standard of proof for such cases was different from standard of proof when applicant is trying to obtain interlocutory injunction against bank to restrain the payment to the beneficiary. He explained that in latter case the "strong prima facie test will apply".[73]

As discussed before, it can be understood that the bank which is trying to resist summary judgement against the payment to beneficiary is subject to the higher standard of proof. However, this does not apply in the occasion that applicant, issuing bank or confirming bank try to resist the summary judgment as a result of being sued for reimbursement by the bank which has paid the fraudulent beneficiary.[74] In such occasions, defendant is expected to provide a real prospect of existing fraud and satisfy the normal test of CRP Part 24.2 at trial.[75]

In case of *Banque Saudi Fransi v Lear Siegler Inc,*[76] the issuer of a performance bond was seeking for summary judgement against the instructing party who provided a counter indemnity. After making the payment to the beneficiary defendant, issuing bank raised the defence of not being bound for payment under the country indemnity due to dishonest claim of the beneficiary. In trial, defendant managed successfully resist against the summary judgement by showing the real prospect which was clearly established.[77] In the above decision, it is implied that although beneficiary might successfully obtain the summary judgement against bank as a result of bank's failure to establish a clear evidence of fraud, there is no guarantee that bank can in return obtain summary judgement for receiving reimbursement against the instructing party. Because the instructing party should only meet requirements of the low test of real prospect of fraud in the trial.[78]

4.2.3 Fraud in deferred payment obligations

Under the deferred payment credits, the nominated bank has the obligation to pay on the maturity date in accordance with the credit terms. As under deferred payment system there is no immediate payment available to seller until the date of maturity of credit, the seller is responsible to ship goods and expects payment on maturity. Such process will impose financial burden on seller. Therefore, market demand in similar conditions resulted in creation of forfaiting practice. In forfaiting practice, nominated bank may agree to discount the beneficiary's documents and expect reimbursement from issuing bank on maturity date. In case of beneficiary's fraud before the maturity date, applicant and issuing bank will definitely try not to reimburse the nominated bank which has paid to fraudulent beneficiary. Despite the fact that establishment of beneficiary's fraud will depend on facts of each

p. 147.

71 Angelica-Whitewear Ltd v Bank of Nova Scotia 36 D.L.R. (4th) , EYB 1987-67726.

72 Ibid., pp. 59, 84.

73 Ibid.

74 ELLINGER, P. – NOE, D.: The Law and Practice of Documentary Letters of Credit. Oxford : Hart Publishing, 2010, p. 147.

75 Ibid.

76 Banque Saudi Fransi v Lear Siegler Services Inc. [2007] 2 Lloyd's Rep 47, 18.

77 Ibid.

78 Ibid.

individual case and in addition guideline for interbank reimbursements under differed payment is provided by UCP 600, it is worth to review the right and obligations of involved financial institutions under deferred payment before and after coming into force of the UCP 600.

4.2.4 The standard of proof

When account party is looking for injunction to prevent beneficiary from demanding payment or bank from enforcing payment on the basis of fraud exception, the first necessary step to take is meeting the standard of proof.[79] In the case of *United City Merchants (Investment) Ltd v Royal Bank of Canada*,[80] the standard of proof for fraud was considered when Lord Diplock held the requirement as "Clear, obvious, or established fraud known to the issuer or confirmer of the letter of credit."[81] Also Ackner LJ , in the case of *United Trading Corp. SA v Allied Arab Bank Ltd*[82] laid down the standard of "only realistic inference" in order to provide an alternative to the "clear evidence" provided by Lord Diplock in *United City Merchants.* Ackner LJ further emphasized that:

(a) "The evidence of fraud must be clear, both as to the fact of the fraud and as to the [guarantor's] knowledge. The mere assertion or allegation of fraud would not be sufficient…We would expect the court to require a strong corroborative evidence of the allegation, usually in the form of contemporary documents, particularly those emanating from the buyer."[83]

Court also commented:

(b) "for the evidence of fraud to be clear, it would be expected that the buyer was given the necessary opportunity to answer the allegation against him and he (buyer) fails to provide any, or any adequate answer in circumstances where one could properly be expected."[84]

Other similar positon was taken by Mance LJ in The Court of Appeal of *Solo Industries UK Ltd v. Canara Bank*.[85] Mance LJ while responding to the contention of bank towards standard of proof which should preclude "any possibility of innocent explanation" took a very close position to the position of *United Trading Corp SA*. From what has been discussed so far, it can be clearly understood that standard of proof for fraud under English law has been formulated differently. One reason can be that courts try to set not too high standard from one hand to safeguard the autonomy principle and on the other hand set it too high not to be attainable in practice. As a result, there are different standards of proof including "established or obvious fraud",[86] "good arguable case which is the realistic inference on the material available for beneficiary to be fraudulent"[87] or the "real prospect"[88] of establishing fraud.

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79 Discount Record Ltd v Barclays Bank Ltd [1975] 1WLR 315; RD Harbottle (Mercantile) v National Westminster Bank [1978] QB 146; Edward Owen Engineering Ltd v Barclays Bank International Ltd [1978] QB 159; Bolivinter Oil SA v Chase Manhattan Bank [1984] Lloyd's Rep 251; Group Josi Re v Walbrook Insurance Co Ltd [1996] 1 WLR 1152.

80 United Trading Corp. SA v Allied Arab Bank Ltd, [1985] 2 Lloyds Rep 554, 561.

81 Ibid.

82 Ibid.

83 Ibid.

84 Ibid.

85 Solo Industries v Canara Bank [2001] 2 Lloyd's Rep 578.

86 Edward Owen Engineering Ltd v. Barclays Bank International [1978]QB 159, per Lord Denning.

87 United Trading Corporation SA v. Allied Arab Bank at FN 27 per Ackner LJ at 561.

88 Solo Industries UK Ltd v Canara Bank [2001] 1 WLR 1800, [2001]EWCA Civ 1059.

The second step for obtaining the injunction is satisfying the balance of convenience.

The issue was not always considered in English court's decision while deciding to grant injunction base on fraud. One reason is that in most cases evidence was not enough to establish fraud and as a result the case did not proceed to the stage for considering the balance of convenience.[89] Therefore, when claimant manages to establish the basis for injunction, court will consider the balance of convenience in order to issue the injunction.[90] It has been mentioned that in the context of injunctions to prevent either beneficiary from claiming the payment or bank form effecting the payment in most cases balance of convenience is against granting the injunction.

The main reasons against granting injunction can be named as resistance of adequate remedies for damages, imminent expiry date of credit, availability of freezing injunction and availability of final accounting between parties.[91]

4.3 UCP's view

The Unified Customs and Practices for Documentary Letters of Credit (currently UCP600) were published by ICC for the first time in 1933. UCP is considered as one the most successful private initiatives in regulating international trade practice. Article 5 of the UCP has recognized the principle of autonomy in LC transaction by emphasizing that bank deals with documents not goods and liability of bank is limited to pay to beneficiary against presentation of complying documents.[92] However, it takes an absolutely silent position towards fraud and leaves it open for national laws.[93] To justify their approach, ICC authorities point at different ways to address the problem of abusive demand and fraud in different jurisdictions and consider protection of parties in good faith as responsibility of national courts.[94] Many scholars confirm the sensitivity of fraud and different approaches of national jurisdictions to it by considering the silent approach of UCP to fraud exception as a ground-breaking success.[95] They argue that current approach of UCP to fraud encourages national courts to deal with this problem without any negative effect on the market position of Documentary Letters of Credit as popular trade finance tool in international trade.[96] In the same vein, Goode comments: "the content and explanation of ICC Uniform Rules are influenced by the fact that these uniform rules are rules of best banking practice, not the rules of law…" while fraud is "the province of the applicable law of the courts of the forum".[97]

89 ENONCHONG, N.: The independence principle of letters of credit and demand guarantees. Oxford: Oxford University Press, 2011, p. 158.

90 Ibid., p. 236.

91 Ibid.

92 UCP 600 , Article 5.

93 Opinions of the ICC Banking Commission – On Queries relating to Uniform Customs and Practice for Documentary Credits 1984-1986. Edited by Bernard Wheble. Paris: ICC Publishing S.A., 1987, p. 23; KURKETLA, M.: Letters of Credit Under International Trade Law: UCC, UCP and Law Merchant. New York, London & Rome: Oceana Publications. Inc., 1985, pp. 31-32; COYLLER, G.: Presentation in Seminar 'UCP 600: Understanding the New Documentary Credits Rules', organized by ICC Finland, Helsinki, 21 March, 2007.

94 Opinions of the ICC Banking Commission 1995-1996, ICC Publication No. 565. Paris: ICC, 1997, p. 22; Query: Rights of Recourse to the Beneficiary in the event of Fraud. In: Latest Queries Answered by the ICC Banking Commission'. In: DCI (ICC), Spring 1997, 3, 2, p. 7.

95 DOLAN, J. F.: Commentary on Legislative Developments in Letter of Credit Law: An Interim Report. In: Banking & Fin. L. Rev., 8, 2002, 53, p. 63.

96 Ibid.

97 GOODE, R.: Abstract Payment Undertakings and the Rules of the International Chamber of Commerce. In: Saint Louis University Law Journal, 1995, 39, pp. 725-727.

This would convey the meaning that despite recognition of the problem of fraud by drafters of UCP,[98] they have intentionally set it aside.[99]

Leacock considers UCP approach to LC fraud as "unqualified liability".[100] He further explains that with reference to independent principle, paying bank does not have any liability for beneficiary's fraud in case of paying against confirming documents even after receiving notice from applicant.[101]

However, UCP's silent approach to fraud has been criticized by other scholars on the basis that regulations should provide secure and predictable environment for trading partners, where different approaches of national laws to fraud is unsatisfactory as there is no certainty provided for businessmen who intend to enter international trade.[102] Inclusion of fraud rule in UCP is one of the recommended solutions for non-harmonized approaches of national laws to this problem.[103] Drafting a set of transnational trade law with special focus on non-harmonized aspects of international LC operation including fraud is another scholarly proposal[104] which does not seem realistic due to time consuming process of ratification of such draft by different nations.[105] In brief, fraud exception is excluded from UCP and left under the discretion of national law. This approach of ICC has been denounced by some scholars who consider it as a reason for uncertainty in international trade while others call it a successful step towards increasing international marketability of Documentary Letters of Credit.[106]

4.3.1 e-UCP

"This is the acronym for the supplement to the uniform Customs and Practice for Documentary Credits for Electronic Presentation".[107] Meeting the needs for electronic trade was the initiative of Banking Commotion of ICC to propose the formation of committee to work on developing a bridge between UCP and processing the electronic equivalent of paper based credits. The working group started to work on preparation of a supplement to the UCP which "would deal with the issues of Electronic Presentation".[108] The result of working group's efforts is known as eUCP. It came into force from 1 April 2002 and the format facilitates further revisions.[109] Current version of eUCP is the

98 DOLAN, J. F.: The Law of Letters of Credit: Commercial and Standby Credits. Rev. Ed. Boston: Warren, Gorham & Lamont, Incorporated, 1996, p. 63.

99 BARSKI, K. A.: Letters of Credit: A Comparison of Article 5 of the Uniform Commercial Code and the Uniform Customs and Practice for Documentary Credits. In: Loy. L. Rev., 1996, 41, pp. 735-751.

100 LEAKOCK, S. J.: Fraud in International Transaction: Enjoining Payment of Letters of credit in International Transactions. In: Vand. J. Transnat'l L., 885,1984 (Fall), 17, p. 912.

101 Ibid., p. 913.

102 BUCKLEY, R.P. – GAO, X.: The Development of the Fraud Rule in Letter of Credit Law: The Journey so Far and the Road Ahead. In: University of Pennsylvania Journal of Economic Law, 2002, 23, p. 701.

103 KUO-ELLEN, L. S.: UCP Needs to Change. In: Journal of Money Laundering Control, 2002, 5, 3, p. 231.

104 ROWE, M.: Do We Need a Transnational Law on Documentary Credits? Michael Rowe & Bernard Wheble Debate. In: DCI (ICC), 1998, Spring, 4, 2, pp. 16-17.

105 Ibid.

106 BUCKLEY, R.P. – GAO, X.: The Development of the Fraud Rule in Letter of Credit Law: The Journey so Far and the Road Ahead. In: University of Pennsylvania Journal of Economic Law, 2002, 23, 676.

107 BUCKLEY, R.P. – GAO, X.: Comparative Analysis of the Standard of Fraud Required under the Fraud Rule in Letter of Credit Law. In: Duke J. Comp. & Int'l L., 2003, 13, p. 113.

108 Ibid.

109 Ibid., p. 114.

version 1.1. Issues covered by eUCP are: "eUCP- UCP relations, format, presentation, originals and copies and examination of electronic records".[110] Article 2 of eUCP emphasized the consistency of all articles of eUCP with UCP while their application is limited only to cases of electronic presentation. While using the eUCP, credit will be also subject to UCP without any express incorporation of it.[111] Alongside with UCP, the same silent position towards fraud has been taken in e-UCP.

4.4 Uniform Rules of Contract Guarantees (URCG)

URCG was introduced by ICC in early 1970s in order to address the need for set of rules which deal with existing inconsistencies in field of "[g]uarantees given by banks, insurance or services or the performance of work."[112] Therefore, unlike UCP which was regulating the process of Letter of Credit, URCG was an attempt to deal with unfair calls for demand guarantees which can be considered as a measure to address problem of fraud.[113] Despite all expectations, URCG was not welcomed by the international business society for few reasons including: the problem that applicability of URCG was only limited to independent guarantees and it had no effect on accessory guarantees.[114]

The other problem was the result of URCG's attempt to prevent unfair call on demand guarantees by requiring beneficiary to produce an evidence of failure in the format of judgement, arbitral award or the principal's written approval at the time of making the claim.[115]

It is submitted that fraud in documentary letters of credit has not been fully addressed under article 9 of URCG.[116] Gao believes that while article 9 of URCG enumerates condition for payment under independent guarantees will be due, fraud rule covers situation that permits instruction of payment under bank guarantee or letter of credit.[117] As a result, it is possible to conclude that drafters of URCG tried to tap on the problem of fraud but the final outcome lacks any sort of precision.

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110 Ibid.

111 Ibid.

112 Int'l Chamber of Commerce. ICC Publication No. 325. Paris: ICC, 1978, p. 7.

113 URCG , Article 9 :

If a guarantee does not specify the documentation to be produced in support of a claim or merely specifies only a statement of claim by the beneficiary, the beneficiary must submit:

(a.) in the case of a tender guarantee, his declaration that the principal's tender has been accepted and that the principal has then either failed to sign the contract or has failed to submit a performance guarantee as provided for in the tender, and his declaration of agreement, addressed to the principal, to have any dispute on any claim by the principal for payment to him by the beneficiary of all or part of the amount paid under the guarantee settled by a judicial or arbitral tribunal as specified in the tender documents or, if not so specified or otherwise agreed upon, by arbitration in accordance with the Rules of the ICC Court of Arbitration or with the UNCITRAL Arbitration Rules, at the option of the principal;

(b.) in the case of a performance guarantee or of a repayment guarantee, either a court decision or an arbitral award justifying the claim, or approval.

114 BUCKLEY, R.P. – GAO, X.: Comparative Analysis of the Standard of Fraud Required under the Fraud Rule in Letter of Credit Law. In: Duke J. Comp. & Int'l L., 2003, 13, p. 114.

115 URCG, Article 8(3) and 9.

116 GAO, X.: The Fraud Rule under the UN Convention on Independent Guarantees and Standby Letters of Credit: A Significant Contribution from an International Perspective. In: George Mason Journal of International Commercial Law, 2010, Fall, p. 64.

117 Ibid.

4.5 Uniform Rules for the Demand Guarantees (URDG)

The failure of URCG in attracting the attention of the business society at global level was the reason for ICC to introduce new set of rules and take a different approach to Demand Guarantees. URDG 458 came into force by 1992 and was based on a model which was applied by British Bankers.[118] Despite the fact that URDG 458 was strongly influenced by UCP, still "[w]orldwide acceptance of the Rules ha[s] been disappointing".[119] URDG 758 which is the revised version of URDG 458 came into force on 1 July 2010. It tries to address problems of previous version and set out functions and obligations of parties to the demand-guarantee by reflecting the best practices in business of guarantees.[120]

Similar to URCG, it is not possible to find a direct approach to fraud in URDG. However, article 20 of the URDG takes an implicit approach to fraud.[121] Clear similarity between article 20 of URDG and article 9 of URCG shows intention of drafters towards providing a safety mechanism for payment under guarantee rather than direct reference to a measure which can prevent fraud.

4.6 International Standard Practice (ISP 98)

"ISP.98 is a set of rules specifically designed for standby letters of credit".[122] It was originally introduced by American institute of International Banking Law and Practice. ISP 98 received approval by ICC in 1998[123] and came into effect by January 1999. Historically, Standby Letters of Credits have been in use for many decades without being subject to specific regulations. They were mostly regulated by UCP, however, application of UCP to Standby Letters of Credits was source of many problems as UCP was «originally written for use only in commercial letters of credit... many of the provisions of the U.C.P. are either inapplicable or inappropriate in a standby credit context.»[124] On the other hand, it was possible for Standby Letters of Credit to be governed by URDG due to similarity between legal character of Demand Guarantees and Standby Letters of Credits. However, URDG

[118] Int'l Chamber of Commerce. ICC Publication No. 458. Paris: ICC, 1992.

[119] KATZ, R.: Report delivered at the I.C.C. Hong Kong meeting. Reprinted in: Int'l Chamber of Commerce, ICC Publication No. 470/893. Paris: ICC, 1999, p. 19.

[120] BARANAELLO, J.: Understanding the URDG 758. Available at: http://www.fpsc.com/DB/TreasuryPulse/ Fall2010/Article4.html

[121] URDG Article 20 :

a) Any demand for payment under the Guarantee shall be in writing and shall (in addition to such other documents as may be specified in the Guarantee) be supported by a written statement (whether in the demand itself or in a separate document or documents accompanying the demand and referred to in it) stating:

(i) that the Principal is in breach of his obligation(s) under the underlying contract(s) or, in the case of tender guarantee, the tender conditions; and (ii) the respect in which the Principal is in breach.

b) Any demand under the Counter-Guarantee shall be supported by a written statement that the Guarantor has received a demand for payment under the Guarantee in accordance with its terms and with this Article.

c) Paragraph (a) of this Article applies except to the extent that it is expressly excluded by the terms of the Guarantee. Paragraph (b) of this Article applies except to the extent that it is expressly excluded by the terms of the Counter Guarantee.

[122] BUCKLEY, R.P. – GAO, X.: Comparative Analysis of the Standard of Fraud Required under the Fraud Rule in Letter of Credit Law. In: Duke J. Comp. & Int'l L., 2003, 13, p. 115.

[123] Int'l Chamber of Commerce, ICC Publication No. 590. Paris: ICC, 1998.

[124] TURNER, P.S.: New Rules for Standby Letters of Credit: The International Standby Practices. In: Banking & Finance Law Review, 1999, 14, p. 459.

is becoming more popular after coming into force of its new revision URDG 758 and «[f]rom the viewpoint of the I.C.C ..... Standby letters of credit continue to be covered by the U.C.P. and are not covered by the U.R.D.G.»[125] Initially, similar to UCP for regulating the function of Commercial Letters of Credits URDG for Independent Guarantees, and ISP 98 was drafted for the purpose of regulating Standby Letters of Credits. However, «Like the UCP and the URDG, ISP98 [applies] to any independent undertaking issued subject to it».[126]

While article 20 of URDG tries to define a safety mechanism and reason for effectuating payment under the demand guarantee, Rules 4.16 ad 4.17 of ISP 98 provide that effectuating payment under the stand by letter of credit does not need any default or conditions relevant to underlying contract where such situation is not required by the credit. Therefore, it is possible to conclude that ISP 98 does not even address problem of fraud in an implied manner.

4.7 United Nation's Convention on Independent Guarantees and Standby Letters of Credits

UNCITRAL Convention has been drafted by an intergovernmental organization which is body of United Nations General Assembly and works on preparation of instruments for harmonization of law regarding international trade.[127] Convention has been adopted by UN General Assembly on 11 December of 1995.[128] Standby letters of credits and independent guarantees or any other international undertaking can be subject to the UCITRAL Convention, if:[129]

«the place of business of the guarantor/issuer at which the undertaking is issued is in a Contracting State,» or «the rules of private law lead to the application of the law of a Contracting State,» «unless the undertaking excludes the application of the Convention.»

In case of Commercial Letters of Credit, by express address of parties to the credit UNCITRAL Convention can be used as the governing law.[130] Although, UCP and URDG have been used as bases for drafting the UNCITRAL Convention, it is possible to distinguish some differences among them. First, UCP and URDG have been drafted by ICC which is a private institute and its approvals might only have application as voluntary rules or self-regulations while UNCITRAL Convention is a uniform law and official regulation applied to signatory countries which has been drafted by an international organization.[131] Therefore, UNCITRAL Convention can be differentiated from ICC rules due to its legal statues. In addition, UNCITRAL Convention, consists of complementary provisions to UCP 600, URDG and ISP 98 including abusive demand, fraud and remedies which are discussed under the section 19 of Convention.

125 Int'l Chamber of Commerce, ICC Publication No. 205-207. Paris: ICC, 1998.
126 BYRNE, J. E.: Preface. In: BYRNE, J. E. et al.: International Standbypractices ISP98 6. Paris: ICC Publishing, 1998.
127 Explanatory Note: UNCITRAL Secretariat on the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit, U.N. Commission on International Trade Law, 30th Sess., note I, at 2, U.N. Doc. A/CN.9/431, 1996.
128 BUCKLEY, R.P. – GAO, X.: Comparative Analysis of the Standard of Fraud Required under the Fraud Rule in Letter of Credit Law. In: Duke J. Comp. & Int'l L., 2003, 13, p. 117.
129 UNCITRAL CONVENTION Art. 1(2).
130 UNCITRAL CONVENTION Art. l(1)(b).
131 UNCITRAL CONVENTION Art. 1(2).

4.7.1 UNCITRAL Convention's View

In late 1995 the United Nations Convention on Independent Guarantees and Standby Letters of Credit came into force with the goal of facilitating the function of Independent Guarantees and Standby Letters of Credit in international trade. The Convention is effective in contracting States and despite the fact that its scope is limited to demand guarantees and standby letters of credit, it has application to Commercial Documentary Letters of Credit as well. This convention is the first international effort to address the problem of fraud in international LC transaction and three of its articles (article 15,19 and 20) directly deal with abusive and fraudulent demand for payment under standby letters of credit and independent guarantees plus ways to prevent them. Therefore, Convention is considered a supportive regulatory framework to UCP. However; the word fraud has not been mentioned throughout the convention following the logic of preventing confusions which may result from different interpretations of the term in different jurisdictions.

Article 15 is the guideline for beneficiary in making the demand under standby letters of credit and independent guarantees. It refers to conditions under which beneficiary's demand can be prevented: "[t]he beneficiary, when demanding payment, is deemed to certify that the demand is not in bad faith (for example by providing confirmation letters from an authorized inspection firm regarding compliance of shipped consignment with terms of LC)and that none of the elements referred to in subparagraphs (a), (b) and (c) of paragraph 1 of article 19 are present."

Article 19 titled: "Exceptions to payment obligation" provides list of situations which tackle issues with the possibility of refusing demanded payment by beneficiary. Paragraph (1) provides that: "Any document is not genuine or has been falsified; no payment is due on the basis asserted in the demand and the supporting documents; or Judging by the type and purpose of the undertaking, the demand has no conceivable basis…" . Paragraph 2 explains the meaning of "no conceivable basis": "(a)The contingency or risk against which the undertaking was designed to secure the beneficiary has undoubtedly not materialised; (b)The underlying obligation of the principal/applicant has been declared invalid by a court or arbitral tribunal, unless the undertaking indicates that such contingency falls within the risk to be covered by the undertaking; (c) The underlying obligation has undoubtedly been fulfilled to the satisfaction of the beneficiary; (d) Fulfilment of the underlying obligation has clearly been prevented by wilful misconduct of the beneficiary; (e) or In the case of a demand under a counter-guarantee, the beneficiary of the counter-guarantee has made payment in bad faith as guarantor/issuer of the undertaking to which the counter-guarantee relates".

Further, paragraph (3) of the same article provides that: "in the circumstances set out in subparagraphs (a), (b) and (c) of paragraph 1 of this article, the principal/applicant is entitled to provisional court measures in accordance with article 20." Scholars consider article 19 of convention successful in achieving its political and technical objectives.

Article 20 continues with providing possibilities for court action under the title of "Provisional court measures":

"1. Where, on an application by the principal/applicant or the instructing party, it is shown that there is a high probability that, with regard to a demand made, or expected to be made, by the beneficiary, one of the circumstances referred to in subparagraphs (a), (b) and (c) of paragraph I of article 19 is present, the court, on the basis of immediately available strong evidence, may: a. Issue a provisional order to the effect that the beneficiary does not receive payment, including an order that the guarantor/issuer hold the amount of the undertaking, or b. Issue a provisional court order to the effect that the proceeds of the undertaking paid to the beneficiary are blocked, taking into

account whether in the absence of such an order the principal/applicant would be likely to suffer serious harm.

2. The court, when issuing a provisional order referred to in paragraph 1 of this article, may require the person applying therefor to furnish such form of security as the court deems appropriate.

3. The court may not issue a provisional order of the kind referred to in paragraph 1 of this article based on any objection to payment other than those referred to in subparagraphs (a), (b) and (c) of paragraph 1 of article 19, or use of the undertaking for a criminal purpose."

From technical point of view, the Convention is successful in addressing major aspects of fraud rule developed by national courts in addition to offering a precise and useful guidelines. Article 19 (1) lists types of misconduct by beneficiary which result in application of fraud rule both under LC contract and underlying sales contract. Also Convention provides guidance for actions which victim of fraud can take by either withholding payment or refusing to honour presentation (bank) and applying for injunction remedy at court (applicant) in order to prevent issuing bank from honouring fraudulent presentation. Gao and Buckley consider fraud related provisions in UNCITRAL Convention as vital and positive development which can be used as a guide for national courts while applying the fraud rule.

There are two main criticisms to UNCITRAL Convention articles on fraud. On one hand, scholars criticize vagueness of provisions which might create problem in practice of independent undertakings. On the other hand, other scholars express concern on possibility for different court interpretations as a result of applying Convention's provisions which might increase the risk for international trade. In conclusion, UNCITRAL Convention has provided a constructive development in international application of LC fraud rule despite existence of different interpretations among national courts.

5 CONCLUSION

Documentary letters of credit are among most popular instruments used by traders and banks in the field of international trade finance. Despite their facilitating nature in smoothing up the process of international transactions, their mere documentary nature makes them vulnerable to the problem of fraud. Situation will become more complicated as the United States of America is the only country which has statutory regulations to regulate fraud in LC operation. England is following fragmented approach based on case law and other countries do not really have significant regulations in above mentioned area. Current paper tried to analyse the problem of fraud as a globally accepted exception to the principle of autonomy in documentary letters of credit by scrutinizing national legal systems in England and the USA as well as international legal framework applicable to LC operation which have been introduced by ICC and UNCITRAL.

Despite the fact that UCC and English law cover the fraud exception to an extensive level, ICC regulations show no trace of paying attention to such important problem. Among internationally accepted norms, Only UNCITRAL Convention provides provisions on how to deal with fraud in LC operations. This is clearly not sufficient as majority of LC users and active traders in international business have no detailed knowledge of American and English legal system. On the other hand, UNCITRAL Convention is only ratified by nominal number of countries which limits its application extensively. It is recommended to include fraud exception in ICC rules particularly UCP due to its

extensive use as applicable law in process of LC Operation. On one hand inclusion of fraud rule in UCP will increase the clarity and expectably of LC operation and on the other hand it will reduce current existing problems of judges who are not familiar with detailed operation of documentary credits and bankers who have no legal expertise on how to deal with legal aspects of LC fraud in national legal systems.

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Contact information:

Hamed Alavi, MBA, LLM, PhD Candidate
hamed.alavi@ttu.ee
Tallinn School of Law
Tallinn University of Technology
Estonia

Faculty of Law
Universitat Autònoma de Barcelona
Spain

ARTICLES

CONSULAR COOPERATION IN THIRD STATES: SOME ASPECTS CONCERNING EUROPANISATION OF FOREIGN SERVICE FOR EU CITIZENS[1]

Erzsébet Csatlós
University of Szeged, Faculty of Law and Political Sciences

Abstract: The EU does not aim to harmonize the public administration of Member States, although, in recent years, there have been several examples which prove that EU legislation in whatever policy inevitably and unavoidably results in some standardization. In 2015 the EU replaced its former decision with a directive to enhance Member States to co-ordinate consular assistance in third States. Every EU citizen has the right to enjoy, in the territory of a third State in which the Member State of which they are nationals is not represented, the protection of the diplomatic and consular authorities of any Member State on the same conditions as the nationals of that State. This provision of Article 23 of TFEU not solely requires the cooperation of administrative authorities of foreign service but implicitly means a kind of harmonization of substantive law, leads to organizational changes and affects administrative procedural rules of Member States.

Key words: consular relations, administrative law, cooperation of administrative authorities, EEAS

1 CONSULAR PROTECTION

People travelling, living or trading beyond the borders of their homeland could have always benefitted a kind of care from their country of origin as the specific link called nationality between the person and the State remains and reciprocally obliges both parties even beyond state borders.[2] This legal relationship is older than the concept of modern State. Foreign Service is the prolongation of a few administrative functions of the State on the territory of another State. It has two main directions: diplomacy primarily serves the interest of the sending State while promoting friendly relations and consular service is to help and serve the citizens there with the consent of the latter, the receiving State. Consular protection is help, advice and the possibility to handle official matters of an administrative nature by the consular or diplomatic agents of a country to citizens of that country who are living or just staying abroad. It has always been a discretional right of the State to decide upon the subject and the scope and extent of this kind of service.

Every state defines the scope of the functions of its consular representatives, considering the legislation of the host country. The main sources of consular law therefore are the many consular agreements concluded by individual countries defining the legal status of consuls and laying down the basic rules under which they function. As for the service given for nationals, it has two main

[1] „SUPPORTED BY THE UNKP-17-4-III-SZTE-10. NEW NATIONAL EXCELLENCE PROGRAM OF THE MINISTRY OF HUMAN CAPACITIES".

[2] AUST, A.: Handbook of International Law. Cambridge: CUP, 2010, p. 42.; SLOANE, R. D.: Breaking the Genuine Link: The Contemporary International Legal Regulation of Nationality. In: Harvard International Law Journal, vol. 50, No. 1, 2009, p. 29 -33.

areas. A part of consular service can be regarded as an outsourced version of domestic administration, for example the possibility of getting travel documents, so it is regulated solely by the laws of the sending state. The other part rather aims to help and protect citizens' interest on the territory of a foreign State, for example in case of detention, it is good to have somebody who can help with knowing local conditions and get professional legal help. In such cases, the scope of procedural rights and possibilities of the consul is basically up to the laws of the receiving State and the agreement of the States concerned.

Consular assistance and protection is a service of domestic competence,[3] so is the public administration of Member States to which the consular and diplomatic representation is an extra territorial organizational unit performing administrative authority functions among others, therefore it shall be strictly examined what is exactly required by EU law.

2 ASPECTS OF COOPERATION OF CONSULAR AUTHORITIES

2.1 Consular protection and EU legislative competences

The concept of EU citizenship exists since the entry into force of the Maastricht Treaty in 1993.[4] It creates a specific relationship to strengthen European identity while it guarantees the right to any EU citizen in a non-EU country where his/her own national state has no representation to ask for protection by the diplomatic or consular authorities of any other EU country. The concept is to strengthen the sense of togetherness and the feeling of being a part of one unified European nation, on the basis of solidarity and loyalty among EU 28 and in the light of non-discrimination and legal equality.[5] As a matter of fact, Member States are all present in only three countries: the US, Russia and China[6] but the need for consular help is increasing in our world of natural disasters and terrorist acts, so the concept of equally providing for help for EU citizens where their State of nationality is not represented or not available is useful and has a growing relevance as there is a tendency of closing foreign services to cut expenses.

Following the Maastricht Treaty, the European Community's decision with its six meaningful articles of nine entered into force in 2002 (95/553/EC) on details of diplomatic protection[7] and a decision on the establishment of an emergency travel document (96/409/CFSP) was adopted along with non-binding guidelines on consular protection and the concept of lead state of coop-

3 CARE Final Report. Consular and Diplomatic Protection. Legal Framework in the EU Member States. 2010. http://www.careproject.eu/images/stories/ConsularAndDiplomaticProtection.pdf, p. 665; VERMEER-KÜNZLI, A: Where the Law Becomes Irrelevant: Consular Assistance and the European Union. In: International and Comparative Law Quarterly, 2011, vol. 60, p. 971.

4 Maastricht Treaty, Art. 8c.; currently Article 23 TFEU (ex Article 20 TEC, Treaty on the European Community).

5 GEYER, F.: The External Dimension of EU Citizenship. Arguing for Effective Protection of Citizens Abroad. CEPS, No. 136. July 2007, p. 2.

6 Green Paper: Diplomatic and consular protection of Union citizens in third countries. Brussels, 28.11.2006, COM(2006)712 final, p. 4. point 1.5.; BALFOUR, R. – RAIK, K.: Equipping the European Union for the 21st century. National diplomacies, the European External Action Service and the making of EU foreign policy. FIIA Report 36, 2013, p. 12.

7 Council Decision of 1995. Decision of the Representatives of the Governments of the Member States meeting within the Council of 19 December 1995 regarding protection for citizens of the European Union by diplomatic and consular representations. OJ L 314 , 28/12/1995, pp. 73 – 76.

eration.[8] These documents were not recognized as part of the EU legal order, as they were adopted by Member States governments and not by the institutions however as *acquis communautaire* they were to be respected.[9] At that time the field of consular and diplomatic cooperation was purely an inter-governmental area of Community legislation, it could not overcome the diversity of national regulations and foreign policies. Since the Maastricht Treaty citizens were entitled to receive consular protection, but this provision rather reflected a non-discrimination clause than an individual right for citizens and an obligation for States under all circumstances, since consular protection is just the possibility of State under general international law, not an obligation to fulfil.

Everything has changed when the EU Charter became a primary source by the Treaty of Lisbon – EU citizens' rights to diplomatic and consular protection echoed in Article 46[10] was reappraised as a fundamental right. Consular protection has become an integral part of the Union's policy on citizens' rights,[11] by the abolition of pillars it was placed under the scope of the EU and the Court of Justice of the EU, and the Council also got the right to regulate related questions in the form of directives adopted in a specific legislative procedure. The concept also changed: the Council, acting in accordance with a special legislative procedure and after consulting the European Parliament, adopted directives establishing the coordination and cooperation measures necessary to facilitate such protection,[12] and within the provisions of external actions of the EU, ordered the establishment of the *European External Action Service*, and as diplomatic mission of the integration, the apparatus of *EU delegations* in third countries and at international organizations was introduced to represent the EU and to act in close cooperation with Member States' diplomatic and consular services.[13] The question is what it means for Member States under specific competency rules and decision-making system.[14] The implementation deadline of the directive is 1 May 2018, however, it leaves some open questions which may not be answered by domestic legislations in a uniform manner.

Consular service is an extra territorial branch of State administration heavily related to foreign policy of the State and inter-state relations, which is still a sensible area even after Lisbon. Consular assistance consists of actions, often performed by authority measures, therefore consular policy has relatively strong relation to administration. As a matter of fact, EU's legislative competence is only to support, coordinate or supplement the actions of the Member States to improve their administrative capacity for a better implementation of EU law. The legislative acts shall not result in any harmonization of the national administrative laws.[15] It does not mean that EU law has no influence on administration, but effective execution and implementation of EU policy is the responsibility of Member States, so the necessary harmonization in administration issues is a domestic competence. The question is to find the limit between the necessary modification to realize and achieve common policies and the implicit expansion of EU competences; even the preamble of the consular directive

8 KRŪMA, K.: EU Citizenship, Nationality and Migrant Status: an Ongoing Challenge. Leiden: Martinus Nijhoff Publishers, 2013, p. 170.

9 CARE Final Report, pp. 24-25.

10 „*Every citizen of the Union shall, in the territory of a third country in which the Member State of which he or she is a national is not represented, be entitled to protection by the diplomatic or consular authorities of any Member State, on the same conditions as the nationals of that Member State.*"

11 Proposal for a Council Directive on consular protection for citizens of the Union abroad, 1.2.; p. 2.

12 Treaty of Lisbon, point 36.

13 Treaty of Lisbon, point 30) on the new Article 13a ; Article 188 Q on delegations.

14 See TEU Title V. especially Article 22 and Articles 29-31.

15 TFEU Article 2.5.; 6 (g); and 197.

set the limitation of its scope: it does not affect consular relations between Member States and third countries, their rights and obligations arising from international customs and agreements.

2.2 Consular directive and Member State obligations: "cooperation and coordination measures to facilitate …"

The directive obliges Member States and does not limit the scope of authorities: it leaves the question open for Member States as to all types of extra-territorial representations, since this depends on the habits and regulations of States to decide upon which organ to authorize to provide consular assistance. Although the text mentions diplomatic and consular protection, the relevant provisions and also legal literature is in agreement that the obligation refers to measures of consular assistance even if it is performed by diplomatic agents in the absence of consuls.[16] Citizens of the EU should be considered to be unrepresented in a third country if their Member State of nationality has no embassy, consulate[17] or honorary consul established there, or if the body is unable for any reason to provide, in a given case, the protection or it is just unavailable for the citizen for distance or any other reasons or circumstances.[18] This possibility is also equally open for the non-EU citizen family members[19]; however, some restrictions might indicate different treatment as emergency travel documents (EDT) can only be issued for EU citizens, for example.[20] As for identification of the citizenship and family ties, the rules are relatively flexible if the persons are unable to produce valid passports or identity cards. Nationality may be proven by any other means, if necessary including verification with the diplomatic or consular authorities of the Member State of which the applicant claims to be a national.[21]

As a matter of fact, in case of non-national EU citizens, apart from extreme cases, consular authorities do not proceed *ex officio,* consular protection needs to be claimed. However, when the

16 Consular functions can be exercised by diplomatic missions in accordance with the provisions of the general international rules of consular and diplomatic relations. VCDR, Article 3.2.; VCCR Article 3.; 70. BATTINI, S.: The Impact of EU Law and Globalization on Consular Assistance and Diplomatic Protection. CHITI, E. – MATTARELLA, B.G. (eds.): Global Administrative Law and EU Administrative Law. Berlin, Heidelberg: Springer-Verlag, 2011, p. 177-178.; SCHIFFNER, I.: A diplomáciai védelem gyakorlásának eszközei, avagy a fogalom-meghatározás és az elhatárolás problémái. In: Acta Universitatis Szegediensis de Attila József Nominatae Sectio Juridica Politica, Tom. LXXII. Fasc. 18, 2009, p. 535- 543; BECÁNICS, A.: Konzuli védelem és segítségnyújtás az Európai Unió perspektívájából. KARLOVITZ, J. T. (ed.): Fejlődő jogrendszer és gazdasági környezet a változó társadalomban. 2014. http://www.irisro.org/tarstud2015aprilis/index.html (02.09.2016.), p. 25-26.

17 The exercise of consular functions does not always mean that the consular service is established on the territory of the State in question. The sending State may, after notifying the States concerned, entrust a consular post established in a State with the exercise of consular functions in another State, unless there is express objection by one of the States concerned (exercise of consular functions in a third State, VCCR, Article 7.). Another solution to the representation is the agreement with a State who already has a consular service in the State concerned to provide for consular protection to citizens of both States. Upon appropriate notification to the receiving State, a consular office of the sending State may, unless the receiving State objects, exercise consular functions in the receiving State on behalf of a third State (exercise of consular functions on behalf of a third State, VCCR, Article 8).

18 Consular directive, (8); Article 6.

19 The right to respect for private and family life is acknowledged by Article 7 of the EU Charter and the family reunification principle also serves the private life of citizens. However, the EU family reunification principle has a narrow scope of family members, see: Directive on family reunification, Article 4. However, the more favourable treatment clause is also to be applied for the meaning of family member. Consular directive, Article 16.

20 Consular directive, (8); EDT Decision, Annex II. 2. (a).

21 Consular directive, Article 8.

consular authority is aware of the need of consular protection, especially in case of travel documents, the family reunification principle[22] may require some positive action like promoting the contacting between the family members and its Foreign Ministry. Over and above, article 23 and the Consular Directive detailing its content exceeded former 'non-discrimination clause' notion and shifted the emphasis to the coordination and cooperation of consular authorities from the simple declaration of the right to consular protection which characterized the previous regime.

The intent of the Consular Directive is to guarantee help and protection in Third States by creating an obligation for consular authorities to coordinate their acts and cooperate with each other while fulfilling the required obligation and taking the necessary measures if the consular authority of nationality (citizenship) is not able to do so.[23] So, it is not required from States to renounce their discretionary right[24] to provide for consular protection, and diplomatic and consular authorities of the Member States are not legally obliged to satisfy all the requests for assistance from EU citizens. But it does mean first, to help citizens to get the assistance needed by his/her own national consular authorities and if it is not possible or it is unable to act, secondly, provide for the necessary consular protection. Indeed, when a Member State receives a request for consular protection from a person who claims to be an unrepresented EU citizen, or is informed of an individual emergency of an unrepresented citizen, it shall consult without delay the Ministry of Foreign Affairs of the Member State of which the person claims to be a national or, where appropriate, the competent embassy or consulate of that Member State, and provide it with all the relevant information at its disposal. This notification includes the identity of the person concerned, possible costs of consular protection, and information on any family members to whom consular protection may also need to be provided and helps and facilitates the exchange of information between the citizen concerned and the authorities of the citizen's Member State of nationality. As for the preparation for a more comprehensive work, local cooperation meetings are held for a regular exchange of information on matters relevant to unrepresented citizens. It is chaired by one of the Member State representatives and it is in close cooperation with the delegation of the EU, if there is any.[25]

Except in cases of extreme urgency, this consultation shall take place before assistance is provided.[26] The obligation therefore primarily refers to being available for EU citizens without representation and the notification to their own State to make it possible that they get the requested protection and assistance by their State. This does not require the acting of the consul, but rather the exchange of information and cooperation during normal times and, above all, during major crises. The need for an active consular cooperation is not just theory as an estimated 8.7% of EU citizens, or 7 million people, travel outside the EU to States where their Member State is not represented and a further 2 million EU citizens live in such countries.[27] A survey of 2015 states that 7 EU citizens from 10 are

22 Member States are required to adopt measures for family reunification concerning residency cases of third country nationals in conformity with the obligation to protect the family and respect family life enshrined in many instruments of international law and in respect of the fundamental rights recognized in Article 8 of the EU Charter. Directive on family reunification, preamble (2).

23 VERMEER-KÜNZLI, A: Where the Law Becomes Irrelevant, p. 969.

24 The practice of Member States is various regarding their attitude to consular protection: whether it is a duty of the State or a discretionary right to decide upon providing for it. SCHIFFNER, I.: Az uniós polgárok konzuli védelmének lehetőségei a tagállamok gyakorlatában. In: Forum: Acta Juridica et Politica, Vol. 2. No. 1, 2012, p. 180.

25 Consular Directive, Article 12.

26 Consular Directive, Article 10.

27 COM(2009) 263 final III.1.2, p. 5.

aware of the right to turn to the representative of any Member States if his or her State is not represented in a third State.[28]

As for the scope of help, the directive, in line with the former decision, does not create new functions for representatives of Member States; although it enlists some typical cases in which consular protection shall be available for all EU citizens in third States: death, serious accident or serious illness, arrest or detention, falling victim of violent crime, loss or theft of identity documents, and situations requiring repatriation or relief especially in armed conflicts, and in case of natural disasters.[29] The measure taken in such cases is up to the consular law of Member States, which is also free to ensure a wider range of protection but it shall be equally available for nationals and for non-nationals (EU citizens).[30] With regard to the nature of the help, according to the latest Eurobarometer survey on the topic done in 2006, arrangement to immediately return to home was the most preferred form of assistance Europeans would like to have in emergency. The Eurobarometer survey published in 2006 states one third (33%) of the overall EU25 population mentioned this as their first preference.[31] In 2016, the statistics of the EEAS show that the number of non-represented EU citizens requesting consular assistance is limited and the cases are manageable; most requests deal with loss of travel documents.[32]

As for travel documents, only the national authorities can replace the damaged, lost or stolen ones, for non-national EU citizens the ETD can be issued upon request which is valid slightly longer than the minimum time needed to complete the journey for which it is issued.[33] It also requires the collaboration of the national authorities as the ETD can only be issued if clearance from the authorities of the person's Member State of origin has been obtained. Problems might occur with non-represented non-EU citizen family members. They are not entitled to get an ETD and this makes the return to home impossible for the family as it is obvious that they will not split up. Consular Directive does not directly create obligation for the consular authority proceeding in the case of the citizen to contact the national authorities of the non-citizen's Member State for that purpose. However, the general rules obliging Member State consular authorities to provide consular protection to the same extent and on the same conditions as the EU citizen[34] can be interpreted to that way to reach this conclusion. As for practical guidance to travel home, its form is up to the situation but concerning financial help, rules are clear: it is a final solution and national and non-national consular authority is also obliged to give financial help with the same conditions as to their nationals. Except for crisis, citizen shall sign an undertaking to repay to his or her Member State of nationality

28 Flash Eurobarometer #430. European Union Citizenship. Eurobarometer, 2015. http://ec.europa.eu/justice/citizen/document/files/2016-flash-eurobarometer-430-citizenship_en.pdf (18.08.2016.), pp. 29-30.; 33. By the way, 75 % of EU citizens were wrong believing that they are entitled to consular protection provided by any Member States' foreign service within the borders of the EU. Flash Eurobarometer #430. European Union Citizenship, pp. 42-46. As for information on the available representations, citizens can use the following website which shall be kept up to date by the Member States - Consular protection for European Union citizens abroad: http://ec.europa.eu/consularprotection/index.action (29.08.2016.) or service Your consulates and/or embassies:http://europa.eu/youreurope/citizens/national-contact-points/embassies/index_en.htm (29.08.2016.) which directs citizens to the consular website of the chosen State to get information on the State's foreign service.

29 Consular Directive, Article 9.

30 Consular Directive, Article 2.

31 Flash EB Series #188 Consular Protection, p. 13. This is the latest survey on the topic.

32 Consular Cooperation Initiatives - Final report. Presented by the CCI Core Team to the EU Working Party for Consular Affairs COCON – 8. CFSP/PESC 345, 29 April 2016 Brussels, p. 3.

33 ETD, Annex II. 4.

34 Consular Directive, Article 5.

the costs incurred, as the cost are directly repaid by the Member State of nationality and then the reimbursement will be the matter of the State and its national under the scope of domestic rules.[35]

2.3 Crisis preparedness: EEAS and its implication on consular law

The Consular Directive makes special references to crisis situations which involves EU organs to the consular cooperation of consular authorities: the *European External Action Service* (EEAS) and its local delegations established under the terms of agreements between the EU and the Third State.[36]

EEAS was created to serve the High Representative to ensure more coherent and effective EU external action without any prejudice to the Member States foreign policy.[37] Being part of the EEAS Crisis Response Department, the *Consular Crisis Management Division* currently has two roles: assisting the Presidency to coordinate consular policies across the EU (e.g. travel advice, issuance of consular guidelines), and to assist the EU Presidency and/or Lead States to coordinate action in times of crises. *Delegations* are placed under the authority of the High Representative of the Union for Foreign Affairs and Security Policy[38] and support the Member States in facilitating cooperation and in helping them to help unrepresented citizens, but since consular protection remains a national competence, delegations do not provide direct assistance to EU citizens. So, the EEAS has contradictory mandates. It is expected to 'coordinate' (policies, institutions, member states, embassies, ministers, collective action, financial resources), provide leadership, and develop new ideas and policy entrepreneurship. But it is not supposed to challenge national foreign policy, to step on the toes of national diplomacies, or interfere with national priorities and interests.[39]

However, crisis is not defined by the Consular Directive; it is relatively obvious that the notion covers natural and man-made disasters which prevent or makes it impossible to apply the normal rules of consular protection while consular protection is needed more than ever.[40] In the event of a crisis, the EU (EEAS and delegations) and Member States (representation) shall closely cooperate to ensure efficient assistance for unrepresented citizens. Within the framework of local cooperation, they shall prepare contingency plans to follow in such situations. Upon their request, Member States may be supported by existing intervention teams at Union level, including consular experts from unrepresented Member States. The protagonist of these situations is the (1) Lead State, the State or the Member State(s) coordinating and leading the assistance of unrepresented citizens during crises in any third country with the support of (2) the other Member States concerned,[41] the (3) Union

35 Consular Directive, Article 14-15.

36 VAN VOOREN, B. – WESSEL, R. A.: External representation and the European External Action Service : selected legal challenges. CLEER Working Papers 2012/5, p. 79.

37 The establishment of an External Action Service "*do not affect the responsibilities of the Member States, as they currently exist, for the formulation and conduct of their foreign policy nor of their national representation in third countries and international organisations.*" Treaty of Lisbon, 13. Declaration concerning the common foreign and security policy.

38 These are situations like Bali bombing in 2002, Indian Ocean tsunami in 2004, and 2006 evacuations from Lebanon or just from the recent past, terrorist attacks in Brussels, when citizens' life and security was threatened. TEU Article 32 al 3., 35. See, EEAS Decision, Article 5.

39 BALFOUR, R. – RAIK, K.: Equipping the European Union for the 21st century, p. 13.

40 TINDALL, K.: Governments' Ability to Assist Nationals in Disasters Abroad: What Do We Know about Consular Emergency Management? In: Journal of Contingencies and Crisis Management, Vol. 20, No. 2, 2012, p. 102. The executive directive to HCA defines crisis as a situation created by extraordinary and exceptional circumstances, which affect or may affect a significant number of citizens and require immediate action of the consular service. HCD, Article 1/A c).

41 See, Consular Directive, (23). In details: Lead State Guideline. Council European Union guidelines on the implementation of the consular Lead State concept (2008/C 317/06) OJ C 317, 12.12.2008, pp. 6-8.

delegation and the (4) EEAS headquarters, and the (5) local authorities of the Third State in which the crisis happened is also a key factor. Member States shall provide the Lead State or the Member State(s) coordinating assistance with all relevant information regarding their unrepresented citizens present in a crisis. Issues of citizenship, as a matter of fact, make it challenging to estimate the number of citizens that may need consular protection mainly in States with a strong history of immigration, like Canada, the USA or Australia for instance.[42] Therefore, the number of Member States concerned is also an unpredictable factor.

However, the consular authority of the Lead State only joins forces and coordinates measures and may request reimbursement of expenses generated by this mission, but is not responsible to provide the consular services.[43] Therefore, the cooperation and support of the background is essential: interoperability between consular staff and other crisis-management experts should be enhanced, in particular through their participation in multi-disciplinary crisis teams, such as those under the EEAS crisis response and operational coordination and crisis management structures and under the Union Civil Protection Mechanism. The EEAS and its delegations, in fact, cannot replace Member States' consular tasks. The EU has no power to do so as the protection of citizens is too much related to the notion of nationality which is a core competence of Member States. Practical reasons might occur to EEAS to practice consular protection in third States but at this stage of EU integration it is not yet possible and by the way, for acting within that competence, under the general rules of international law, the consent of the Third State would also be needed.[44]

To coordinate actions and share tasks, Member States' authorities should closely cooperate and coordinate with one another and with the EU, the Commission and the EEAS, in a spirit of mutual respect and solidarity. The way of collaboration is the secure website of the EEAS (Consular OnLine) where Member States are obliged to provide and continuously update information on relevant contact points in the Member States to ensure swift and efficient cooperation.

2.4 Some legal questions of the application of EU consular policy in Third States

The model sounds simple, cooperation and sharing of information is at the heart of the process. However, a few questions arise concerning information sharing mechanism which is the frame of the whole consular policy in third States. First and foremost: consular services on the territory of a State can be performed only with the previous consent of the State of territory. So, the margin for help of the State of nationality is limited even if it is willing to help its national in lack of representation in a Third State or wish to entrust another State to act on behalf, since this latter also requires the consent of the State of territory. Additionally, the mechanism operates with a wide range of personal data the protection of which is also a fundamental right acknowledged by the Charter. There are two types of cooperation in this context: (1) The classical legal assistance when the consular authority needs information from another Member State's authority in a concrete case which is to be handled, for example when the clearance of the citizen is needed by his/her national authority for the issue of an ETD. (2) The cooperation mechanism is, in contrast, a continuous data sharing process without exact prior request as information management process is based on EU rules. It should be based

42 TINDALL, K.: Governments' Ability to Assist Nationals in Disasters Abroad, p. 105.

43 Lead State Guideline, 5.4.

44 VCCR 2. 1. The establishment of consular relations between States takes place by mutual consent. 4. 1. A consular post may be established in the territory of the receiving State only with that State's consent.

on legally binding sources to make the procedure predictable and transparent with clearly defined tasks and competences, aspects of responsibility, applicable law and finally: supervision and legal remedy.[45] The Consular Directive does not serve as a general legal background for cooperating mechanism with such details; it just outlines the frames and remains silent on details and calls for further negotiation on the procedural aspects. In lack of general EU legislation, how shall this new consular protection policy be more efficient than the previous inter-governmental regime?

Consular authorities act as public authorities on behalf of their sending State and with their acts and decisions they affect the legal position and situation of the individuals, and finally, their fundamental right to consular protection in third countries. Therefore, legal remedy is crucial for its proper enforcement.[46] In case of need, the consular authority decides whether consular protection is exercised and which measure shall be taken. Being the fact that the right to consular protection has become a basic right by Article 46 EU Charter, the Member States are also obliged to ensure the review of the decisions of the consular authority. To protect a right created by European law, judicial remedy shall be available. The European citizen who asks for consular assistance from the authorities of another Member State, and receives a refusal which he/she considers unfair or discriminatory, shall have the possibility to appeal to a national judge capable of exercising judicial review of the contested administrative decision.[47] The Hungarian Consular Act (HCA) for example enlists those consular protection functions which require authority act, and if a consular officer takes a decision of first instance, the Minister of Foreign Affairs is entitled to proceed on appeal, but as for denial of those kind of measure which do not explicitly require authority procedure (as not all the tasks and functions of consular protection are considered as authority procedure), no provision exists.[48]

Besides that, the Consular Directive does not give any guidance on double citizenship, for instance. The citizenship policy of the EU is flexible in favour of the citizens and definitely not following the 'effective citizenship' or 'genuine link theory'.[49] In case of both citizenships of EU States one would think that the forum decides upon the competent consular authority, but according to the case-law of the Court of Justice of the European Union (CJEU) the jurisdiction does not automatically rely on the forum.[50] In such cases, which State shall provide for consular protection? Does the citizen have the right of forum shopping in favor of a more expanded consular assistance if he or she is aware of both Sates consular protection legislation? What is the obligation of the consular authority? Does the citizen with double nationality choose the competent national authority, and is the consular authority obliged to check whether a citizen has double nationalities? General principles like acting in good faith do not give enough rules for responsibility limits of the authorities taking part in the cooperative mechanism. And this guides us to another topic which is not discussed by EU norms.

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45 Model Rules. Welcome to ReNEUAL – the Research Network on EU Administrative Law. http://www.reneual.eu/ (31.08.2016.), VI-3., VARGA, ZS. A.: Gyorsértékelés az európai közigazgatási eljárási modell-szabályokról. In: Magyar Jog, 2014/10, 2014l, p. 547.

46 "*Everyone whose rights and freedoms guaranteed by the law of the Union are violated has the right to an effective remedy before a tribunal in compliance with the conditions laid down in this Article. Everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal previously established by law.*" EU Charter, Article 47.

47 BATTINI, S.: The Impact of EU Law and Globalization on Consular Assistance and Diplomatic Protection, p. 179.

48 HCA, Article 19 (7).

49 *"[t]he mere fact that a national of a Member State is also a national of a non-member country, in which he is resident, does not deprive him of the right, as a national of that Member State, to rely on the prohibition of discrimination on grounds of nationality."* Case C-122/96, paragraph 15.

50 GYENEI, L.: Kettős állampolgárság az Európai Unió erőterében. In: Iustum Aequum Salutare, IX. 2013, 2, p. 160.

Organizational problem might occur in case of crisis when the EEAS and its delegation appear as players in the procedure along with the Lead State. State administration is hierarchical; the chief a consular authority is under the direction of its own State, in particular the Minister of Foreign Affairs. In a crisis when the cooperative mechanism starts its real operation, there are usually no exact legislative provisions for handling those situations, when the Lead State or the EEAS gives order to Member States consular authorities. In fact, the EEAS decision suggests that EEAS and delegations help Member States and are not superior to their consular agents, but since Member States are required to act in conformity with EU interests, even if foreign policy is still a domestic field in majority, general obligations mean a kind of determination of activity. What happens if EU organs representing EU interests collide with the Member State's foreign policy? Which is stronger: loyalty and solidarity towards the EU and other Member States or the domestic hierarchical order in administration and the foreign policy of the sending State in the Third State? The Consular Directive declares that it does not concern consular relations between Member States and third countries.[51] But it tacitly does - when it obliges Member States to widen the scope of consular agent's activity to protect any EU citizens and non-EU citizen family members. Therefore, an effective protection requires a reflection on bilateral consular agreements with Third States but this is still awaited. It also calls the Member States' embassies or consulates to, wherever deemed necessary, conclude practical arrangements among themselves on sharing responsibilities for providing consular protection to unrepresented citizens. Insofar, since the existence of EU citizenship, no such arrangements have been made. So, again, why is this Directive better than the former intergovernmental regime? Now, involving the EEAS and delegations, the common consular policy might get an extra impetus by implicitly giving a primacy of common interests, but can it be required under the present competency rules? All these problems reveal the necessity of a European regulation of administrative procedural law, mainly in the field of administrative cooperation mechanisms which is even more important in case of a crisis and highlights the fact that the EU is expanding on foreign policy issues where it still lacks the necessary power and competence to reach direct results.

3 CLOSING REMARKS OR WARNING?

From the viewpoint of rationality and efficiency, as *Balfour* and *Raik* states, there are compelling reasons for transferring at least some of the functions of national diplomacies to the EU, rather than having numerous representations of Member States in Third States where the EU also has delegation and time and resources are spent on coordinating among authorities. It would make sense to have just one large EU delegation representing the whole Union, centralize at least some consular services and limit national missions to a minimum.[52] For this, EEAS needs to be at the center of an emerging EU system of diplomacy, shaping it and not just being shaped, and it must create a new sense of unity. It is true, that CFSP rules introduced by the Treaty of Lisbon and the creation of the EEAS are supposed to stimulate an internal logic towards more EU integration and burden-sharing in foreign policy,[53] but the Treaty of Lisbon also made it clear that the provisions covering the CFSP

51 Consular Directive, Article 1.

52 BALFOUR, R. – RAIK, K.: Equipping the European Union for the 21st century, p. 37-38.

53 BALFOUR, R. – RAIK, K.: Learning to dance to the same tune? The European External Action Service and National Diplomacies. European Policy Center, 17 January 2013. http://epc.eu/documents/uploads/pub_3231_learning_to_dance_to_the_same_tune.pdf (31.08.2016.), p. 1-2.

including relation to the High Representative the EEAS, will not affect the existing legal basis, responsibilities, and powers of each Member State in relation to the formulation and conduct of its foreign policy, its national diplomatic service, or relations with third countries.[54] Anyway, the expansion of EU policies, the Europeanisation of non-European legal areas is a question of the future; now the actual challenges shall be faced which concern the detailed procedural rules of consular authorities' cooperation in order to make it conform to the requirements of good administration.

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[54] Treaty of Lisbon, 14. Declaration concerning the common foreign and security policy.

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Contact information:

Erzsébet Csatlós, PhD, senior lecturer
csatlos.e@juris.u-szeged.hu
University of Szeged, Faculty of Law and Political Sciences,
Department of Administrative Law
Bocskai u. 10-12.
6721 Szeged, Hungary

VALUE PROMOTION AND EUROPEANISATION BY EU TRADE AGREEMENTS

Balazs Horvathy
HAS Centre for Social Sciences, Institute for Legal Studies

Abstract: Promoting values of the European Union has been on the EU's external trade agenda since the 1990s. The Treaty of Lisbon established a general framework for values and principles, requiring the Union to pursue these concepts in the whole range of EU external relations, including the Common Commercial Policy (CCP). Therefore, the operation of CCP is governed not only by trade-related concepts such as progressive liberalisation, but it also reflects on non-trade concerns – e.g. protection of human rights, fair trade, or sustainable development – as well. This inclusive character of CCP is anchored also in the new external trade strategy of the European Union ('Trade for all'), which stresses the importance of trade agreements concluded by EU in promotion of values towards third countries. The paper aims at addressing a conceptual and a procedural question related to this context: First, what kind of values of the European Union integrated in trade agreements can lead to the Europeanisation of domestic legal order of the third countries; and second, how these concepts can be implemented, i.e. how the process of Europeanisation is taking place using the example of the human rights promotion.

Key words: Europeanisation, Common Commercial Policy, values, human rights

1 INTRODUCTION

The Common Commercial Policy (CCP) has become an integral part of the European Union's external action as a result of the Treaty of Lisbon,[1] which also established a general framework for values, principles and objectives, requiring that the Union shall pursue these concepts in the whole range of the EU external relations. Therefore, the functioning of the CCP is based on a two-level structure of principles and objectives, which encompasses not only the proper, trade-related goals, such as progressive liberalization, but includes several non-trade concerns, like protection of human rights, or promotion of sustainable development as well. At first glance, these changes seem to be unimportant, knowing that the European Union has been committed to implementing an inclusive, 'values-driven' trade policy for many decades towards third countries.[2] This latter process is labelled here as

[1] The paper does not address all achievements of the Lisbon Treaty regarding the CCP. For a comprehensive analysis, see BUNGENBERG, M. – HERRMANN, C. (eds.): Common Commercial Policy after Lisbon. In: European Yearbook of International Economic Law, Special issue, 2013; KRAJEWSKI, M.: The Reform of the Common Commercial Policy. In Biondi A. and others (eds.): EU Law after Lisbon. Oxford: Oxford University Press, 2012, pp. 292–311.; DIMOPOULOS, A.: The common commercial policy after Lisbon: Establishing parallelism between internal and external economic relations? In: Croatian Yearbook of European Law and Policy, 2008/4, pp. 101–129.; MARISE, C.: Balancing Union and Member State interests: Opinion 1/2008, Choice of Legal Base and the Common Commercial Policy under the Treaty of Lisbon, pp. 678–694.; TIETJE, C.: Die Außenwirtschaftsverfassung der EU nach dem Vertrag von Lissabon. In: Beitrage zum Internationalen Wirtschaftsrecht. Heft 83. Halle: Universität Halle-Wittenberg, 2009.

[2] The "values-driven trade policy" is recent issue in the international trade law circles, predominantly in the USA, however the discussion is focusing on the policy issue itself, and not at all on its axiological, sociological context. (The discussion

'Europeanisation.' In other terms, Europeanisation is a converging tendency[3] of third countries' legal order to the EU law.[4] Europeanisation plays, however, also the role of an evocative term, since it can recall the permanent expansion of the legislative and rule-making procedures of the EU and refers to consequent fact that more and more areas of law have been becoming progressively subject to EU legislative procedures in the last decades. Thus, the evolving process of Europeanisation requires more convergence at domestic level and attempts to minimize the diverging elements of the legal orders, therefore the Member States face increasing level of legal sources, which originate from the EU law and should be adapted and implemented at domestic level. Even though the trends of divergence and convergence and the Europeanization are commonly used and well established in the political science[5] (and fall partly within the scope of the economics), this paper will not contextualise the insights of these disciplines, but it makes attempt to contribute only to the legal scholarship. The paper, first, lays down the conceptual background, and second, the analysis will highlight a specific example of Europeanisation process taking place in the EU human rights promotion towards third countries.

2 VALUES AND OTHER RELEVANT CONCEPTS OF THE COMMON COMMERCIAL POLICY

In the light of the current constitutional structure of the European Union, the formulation and implementation of the CCP, as an integrated part of the Union's external action, are guided by three major categories: values, principles, and objectives. It is worth limiting and clarifying the three concepts at hand briefly.

2.1 Values

The 'values' are appearing in Article 2 TEU,[6] declaring that "[t]he Union is founded on the values of respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights, including the rights of persons belonging to minorities […]." These values are common to the

was triggered in February 2014, when the U.S. Trade Representative, Michael Froman delivered a speech on the US post-crisis trade strategy, and brought non-trade issues, as 'values' into prominence. See FROMAN, M.: A Values-Driven Trade Policy. Speech of U.S. Trade Representative Michael Froman of February 18, 2014. Available at: http://cdn.americanprogress.org/wp-content/uploads/2014/02/Center-for-American-Progress-Remarks-Ambassador-Froman-2-18-14.pdf.

3 In other words, the basic concept are based on their original meaning; for similar approach, see LEGRAND, P.: Public Law, Europeanisation, and Convergence: Can Comparatists Contribute? In: BEAUMONT, P. and others (eds.): Convergence and Divergence in European Public Law. Oxford: Oxford University Press, 2002, pp. 225–226.

4 Similarly, 'Europeanization' is meant restricted geographically to EU integration: LEGRAND, P.: Public Law, Europeanisation, and Convergence: Can Comparatists Contribute?, p. 225.

5 For definitions see especially, BÖRZEL, T.: Europeanization: How the European Union Interacts with its Member States. In: BULMER, S. and others (eds): The Member States of the European Union. Oxford: Oxford University Press, 2005, pp. 45–76.

6 Previously, the TEU put emphasis on the 'common values' of the Union, as a specific objective of the Common Foreign and Security Policy ("The Union shall define and implement a common foreign and security policy covering all areas of foreign and security policy, the objectives of which shall be […] to safeguard the common values, fundamental interests, independence and integrity of the Union in conformity with the principles of the United Nations Charter." Article 11 TEU as amended by the Treaty of Nice). The current text of Article 2 TEU was originally formulated by the European Convention (see Article I-2 of Treaty establishing a Constitution for Europe), which was incorporated into the Treaty of Lisbon later.

Member States in a society in which pluralism, non-discrimination, tolerance, justice, solidarity and equality between women and men prevail.[7] In the proper sense of this formulation, the 'values' are expressing the consensual wish of the Member States to submit the whole construction and operation of the Union under these ultimate criteria, representing a community of values.[8] In other terms, the 'values' can be regarded as fundamental orientations and expectations, which are common, as well as are of a significant nature in the European societies.

However, it is questionable, whether Article 2 TEU does have a sort of meta-legal nature, or it possesses normative quality.[9] On the one hand, the positioning of the values in the whole structure of the founding treaties suggests, the respect and implementation of values are a *conditio sine qua non* of the EU membership in accordance with Article 49 TEU.[10] On the other hand, several specific Treaty provisions are referring to the values, or incorporate it into principles, or Treaty objectives. Accordingly, the provisions of the Treaty oblige the Union, or the Union's institutions to 'promote', to 'uphold', to 'safeguard', to 'protect', to 'assert' the values, [11] and addresses also the Member States, which are risking possible sanctions in case of serious and persistent breach of the fundamental values of the European Union.[12] Interestingly, the Treaty makes reference in context of the external relations to the same six 'values' as 'principles', and the promotion, upholding etc. of these values in international relations are set down as 'objective' as well. [13] In view of the previous reasons, it seems to be plausible, that the listing of values in Article 2 TEU itself has not distinctive character, neither within general scope, nor in context with the external relations and CCP. However, the Treaty lays down legal obligations, when the 'values' are contextualized within more specific principles, the promotion of which is set as an objective of the European Union. In other words, the distinction between the abstract values and the principles seems to be quite elusive, and from this perspective, the values, without denying its fundamental role in the structure of the founding Treaties, might have rather axiological, than legal nature.

7 Article 2 TEU, second sentence.

8 The concept of 'Union of interest' is rather a political category, which is frequently praised in the literature regarding the European identity. However, the legal scholarship (predominantly the German literature) brings the category of Community of Values (*Wertegemeinschaft*) into the context of the constitutionalisation process of the European Union. See RENSMANN, T.: Grundwerte im Prozeß der europäischen Konstitutionalisierung. Anmerkungen zur Europäischen Union als Wertegemeinschaft aus juristischer Perspektive. In: BLUMENWITZ, D. and others (eds.): Die Europäische Union als Wertegemeinschaft. Berlin: Duncker & Humblot, 2005, pp. 49–71.

9 Moreover, it is worth paying attention to the background and the history of origin of the text of Article 2. In light of the explanatory note of the Praesidium of the European Convention, which formulated the original text in 2003, this provision contains only a hard core of values. On the one hand, these values are "[…] fundamental that they lie at the very heart of a peaceful society practising tolerance, justice and solidarity; on the other hand, they must have a clear non-controversial legal basis so that the Member States can discern the obligations resulting therefrom which are subject to sanction." CONV 528/03. Draft of Articles 1 to 16 of the Constitutional Treaty (6 February 2003), 11. http://european-convention.europa.eu/pdf/reg/en/03/cv00/cv00528.en03.pdf

10 Pursuant to Article 49 TEU, any European state which respects the values and is committed to promoting them may apply to become a member of the Union.

11 See Article 3 (1), Article 3 (5), Article 13 (1), Article 8, Article 21 (2), and Article 42 TEU.

12 Article 7 TEU.

13 E.g., the values of Article 2 TEU are shown up in Article 21 TEU as 'principles.' The other striking example can be found in the preamble of the Charter of Fundamental Rights of the European Union that seems to be not fully compatible with the wording of Article 2 TEU. In the Charter's preamble, the human dignity, freedom, equality and solidarity are cited as 'universal values', however it refers to the "principles of democracy and the rule of law."

[14] Disregarding the axiological significance of the values, this all means that the same orientation can be formulated as value and as a principle, which is depending mainly on the wish of the legislator.[15]

2.2 Principles

Similarly to the values, the '*principles*' are expressing orientations and requirements; however the nature of principles are less abstract and more concrete, than the concept of values is. The principles have normative quality, and in addition to that, are helpful tools in interpretation and legal argumentation. It covers also the general principles developed by the Court of Justice of the European Union inspired by the general rules, objectives, principles laid down in the treaties; common constitutional traditions of the Member States, or international agreements concluded by all Member States. The 'interpretative activism' of the Court led to recognition of several general principles of EU law, which have been made explicit and incorporated into the founding Treaties as 'principles,' or as 'values'.[16] Even though the principles encompass more concrete content than the values, the level of abstraction of the principles is variable. Some principles cover larger EU activities (e.g. principles of EU external actions in Article 21 TEU), and other determine specific policy fields (e.g. principles of CCP in Article 207 TFEU).

The proper principles of the EU external relations are enshrined in Article 21 (1) TEU that the European Union "seeks to advance in the wider world."[17] The Article highlights the below principles of the EU external relations in the following order:

- democracy;
- rule of law;
- universality and indivisibility of human rights and fundamental freedoms;
- human dignity;
- principles of equality and solidarity;
- respect for the principles of the United Nations Charter and international law.

These principles are based partly on the values, however, it cannot be passed over, that the emphasis, e.g. the order of the listing is not identical to the values laid down in Article 2 TEU. In addi-

[14] Bogdandy presumes, that even Article 2 TEU refers to 'values', we have to regard these categories as normative provisions and the values as indicated in Article 2 are, in fact, identical to principles. Bogdandy does not deny the distinction between constitutional values and principles, however he does not overlook the dual character of values in Article 2, namely that the same values are present in other places in the Treaty and playing also normative roles (e.g. in Article 3 as objective). See BOGDANDY, A.: Grundprinzipien. In: BOGDANDY, A. – BAST, J.: Europäisches Verfassungsrecht: Theoretische und dogmatische Grundzüge. Berlin: Springer-Lehrbuch, 2009, pp. 13–71, specifically at pp. 28–29.

[15] See below the objectives of the Articles 3 and 21 TEU. It is deemed in the literature that the reference to the 'values' is to be understood as something that cannot be reduced to the notion of legal principle, but it maintains an axiological nature, despite the fact that it is found in the text of the Treaty. See BLANKE, H-J. – MANGIAMELI, S. (eds.): The Treaty on European Union (TEU). A Commentary. Wien: Springer, 2013, p. 116, note 26.

[16] The Court's case law offers several examples, e.g. the principles related to the rule of law has been recognized even before the founding treaties made any reference to these principles (e.g. 169/80. Administration des douanes v. Société anonyme Gondrand Frères), or as standard example, the Court's rulings on fundamental rights can be highlighted as well (e.g. 9/74. Casagrande v. Landeshauptstadt München; 44/79. Hauer v. Land Rheinland-Pfalz, 36/75. Rutili v. Ministre de l'intérieur, C-159/90 Society for the Protection of Unborn Children Ireland v. Grogan et a., etc.).

[17] Article 21 (1) TEU: "The Union's action on the international scene shall be guided by the principles which have inspired its own creation, development and enlargement, and which it seeks to advance in the wider world: democracy, the rule of law, the universality and indivisibility of human rights and fundamental freedoms, respect for human dignity, the principles of equality and solidarity, and respect for the principles of the United Nations Charter and international law."

tion to the different listing order, Article 21 (1) TEU does not give emphasis neither to the 'freedom', nor to the 'rights of persons belonging to minorities', however, it highlights a specific aspect of human rights ('universality and indivisibility'), and adds to that 'fundamental freedoms', and makes mention of the 'respect for the principles of the United Nations Charter and international law,' and of 'solidarity' as well (although the solidarity is not a component of the six fundamental values, it is also included into the second sentence of Article 2 TEU).

If we accept the conclusion of the above analysis of the character of values, namely that the principles put the values into legal context, more precisely, in the legal context of the EU external relations, these differences can be well explicable. From this perspective, e.g. the 'freedom' is too abstract category (the degree of its abstraction is much higher, than the democracy, or human rights etc.), therefore it would have been hardly contextualized within the EU external relations. The emphasis of the universal and indivisible characteristics of human rights, or at least its universality, and the reference to the principles of the United Nations Charter and international law might be well explained in the same way, namely by the fact that the values are here incorporated into the dimension of the international relations. Finally, it is also notable, that the formulation of the paragraph implicitly covers the EU's commitment to promote these values towards third countries, as the EU "seeks to advance" these principles in the "wider world."[18] In other terms, these principles (in fact, the inherent values) establish not only a general guiding function to the Union's action, but it requires the EU to share these values with the "wider world," underpinning *e.g.* the human rights conditionality in trade policy *vis-à-vis* the developing countries.[19]

2.3 Objectives

The values and the principles have to be distinguished from the category of '*objectives*.' The Treaty objectives can take various forms, [20] and express aims, goals and intentions of the Union, the Union's institutions or the Member States. Having recourse to analogy, the objectives can be regarded as some sort of supranational *raison d'État* (reasons, objectives of the state). Even though this comparison might not be fully appropriate, the Treaty objectives set the main direction of the Union's actions in a similar way to the reasons of state that also determine the fundamental objectives of a state. Moreover, the Treaty objectives played an important role to define the limits and the content of the Community competences, which was a consequence of the Community model based on a functional integration and the principle of conferral of powers. This function of the objectives was more apparent in the pre-Lisbon era, specifically in the field of the external relations, because the founding treaties did not clarify the division of competences between the European Union and Member

[18] For this reason, this commitment is called 'missionary principle' in the literature, see BROBERG, M.: What is the Direction for the EU's Development Cooperation After Lisbon? In: European Foreign Affairs Review, 2011/4, p. 539.; BROBERG, M.: Don't Mess with the Missionary Man! On the Principle of Coherence, the Missionary Principle and the European Union's Development Policy. In: CARDWELL, P. J. (ed.): EU External Relations Law and Policy in the Post-Lisbon Era. Wien: Springer, 2012, pp. 181–198.

[19] See CREMONA, C.: A Constitutional Basis for Effective External Action? An assessment of the Provisions on EU External Action in the Constitutional Treaty. In: EUI Working Papers no. 2006/30, p. 30.

[20] The Article 2 of TEC (as amended by the Treaty of Nice) referred to the 'tasks' of the Community ("[…] The Community shall have as its task […]"), even though the article implies provisions maintaining nature of objectives or goals. The Article 4 TEC conformed to this assumption, when made a reference back to the previous provision as "[…] purposes set out in Article 2".

States.[21] The Treaty objectives helped the Court shape the borders of the Community's action, i.e. the objective of liberalization constantly provided the basis for justification in the Court's argumentation, when competence conflicts had to be resolved. Therefore, the most important function of the EU Treaty objectives is to give a tool in the interpretation and in removing the gaps in the EU law.[22]

As mentioned above, the relevant objectives of the external relations are set down in two parts of the Treaty. As a part of the general Treaty objectives, Article 3 (5) TEU are underlining a number of objectives, which the European Union "[i]n its relations with the wider world" has to "uphold and promote", or "shall contribute" to. The relevant objectives are as follows:

- upholding and promoting values and interests of the EU;
- protection of the EU citizens;
- peace;
- security;
- the sustainable development of the Earth;
- solidarity and mutual respect among peoples;
- free and fair trade;
- eradication of poverty;
- protection of human rights, in particular the rights of the child;
- the strict observance and the development of international law, including respect for the principles of the United Nations Charter.

The second layer of the objectives is specified in the general provisions of the Union's external actions. According to the Article 21 (2) TEU, the EU "[…] shall define and pursue common policies and actions, and shall work for a high degree of cooperation in all fields of international relations […]" with the purpose of realizing the following objectives:

- safeguard its values, fundamental interests, security, independence, and integrity;
- consolidate and support democracy, the rule of law, human rights and the principles of international law;
- preserve peace, prevent conflicts and strengthen international security, in accordance with the purposes and principles of the United Nations Charter, with the principles of the Helsinki Final Act and with the aims of the Charter of Paris, including those relating to external borders;
- foster the sustainable economic, social and environmental development of developing countries, with the primary aim of eradicating poverty;
- encourage the integration of all countries into the world economy, including through the progressive abolition of restrictions on international trade;
- help develop international measures to preserve and improve the quality of the environment and the sustainable management of global natural resources, in order to ensure sustainable development;

[21] Not only the exclusive competence character of the Common Commercial Policy was disputed, but also the material extent of the trade policy, i.e. how can the Community's competence go beyond the international trade in goods, and involve the regulatory field of services, commercial aspects of IP rights etc.

[22] The functions of the Treaty objectives are systematically analysed by Reimer, distinguishing between meta-legal and legal functions. The first category encompasses the informative function and the function of integration. The components of the second category are the competence extending function, referring function, regulatory function, and the specific role suggesting that that function can be considered as a standard of the Community's activity. REIMER, F.: Ziele und Zuständigkeiten. Die Funktionen der Unionszielbestimmungen. In: Europarecht, 2003/6, pp. 992–1012. For detailed analysis of the Treaty objectives, see MÜLLER-GRAFF, P.-C.: Lissabonner Umwertung oder Kontinuität der EU-Vertragsziele? In: Festschrift 50 Jahre ZfRV. 2013, pp. 139–153.

– assist populations, countries, and regions confronting natural or man-made disasters;
– promote an international system based on stronger multilateral cooperation and good global governance.

Even if this listing is not new – for the most part, they are rooted in previous Treaty provisions[23] –, it is significant, that these objectives are aiming to determine and influence horizontally the specific fields of external relations, including the CCP. Even a quick reading of the objectives listed in these Articles uncovers more overlapping components, not only within the objectives, but in relation to the principles as well. Due to its complexity, the deep analysis of all objectives is unrealizable within the framework of this paper, [24] however, it is questionable, how these objectives do relate to the external trade policy, more specifically how it may imply the objective of liberalization of the CCP, since both Article 3 (5) and Article 21 (2) TEU refer to objectives, which can shape the content and interpretation of liberalization objective of the CCP.

2.4 Consistency requirement

The question is still to be answered, how the principles and objectives of general and specific levels are relating to each other. Earlier, the possible conflict between the trade-related objectives and general objectives could be resolved by the specificity of the trade policy, i.e. the goals of the CCP, as *lex specialis*, was deemed to prevail over the general objectives of the Community.[25] Later, the Single European Act introduced a requirement for coherence and consistency within the external Community policies, stipulating that "the external policies of the EC and the policies agreed in European Political Cooperation must be consistent." Moreover it has referred also to the institutional aspect of consistency, as stated that "the Presidency and the Commission, each within its own sphere of competence, shall have special responsibility for ensuring that such consistency is sought and maintained."[26]

The Treaty of Lisbon applied the same method and added the consistency requirement to the unified structure of external objectives and principles, ensuring the consistency of general and specific, trade-related principles and objectives. The consistency requirement is reinforced by institutional cooperation as well, obliging the key players of external action: the Council and the Commission, assisted by the High Representative for Foreign Affairs and Security Policy, who have to cooperate in order to ensure this consistency.[27] The consistency requirement is still handled more

[23] See the former Article 11 TEU Paragraph 1 (as amended by the Treaty of Nice), and specifically, Articles 131, 174, and 177 in the TEC.

[24] See detailed commentary for the principles: GRABITZ, E. and others (eds.): Das Recht der Europäischen Union. Art. 21 TEU. München: C.H. Beck, 2011; BLANKE, H-J. – MANGIAMELI, S.: The Treaty on European Union (TEU). A Commentary, pp. 831–910.

[25] In context with the pre-Lisbon structure of founding treaties, Basedow made reference to the principle of *lex specialis derogat legi generali*: BASEDOW, J.: Zielkonflikte und Zielhierarchien im Vertrag über die Europäische Gemeinschaft. In: Due and others (eds.): Festschrift für Ulrich Everling. Baden-Baden: Nomos, 1995, p. 51. Contrary to this view, the TEU commentary of Blanke – Mangiameli highlights the equal status of the Treaties after Lisbon pursuant to Article 1 TEU, consequently, neither the rule of *lex superior derogat legi inferiori* nor *the rule of lex posterior derogat legi priori* may apply. See BLANKE, H-J. – MANGIAMELI, S.: The Treaty on European Union (TEU). A Commentary, p. 87.

[26] Single European Act (OJ L 169, 29. 6.1987), Article 30 (5). Similarly, the preamble of the SEA gave emphasis to the consistency: "Aware of the responsibility incumbent upon Europe to aim at speaking ever increasingly with one voice and to act with consistency and solidarity in order more effectively to protect its common interests and independence […]" Single European Act, preamble, fifth recital.

[27] Article 21 (3) TEU: "[…] The Union shall ensure consistency between the different areas of its external action and be-

clearly on the level of the CCP (and other external policies laid down in the TFEU), because the provisions of Article 21 TEU on consistency is repeated in Article 205 TFEU.[28] In addition, the reference to the principles and objectives of Union's external action is stressed – unnecessarily again – in Article 207 TFEU.[29]

According to the grammatical and systematic interpretation of these provisions it is plausible that the inherent principles and objectives of CCP governed by free trade ideas are not strictly subordinate to the general principles of external relations, but the EU trade policy should be 'guided' by the principles and objectives of general level. In other terms, the EU, at least, has to take into account these concepts, which encompass a sort of non-economic and non-trade factors.[30] In the subsequent chapter, the inclusion of the human rights is highlighted within a short analysis.

3 PROMOTING VALUES IN THIRD COUNTRIES – THE EXAMPLE OF THE HUMAN RIGHTS

Originally the external trade and development policy of the European Community was predominantly driven by economic and commercial factors. The trade and human rights nexus in these external policies has become palpable in the 1970s, and particularly the 'Uganda-crisis' brought the human rights conditionality to the Community's trade agenda.[31] Uganda was contracting party of the Lomé Convention concluded by the Community with African, Caribbean and Pacific group of states with the purpose of laying down the framework of trading relations and providing supporting to these countries. In line with the Stabex system covered by this agreement, Uganda was provided supports of different art (concessions, trade incentives, humanitarian support etc.). However, this support has been suspended in the year of 1977 as a response to the human right violations committed by the governing regime, which came to power by a military coup d'etat in 1971. The suspension was initiated by the European Parliament,[32] which political initiative was later accepted by the European Commission, reinforced by a Council Declaration.[33] The Council Declaration – called also as 'Uganda Guidelines' – made evident the basic layout of the conditional policy, namely, no support or concession could be provided to a country, when the supports could help the ruling governments to maintain their power including the suppression and human right violations against their population. From technical point of view, the Declaration has not ceased the Lomé Convention vis-á-vis Uganda,

tween these and its other policies. The Council and the Commission, assisted by the High Representative of the Union for Foreign Affairs and Security Policy, shall ensure that consistency and shall cooperate to that effect."

28 Cf. with Article 205 TFEU.

29 Article 207 TFEU paragraph 2: „The Common Commercial Policy shall be conducted in the context of the principles and objectives of the Union's external action."

30 Tietje regards that as 'politisation' of the CCP and makes some critics on that, see TIETJE, C.: Die Außenwirtschaftsverfassung der EU nach dem Vertrag von Lissabon. Beitrage zum Internationalen Wirtschaftsrecht, p. 20.

31 See BARTELS, L.: The Trade and Development Policy of the European Union. In: European Journal of International Law, 2007/4, p. 737.

32 ARTS, K.: Integrating Human Rights into Development Cooperation: The Case of the Lomé Convention. Hague: Martinus Nijhoff Publishers, 2000, p. 322.

33 Council Declaration on the situation in Uganda (21 June 1977) Bulletin of the European Communities, 6-1977. para 2.2.59.

but the application of the Convention has resulted in a de facto suspension concerning Uganda.[34] In other terms, the Uganda affaire introduced the policy of the human rights conditionality in the field of the EC external trade and development policy and clearly manifested that the EC was committed to include the human rights into its external trade relations.

This policy later influenced also the content and conclusion of agreements in this field. Even the third Lomé Convention referred to human rights as principles,[35] and the first human rights clause was integrated in the fourth Lomé Convention concluded with the ACP countries in 1989. The formulation of the human rights clause has been shaped later, and the Commission made efforts to include these clauses as standard elements into the EC agreements. In doing so, the Commission adopted a communication in 1991[36] that led to a Council decision, which stressed the importance of the application of human rights clauses in this field.[37] Following the Council decision, the EC/EU has always put in the negotiation agenda several types of agreements, including development, association, or partnership agreements and applied the clauses in more 'style forms' (e.g. ‚Baltic Clauses', ‚Bulgarian Clauses' etc.). After 1995, the EU attempted to standardise the rules to be integrated as 'essential elements clause.' This standardisation did not mean totally uniform contents, since the negotiations was conducted always in a tailor-made approach, however the clauses applied had common features and standard elements. Principally, the clause is based on positive incentives (e.g. trade preferences) coupled with general objectives, e.g. cooperation, dialogue and transparency, good governance etc., and at the same way, is linked to negative consequences in case of breach or non-fulfilment of the requirements laid down and specified separately (non-execution clause). The clause itself is composed of four main elements:

- emphasising the importance of respect of human rights, democratic principles etc.;
- it usually cites important relevant international law, sources, documents, conventions to be taken into consideration;
- stating how the agreement underpins inner and international policies;
- and finally, the clause stressed out that it constitutes an essential element of the treaty.

In addition to the essential elements clause, the non-execution clause can be regarded as guarantee of the human rights requirements, describing the possible consequences of the breach of these essential parts of the agreements. The EU has been always a dominant promoter of the inclusion of social policy concerns into the external trade policy, which approach has been continued subsequently. After adopting the Global Europe Strategy in 2006,[38] the European Commission is intending to conclude new generation of free trade agreements with emerging markets, which go already beyond the 'classic' free trade agreements, including not only rule of law and human rights clauses, but also environmental objectives, and sustainable development. Moreover, it is worth noting, however, that this inclusive approach of the EU is not only a part of the policy agenda towards

34 ARTS, K.: Integrating Human Rights into Development Cooperation: The Case of the Lomé Convention, p. 323.

35 Ibid., p. 329.

36 Human Rights, Democracy and Development Cooperation Policy. Commission Communication to the Council and Parliament. SEC(91) 61 final. 25 March 1991.

37 Resolution of the Council and of the Member States meeting in the Council on human rights, democracy and development. 28 November 1991. Bulletin of the European Communities, 11 1991. para. 122-3

38 The strategy emphasised, that the new free trade agreements concluded by the EU, should include "new co-operative provisions relating to labour standards and environmental protection." These combined clauses are standard component in the FTAs today. See Global Europe – Competing in the world. A contribution to the EUs Growth and Job Strategy, COM (2006) 567., p. 12.

the developing countries. Even the recent trade and investment partnership agreements, such as 'mega-regionals' (e.g. CETA or TTIP), aim at integrating several non-trade concerns including the principles of human rights into the body of the agreements.

3 CONCLUSION

Since the Treaty of Lisbon introduced the unified concept of EU external action, the above mentioned concerns should be integrated into the agreements concluded by the EU with third countries, which can have implications on the third countries' legal order as well. This process of Europeanisation and specific approach can signalise that the Walter Hallstein's concept on Community of Law ("*Rechtsgemeinschaft*") is even developing, and also a Community of Values ("*Wertegemeinschaft*") is emerging and has become the centre of action of the European Union external action. However, as the above analysis has shown, the values and other relevant constitutional concepts are forming a colourful set of categories, which are sometimes of contrasting nature. In other terms, if several principles and objectives are incorporated in a systematic order, the question concerning the potential conflicts between the different areas, principles and objectives might always arise. This issue is specifically relevant now, because the Treaty of Lisbon has inserted several principles and objectives which could be hardly reconciled with the logic of the trade policy and principally with the objective of liberalisation. Therefore, conflict or tensions can be expected in the relation of trade and non-trade concerns, e.g. in issues of the above examined trade and human rights, trade and environment, trade and labour rights and social policy concerns, etc. It is notable, from this perspective, that these topics have significance not only at the level of the European Union, but also in the field of international trade law, namely within the World Trade Organization. The core argument of the debate behind these potential tensions focuses on the fact that the abolition of trade barriers may not have only beneficial impacts. However, the harmful implications caused by the liberalisation most often come up not in the field of trade but areas of other social dimensions can be negatively affected. Therefore, it is highly important to put the values incorporating social policy concerns into the external trade agenda of the European Union.

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Contact information:

Dr. Balazs Horvathy PhD
horvathy.balazs@tk.mta.hu
HAS Centre for Social Sciences Institute for Legal Studies
H-1014 Budapest
Orszaghaz utca 30.
Hungary

DOES THE GRANTED ACCESS TO THE COURT AUTOMATICALLY GUARANTEE THE CITIZEN THE ACCESS TO JUSTICE?

Michal Mrva – Michal Krajčovič
Comenius University in Bratislava, Faculty of Law

Abstract: The authors examine the content of the terms *access to the court* and *access to justice*. These terms can be considered identical in a system based on the material rule of law (material legal state), that respects its principles. Social reality, sometimes, however, proves the opposite. The successfulness of ensuring (guaranteeing) the *access to justice* is determined, first and foremost, by the quality of the personal substrate of the judicial authorities – mainly judges themselves. The authors identify which personal characteristics are crucial in this regard. These include the judge´s level of professionalism (due professional care), moral integrity and communication competence. In order to consider the judicial decision-making process as the process (procedure) leading to justice, all of these requirements must be met at the same time.

Key words: justice, court, Bangalore principles

Motto
Licet hoc iure contingat, tamen aequitas doctat.
Although it is happening according to the law, after all it requires politeness (justice).

Domitius Ulpianus[1]

1 THE ACCESS TO THE COURT IN COMPARISON WITH THE ACCESS TO JUSTICE

Access to justice is by most people (therefore not just by lawyers or academics) automatically associated with the *access to the court*. But does one´s right for the access to the court (art. no. 46 (1) of the Constitution of the Slovak Republic, further as „Constitution") simultaneously guarantee the *access to justice*? If not, what requirements have to be met in order to consider these terms equal?

The successfulness of ensuring equality of the terms *access to the court* and *access to justice* is dependent on different requirements. In a system based on the rule of law (in theory) the mathematical symbol „ = " may be put between these terms. The reason is the fact that justice is a function of the law (legal system)[2] and basic value as well, therefore the judge is legitimately expected to seek its fulfilment in the courtroom. When considering the contrary social reality in many cases, one should strengthen the desire and will to fulfil the principle of legal state and not abandon the belief in achieving it.

[1] D.15,1,32,pr. REBRO, K.: Latinské právnické výrazy a výroky. Bratislava: OBZOR, 1984, p. 20 and 156.
[2] Supreme Administrative Court of the Czech republic, judgement 2 Afs/107/2007 of 23 January 2008.

One must, however, take into account that the judge is a human being, thus naturally tempted to usurp the power and misuse it in order to satisfy a private interest at the expense of the interest of the general public. The judge (through his personal qualities) must therefore provide a guarantee, that the civil society will not remain disappointed in its trust in legal, legitimate and fair exercise of power by the state.[3] Interpretation of law (legal texts) within the process of its application performed in breach of the requirement of professional diligence[4] often leads to an unjust ruling. Although supported by sophisticated legal argumentation, an unfair decision cannot be convincing and capable of fulfilling the principle of legal certainty in the eyes of the general public.[5] A ruling arbitrary or circumventing the law thus cannot be considered to be the result of the exercise of one´s right for a fair trial (*access to justice*), although the *access to the court*, a public body acting on behalf of the state, was maintained.

The authors perceive the *access to the court* solely in terms of ensuring access to a judicial authority (public body), that will perform the subsumption of the factual findings in a certain case under the legal norm and afterwards set an authoritative discourse in a particular legal relationship or answer the raised legal question. On the other hand, *access to justice* is determined **by the qualitative aspect of the process of application of law** which is performed by the courts in the name of the state. The quality level of this legal procedure is mainly determined by the reflection of legal principles in the decision-making process, because otherwise the court´s approach to law is formalistic, that is extremely unjust. Legal principles fulfil the reception function, fixing the societal values in the legal order in order to provide legal protection for these moral standards.[6]

One can afterwards accept and identify with the conclusion of J. Wintr, that the constitutional system of values, in a state based on the rule of law, must be taken into account during the interpretation of any legal norm.[7]

A firmly established guarantee of fairness and high standard of the decision-making process can be found (not only) in the advanced legal culture of the European continent. This guarantee is widely recognized as one of the most fundamental principles of constitutional orders of states belonging to this legal culture, that naturally falls within the material core of the their constitution.[8] The mentioned principle is the *principle of the independence of the judiciary*, which includes coexisting guarantees of judicial independence (in organizational and functional terms[9]) and guarantees of independence of the judges themselves, acting on behalf of the judicial branch of state power.

Therefore the *access to justice* relies, first and foremost, on quality of the personal substrate of the judicial authorities represented mainly by judges themselves. The judge is an irreplaceable part of

[3] This fact was known throughout the history. For instance, in the Gortyn law code, considered to be the oldest legislative text in Europe, the judge (*dekastas*) had to rule in accordance with justice and the main guarantees of the fairness of his rulings were his moral characteristics. VASILAKIS, A.: The Great Inscription of the law code of Gortyn. Heraklion: MYSTIS, 2007, pp. 78-79.

[4] Professional diligence can be perceived as the standard of special skill and care which the judge may reasonably be expected to exercise towards the subjects of the proceedings.

[5] One can take into account the words of the Roman lawyer and theoretician Iulius Paulus „*In fraudem legis, facit, qui salvis verbis legis sententiameius circumvenit*" - REBRO, K.: Latinské právnické výrazy a výroky. Bratislava: OBZOR, 1984, p. 131.

[6] The legal principle is (should be) an normative expression of a certain value. Afterwards the value is the explicit appellation of good and every value can be used for the purposes of forming a legal principle. MELZER, F.: Metodologie nalézání práva. Úvod do právní argumentace. 2nd ed. Praha: C. H. Beck, 2011, p. 53.

[7] WINTR, J.: Metody a zásady interpretace práva. Praha: Auditorium, 2013, p. 136.

[8] The argument whether the material core is explicit or implicit is, however, not relevant.

[9] Or static and dynamic point of view.

the judiciary and it is mainly up to his character and professionalism to guarantee, that by granting the access to the court a citizen is automatically and simultaneously granted the access to justice, regardless of the outcome of the proceeding.

2 FULFILLING JUSTICE

A certain consensus can be found both in the legal doctrine[10] and judicial environment regarding the attributes of a judge´s independence. The attributes include his *professional level* (further as „*professionalism*") and *moral integrity*. A righteous judge can only be an independent judge and thus the determinants of a judge´s independence determine the fairness of his rulings and the actions taken. It needs to be pointed out, that rulings and actions taken (not only in exceptional cases) significantly interfere with one´s human rights guaranteed by the constitution.

Nevertheless, justice may be granted only if the judge´s behaviour in the courtroom, his way of communication with the parties of the proceeding (including the reasoning of the decision) and his attitude to any other person interested in the proceeding (e.g. witness) are conducted in a way which does not give rise to any doubts about the person of the judge as an „independent arbiter" trying to ensure justice in the case at hand. In this regard, the existence of the judge´s communication competence, i.e. certain personal skill of the judge consisting in the ability to communicate during the proceedings and by rendering the judgment, is presupposed.

2.1 Professionalism and moral integrity

Under *professionalism* the authors understand the level of judge´s expert knowledge in the field of law, his previous experience, as well as readiness to apply them. The guarantees of expert knowledge of a certain judge are represented by the undertaken professional judicial examination, required master´s degree in law, the selection procedure etc. The appropriate level of expertise is required mainly in the area of the rule of law itself, interpretation of legal norms (advanced legal methodology) and legal reasoning (legal hermeneutics).

As a consequence of meeting all the mandatory requirements, the civil society legitimately presumes, that the application of law procedure will be carried out in accordance with due professional care (professional diligence as already stated). The content of the term professional care can be identified by the conjunction of the meanings of *professional* (adjective) and *care* (noun). *Professional* standardly means related to or connected with a certain profession. Under the term *care* one can generally understand all activities aimed at observing the good condition of something or observing the successful course of something. Due professional care of a judge is therefore the attention paid to the successful course of the judicial proceedings, enabling the judge to deliver a fair ruling as a result of the application of recent scientific knowledge in the field of law. The referred presumption is needed to be materially fulfilled in every single action taken by the judge, as it ensures the European standards of human rights protection, included in various international multilateral agreements.

[10] *Per exempla* ČENTÉŠ, J. et al.: Trestné právo procesné. Všeobecná časť. Šamorín: Heuréka, 2016, p. 88 or DRGONEC, J.: Ochrana ústavnosti Ústavným súdom Slovenskej republiky. Bratislava: EUROKÓDEX, 2010, p. 83.

As a presumed expert in legal methodology, the judge has to decode the idea of the rational legislator[11] standing above the legal norm that is prior to the norm from a comparative perspective from the view point of time. Each legal norm needs to be interpreted[12] with a holistic approach to the legal system, in which the norm is incorporated. Objective law (legal order) cannot be understood solely as a summary of legal norms. Objective law includes both legal norms and the systematic bonds between them, because these internal bonds guarantee that legal order (or the legal state) will not fall into the state of chaos, regardless of its complexity and diversity. When the approach to a certain legal norm differs from the approach previously described, the interpreter (judge) can negate the true will of the legislator standing behind the written text of the norm and depart from the pathway of seeking justice. Teleological interpretation of the applicable legal norms always has to be taken into account before reaching a decision. This obligation is coherent with the model of ideology of legal and rational application of law, that is favoured in the conditions of a material legal state.

It has to be stated in this regard, that one can distinguish two types of cases – an *easy (clear)case* and *hard case*.[13] The *easy cases* are governed by the rules *clara non sunt interpretanda and interpretatio cessat in claris.*[14] The process of interpretation and subsequent application of law executed by the judge is more mechanical (automatic) in comparison with a *hard case*. In a *hard case* the legitimate answer to the question *quid iuris?* relies on the judge´s creative approach to law, perceiving it in its necessary complexity. Textual interpretation of the applicable legal text does not hint the judge the fair decision ought to be rendered. Nevertheless, even a *hard case* must be decided in accordance with the true will of the rational legislator, while preserving the principle banning *denegatio iustitiae*. The judge has to find the fair decision through other methods of interpretation – mostly through teleological and authentic method of interpretation, which enable to unfold the true will of the rational legislation (either the historical legislator or the recent legislator). Mainly teleological interpretation enables the judge to identify, whether a particular decision (which is being considered) would be in accordance or in breach of the basic societal values, incorporated into the legal order in the form of legal principles.

It must be stated, that principles fulfil the rulemaking function as well. The legislator must therefore consider the principles (in relation to one another; proportionally to their importance for certain societal relationships) before formulating the legal norms, before formulating the text of the norm. No matter how strongly we perceive the legislator to be rational, even the legislative body causes errors and thus the legal norm may be contrary to the legal principle (basic societal value). A certain tension between these sources of law naturally occurs and it is up to the interpreter to interpret the norm in the way (in the legal state). When the tension between the applicable law (legal certainty) and basic societal values (e.g. Justice) is of extreme measures, the judge has to decide in accordance with the principles, which find their way into the process of legal interpretation through material-systematic method of interpretation. This method falls both under teleological method of

11 It is a basic assumption of the jurisprudence to consider that the legislator is a rational one.

12 Positive law does not bind interpretation merely to formal legality; rather, the interpretation and application of legal norms are subordinated to their substantive purpose. Law is qualified by respect for the basic values of a democratic society and also measures the application of legal norms by these values. Constitutional Court of the Czech republic, judgement, PL. ÚS 19/93 of 21 December 1993.

13 For doctrinal interpretation of the issue in question see WRÓBLEWSKI, J.: The judicial application of Law. Dordrecht, Boston: Kluwer Academic Publishers, 1992, 357 pgs. or KÜHN, Z.: Aplikace práva ve složitých případech. K úloze právních principů v judikatuře. Praha: Karolinum, 2002, p. 41 ff.

14 The clear does not have to be interpreted and Interpretation ends there, where it is clear.

legal interpretation and systematic method as well. When understood in the second meaning, the legal norm has to be interpreted in the light of *lex superior* - the constitutional order, thus preserving the axiological coherence of the decision-making process with the constitutional system of values (material core of the constitution). Only then may one consider the rendered decision to be legal, legitimate and fair at the same time. These cases are, however, quite rare and need to be addressed with sufficient caution in order to prevent the legal order from destabilization and its substitution by arbitrary and objectively unfair judicial decisions. This model of judicial decision-making therefore requires the justification of the ruling in a hard case by diverse sources of law, including legal principles. This approach is mandatory in order to fulfill the guaranteed right to a fair trial at the constitutional level.[15] However, as mentioned before, when using a principle to optimalize a legal norm, caution is mandatory and advised at the same time by the legal doctrine. Professionalism along with the moral integrity of the judge represent a guarantee for the civil society, that the society will not remain disappointed in its trust in the legal and legitimate exercise of power by a certain judge, acting on behalf of a judicial body and the judicial branch of state power.

The mentioned *moral integrity* is a highly abstract term, ranging to different normative systems (other than law). Even despite the absence of a legal definition, it expresses the close relationship between the law and moral rules (standards), which should optimalize societal behaviour. The highest category of morality is *good*, but it has to be stated that „morality differs from law also in the fact, that it is a kind of internal order, a form of internal felt liability. Its aim is the inner development of a person."[16] A moral imperative can therefore be perceived as a strongly-felt principle, forcing a person to act under certain circumstances in a certain way. The close relation and connection between law and morality is therefore mandatory in order to achieve the voluntary subordination under the authority of law. The meaning of moral integrity can be explained with reference to the meaning of the Latin words: *mores* an *integer.*

Mores expresses a convention (custom) in social behaviour. Synonyms corresponding to the word *integer* include: *whole, entire, complete, pure, correct, honest, just*.[17] One can affirm that a morally mature judge (with moral integrity) disposes with detailed knowledge of moral standards and thus their preservation in personal and professional life is naturally expected.

It can be said from the opposite point of view that a judge with moral integrity is corruption-proof, having a strong character and inner strength. If the highest category of morality is the *good*, this judge must be capable of, be ready and of course willing to exercise and protect it by all for this purpose authorized instruments by the state, under the concept *secundum et intra legem* (art. 2 of the Constitution; principle of legality). Moral and axiological coherence of the exercise of power is mandatory for reaching a high legitimacy rate of a ruling. The eligibility of morality in the legal system was recognized also according to the Roman tradition.[18]

The *good manners* closely relate to this issue, requiring the consideration of the individual and specific circumstances of every single case. The issue of good manners was also discussed by the Constitutional Court of the Czech republic in its ruling II. ÚS 544/2000 of 12 March 2001. The court

[15] Some interesting rulings (from the viewpoint of sources of law used to justify them) were pointed out by *M. Turčan*, e. g. the reference to *The Little Prince* by *Exupéry* in the *obiter dictum* of the ruling of the Constitutional court of Slovak republic, PL. ÚS.13/2012-90 of 19. June 2013. MRVA, M. – TURČAN, M.: Interpretácia a argumentácia v práve. Bratislava: Wolters Kluwer, 2016, pp. 148-151.

[16] OTTOVÁ, E.: *Teória práva*. 3rd ed. Šamorín: HEURÉKA, 2010, p. 24.

[17] WHITE, J.T.: Latin-English Dictionary. For the use of junior students. Boston: GINN AND COMPANY, 1904, p. 302.

[18] One of the most legendary quotes in the legal area is *Ius est ars boni et aequi – the law is the art of the good and fair.*

identified them as ethical and generally recognized principles and their obeying is often ensured under the sanction of the legal norms.[19] Referring to this legal opinion in the ruling I. ÚS 643/04 of 6 September 2005, the court stated that good manners cannot be perceived solely as a set of moral rules used as a corrective for the exercise of subjective rights, but instead as a command for the judge to rule in accordance with equity [...], which in its consequences means the **accession to the path of finding justice**.

Good manners are therefore a mandatory component of the process of legal interpretation and only a morally uncorrupted judge may be prepared to reflect them in the rendered judgements. Their upholding, even at the price of ruling *contra verba legis* although *intra legem*, is in accordance with the true will of a rational legislator. The judiciary doesn´t stand as an enemy towards the legislator, but instead acts as a partner prepared to cooperate in reaching a common goal – upholding the rule of law (material legal state) and the elementary principles it consists of. The reference to them in the *obiter dictum* part of the judgment enables the judicial authority (solely in legitimate cases) to reduce the hardness of law (the rule *dura lex sed lex* will not apply under these circumstances) by applying the rules of politeness.[20]

Even the way of a judge´s private life must simultaneously adhere to the highest moral standards. It has to be stated though, that the judicial function cannot force the judge to regulate his private life in an unlimited way. Proportionality is inherent with the idea of rule of law (legal state) and therefore every requested or prescribed limitation of one´s right has to be reasonable (proportional to the selected aim). The judicial function thus cannot require the judge to live a „clerical" life. Every judge is a human being, making mistakes and however strong the effort, no one can completely adhere to the moral rules of the society throughout his life without a single breach. Excesses in behaviour thus frequently occur and it is up to the judges themselves to determine the seriousness of the act, by which the judge breached the moral norms of the society. The judges form disciplinary senates in order to address these issues whilst protecting the independent status (constitutionally guaranteed) of the judicial branch of state power. Even a slightly immoral behaviour is tolerable under certain circumstances. It is necessary that the excess in behaviour is of non-regular nature and doesn´t objectively interfere with the performance of the judge´s duties, leading to general loss of trust[21] in the eyes of the general public which cannot be recovered.

Moral integrity must always remain closely connected with the judge´s level of expertise in the field of law. Otherwise the material fulfilment of the right to a fair trial would be threatened. This right would then exist solely in a formal way – as a form without its inner content. From the formal sources of law the law would not be transformed to the area of societal relationships – the material sources of law.

2.2 Judge´s communication competence

Even if the judge was a perfect lawyer knowing the law and the methods of its interpretation and also an honest, moral person, it would not be sufficient. In order to guarantee justice, the judge also has to have some skills for conducting the court proceedings. Especially the competence to communicate

[19] Paragraph 10c of the Act no. 233/1995 Coll. – Executor´s Code could serve as an example.

[20] Ruling of the Constitutional Court of the Czech republic I. ÚS 643/04 of 06. September 2005. See also MRVA, M: Dobré mravy v judikatúre *contra legem* s ohľadom na princíp právnej istoty. In: Vybrané aspekty súdneho precedensu v podmienkach Slovenskej republiky. Bratislava: Univerzita Komenského v Bratislave, Právnická fakulta, 2013, pp. 66-79.

[21] Trust in the fairness and legitimacy of the rendered judicial decisions.

with the parties of the dispute and its representatives as well as with other persons interested in the proceedings (e.g. witnesses), both oral (in the proceedings) and written (in the decisions).

To the written communication of the courts in relation to the parties of the dispute the amount of legal literature is devoted, mostly dealing with the problem of proper and persuasive reasoning of the judicial decisions. The courts are obliged to render persuasive decisions, i.e. decisions with premises and conclusions resulting from these premises which are acceptable, rational and deemed as fair by broader juristic (but also laic) public.[22] The decision must contain a brief and clear description of issues of fact, evaluation of performed evidence and consolidation of issues of fact reached by the court. In the reasoning, the court also has to explain why it did not take into consideration certain facts, respectively why it considered these to be irrelevant or not corresponding with the reality. Furthermore, the court has to state the legal qualification of the issue, the procedural defence of the party of the proceedings and reflect also the jurisprudence (if existing). Of course, the necessity to mention the rational consideration leading to the judgment cannot be omitted. From the reasoning, it must be evident why the court decided in the way it did. It is inadmissible that the reasoning contained the solution of personal problems or conflicts between judges or representatives of the parties in the dispute. The decision cannot in any case contain an insult or criticism of the subordinate court or the representatives or even the parties in the dispute. Such a content of the reasoning would be a demonstration of the lack of professionalism of the judge and would also have a negative impact on the persuasiveness of the decision and thus on justice itself.

Equally important is the communicative competence of the judge consisting in the oral communication with the parties in the dispute, their representatives and other persons involved in the proceedings. This competence is realized during the proceedings (or by conducting other judicial actions such preliminary examination, search of premises, etc.). The judge who should be capable of persuading the parties about fairness of the judicial decision and also the proceedings itself has to be able to properly communicate with the parties in the dispute. This skill is demonstrated in the communication which is adequate to the intelligence, age, but also emotional state of the party in the dispute. The judge cannot address the party with disdain regardless of its social statute, education, age, ability to understand the conduct of the proceedings, etc.; if the judge fails in this role, the party has necessarily an impression that it is not impartial. In such a situation no one can persuade the party about the fairness and justice of the decision in the case. Therefore, the judge has to communicate with the parties in the dispute in a clear, rational and tactful manner. It is absolutely inadmissible for the judge to look down on the parties. The judge represents the court in the particular case and has to be therefore authoritative. It does not, however, mean snobby.

Furthermore, the judge must be able to communicate properly also with the representatives of the parties in the dispute. His role is not to solve personal problems with them during the proceedings, he must remain neutral. Nevertheless, it does not mean that he cannot guide them when they behave in an improper or rude manner or when their expression is not relevant.

Last but not least, we cannot omit the importance of the communication of the judge with other persons involved in the proceedings (especially witnesses and authorized experts) who are present in the proceedings only at a certain point. In the communication with them, the judge has to behave in the manner not to raise any doubts about his impartiality and independence, especially towards parties in the dispute. Especially by asking questions, he has to be distant and eliminate suggestive and captious questions and also questions irrelevant to the merit of the case.

22 VRCHA, P.: Odůvodnění civilního rozsudku. 2nd ed. Praha: Leges, 2016, p. 64.

There is no general rule applicable to all persons mentioned above. The judge must be polite and tactful which requires communication competence consisting in the ability to adapt the rules of social intercourse to every individual case, i.e. an adequacy of the judge`s behaviour. The basis of this adequacy must be empathy – the judge should behave to the parties in the dispute, their representatives and other persons involved in the proceedings in the manner he would anticipate in their position in the court's proceedings. Without being tactful and communication competent (both in oral and written communication), we cannot speak about the access to justice. Even the best and most intelligent judge seeking for justice is not capable to render a decision which would be perceived by the parties in the dispute as just when he lacks the communication competence.

2.3 The Bangalore principles of judicial conduct

In the UN Economic and Social Council resolution[23] no. 2006/23: Strengthening Basic Principles of Judicial Conduct of July 27th 2006, the UN has recognized the Bangalore principles as the advancement and amendment of the Basic Principles of the independence of the Judiciary. These are designed to provide guidance to judges and to afford the judiciary a framework for regulating judicial conduct.

The aim of the Bangalore principles[24] of Judicial conduct is to strengthen the judicial integrity. They can be considered as a tool for better understanding and for the support of the role, that the independent judiciary has (plays) in all states declaring the preservation of the rule of law (the concept of legal state in the continental legal system) and its principles. The system of values protected through these principles[25] include the mentioned moral integrity of the judge and his competence and diligence (professionalism). These norms of ethical conduct should moderate the conduct (behaviour) of the judges and provide the necessary direction on the path of meeting them. There are six basic values mentioned in this regard – independence, impartiality, integrity, propriety, equality, competence and diligence. The mentioned values are essential for the judge and, according to the provided legal definition, the term *judge* for the purposes of the *The Bangalore Draft Code of Judicial Conduct 2001(adopted in 2002)* means any person exercising judicial power, however designated.

The integrity along with his professional level (competence and diligence) are considered to be the core of the proper execution of judicial power which has been entrusted to the judges as individuals. Every decision-making process conducted in conformity with the monocratic principle has a sensibly higher demand for the level of moral integrity of the person conducting the process.

The judge´s conduct along with the professional behaviour must reaffirm the faith of the society and its members in the integrity of the judiciary. The way a judge behaves also sensibly affects the opinion that the general public has in relation to judiciary and to the way it performs its role in the declared legal state. Even one misconduct may result in the loss of trust of the general public in the legal and legitimate execution of power by one of its branches – judicial branch of power. The judge should serve as the example of professional and moral behaviour in the civil society, guaranteeing

23 In terms of international law a resolution is considered to be a *soft law* norm, that is legally non-binding, however, it has relevance in legal interpretation - interpretation of the binding legal acts. KALESNÁ, K. – HRUŠKOVIČ, I. – ĎURIŠ, M.: Základy Európskeho práva. Bratislava: Univerzita Komenského v Bratislave, Právnická fakulta, 2008, p. 103.

24 The Bangalore principles of judicial conduct (2002). In: http://www.unodc.org/pdf/crime/corruption/ judicial_group/ Bangalore_principles.pdf

25 The elementary principles can be considered as the reflection (recepcion) of societal values into the normative legal system.

the trust of the society in his office, through which the judge partially fulfils the functions of a state body in a society.

In order to meet the condition of competence and diligence, the judge is required to take reasonable steps to maintain and enhance his knowledge, skills and personal qualities necessary for the proper performance of judicial duties. A requirement of great importance is to keep himself or herself informed about the relevant developments of international law, including international conventions and other instruments establishing human rights norms. That implies the essentiality of human right which are a condition of the legitimacy of the constitutional proclamation of the legal state.

Specifically, the judge is required to maintain order and decorum in all proceedings before the court and to be patient, dignified and courteous in relation to litigants, jurors, witnesses, lawyers and others with whom he or she deals in an official capacity. The judge shall require similar conduct of legal representatives, court staff and others subject to the judge's influence, direction or control. In regard to meeting the set judicial duties the judge is required to meet the conditions of effectiveness, fairness and proportionality of their acquitting in terms of time.[26]

3 CONCLUSION

The identity of the terms *access to the court* and *access to justice* depends on the guarantees of *level of professionalism* along with the level of *moral integrity* of the judge who is setting an authoritative discourse in a certain legal relationship. Only then is the judge capable of approaching the legal system in its necessary complexity and deliver an objectively fair and legitimate ruling. The legitimacy is achieved greatly by the reflection of principles, which represent the societal values fixed in the legal system. Law should serve the people and not the opposite. Therefore, legal actions and rulings should always comply with the system of moral values to the maximum extent. This goal may be achieved only if these are also known to the judge as a person endowed with the trust of the civil society in the fair exercise of power.

It is considered a legitimate expectation of the general public that the public authorities will have an interest in delivering justice to the everyday life of the civil society, thus fulfilling the ideals hidden behind the artistic depiction of the goddess *Iustitia*. These ideals are hidden behind the symbol of the scales, the sword, and tape and the downtrodden snake against the codex.[27]

Justice is the attribute of law and can be considered its core. The rule of law preserves the state of trust in law. If the trust is lost, the distrust is also applicable to the rulings and decision-making activity conducted by the courts.

An unprofessional judge without moral integrity and communication competence is not capable of providing the access to justice in a material way and thus acquire the trust of the general public. To guarantee the access to justice in a judicial proceeding, the highest possible professional and moral standards for the judges are required. The judge does not act only on behalf of the judicial branch of power, but also represents the goddess of *Iustitia* and its symbols in the eyes of the gen-

[26] Thus guaranteeing one´s right for a fair trial. A judge must therefore uphold and exemplify judicial independence in both its individual and institutional aspects (Value 1 Independence).

[27] With reference to the meaning of these symbols the authors refer the reader to the study KRAJČOVIČ, M.: Nezávislosť súdnej moci z pohľadu právneho princípu. In: Justičná revue, 68, 2016, č. 8-9, pp. 829-856.

eral public. For these reason the courts have a special status among all of the public bodies, acting on behalf of the state.

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Contact information:

JUDr. Mgr. Michal Mrva, PhD., LL.M.
michal.mrva@flaw.uniba.sk
Comenius University in Bratislava, Faculty of Law,
Department of Financial Law
Šafárikovo nám. 6
810 00 Bratislava
Slovak Republic

Mgr. Michal Krajčovič
michal.krajcovic@flaw.uniba.sk
Comenius University in Bratislava, Faculty of Law,
Department of Financial Law
Šafárikovo nám. 6
810 00 Bratislava
Slovak Republic

PREVAILING TENDENCIES IN LOCAL SELF-GOVERNANCE: SCOPE OF LOCAL PUBLIC AFFAIRS AND TERRITORIAL TRENDS IN EUROPE

Judit Siket
University of Szeged, Faculty of Law and Political Sciences

Abstract: Focusing on the content of local autonomy, congruent trends could be identified in European countries. Fundamental values of local self-governance prevailing in Europe are included in the European Charter of Local Self-Government. Having regard to the constitutional principle of separation of powers, Charter takes into consideration local self-governments as part of the executive power. Even though the basic principles specify the political and institutional framework of territorial and local administration, the intergovernmental relations also show changing nature. The public administration systems of the Member States of the European Union do not fall within the scope of the EU law, nevertheless, should be analyzed to what extent these processes are influenced by Europeanization progress and what other factors may occur. Remarkable territorial and competence-theory changes were implemented in some States recently, like the Big Society concept in the United Kingdom and the territorial reforms in France.

Key words: local governance, territorial reforms, the scope of local public affairs

1 INTRODUCTION

After World War II some typical trends, a kind of harmonization could be observed in the local self-governance. Research has shown that at least two main sources can be distinguished, on one hand the activity of Council of Europe and on the other hand the implementation of EU policies. The European Charter of Local Self-Government (hereinafter: Charter) serves as a framework for the analysis, nevertheless, the implementation of EU policies, especially the regional policy cannot be ignored either. Having regard to the constitutional principle of separation of powers, Charter takes into consideration local self-governments as part of the executive power. The current paper attempts to review the general European values in the field of local self-governance, and to introduce the key elements of European local self-government models. Even though the basic principles specify the political and institutional framework of territorial and local administration, the intergovernmental relations also show changing nature. Recently, remarkable territorial and competence-theory changes were implemented in some States, like the Big Society concept in the United Kingdom and the territorial reforms in France.

The study attempts to give a comprehensive overview of prevailing tendencies in local self-governance, especially in the constitutional and legal status of local self-government, and in the scope of local public affairs. The paper could be divided into three main sections, the first part aims to

illustrate the decentralization processes in Europe after World War II, and the Europeanization of local self-government; the second unit examines the content of right to self-governance and modelling of local self-governance. The third section refers to the significant reform steps that are taking place in some European countries, such as territorial and theoretical changes in the United Kingdom and in France.

2 DECENTRALIZATION AND EUROPANIZATION IN THE FIELD OF LOCAL SELF-GOVERNANCE

2.1 Decentralization from theoretical aspect and decentralization trends in Europe

Decentralization is a key element of the governance in a modern democratic state, as an important state organizational principle. Two main methods of decentralization are well-known, on one hand the territorial decentralization and on the other hand the functional decentralization. The paper only covers the former form; the functional decentralization as transfer of public administration powers to non-public administration bodies is not the subject of this paper. There are three dimensions of the territorial decentralization: political, administrative and fiscal decentralization. The political decentralization means generally the transfer of decision-making powers and financial resources to local self-government units. The administrative decentralization implies that the local administration gets major, decisive role in local public affairs. The financial decentralization (known as fiscal federalism) is resulting in the transfer of financial resources for regional or local level government bodies that have decision-making power, ensuring efficient and transparent use of these resources.

The concept of decentralization should be distinguished from the concept of devolution. The devolution entails transferring of decision-making authority, whereby the empowered state unit has decision-making power in the field of public affairs. The United Kingdom is an example for the operation of compound state where England, Northern Ireland, Scotland, Wales as independent states have devolved powers, however, not being classified as a federal state.[1]

Decentralization could be identified as the feature of local self-governance. Ilona Pálné Kovács considered decentralization as the measure of democracy.[2] The legal approach to the decentralization was developed also by Hans Kelsen: 'The definition of self-governance includes the incorporated theory of decentralization and democracy, and autonomy... Fighting for self-government can be regarded just as the struggle for democracy'[3] Edward C. Page interpreted the theory of decentralization on the political and legal basis following the thesis of H. Kelsen. Page examined options that are available for the local political elite to shape public services in political and legal aspects in seven nation states in Europe (France, Britain, Italy, Spain, Norway, Denmark and Sweden).[4] Fuhi-

1 See for further details: Wagana, D. M. – Iravo, M. A. – Nzulwa, J. D.: Analysis of the Relationship Between Devolved Governance, Political Decentralization, and Service Delivery: A Critical Review of Literature. In: European Scientific Journal, vol. 11, November 2015, No. 31, p. 457-472.

2 PÁLNÉ, K. I.: A helyi-területi önkormányzati rendszerek. In: Összehasonlító alkotmányjog (szerk. Tóth Judit - Legény Krisztián). Budapest: Complex Kiadó, 2006, p. 282.

3 Kelsen, H.: Az államélet alapvonalai. Prudentia Iuris 7. Miskolc, 1997, Art. 45, par. 70-71.

4 Page, E. C.: Localism and Centralism in Europe. The Political and Legal Bases of Local Self-Government. Oxford: Oxford University Press, 1991, p. 6.

miko Saito, examining the characteristics of democratic decentralization, considered decentralization desirable, especially since the municipalities are able to recognize the needs of the population in the area of public services better.[5] The principle of subsidiarity also appears in this interpretation.

The completion of 'devolution revolution " has been shown by Merilee S. Grindle as a transfer of financial, political, administrative, public service powers which resulted in a radical structural change in the public responsibility and in the field of sharing of autonomy. The new formations of international governance – which are inherent to globalization and decentralization – also help to redefine the role of central government.[6]

In the 1950s and 1960s a strong decentralization process was typical in the Western European States. This process resulted in reorganization of the public tasks of local government in a number of states. Requirement of effectiveness was one of the root causes.

Prevailing local government reforms can be identified in two main streams. On one hand the so called traditional reform steps, and on the other hand the impact of the New Public Management reforms. Traditional reforms aimed primarily at strengthening the political and administrative institution system in the welfare states of the 1960s. The New Public Management reform steps in the 1970s focused on reduction of the role of state, correcting the deficiencies of the welfare state and public administration. Parallel to the welfare state concept expansion, the significance and role of municipal autonomy diminished. However, in the 1970s there were cracks in the foundations of the welfare state. In contrast, the neo-liberalist ideological, political and economic system became dominant. The influence of neo-liberalism can be traced in the state decentralization process. The NPM movement therefore constituted a kind of internal modernization efforts. It can be considered an effect of neo-liberal economics in the field of public administration. The primary objective to increase the efficiency of the redistribution determined public tasks. Regarding the public administration political and administrative reforms (NPM), privatization and deregulation have served as a tool to create market conditions. The penetration of neo-liberalism increased the importance of the public choice for the citizens.

The demand of decentralization, in form of concept of 'Power to the people' heavily logged in the 1970s and 1980s in America and in the late 1980s and early 1990s in Central and Eastern European countries. This effort soon caused that the local policy and accountability have been raised to the level of democratically elected local government. The requirement of decentralization apparently started from the premise that local governments are better able to learn about the needs of the people and act accordingly, since it is much closer to the population than the central government.

After the collapse of soviet-type regime, the most important issue under discussion was the optimal size of local governments. After the financial crisis of 2008/2009 and the following economic recession, local governments in European countries were seriously affected by the consequences of the economic downturn. There were numerous attempts to improve service delivery through rationalization, cooperation of private and public entities. Energy efficiency programs were launched, local economic development programs were implemented.[7]

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5 Saito, F. (ed.): Foundations for Local Governance. Decentralization in ComparativePerspective. Heidelberg: Physica-Verlag, 2008, p. 2-4.

6 GRINDLE, M. S.: Going Local. Decentralization, Democratization, and the Promise of Good Governance. Princeton and Oxford: Princeton University Press, 2007, p. 4.

7 PÉTERI, G.: Decentralization in Eastern Europe: Grab the Moment!, p. 47. Available at: http://www.kozjavak.hu/en/decentralization-eastern-europe-grab-moment

2.2 Decentralization in the practice of international institutions

The importance of local democracy and local autonomy can be seen in the development of localism. The issue of decentralization has high priority within the United Nations Development Organization's policy. It is worth emphasizing that a number of definitions of decentralization is determined in the United Nations Development Program (UNDP). What is common is that the democratic decentralization is essentially linked to the exercise of local public power.[8]

Jesse C. Ribot admitted the following demand: 'Decentralization requires both power transfers and accountable representation. … Decentralization is not about the downsizing or dismantling of central government; rather, it calls for mutually supportive democratic central and local governance.'[9]

The United Cities and Local Governments (UCLG) in close cooperation with the United Nations plays an important role in protecting the interests of local governments.[10] The nature of decentralization was defined as follows in a report of 2008: 'The local self-government is a component of decentralization. [...] It presumes the free exercise of power and establishing organizations within the framework of law; the extent of freedom could prevail widely in different fields, but the idea itself is not affected.'[11]

Finally, the International Association of Local Authorities (IULA) adopted a Declaration in 1993, the essential elements and the principles of local governance being summarized as follows. 'Article 2: Concept of local self-government 1. Local self-government denotes the right and the duty of local authorities to regulate and manage public affairs under their own responsibility and in the interests of the local population. 2. This right shall be exercised by individuals and representative bodies freely elected on a periodical basis by equal, universal suffrage, and their chief executives shall be so elected or shall be appointed with the participation of the elected body.'[12]

2.3 The principle of subsidiarity

Parallel to the application of the decentralization – being related to the state organizational principles – it is necessary to examine the interpretation possibilities of subsidiarity principle. It means generally that decisions should be taken at the closest level to the citizen, in compliance to requirements of efficiency. The United Nations Centre for Human Settlements gave the following definition of the principle of subsidiarity: 'The principle of subsidiarity constitutes the rationale underlying to the process of decentralization. According to that principle, public responsibilities should be exercised by those elected authorities, which are closest to the citizens.'[13] In April 2007 the Governing Council issued a guideline for further development of the European Charter of Local Self-

8 See for further details: Decentralization: A Sampling of Definitions (Working paper prepared in connection with the Joint UNDP-Government of Germany evaluation of the UNDP role in decentralization and local governance) October 1999. Available at: http://web.undp.org/evaluation/evaluations/documents/decentralization_working_report.PDF

9 RIBOT, J. C.: Democratic Decentralization of Natural Resources: Institutionalizing Popular Participation.. Washington DC: World Resources Institute, 2002, p. 1-2. Available at: http://pdf.wri.org/ddnr_full_revised.pdf 1-2.

10 KOVÁCS, L.: Helyi önkormányzatok hálózatainak szerepe a globális kormányzásban. In: Tér és Társadalom, 24. évf. 2010/1, p. 106-107.

11 United Cities and Local Governments (UCLG). Decentralisation and local democracy in the world. First UCLG World Report. Barcelona: UCLG, 2008.

12 IULA World Wide Declaration of Local Self-Government. Adopted by the IULA Council, Toronto, June 1993. Available at: http://www.bunken.nga.gr.jp/siryousitu/eturansitu/charter/iula_decl_txt.html

13 UN-Habitat. UN-Habitat Guidelines on Decentralisation and Strengthening of Local Self-government, 2007, p. 4.

Government regarding the relationships between local authorities and citizens and participatory democracy, in Nairobi.

Encouragement of the decentralization process has outstanding importance in activity of the Council of Europe aimed at protection of the fundamental values of local democracy, which is naturally linked with the strengthening of forms of regional governance. In this area, European Charter of Regional Self-Government[14] was drafted in. The Regional Charter defined at regional, and sub-regional level the fundamental values, but it did not receive adequate support from Member States and therefore its provisions are not binding. The so-called 'Helsinki principles' were then adopted in 2002.[15] The Congress of Council of Europe approved the European Charter for Regional Democracy in 2008, on the basic values of the dominant regional democracy, which served as the basis of the Regional Framework of Reference for Democracy, adopted in 2009. The Framework arranges the principles of the regional organizational structures, their powers and resources. It defines their role within the state organization system, and their relationship to other authorities, as well as to citizen.

2.4 Europeanization

The process of decentralization, the transfer of specified tasks from the central government level to the lower level bodies, and the regional policy of the European Community and later of the European Union are in a close relationship. The regionalization process, strengthening the sub-national government structures, determining the framework of regional policy, and strong expansion of development funds have resulted in strengthening of regional territorial units as a kind of attempt to modernize the political system in the 1990s.[16]

Harmonization of EU law, as well as regional and cohesion policy implementation at local level have resulted in Europeanization of municipalities in the European integration process. Local self-governments have become part of the EU's multi-level system of government in the sense that local governments can influence the shaping of EU policies. Naturally the intensity of this process varies from state to state.

As a result of the decentralization process in Europe, the role of local self-government has changed significantly in the exercise of public power. As an assessment of European decentralization processes it is worth recalling the review of Committee (2013) that summarizes the role of local and regional authorities in EU policies. The Committee expressed its confidence that "... the effective decentralization of subsidiarity, proportionality and multilevel governance should rest on the principles," and that "the principle of subsidiarity is a political-legal crucial driving force of decentralization".

Although a single definition of Europeanization has not been established, its terminology commonly refers to the impact of European integration as the process of creating the EU's polity and the corresponding adaptation of activities and institutions within the Member States. Europeanization

[14] Draft European Charter of Regional Self-Government. Available at: http://groups.csail.mit.edu/mac/users/rauch/misc/regions/charter_self_government.html

[15] Helsinki Ministerial Conference : Declaration (2002) 19 December 2008. Available at: https://wcd.coe.int/ViewDoc.jsp?p=&id=1390053&Site=DG1-CDLR&BackColorInternet=B9BDEE&BackColorIntranet=FFCD4F&BackColorLogged=FFC679&direct=true

[16] SOÓS, E.: A regionalizmus hatása az állami szuverenitásra. In: A 21. század eleji államiság kérdőjelei. (szerk.: Hervainé Szabó Gyöngyvér). Székesfehérvár: Kodolányi János Főiskola, 2015, p. 261-276.

encompasses a range of different meanings within the academic literature. The most common usage includes processes such as changes in policies, practice and preferences within cities; bottom-up mobilisation, meaning the transfer of innovative urban practices to the supranational arena; horizontal processes of Europeanization for local authorities, which involve cooperation and the exchange of best practice and innovations through transnational networks; and organisational adaptation within the administrative structures of local authorities.[17]

The public administration systems of the Member States of European Union do not fall within the scope of the EU law, nevertheless, it should be analysed to what extent are these processes influenced by Europeanization progress and what other factors may influence these. The European Union in general considers the structure and functioning of public administration as a national internal affair. Nevertheless, public administrations of the Member States undergo a strong Europeanization and convergence process, since the implementation of European public policies depends mainly on the performance of national administrations, including local self-governments.

The impact of globalization itself influences the form and content of government. The deepening of European integration can be interpreted as a kind of response to this trend. Multilevel governance could result in lesser significance of government at national level and higher importance for the regional and local level. As a consequence of this process, national sovereignty issues can be arising. Currently, European integration and economic globalization have a powerful influence on the functions of local government and their democratic legitimacy.

3 RIGHT AND ABILITY TO SELF-GOVERNMENT AND EUROPEAN REGIMES

3.1 The scope of the European Charter of Local Self-Government

Council of Europe's aim is not to harmonize the various national laws through the adoption of common rules, but rather it lays down and specifies the fundamental principles and values, and promotes their adoption both in law and in practice. The Council of Europe is one of the most important defenders of human rights and of the institutions of democracy in the world. The activity of the Council has significant importance in the field of local democracy and local self-governance.

The basic document of local self-government's core values is the Charter of Local Self-Government which was adopted under the auspices of the Congress and was opened for signature on 15 October 1985. At present, all Member States are parties to the Charter. The Charter is the first binding international convention to reach a minimum level of legal coherence in Europe and to ensure rights for local communities and their elected local self-governing bodies.

In the focus of the Charter is the right and ability of self-governance to regulate and manage a substantial share of public affairs under their own responsibility and in the interests of the local population within the limits of the law.[18] The core values of the local democracy like decentralization and subsidiarity are also in the scope of the Charter.

[17] GUDERJAN, M.: Local Government and European integration – beyond Europeanisation? Political Perspectives 2012, vol. 6 (1), p. 107. Available at: http://www.politicalperspectives.org.uk/wp-content/uploads/PP_final-article6_Europeanisation-or-integration-of-local-government1.pdf

[18] European Charter of Local Self-Government, Art. 3. par. 1.

3.2 Systematization of local self-government regimes

As regards the practice, in this subsection the systematization of local self-government regimes can be examined.

Analysis of the European local self-government models cannot be uprooted from the socio-historical embedded circumstances. The standardization could be based on special constitutional rules for local authorities, the position among the state organizations, the definition of tasks and responsibilities, as well as the internal structure of local governments.[19]

István Hoffman distinguished two classic models in pursuance of the interpretation of local self-government – following the arrangement of M. Tamás Horvath – on one hand the local self-government and local administration. In addition, a third one, the so-called interactive model was also proposed by them. The interactive model includes the social relationship between local governments and local citizens.

On the basis of the examination of the constitutional position of local government, the British model and the United States model based on ultra vires principle can be distinguished. The ultra vires principle of a single administration was introduced since the 1990s in several states outside the Anglo-Saxon legal culture as well - Ukraine, Moldova, Armenia, Georgia, etc. The other large group of countries is based on general clause, general competences. These states represent differentiated responsibilities and powers in the field of local public affairs. Subgroups can be formed within this groups, where strong state control and influence prevails or the broad legal protection of self-government is guaranteed by the central government. Examples of the former subgroup are France and Italy, as well as Romania and Russia. The latter one includes the Federal Republic of Germany, Poland and Czech Republic.[20]

In determining models of local self-governments, another distinguishing – into a monistic and a dualistic model – is also possible.

The monistic management model is based on the uniformity of the tasks carried out by local governments. In the dualistic model, in contrast, the municipal tasks and administrative tasks delegated by the State are separated.[21]

These models more or less exist either in a pure form, or overlapping coincidences can occur.

4 NEW THEORETICAL APPROACH IN THE UNITED KINGDOM AND REGIONAL REFORM MEASURES IN FRANCE

4.1 The Big Society concept

In the United Kingdom, the Big Society concept is in the forefront of the government policy. The focus of the concept is on local communities and is designed to provide them stronger powers and

[19] See for further details: Hoffman, I.: Gondolatok a 21. századi önkormányzati jog fontosabb intézményeiről és modelljeiről. A nyugati demokráciák és Magyarország szabályozásainak, valamint azok változásainak tükrében. Budapest: Eötvös Kiadó, Eötvös Loránd Tudományegyetem, 2015.

[20] Ibid., p. 78-95.

[21] Ibid.

more opportunities, as well as to create a new generation of community organizations, charities which are able to take part in supplying public service tasks.

There is a radical devolution of powers, which is directed from the central government towards local communities. This devolution process is accompanied by greater economic autonomy for local governments, as well as by enforcement of the principle of general authorization.[22] In accordance with these efforts a Bill has been submitted in 2011, which resulted in substantial changes in the functions of local government and in greater freedom for local authorities and communities. The Local Government Act of 2011 includes a provision on general power of local government, the community, to bring any infringement to the courts, and the possibility of obtaining community assets. In sum, the ultra vires system has been replaced by a limited general clause model. New rules were also introduced: a referendum on the local tax, when excessive taxes are imposed by the local government, as well as new regulation of referenda held in other cases. A new general empowerment clause has been fixed: the local government can do anything what an individual can do, in general.[23]

4.2 The French regional reforms

The central public power has been dominant in the French public sector in which centralization has significant effects, while the administrative decentralization prevails since the 19th century. Territorial organization of the French administrative system currently includes all forms of decentralized and de-concentrated administrative and territorial bodies. The municipalities are based on the principle of general competence in the field of local governance, which demonstrates local interests, with wide administrative powers.

The essential feature in France is the association system of local authorities. Now, the aim is to reduce the number of associations in order to foster efficiency.

Nowadays decisive reform processes have taken place in the French local government system.[24] The local government system is basically influenced by the Act of 2015 on territorial subdivisions which redefined the local and regional authorities' powers and reshaped the French regional system. Substantial measure of the Act was to reduce the number of regions - from 22 to 13 – as of 1 January 2016. The Act aims to support regional level governance, and to strengthen the economic decision-making skills and capacities that are not within the competence of the state. The new regional competences will include the economic development and business promotion, regional planning, organizing transport, training, employment and public employment. In addition, the culture, sports and tourism will be shared competencies with the regions. The legal changes will fully come into force by 2017.[25]

22 Building the Big Society.

23 Localism Bill 2010-11, Localism Act 2011, 15th November 2011.

24 See for further details: BALÁZS, I.: A francia helyi önkormányzati rendszer átalakulása napjainkban. Állam- és Jogtudomány LVII. évfolyam 2016. 2. Szám, p.16-39.

25 France Approves a Territorial Reform. Available at: http://www.regionsunies-fogar.org/en/media-files/107-france-approves-a-territorial-reform

5 CONCLUSION

After World War II, in the Western European countries first decentralization efforts in the field of local governments appeared, while, on the other hand, the New Public Management-induced tendencies appeared as well. Summarizing the dominant prevailing tendencies in the field of local self-government, we can conclude that decentralization, requirement of subsidiarity and the Europeanization of municipalities cannot be clearly separated. Since the local self-government units are – inter alia – the executive bodies of the European common policies, a kind of Europeanization process can be recognized. As result, the role of local governments has become stronger.

Finally, we can conclude that the European Charter of Local Self-Government, as an internationally binding convention of the Council of Europe, has a general impact on the local self-government system, while on its basis different models can be created. Secondly, the field of local self-governance is not a part of EU legal agenda, but a lot of common features can be identified among EU Member States.

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Contact information:

dr. Judit Siket
Siket.Judit@juris.u-szeged.hu
University of Szeged, Faculty of Law and Political Sciences
54. Tisza Lajos bld.
6720 Szeged
Hungary

HARMONIZING POTENTIAL OF EQUITY-BASED CROWDFUNDING REGULATION

Jan Mazur
Comenius University in Bratislava, Faculty of Law

Abstract: Equity-based crowdfunding shows promising potential for funding the micro, small and medium sized enterprises. So far, only several countries have adopted a specific regulation of crowdfunding, while there is no crowdfunding-specific regulation (harmonization) on the EU level. As we already observe diverging tendencies of the crowdfunding market and its regulation in respective member states, there seems to be an untapped potential of harmonizing certain aspects of capital markets law, such as Prospectus Directive. We will assess the needs of the crowdfunding market and reflect them against the Prospectus Directive and its implementation in selected member states. The assessment serves as a basis for discussion on harmonization potential.

Key words: crowdfunding, harmonization, capital markets

1 INTRODUCTION

The article aims to describe the main barriers and obstacles to proliferation of equity-based crowdfunding for small and medium enterprises (SMEs) in relation to the Prospectus Directive. As was acknowledged repeatedly by the EU, SMEs play a crucial role in European economy.[1] However their access to finance remains limited mostly to banking finance and self-finance. Innovative means of finance, such as crowdfunding, appear to offer another viable conduit for securing finance, especially for micro and small SMEs. Yet the capital markets regulation currently presents a significant barrier to mainstream crowdfunding takeoff, especially crowdinvesting, since the regulation has not been adopted to regulate crowdinvesting at the first place. On-going academic endeavors continue to map regulatory implications of the EU capital markets regulation on crowdfunding market and its further development. The ambition of this article is to contribute to this debate and provide ideas on harmonization potential of prospectus requirements.

The structure of the article is the following. We start with the describing the importance and financing of SMEs based on the cumulated academic and other knowledge and evidence. Second, we introduce the basic definitions, elements and taxonomy of crowdfunding with a special focus on the equity-based crowdfunding. Finally, we sum up the identified barriers and obstacles of equity-based crowdfunding.

[1] See: EUROPEAN COMMISSION: Communication From The Commission An action plan to improve access to finance for SMEs /* COM/2011/0870 final */, or EUROPEAN COMMISSION: Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions - "Think Small First" - A "Small Business Act" for Europe {SEC(2008) 2101} {SEC(2008) 2102} /* COM/2008/0394 final */.

2 EQUITY-BASED CROWDFUNDING AND SMES

2.1 Financing SMEs

It has long been established that SMEs play a crucial role in economy[2]. SMEs constitute 99,8% of all businesses in non-financial business sector of the EU; they employed almost 90 million employees in 2014 (67% of total employment). SMEs also contributed significantly to the employment growth - 71,4% of the increase in employment in the non-financial sector in 2014 is attributed to SMEs. Moreover, in 2014 micro SMEs accounted for 29,2% of total employment, whereas small SMEs for 20,4% and medium SMEs for 17,3% of total employment respectively.[3]

SMEs are considered the main drive behind the job creation; they are the main vehicles for the creation and dissemination of innovation and are crucial in achieving development objectives.[4] Moreover, SMEs tend to have strong capacity for exploiting strong synergies. However, SMEs also face specific factors that inhibit their development and growth, such as limited access to finance, poor managerial skills, lack of training opportunities, or high input costs. Many of these factors could be attributed to the limited access to finance in general. These factors are even more exaggerated when it comes to microenterprises, which also face the following challenges: (i) low net profits limiting their ability to self-finance growth; (ii) weak financial structures; or (iii) lack of relationships with the banking system limiting their access to the (only) viable source of finance.[5] EC DG Growth and ECB's joint 2014 survey of financing conditions faced by SMEs further states the six major problems faced by SMEs (self-reported): (i) finding customers; (ii) competition; (iii) access to finance (though having improving tendency); (iv) costs of production or labor; (v) availability of skilled staff or experienced managers; and (vi) regulation.[6]

2.2 Crowdfunding

In general, crowdfunding usually refers to an open call to the public to raise funds for a specific project.[7] It is a promising way of financing various civic projects and endeavors, scientific projects, politics, creative industries, but also SMEs, micro and small enterprises in particular.[8] A very broad

2 An SME (micro, small and medium-sized enterprises) is defined along two thresholds: (i) fewer than 250 employees, and (ii) an annual turnover not exceeding 50 million EUR, and/or an annual balance sheet total not exceeding 43 million EUR. EUROPEAN COMMISSION: Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises (Text with EEA relevance) (notified under document number C(2003) 1422). OJ L 124, 20.5.2003, p. 36–41.

3 MULLER, P. – CALIANDRO, C. – GAGLIARDI, D. – MARZOCCHI, C.: Annual report on European SMEs 2014/2015. Brussels: European Commission, 2015, p. 4-8.

4 EDWARDS T. – DELBRIDGE R. – MUNDAY, M.: Understanding innovation in small and medium-sized enterprises: a process manifest. In: Technovation, 2005, 25, 10, pp. 1119–1127.

5 The section is drawn from: PES, G. N. – PORRETTA, P.: Microfinance, EU Structural Funds and Capacity Building for Managing Authorities. A Comparative Analysis of European Convergence Regions. Houndmills: Palgrave Macmillan, 2015, p. 11-23.

6 Available at: <https://www.ecb.europa.eu/stats/money/surveys/sme/html/index.en.html>.

7 EUROPEAN COMMISSION: Communication From The Commission To The European Parliament, The Council, The European Economic And Social Committee And The Committee Of The Regions Unleashing the potential of Crowdfunding in the European Union /* COM/2014/0172 final */.

8 See for instance: civic and non-profit projects, Generosity.com, creative industries, Kickstarter.com, art, Arthena.com, politics, Crowdpac.com, scientific projects, SMEs, Seedrs.com, Symbid.com.

approach to crowdfunding allows us to understand crowdfunding as enabled by the internet/web 2.0.[9] Specifically, the internet enabled huge amounts of people to participate on creative processes of others, get engaged with creators and support them financially while maintaining very low transaction costs for the participants. ESMA defines crowdfunding as "a means of raising finance for projects from 'the crowd' often by means of an internet-based platform through which project owners 'pitch' their idea to potential backers, who are typically not professional investors".[10]

Crowdfunding has developed into many forms: from pure donation-based, through more elaborate reward-based, to complex investment-based crowdfunding. Donation-based crowdfunding represents one of the earliest forms of crowdfunding, which allows a large number of people donate money for a certain cause or project without receiving anything (material) in return. On the other hand, reward-based crowdfunding offers an opportunity to finance a production or project in return for a material reward, typically a product, work of art, or service. Finally, investment-based crowdfunding usually takes four forms: (i) crowdlending (peer-to-peer lending), (ii) equity-based crowdfunding, (iii) profit-sharing crowdfunding, and (iv) invoice trading crowdfunding. Naturally, the regulatory requirements will be most manifested in the investment-based crowdfunding, which creates a more complex legal relationship between project owners and backers.

The volume of crowdfunding market has been increasing for the past years since its inception.[11] The total global crowdfunding volume is estimated at 34 billion USD in 2015, whereas peer-to-peer lending amounted to 25 billion USD, reward- and donation-based crowdfunding to 5,5 billion USD and equity-based crowdfunding to 2,5 billion USD. The EU crowdfunding market shows significant volumes as well, yet its volumes are still considered below its full potential: (i) equity-based crowdfunding amounted to over 422 million EUR of raised capital with average campaign of over 0,5 million EUR raised funds, performed on 60 EU-based platforms via 836 campaigns, and (ii) peer-to-peer loans amounted to over 3,2 billion EUR with an average campaign of 15.688 EUR raised funds, performed on 77 EU-based platforms via 204.575 campaigns.[12] The crowdfunding market is expected to continue to grow exponentially for several years and eventually become a significant, yet complimentary source of finance to traditional sources.[13]

2.3 Regulatory issues

In relation to the above mentioned definitions of crowdfunding, academia understands the terms as "a collective effort by people who network and pool their money together, usually via the internet, in order to invest in and support efforts initiated by other people or organization"[14], or as a " pooling

[9] For history of crowdfunding see: FREEDMAN, D. M. – NUTTING, M. R.: A Brief History of Crowdfunding. Including Rewards, Donation, Debt, and Equity Platforms in the USA. 2015. Available at: <http://www.freedman-chicago.com/ec4i/History-of-Crowdfunding.pdf>

[10] ESMA. „Opinion. Investment-based crowdfunding. ESMA/2014/1378." 2014.

[11] See: <http://crowdexpert.com/crowdfunding-industry-statistics/>

[12] EUROPEAN COMMISSION: Commission Staff Working Document: Crowdfunding in the EU Capital Markets Union, Brussels, SWD(2016) 154 final, p. 10.

[13] Although, peer-to-peer lending appears to have more disruptive potential on traditional sources of finance, especially on non-bankable market segments.

[14] ORDANINI, A. – MICELI, L. – PIZZETTI, M. – PARASURAMAN, A.: Crowd-funding. Transforming customers into investors through innovative service platforms. In: Journal of Service Management, 2015, 22, 4, pp. 443–470. DOI 10.1108/09564231111155079.

money from a group of people, typically comprised of very small individual contribution, to support another's effort to accomplish a specific goal".[15] Hence we can draw certain common features of crowdfunding, which will be relevant for regulatory implications:

- backers are usually a large amount of rather unprofessional people/investors (in contrast with professional investors on capital markets);
- the internet platform provides the third party intermediary service (transaction management) and infrastructure (marketplace) in return for a fee;
- in crowdinvesting, further exercise of rights is required: voting rights, distribution of gains/profits/interests;
- in crowdinvesting, campaigns are of rather low volume in contrast with traditional capital market typically in 100.000s EUR up to several million;
- project owners raising funds are normally unlisted, micro and small SMEs, startups.

Usual business setup of crowdfunding involves three main actors:[16] (i) project owners or creators who propose, market and run their projects; under crowdinvesting, this actor typically issues an instrument (e.g. security); (ii) funders or investors (also known as backers) who fund or invest into projects or companies; and (iii) crowdfunding platforms, which are virtual spaces for creators and funders to exchange resources, and provide transaction and post-transaction services.[17] Crowdfunding platforms typically operate as intermediaries in return for a share on raised funds. This setup may be prone to certain conflicts of interest and moral hazard, where a platform may advertise a project, which lacks the quality, without performing due diligence, because it is motivated by the fees it charges. Moreover, crowdfunding may be prone to frauds, especially when platforms either fail to perform quality due diligence, or do not perform any as their policy. The unprofessional character of backers/investors typically translates into the lack of investment skills, manifested in behaviors, such as failure to perform basic investor's diligence, failure to understand and assess multiple and typically high risks attached to the investment, failure to diversify portfolio, or even improper use of leverage.[18] Also, as any human behavior, crowdfunding is prone to herding behavior of backers and investors.[19]

The main regulatory issues related to crowdfunding are clustered around the information asymmetry and herding behavior. In fact, the ambition of regulator in regulating crowdfunding may be understood as finding the right balance between encouraging crowdfunding investments to fulfill its potential while maintaining investors' protection. As of now, it is generally understood that there are no known systemic regulatory issues related to crowdfunding, unlike to the capital markets and banking industries.

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15 GRIFFIN, Z.: Crowdfunding. Fleecing the American masses. In: Case Western Reserve Journal of Law, Technology & the Internet, 2012. Available at: <http://ssrn.com/abstract=2030001>.

16 DE BUYSERE, K. – GAJDA, O. – KLEVERLAAN, R. – MAROM, D.: A Framework for European Crowdfunding, 2012.

17 AGRAWAL, A. – CATALINI, C. – GOLDFARB, A.: Entrepreneurial Finance and the Flat-World Hypothesis. Evidence from Crowd-Funding Entrepreneurs in the Arts, 2010. Working papers.

18 Risks are in general higher in investment-based crowdfunding forms and typically involve risk of capital loss, risk of dilution, inability to liquidate an investment, late or no share on profit/dividend payments, limited access to information, limited access to execute voting rights, etc. Some risks are exemplified by ESMA. „Opinion. Investment-based crowdfunding. ESMA/2014/1378." 2014.

19 For a wider discussion on when crowds fail and when they succeed see: SUNSTEIN, C. R. – HASTIE, R.: Wiser: Getting Beyond Groupthink to Make Groups Smarter. N.p.: Harvard Business Review, 2014.

2.4 Barriers and obstacles

Drawing from above, we may sum up the barriers and obstacles inhibiting the growth-enabling regulatory setup of crowdfunding as following. First, it is understood that there is still no commonly accepted taxonomy of crowdfunding, which is a result of the fact that crowdfunding is a relatively new phenomenon and the academic and policy knowledge is still being established. There is no common EU-wide and EU-based approach to regulation of crowdfunding. This fact is rather insignificant in donation- and reward-based crowdfunding markets, but becomes significant in investment-based crowdfunding market. As a result, certain forms of crowdinvesting cannot benefit from the single passport rule established by the MiFID.[20] Moreover, regulatory minimum may be beneficial in order to create confidence towards the new industry and level playing field for the market participants. There is also lack of information sharing and data gathering on respective forms of crowdfunding, which disallows structured action by policy makers.[21]

In general it can be argued, along with ESMA, that "EU financial services rules were not designed with the industry in mind."[22] Contemporary regulation of crowdfunding appears to be a regulatory by-product, rather than a structured regulatory and policy response. Unclear regulatory implications and interpretations lead to different level playing fields within the EU. ESMA mentions among the key components of appropriate regulatory response the following features:

- proportional capital requirements or similar mechanisms for safeguarding operational continuity. This point is also very dependent on the operational business models of respective platforms;
- a mechanism to make sure that investment opportunities are proposed to appropriate investors;
- a mechanism of proper risk informing and warning;
- proper segregation of the client assets;
- mechanisms to identify and mitigate conflicts of interest;
- certainty about the nature and extent of the platform's duties towards clients.

It is worth mentioning that there are regulatory issues not related directly to crowdinvesting platforms, but to project owners or companies that market their projects on these platforms. The main issues are related to various corporate law regimes that inhibit or strengthen their crowdinvesting options, but also to higher costs attached to transparency requirements in relation to the Prospectus Directive.

2.5 Prospectus regimes and harmonizing potential

Crowdfunding is positioned among the policy areas, where the European Commission is active in terms of sharing good policies and best practices. Also, ESMA states that "while risks to investors could be mitigated by action at national level, such action will not address the scalability issues."[23] Moreover, as is evidenced by the EC Communication 49% of the respondents called on the EU to

20 EUROPEAN COMMISSION: Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC (further as „MiFID").

21 EUROPEAN COMMISSION: Commission Staff Working Document: Crowdfunding in the EU Capital Markets Union, Brussels, SWD(2016) 154 final. 6.

22 ESMA. „Opinion. Investment-based crowdfunding. ESMA/2014/1378." 2014, p. 4.

23 ESMA. „Opinion. Investment-based crowdfunding. ESMA/2014/1378." 2014, p. 5.

promote the single market for financial return crowdfunding and 51% saw a need for EU action to secure a proper investor protection for crowdinvesting.[24]

Harmonizing potential exists on various issues mentioned above. We focus on the potential for further harmonization of the Prospectus Directive 2003/71/EC[25]. PD puts forward requirements of prospectus publication before the offer of securities to the public is made or the admission to trading on regulated markets takes place. PD article 1(1) "harmonizes requirements for the drawing up, approval and distribution of the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market." Whereas the obligation to publish a prospectus is an important element of the EU capital markets and the EU regime offers passporting benefits, it may be related to relatively huge costs on the account of especially smaller SMEs.

First of all, it is important to take into account that PD applies on transferable securities as defined by MiFID. Second, the PD establishes two import thresholds:

- article 1(2)h: securities included in an offer where the total consideration for the offer in the EU is less than 5 million EUR, calculated over a period of 12 months, are outside of the scope of the PD;
- article 3(2)e: offers a total consideration below 100.000 EUR, calculated over a period of 12 months, are excluded from the obligation to publish a prospectus;
- that implies that Member States are free to regulate the obligation to publish a prospectus of offers where the total consideration is between 100.000 EUR and 5 million EUR (over 12 months) at their own discretion.

Third, the PD article 3(2) constitutes certain exemptions from the obligation to publish a prospectus, such as: (i) an offer is addressed only to 'qualified investors' (under MiFID); (ii) an offer is addressed to fewer than 150 natural or legal persons per Member State other than 'qualified investors', (iii) an offer of securities of minimum 100.000 EUR per each investor; and (iv) an offer of securities worth at least 100.000 EUR per security.

If we take into consideration the typical operational and business models of crowdinvesting platforms, i.e. mainly the equity-based crowdfunding, we see that the following features are relevant and typical for crowdinvesting:

- as was mentioned above, typical funds raised range between 100.000s EUR to several million EUR;
- typical investors are unprofessional clients;
- typical investors invest up to several thousands EUR, way below 100.000/investor or security;
- crowdinvesting opportunities often take form of instruments other than MiFID securities/instruments; if platforms opt for MiFID license to obtain single passport rule benefits, they may lose certain market segments as a result.

Disclosure requirements in relation to prospectus of offers below 5 million EUR (and of at least 100.000 EUR) are left to the discretion of respective Member States. In fact, these regimes vary significantly among Member States. In Slovakia, basically the same regime as over 5 million EUR

[24] EUROPEAN COMMISSION: Communication From The Commission To The European Parliament, The Council, The European Economic And Social Committee And The Committee Of The Regions Unleashing the potential of Crowdfunding in the European Union /* COM/2014/0172 final */

[25] Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC (further as „PD").

offers applies, whereas the National Bank of Slovakia has a discretionary power to lower the requirements in individual cases.[26] French regulation is more flexible as it allows for "light-prospectus" to be issued for offers of up to 1 million EUR over 12 months. The light-prospectus is supposed to give simple, clear and balanced information on the specific features of the project and the type of offering, which could be rationally expected as a solid industry standard nonetheless.[27] Similarly, Austria requires a simplified prospectus for offers between 250.000 EUR and 5 million EUR offers.[28] In Spain, a specific crowdfunding regulation limits the size of offers to 2 million EUR per project per platform per year, or 5 million EUR if the offer is directed exclusively to accredited investors. The issuers are not required to publish prospectus in such cases.[29] Several other Member States have put forward custom regulation of the crowdfunding or crowdinvesting with specific rules governing the obligations to publish prospectus. As of now, it is clear that offers between 100.000 EUR and 5 million EUR have varying and incomparable regimes within the EU; in fact 17 Member States require a prospectus below the 5 million EUR threshold.[30]

The Commission's recent initiative for legislative proposal of Prospectus Regulation replacing the PD puts forward an exemption for the smallest capital raisings from the prospectus obligation, "under the premise that imposing an EU-prospectus for offers of securities to the public of a consideration below EUR 500,000 (as is often the case on crowdfunding platforms) is disproportionately costly in relation to the envisaged proceeds of the offer."[31] It is also required that Member States refrain to impose disclosure requirements that would be disproportionate or unnecessary burden in relation to such offers.

The Commission's Impact Assessment based the proposal of increasing the lower limit of 100.000 EUR to 500.000 EUR on the research suggesting that the average fund raising campaign on crowdfunding platforms in the EU was worth around 220.000-250.000 EUR.[32] This finding appears to be obsolete and contradictory to the other sources used by the Commission just recently, stating the average amount at around 500.000 EUR.[33] The Impact Assessment mentions other options that were considered by the Commission as a way of supporting growing crowdfunding market without endangering the consumers' rights, such as increasing the amount of non-qualified investors without triggering the obligation to publish a prospectus. The Commission's approach to regulating the minimum prospectus obligations also takes into consideration the total potential amount of raised

26 Sec. 125h(3) + 125h(4) of the Act no. 566/2001 Col. on Securities and Investment Services as amended.

27 Authorité des Marchés Financiers' instruction on investor information to be provided by the issuer and crowdfunding investment advisers or investment services providers within the framework of a crowdfunding offering (DOC-2014-12). Various AMF decrees, orders, instructions and ordinances regulate this; available at: <http://www.amf-france.org/en_US/Acteurs-et-produits/Prestataires-financiers/Financement-participatif---crowdfunding/Cadre-reglementaire.html>

28 The Alternative Financing Act 114/2015. Available at: <https://www.ris.bka.gv.at/GeltendeFassung.wxe?Abfrage=Bundesnormen&Gesetzesnummer=20009241>

29 Article 68(2) and 83(1)b of the Law 5/2015 of 27 April on Promoting Business Finance. Available at: <https://www.boe.es/buscar/doc.php?id=BOE-A-2015-4607>

30 Proposal for a Regulation Of The European Parliament And Of The Council on the prospectus to be published when securities are offered to the public or admitted to trading. COM/2015/0583 final - 2015/0268 (COD).

31 EUROPEAN COMMISSION: Commission Staff Working Document: Crowdfunding in the EU Capital Markets Union, Brussels, SWD(2016) 154 final. 6.

32 EUROPEAN COMMISSION: Commission Staff Working Document Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading. SWD/2015/0255 final - 2015/0268 (COD).

33 EUROPEAN COMMISSION: Commission Staff Working Document: Crowdfunding in the EU Capital Markets Union, Brussels, SWD(2016) 154 final. 10.

retail money, though not absolutely, since the PD never meant to impose any limits on the amount of individual investors' investments. It is therefore conceivable that even under current PD regime millions of EUR could be fundraised without appropriate disclosure. Most of the Member States' bespoke regulation of crowdfunding takes a different approach and aims at higher 'de minimis' limits combined with relatively low maximum amounts of individual investor's investments (typically in thousands of EUR/campaign). The Commission's proposal is nevertheless a step forward, though it may have been advisable to adopt a more straightforward approach to supporting the harmonization of crowdfunding markets and adopting structural limits on the individual investors' investments while allowing companies to raise funds of up to 1.000.000-2.000.000 EUR without undergoing the prospectus obligation. As of now, it is clear that Member States' discretion does not lead to comparable regimes and therefore the development of the EU-wide crowdfunding market may be hindered as a result.

3 CONCLUSION

In the paper, we briefly discussed the requirements and needs of equity-based crowdfunding. We mentioned several identified barriers that hinder the development of crowdfunding markets, while it is also necessary to account for specific risks related to this novel means of finance, primarily for SMEs. One of the critical points in developing the crowdfunding regulation is to admit that the actual EU capital markets regulation was not prepared with crowdfunding in mind. Therefore the regulation has not yet developed responses suitable for the online, almost frictionless and borderless, phenomenon of crowdfunding. One such example is the obligation to publish a prospectus, which leaves the harmonizing potential for better coherence of crowdfunding markets unmet, in its actual and also revised versions. The discretionary power of states in terms of regulating the offers between 500.000 EUR to 10 million EUR under the new Prospectus Regulation leaves huge room for unpredictability and incompatibility of respective Member States' regimes. It does not encourage the single market in one of its most smooth conduits, natural to crowdfunding: the internet economy.

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Contact information:

Mgr. Ján Mazúr
jan.mazur@flaw.uniba.sk
Comenius University in Bratislava, Faculty of Law,
Department of Financial Law
Šafárikovo nám. 6
810 00 Bratislava
Slovak Republic

(POSSIBLE) IMPACT OF CETA ON CREATION OF LAW[1]

Ondrej Blažo
Comenius University in Bratislava, Faculty of Law

Abstract: The paper brings an analysis, and possible solutions, regarding "threats" to regulatory sovereignty of the parties to the CETA. Hence technical trade barriers, sanitary and phytosanitary measures, regulatory cooperation, liberalization of services and protection of investors are focal points for estimating future development of legal regime in both the EU and Canada. The analysis assesses only "possible" impact of the CETA because it will be subject to ratification and the outcome of this process is insecure.

Key words: CETA, commercial policy, European Union, Canada, investment

1 INTRODUCTION

After civil protests, hesitation of Wallonia, as well as efforts to obtain judicial injunction preventing its signature at Federal Constitutional Court of Germany, the Comprehensive Economic and Trade Agreement (CETA) between the European Union and its member states as a one party and Canada as other party was finally signed in Brussels on 28 October 2016. Major doubts regarding this treaty focused on possible losing regulatory sovereignty of EU's member states, favouring transnational corporations in regulation procedures, and mainly offsetting democratic principles via the dispute-settlement system in state-investor claims. As a partial response for these discussions, the following article will bring an analysis, and possible solutions, regarding aforementioned "threats" to regulatory sovereignty of the parties to the CETA. Hence technical trade barriers, sanitary and phytosanitary measures, regulatory cooperation, liberalization of services and protection of investors are focal points for estimating future development of legal regime in both the EU and Canada. The analysis assesses only "possible" impact of the CETA because it will be subject to ratification and the outcome of this process is insecure.

2 TECHNICAL REGULATORY BARRIERS

Technical regulations can on the one hand constitute obstacles to free movement of goods between states, on the other hand they represent a tool ensuring protection of market of particular state against goods that can be harmful for consumers, infrastructure, can lead to mutual incompatibility of goods sold on a particular market, etc. Therefore, standardization is an effective measure for the effectiveness of market in favour of industry and final consumers, too, but also a tool of open or hidden discrimination or limitation of import.

First of all it must be noted, that the CETA incorporates Agreement on Technical Barriers to Trade (TBT Agreement) that is an annex of WTO Agreement.[2] Being a party of WTO Agreement,

[1] The article was prepared within project VEGA 2/0109/16 Institutional competitiveness in the light of changes of external environment.

[2] CETA, Art. 4.2.

cooperation in technical barriers is *nihil novum sub sole* for the EU and its members, as well as Canada. Basic principles of technical barriers can be read in Art. 2 TBT Agreement:

a) national treatment, i.e. products originated from other country are subject to technical regulations that are not less favourable than those covering domestic products;
b) necessity and legitimacy of regulation, i.e. technical regulations are not prepared, adopted or applied with a view to or with the effect of creating unnecessary obstacles to international trade and shall not be more trade-restrictive than necessary to fulfil a legitimate objective, taking account of the risks non-fulfilment would create; such legitimate objectives are, inter alia: national security requirements; the prevention of deceptive practices; protection of human health or safety, animal or plant life or health, or the environment.
c) time and condition adaptiveness, i.e. technical regulations shall not be maintained if the circumstances or objectives giving rise to their adoption no longer exist or if the changed circumstances or objectives can be addressed in a less trade-restrictive manner.
d) internationalization of standards, i.e. where technical regulations are required and relevant international standards exist or their completion is imminent, they or the relevant parts of them shall be used as a basis for their technical regulations except when such international standards or relevant parts would be an ineffective or inappropriate means for the fulfilment of the legitimate objectives pursued, for instance because of fundamental climatic or geographical factors or fundamental technological problems.

The CETA does not incorporate procedural provisions of the TBT and introduces its own rules of cooperation. Although the parties of the CETA committed themselves to cooperate in areas of standards and technical regulation (Cf regulatory cooperation)[3] , aim to mutual compatibility[4], as well as follow conformity procedures[5], it is obvious that Canada and the EU are allowed to maintain their respective technical regulations. The CETA, hence, does not mean creation of a single market including *Cassis-de-Dijon*-like automatic market-acceptance of goods produced under the regulations of the respective country.

Nevertheless, Canada and the EU committed themselves "to cooperate to the extent possible, to ensure that their technical regulations are compatible with one another", however this legal duty can be hardly considered mandatory harmonization or duty to lower requirements of technical standards. The cooperation and harmonization can be described more as a mutual inspiration than an obligation to find the common denominator.[6] Mutual recognition of standards and mutual acceptance of the results of conformity assessment follow up Agreement on Mutual Recognition between the European Community and Canada of 1998 and it can be noted that it explicitly does not cover the agriculture sector.[7] It is obvious that mutual recognition of accredited conformity assessment bodies does not mean mutual recognition of technical standards.

The CETA does not remove technical standard regulations and does deprive neither Canada nor the EU right to adopt own standard regulation. Standard regulation harmonisation is a global

[3] CETA, Art. 4.3.
[4] CETA, Art. 4.4.
[5] CETA, Art. 4.5.
[6] „... if a Party expresses an interest in developing a technical regulation equivalent or similar in scope to one that exists in or is being prepared by the other Party, that other Party shall, on request, provide to the Party, to the extent practicable, the relevant information, studies and data upon which it has relied in the preparation of its technical regulation, whether adopted or being developed."
[7] CETA, Protocol on the mutual acceptance of the results of conformity assessment, Art. 2(5)e).

process that can be observed within the UN and the WTO and is not a novelty in the EU-Canada relations.

3 SANITARY AND PHYTOSANITARY MEASURES

Similarly to TBT, the CETA complements WTO rules on sanitary and phytosanitary measures and confirm the obligation of the parties under SPS Agreement as annexed to WTO Agreement. Comparing to TBT, the parties committed themselves for mutual recognition of equivalence of SPS measures: "The importing Party shall accept the SPS measure of the exporting Party as equivalent to its own if the exporting Party objectively demonstrates to the importing Party that its measure achieves the importing Party's appropriate level of SPS protection."[8]

However, even this recognition of equivalence does not mean duty of harmonisation of SPS rules and aims merely to recognize existing equivalent measures that can lead to simplification of import formalities.

4 RIGHT TO REGULATE

International trade agreements usually face criticism of offsetting regulatory power of states, binding regulatory stability and limiting democratic institutions in their ability to adapt national regulations in favour of their citizens.[9] There appear suggestions that CETA could open the door to investors' claims against EU states because of employment of sovereign rights to change national regulatory regime. Usually Vattenfall , TransCanada, PhilipMorris or Bilcon cases are referred to as cautionary tales of exuberant demands of multinational corporations victimizing host states.[10] Following issues are the main target of the criticism: investor protection and its legitimate expectation, inability to introduce environmental and labour standards and regulatory cooperation that enable multinational corporations to influence the preparation of regulatory framework in EU-Canada area.

In order to calm these objections Canada and the EU attached to the CETA Joint Interpretative Instrument on the Comprehensive Economic and Trade Agreement (CETA) between Canada and the European Union and its Member States (hereinafter "Joint Interpretative Instrument). Under Joint Interpretative Instrument "CETA preserves the ability of the European Union and its Member States and Canada to adopt and apply their own laws and regulations that regulate economic activity in the public interest, to achieve legitimate public policy objectives such as the protection and promotion of public health, social services, public education, safety, the environment, public morals, social or consumer protection, privacy and data protection and the promotion and protection of cultural diversity." It must be noted that even Joint Interpretative Instrument does not give full liberty in their regulation – their freedom is restricted to "regulation in the public interest" and

8 CETA, Art. 5.6(1).

9 For these objections see e.g. STIGLITZ, J. E.: Regulating Multinational Corporations: Towards Principles of Cross-Border Legal Frameworks in a Globalized World Balancing Rights with Responsibilities. American University International Law Review, vol. 23, issue 3, 2007, p. 451-558.

10 See e.g. CINGOTTI, N. et. al.: Investment Court System put to the test. Amsterdam/Brussels/Berlin/Ottawa, April 2016 [online] https://www.tni.org/files/publication-downloads/investment_court_system_put_to_the_test.pdf

to "achieve public policy objectives". The CETA therefore does not recognize unfettered powers of regulators and aims more at ordo-liberal understanding the tasks of state.

4.1 Investment protection

Investment protection is always a neuralgic point of trade agreement because in the case of diminishing rights of investors, particularly via direct or indirect expropriation, actual or alleged, it can lead to substantial claims against states. The CETA introduced several conceptually brand new safeguards against abusive claims of investors:

First, it manifestly declares right to regulate: "…Parties reaffirm their right to regulate within their territories to achieve legitimate policy objectives, such as the protection of public health, safety, the environment or public morals, social or consumer protection or the promotion and protection of cultural diversity."[11]

Secondly, it is possible to regulate or change regulation to the detriment of investors: "…mere fact that a party regulates, including through a modification to its laws, in a manner which negatively affects an investment or interferes with an investor's expectations, including its expectations of profits."[12]

Thirdly, the parties are in general free in their decision on subsidies: "…a Party's decision not to issue, renew or maintain a subsidy:

(a) in the absence of any specific commitment under law or contract to issue, renew, or maintain that subsidy; or
(b) in accordance with any terms or conditions attached to the issuance, renewal or maintenance of the subsidy,

does not constitute a breach of the provisions of this Section".[13]

Fourthly, it is possible to withdraw subsidy granted against domestic law: "…nothing in this Section shall be construed as preventing a Party from discontinuing the granting of a subsidy or requesting its reimbursement where such measure is necessary in order to comply with international obligations between the Parties or has been ordered by a competent court, administrative tribunal or other competent authority, or requiring that Party to compensate the investor therefor."[14]

Fifthly, the CETA introduces *numerus clausus* list of practices, which constitute breach of the obligation of fair and equitable treatment that can be extended by CETA Joint Committee only:

"…(a) denial of justice in criminal, civil or administrative proceedings;
(b) fundamental breach of due process, including a fundamental breach of transparency, in judicial and administrative proceedings;
(c) manifest arbitrariness;
(d) targeted discrimination on manifestly wrongful grounds, such as gender, race or religious belief;
(e) abusive treatment of investors, such as coercion, duress and harassment;…"[15]

[11] CETA, Art. 8.9(1).
[12] CETA, Art. 8.9(2).
[13] CETA, Art. 8.9(3).
[14] CETA, Art. 8.9(4).
[15] CETA, Art. 8.10(2).

Mere infringement of domestic law does not constitute infringement of fair and equitable treatment per se.[16]

Sixthly, general public policy regulations are excluded from terms of expropriation: "…except in the rare circumstance when the impact of a measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, non-discriminatory measures of a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations."[17]

Along these safeguards included into substantive provisions on investment protection, the CETA parties can influence the decision-making of tribunals deciding on investors' claims via interpretation rulings of the CETA Joint Committee[18] that shall be binding for the tribunal.

From analysed provisions, it is evident that the EU and Canada tried to shrink manoeuvring space for non-legitimate investor claim., However, some notions are still open for further interpretation: "manifest arbitrariness", "fundamental breach of due process", "denial of justice". On the other hand, these concepts are immanent to principles of rule of law and therefore shall be observed in all actions of the actions of the EU and its members and in the case of infringement of these rules, everyone, including investor, deserves a compensation. While due process, non-arbitrariness, right for fair trial are legal requirements for functioning of modern state, link between regulation and legitimate goals, its necessity and proportionality of regulation is a political question of the functioning of state. If citizens in their particular country accept or require policies and regulations that do not follow legitimate public policies, it can be considered out of the protection shell of Art. 8.9 CETA. Nevertheless, a regulation that is not following legitimate goals will still not constitute infringement of investors' rights if it does not fulfil criteria laid down for behaviour that is not fair or equitable or for expropriation.

4.2 Environmental and labour standards

The EU, as well as many European states, describe themselves as social market economies that respect protection of life environment.[19] Hence, standards of protection of workforce and environment are essential for such policy. Gradual changes of labour protection standards and rules for protection of environment can be considered measures offsetting or diminishing investment or profit of a particular investment. Such changes can be sometimes very hard to estimate since they are connected with collective bargaining and technical development.

Protection of workers' rights and environment is two-fold:

First, the CETA confirms regulatory powers of the parties: the right of each Party to set its labour priorities, to establish its levels of labour protection and to adopt or modify its laws and policies accordingly in a manner consistent with its international labour commitments, is recognized.[20] Reference to "international labour commitments" can be considered a limiting factor of changes of labour standard of respective Parties of the CETA. The question is, if the Party can regulate only in a way

16 CETA, Art. 8.10(7).
17 CETA, Annex 8-A, par. 3.
18 CETA, Art. 8.31(2).
19 See e.g. ŠMEJKAL, V.: The Social Market Economy Goal of Article 3(3) TEU – A Task for EU Law? In: Zborník z medzinárodnej vedeckej konferencie Bratislavské právnické fórum 2015, Bratislava: PraF UK, 2015, pp. 1519-1529.
20 CETA, Art. 23.2.

following international agreements, commitments or other instruments or if such provision refers only to non-violation of international commitments requirement. Nevertheless, the CETA creates also a direction for future development of labour law setting minimal standard framework (obligations of the members of the International Labour Organization and the commitments under the ILO Declaration on Fundamental Principles and Rights at Work and its Follow-up of 1998 adopted by the International Labour Conference at its 86th Session)[21].

Similarly, the CETA recognises Parties' the right to "set its environmental priorities, to establish its levels of environmental protection, and to adopt or modify its laws and policies accordingly and in a manner consistent with the multilateral environmental agreements …" and the CETA.[22]

Furthermore, parties of the CETA have the legal obligation to "seek to ensure that those laws and policies provide for and encourage high levels of … protection, and shall strive to continue to improve such laws and policies and their underlying levels of protection" in both areas – labour protection and environmental protection.[23]

Secondly, as a counterpart to the right to regulate in favour of increasing level of protection of workers' rights, the parties of the CETA prevented from decreasing the level of standards in labour and environment protection[24]. Despite the title of Art. 23.4 and 24.5 "Upholding levels of protection parties to the CETA are not obliged to uphold a level of protection of labour and environment in general. The CETA prohibits to "waive or otherwise derogate from, or offer to waive or otherwise derogate from, its …" labour law and standards of environmental law "…, to encourage trade or the establishment, acquisition, expansion or retention of an investment in its territory."[25] Moreover, parties are not only obliged to uphold labour protection and environmental laws but also effectively enforce them. However, again vis-à-vis trade and investment, only ("A Party shall not, through a sustained or recurring course of action or inaction, fail to effectively enforce its labour law and standards to encourage trade or investment", and *mutatis mutandis* environmental laws).[26]

Although the CETA acknowledges the right to introduce environmental laws, the parties shall be cautious in cases when such measures can affect trade between parties. In these cases they are obliged to "take into account relevant scientific and technical information and related international standards, guidelines, or recommendations"[27]. Paraphrasing this provision, parties to CETA cannot introduce environmental law affecting trade if they are not based on scientific and technical information. Precautionary measures aimed to prevent environmental degradation can escape from this obligation: "where there are threats of serious or irreversible damage, the lack of full scientific certainty shall not be used as a reason for postponing cost-effective measures to prevent environmental degradation".[28]

21 For the list of these requirements see CETA, Art. 23.3.
22 CETA, Art, 24.3.
23 CETA, Art, 23. and Art. 24.3.
24 CETA, Art. 23.4 and Art 24.5.
25 CETA, Art. 23.4(2) and Art. 24.5(2).
26 CETA, Art. 23.4(3) and Art. 24.5(3).
27 CETA, Art. 24.8(1).
28 CETA, Art. 24.8(2).

5 REGULATORY COOPERATION

Chapter twenty-one of the CETA introduces framework of regulatory cooperation and prudently the right to regulate is confirmed[29]. The wording of CETA also confirmed voluntary basis for regulatory cooperation (moreover obligation to "be prepared to explain the reasons for its decision to the other Party"[30] in case of refusal or withdrawal of regulatory cooperation cannot be read as a duty to give legitimate reasons). Due to strict voluntary basis for regulatory cooperation, rules on objectives of cooperation and regulatory cooperation activities[31] do not establish any further obligation for parties. Similarly, under Art. 21.5 CETA, parties can either consider the regulatory measures or initiatives of the other Party on the same or related topics or adopt „different measures or pursuing different initiatives for reasons including different institutional or legislative approaches, circumstances, values or priorities that are particular to that Party."

Specific area of regulatory cooperation (even though it is not included in chapter twenty-one) can be identified in mutual recognition of professional qualifications.[32] Recognition of qualifications is not an obligation under the CETA and party can establish their qualification criteria for particular professions. The recognition is mandatory only if MRA (mutual recognition agreement) is adopted by the Joint Committee on Mutual Recognition of Professional Qualifications ("MRA Committee") in the form of decision and after notification to the MRA Committee by each Party of the fulfilment of its respective internal requirements.[33]

6 ONE-WAY LIBERALIZATION

The CETA requires free market access, national treatment (NT), most-favoured-nation (MFN) treatment in investment,[34] providing services,[35] particularly financial services,[36] as well as removes performance and senior management requirements in investment and senior management requirements in financial services. Parties to the CETA established a vast list (more than 850 pages) annexed to the CETA of reservations regarding this liberalization requirements (Art. 8.15 – Investment, Art. 9.7 – Services, Art. 13.10 – Financial Services). Derogation from liberalization is not permanent and changes can be performed in one way. Exemption from free market access, NT and MFN applies due to

(a) an existing non-conforming measure that is maintained by a Party;
(b) the continuation or prompt renewal of a non-conforming measure;
(c) an amendment to a non-conforming measure to the extent that the amendment does not decrease the conformity of the measure, as it existed immediately before the amendment.

29 CETA, Art. 21.2.
30 CETA, ART. 21.2(7).
31 CETA, Art. 21.3 and Art. 21.4.
32 CETA, Chapter eleven.
33 CETA, Art. 11.3(6).
34 Art. 8.4 for market access, Art. 8.6 for NT, Art. 8.7 for MFN.
35 Art. 9.6 for market access, Art. 9.3 for NT, Art. 9.5 for MFN.
36 Art. 13.6 for market access, Art. 13.3 for NT, Art. 13.4 for MFN.

Henceforth the Party liberalizes sector or service, it cannot later renew restrictive measure in the future, even though it was existent at the date of force of CETA and included into reservations (only prompt renewal is allowed). Similarly, the Party cannot renew previous intensity of restrictive measure if it once raises compatibility with liberalization requirements.

In the case of domestic regulation on licensing requirements, licensing procedure, qualification procedure and requirements (chapter twelve) is liberalization pressure even stronger – derogation from application of CETA rules is applicable on existing rules only.[37]

7 CONCLUSIONS

Influence of the CETA on domestic regulation, offsetting regulatory powers, impossibility to introduce and enforce labour protection and environmental protection laws are one of the major objections against the CETA. The CETA itself as well as the EU and Canada via Joint Interpretative Instrument were very prudent to stress acknowledgement of untouched right to regulate. This regulatory autonomy vis-à-vis "threats" of investors' claims was also supported by *numerus clausus* list of practices that constitute behaviour that cannot be considered fair and equitable. On the other hand, regulatory autonomy of states is restricted to legitimate purposes. The power to regulate and impossibility to challenge regulation by investors is particularly evident from rules dealing with labour protection and standards and environmental law. It must be noted, however, if environmental law affects the trade between parties, they must be supported by outcomes of scientific and technical information what can, from the one side point of view, protect from unfettered arbitrariness, from the other point of view, can make every environmental regulation questionable.

The CETA does not contain "hard law" rules of mandatory harmonisation and it opens door for mechanisms for voluntary convergence, only, via regulatory cooperation. However, incentives for convergence of law in the fields of TBT, SPS and recognition of professional qualification can stem more from stakeholders than from legal obligations laid down in the CETA.

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Contact information:

JUDr. Ing. Ondrej Blažo, PhD.
ondrej.blazo@flaw.uniba.sk
Univerzita Komenského v Bratislave, Právnická fakulta
Šafárikovo nám. 6
810 00 Bratislava
Slovak Republic

[37] CETA, Art. 12.2(3).

MULTINATIONAL TAX AVOIDANCE VS. EUROPEAN COMMISSION[1]

Kristína Považanová, Hana Kováčiková
Comenius University in Bratislava, Faculty of Law

Abstract: This paper deals with recent actions of the Commission with respect to EU State Aid rules. The Commission is looking at the compliance with EU State Aid rules of certain tax practices in some Member States in the context of aggressive tax planning by multinationals, with a view to ensure a level playing field. A number of multinational companies are using tax planning strategies to reduce their global tax burden, by taking advantage of the technicalities of tax systems, and substantially reducing their tax liabilities. This aggressive tax planning practice erodes the tax bases of Member States, which are already financially constrained.

Key words: the Commission, State Aid, tax planning, tax ruling, investigation

1 EU COMPETITION LEGAL FRAMEWORK

In order to ensure fair competition, functioning market and competitive economy with the common market, the European Union (hereinafter "EU") developed the competition policy. Competition puts businesses under constant pressure to offer the best possible range of goods at the best possible prices, because if they don't, consumers have the choice to buy elsewhere. In a free market, business should be a competitive game with consumers as the beneficiaries.

Sometimes companies try to limit competition in order to gain the advantages compared to their competitors. To preserve well-functioning product markets, authorities like the European Commission (hereinafter "Commission") or national competition authorities (hereinafter "NCA") must prevent or correct anti-competitive behaviour. To achieve this, based on the powers granted by the EU legislation, the Commission monitors agreements between companies that restrict competition[2] – agreements between undertakings, decisions by associations of undertakings and concerted practices in which companies agree to avoid competing with each other and try to set their own rules; abuse of a dominant position[3] – where a major player tries to squeeze competitors out of the market; mergers[4] (and other formal agreements whereby companies join forces permanently or temporarily) – legitimate provided they expand markets and benefit consumers, as well as efforts to open markets up to competition (liberalisation) – in areas such as transport, energy, postal services and telecommunications. Many of these sectors used to be controlled by state-run monopolies and it is essential to ensure that liberalisation is done in a way that does not give an unfair advantage to these old monopolies. Moreover, the

1 Tento príspevok vznikol za podpory Agentúry na podporu výskumu a vývoja, Grantu č. APVV-0158- 2 (Efektívnosť právnej úpravy ochrany hospodárskej súťaže v kontexte jej aplikácie v praxi). This paper was supported by the Grant APVV-0158- 2 The Effectiveness of Competition Law in the Context of its Application in Praxis.

2 Article 101 TFEU.

3 Article 102 TFEU.

4 Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings.

Commission monitors financial support (State Aid) for companies from national governments and cooperation with national competition authorities in EU countries (who are also responsible for enforcing aspects of EU competition law) – to ensure that EU competition law is applied in the same way across the EU.[5]

Given the topic of this paper, the text will only focus on the application of EU State Aid rules. According to Article 107 (1) Treaty on the Functioning of the European Union (hereinafter "TFEU"): "*Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.*"[6] Based on the above mentioned, it can be concluded that prohibited State Aid exists, if four cumulative conditions are fulfilled: Firstly, the measure confers an advantage on its recipients which relieves them from charges that are normally borne from their budget. Secondly, the advantage is granted by the state or through state resources by national public authorities. Thirdly, the measure affects competition and trade between Member States. Last but not least, the advantage conferred is specific or selective in that it favours certain undertakings or the production of certain goods.[7]

2 DEVELOPMENT OF APPLICATION OF THE PROHIBITION OF STATE AID IN TAX MATTERS

Application of EU State Aid rules should serve a double purpose, and thus preventing waste of public resources via inefficient subsidies, therefore helping Member States to manage their budgets more wisely[8] and preventing the crowding out of efficient private investments[9] by preserving competitive and open internal market.[10] As of 1998 the Commission applies the prohibition of State Aid to tax reliefs, which is accompanied by an extensive campaign, aiming to gain the support of Member States.[11] The campaign itself focuses on the use of "soft law" instruments such as notices, communications and other non-binding documents that depict the application of EU State Aid prohibition to direct business taxation as being required in order to promote good governance, tackle harmful tax competition, combat avoidance of taxation. The following text will provide brief overview of key milestones of this effort:

The Code of Conduct for business taxation was set out in the conclusions of the Council of Economics and Finance Ministers (ECOFIN) of 1 December 1997. The Code is not a legally binding instrument but it clearly does have political force. By adopting this Code of Conduct, the Member States have undertaken to roll back existing tax measures that constitute harmful tax competition and

5 http://ec.europa.eu/competition/consumers/what_en.html (online; accessed 1/11/2016).

6 Article 107 (1) Treaty on the Functioning of the European Union.

7 LANG, M. – PISTONE, P. – SCHUCH, J. – STARINGER, C.: Introduction to European Tax Law on Direct Taxation. 4th edition. Vienna: Linde Verlag GmbH, 2016, p. 97.

8 ALMUNIA, J.: The State Aid Modernization Initiative. Brussels. 7 June 2012 (Speech/12/424), p. 8

9 Ibid., p. 3

10 Communication from the Commission and the Committee of the Regions – EU State Aid Modernisation (SAM), Brussel. 8 May 2012, COM (2012) 209 final, para. 5

11 LANG, M. – PISTONE, P. – SCHUCH, J. – STARINGER, C.: Introduction to European Tax Law on Direct Taxation, p. 98.

refrain from introducing any such measures in the future ("standstill").[12] The Council, when adopting the Code of Conduct, acknowledged the positive effects of fair competition, which can indeed be beneficial. Mindful of this, the Code of Conduct was specifically designed to detect only such measures which unduly affect the location of business activity in the EU by being targeted merely at non-residents and by providing them with a more favourable tax treatment than that which is generally available in the Member State concerned. For the purpose of identifying such harmful measures the Code of Conduct sets out the criteria against which any potentially harmful measures are to be tested.[13] The Code of Conduct has also anticipated the establishment of a group to assess tax measures of Member States that may fall within its scope and to oversee the provision of information on those measures.[14] The Code of Conduct Group (Business Taxation) was established at a Council meeting on 9 March 1998. Since then, the Code of Conduct Group has been monitoring standstill and the implementation of rollback and reported regularly to the Council. Currently, the Code of Conduct Group is mainly working on anti-abuse rules, exchange of information and transparency in the area of transfer pricing, administrative practices and promotion of its rules in third countries (non-EU countries).[15]

On the occasion of adoption of the Code of Conduct, the Commission undertook to draw up guidelines on the application of Articles 92 and 93 of the EC Treaty (Article 107 and 108 TFEU) to measures relating to direct business taxation and committed itself 'to the strict application of the State Aid rules concerned'. Since the Code of Conduct aims to improve transparency in the tax area through a system of information exchanges between Member States and of assessment of any tax measures that may be covered by it, the Commission claimed that for their part, EU State Aid rules will also contribute through their own mechanism to the objective of tackling harmful tax competition. The Commission's undertaking regarding State Aid in the form of tax measures forms part of the wider objective of clarifying and reinforcing the application of the State Aid rules in order to reduce distortions of competition in the single market.[16]

Generally, it has to be concluded that between harmful tax competition as interpreted in the Code of Conduct and the scope of the prohibition on State Aid as implemented to direct business taxation measures there is a gap which is not disputed by the Commission. With respect to the mentioned, the Commission notice on the application of the State Aid rules to measures relating to direct business taxation (hereinafter "Commission Notice") provides: *"The qualification of a tax measure as harmful under the code of conduct does not affect its possible qualification as a State aid. However the assessment of the compatibility of fiscal aid with the common market will have to be made, taking into account, inter alia, the effects of aid that are brought to light in the application of the code of conduct."*[17] According to Kronthaler and Tzubery some decisions of the Court of Justice of the European Union (hereinafter "CJEU") and the Commission[18] can be understood as attempts to bridge the gap between application of prohibition of State Aid in the area of direct taxation and the Code of Conduct.[19]

12 http://ec.europa.eu/taxation_customs/business/company-tax/harmful-tax-competition_en (online; accessed 2/11/2016).

13 http://ec.europa.eu/taxation_customs/business/company-tax/harmful-tax-competition_en (online; accessed 2/11/2016).

14 Code of Conduct, OJ C 2/2 of 6 January 1998, pp. 2-5, para. H.

15 LANG, M. – PISTONE, P. – SCHUCH, J. – STARINGER, C.: Introduction to European Tax Law on Direct Taxation, p. 100.

16 Commission notice on the application of the State aid rules to measures relating to direct business taxation, OJ C 384 od 10 December 1998, pp. 3-9, para. 1-2.

17 Ibid., para. 30.

18 E.g. Case C-143/99 Adria-Wien Pipeline, Joined cases C-106/09 P and C-107/09 P Commission v Gibraltar.

19 LANG, M. – PISTONE, P. – SCHUCH, J. – STARINGER, C.: Introduction to European Tax Law on Direct Taxation,

The further development is connected with the adoption of another "soft law" instrument and thus Communication on promoting good governance in tax matter.[20] Among the measures of existing tax cooperation designed to promote better governance within the EU, the Communication highlights the Code of Conduct and the State Aid prohibition.

Lastly, in the 2014, the affair well known as "Luxembourg Leaks" contributed to the recent development of EU State Aid prohibition in relation to tax matters. Hundreds of tax ruling of the Luxembourg tax authorities were made available for public. According to these rulings, the Luxembourg tax authorities helped multinational companies to avoid payment of taxes in other jurisdictions by granting beneficial tax treatments. According to Commission press releases this could constitute a prohibited State Aid.[21] However, being aware of the sensitivity of the Member Stater to their tax revenues, the Commission chose to depict its actions as an effort to combat corporate tax avoidance that exploits disparities in the tax policies of the Member States.[22]

3 COMMISSION'S INVESTIGATION OF TRANSFER PRICING ARRANGEMENTS ON CORPORATE TAXATION

The Commission's actions in late 2014 confirmed that the application of EU State Aid rules to Member States' tax ruling practices will be a priority for the new Commission. On 20 November 2014, Margrethe Vestager, who replaced Joaquin Almunia as competition commissioner indicated that by the second quarter of 2015 the Commission aims to conclude investigations aimed at four companies: Amazon, Apple, Fiat Finance and Trade, and Starbucks.[23]

On the 11 June 2014, the European Commission opened three in-depth investigations to examine whether decisions by tax authorities in Ireland, the Netherlands and Luxembourg with regard to the corporate income tax to be paid by Apple, Starbucks and Fiat Finance and Trade, comply with the EU rules on State Aid. Moreover, on the 7 October 2014, the Commission has opened an in-depth investigation to examine whether the decision by Luxembourg's tax authorities with regard to the corporate income tax to be paid by Amazon in Luxembourg complies with the EU State Aid rules.[24]

All four cases concern tax rulings dealing with transfer pricing arrangements between entities of the same corporate group, which the Commission believes may involve illegal State Aid.

Former competition commissioner stated in this respect: "In the current context of tight public

p. 101.

20 Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee – Promoting Good Governance in Tax Matters. Brussels. 28 April 2009, COM (2009) 201 final, p. 4.

21 http://europa.eu/rapid/press-release_IP-14-663_sk.htm (online; accessed 2/11/2016).

22 LANG, M. – PISTONE, P. – SCHUCH, J. – STARINGER, C.: Introduction to European Tax Law on Direct Taxation, p. 102.

23 https://www.euractiv.com/section/competition/news/vestager-says-will-use-luxleaks-documents-in-eu-tax-probe/ (online; accessed 3/11/2016).

24 The latest case in this respect concerns McDonald's. On the 3 December 2015, the Commission has opened a formal probe into Luxembourg's tax treatment of McDonald's. Its preliminary view is that a tax ruling granted by Luxembourg may have granted McDonald's an advantageous tax treatment in breach of EU State aid rules, In particular, the Commission would like to assess whether Luxembourg authorities selectively derogated from the provisions of their national tax law and the Luxembourg-US Double Taxation Treaty and thereby gave McDonald's an advantage not available to other companies in a comparable factual and legal situation.

budgets, it is particularly important that large multinationals pay their fair share of taxes. Under the EU State Aid rules, national authorities cannot take measures allowing certain companies to pay less tax than they should if the tax rules of the Member State were applied in a fair and non-discriminatory way."[25]

It has to be highlighted that the Commission has no direct authority over national tax systems. However, it is authorized to investigate whether certain fiscal regimes, including the form of tax rulings, could constitute "unjustifiable" State Aid to companies on a selective basis. As stated in the first part of this paper, the EU State Aid rules are set out in TFEU and constitute part of the TFEU provisions on competition law. Generally, Member States are prohibited from granting financial support in a way that distorts competition, unless measure concerned has been notified to and authorized by the Commission. The prohibition applies to any form of financial aid, including in the form of tax rulings. "Although not problematic in themselves, tax rulings may amount to unlawful State Aid if they provide selective advantages to a specific company or group of companies that are not approved under EU State Aid rules." [26]

Article 108(3) TFEU requires Member States to notify non-exempted State Aid measures, including in the form of tax measures, to the Commission before their implementation, and to await the Commission's approval before implementing such measures (the so-called "standstill obligation").[27] If either of those obligations is not fulfilled, the State aid measure is considered to be unlawful.

Such a notification usually triggers a preliminary investigation by the Commission. The Commission can also investigate unnotified State Aid that has already been granted on its own initiative or following a complaint from the third party. If, following an in-depth investigation, the Commission finds that a measure constitutes unjustified State Aid, the Commission requires the Member State to recover the financial support from the beneficiary (unless such recovery would be contrary to a general principle of EU law). In the case of tax measures, the amount to be covered is calculated on the basis of a comparison between the tax actually paid and the amount that should have been paid if the generally applicable rule had been applied. Interest is added to this basic amount. Recovery of past benefits can be ordered for up to ten years.

Measures taken to exempt a company from an obligation to pay taxes can amount to unlawful State Aid if the following conditions are met:

Firstly, the tax measure must grant a financial advantage. In the case of tax rulings, an advantage would in principle exist where the tax payable under the tax ruling is lower than the tax that would otherwise have to be paid under the normally applicable tax system. The general rule is that the allocation of profit between companies of the same corporate group must comply with the "arm's length principle" as set in Article 9 of the OECD Model Tax convention. In the case of transfer pricing agreements, this means that arrangements between companies of the same corporate group must not depart from arrangements that a prudent independent operator acting under normal market conditions would have accepted. The CJEU has confirmed that if the method of taxation for intra-group transfers does not comply with the arm's-length principle and leads to a lower taxable base than would result from a correct implementation of that principle, it provides a selective advantage to the company concerned.[28]

25 http://europa.eu/rapid/press-release_IP-14-663_sk.htm (online; 3/11/2016).

26 http://www.nortonrosefulbright.com/knowledge/publications/120029/tax-rulings-on-transfer-pricing-may-violate-eu-state-aid-rules#autofootnote6 (online; 4/11/2016).

27 Article 108 (3) Treaty on the Functioning of the European Union.

28 Joined cases C-182/03 and C-217/03 Belgium and Forum 187 v Commission.

Secondly the financial advantage must be financed through State resources. In cases where a tax authority lowers the effective tax rate that would otherwise be payable, the resulting loss of revenue for the State is equivalent to the use of State resources.[29]

Thirdly, the tax measure must distort or threaten to distort trade and competition between Member States. Where the beneficiary carries out an economic activity in the EU, this criterion is easily met.

Last but not least, the tax measure must be specific or selective in that it benefits "certain undertakings or the production of certain goods". According to the Commission, "every decision of the administration that departs from the general tax rules to the benefit of individual undertakings in principle leads to a presumption of State Aid and must be analysed in detail."[30] Thus, a tax ruling that merely interprets general tax rules or manages tax revenue based on objective criteria will generally not constitute State Aid, while a ruling that applies the authorities' discretion to apply a lower effective tax rate than would otherwise apply may amount to State Aid. In the case of transfer pricing agreements, a tax ruling that deviates from the arm's-length principle is likely to be considered as specific and hence qualify as State Aid under EU law.[31]

If tax authorities' measures in question constitute State Aid, they could be in principle justified and benefit from an exemption under TFEU, but generally such exemption apply to tax reliefs granted for specific purpose, such as promoting cultural and heritage conservation. However, the Commission has stated several times that at this stage of the investigations, it has no indication that the contested rulings can benefit from an exemption under the TFEU.

4 PRELIMINARY CONCLUSIONS OF THE COMMISSION'S INVESTGATION IN STARBUCKS AND FIAT

Following in-depth investigations that were initiated in June 2014, the Commission has concluded that Luxembourg has granted selective tax advantages to Fiat's financing company[32] and the Netherlands to Starbucks' coffee roasting company.[33] In each case, a tax ruling delivered by the national tax authority allowed the companies concerned to artificially lower the tax paid in the respective country.

In is necessary to state that tax rulings as such are perfectly legal. They are proper decisions issued by national tax authorities to give a company guidance and clarity on how its corporate tax will be calculated or on the use of special tax provisions. However, these two tax rulings subject to the Commission's investigation endorsed artificial and complex methods to establish taxable profits for the companies. According to the Commission, they do not reflect economic reality.[34] "*This is done,*

29 See more: http://www.nortonrosefulbright.com/knowledge/publications/120029/tax-rulings-on-transfer-pricing-may-violate-eu-state-aid-rules#autofootnote6 (online; 4/11/2016).

30 Commission notice on the application of the State aid rules to measures relating to direct business taxation, OJ C 384 od 10 December 1998, pp. 3-9, para. 22

31 See more: http://www.nortonrosefulbright.com/knowledge/publications/120029/tax-rulings-on-transfer-pricing-may-violate-eu-state-aid-rules#autofootnote6 (online; 4/11/2016).

32 Decision of the Commission - SA.38375 http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_SA_38375

33 Decision of the Commission - SA.38374 http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_SA_38374

34 http://europa.eu/rapid/press-release_IP-15-5880_en.htm (online; 5 November 2016).

in particular, by setting prices for goods and services sold between companies of the Fiat and Starbucks groups (so-called "transfer prices") that do not correspond to market conditions. As a result, most of the profits of Starbucks' coffee roasting company are shifted abroad, where they are also not taxed, and Fiat's financing company only paid taxes on underestimated profits."[35]

The Commission concluded that this is illegal under EU State Aid rules: Tax authorities when issuing tax rulings shall not use methodologies, no matter how complex, to establish transfer prices with no economic reason and which unduly shift profits to reduce the taxes paid by the company. With respect to EU State Aid rules, such tax rulings give companies an unfair competitive advantage over other companies that pay taxes from the tax base calculated in respect of their actual profits because they pay market prices for the goods and services they use.

Therefore, the Commission has ordered Luxembourg and the Netherlands to recover the unpaid tax from Fiat and Starbucks, respectively, in order to remove the unfair competitive advantage they have enjoyed and to restore equal treatment with other companies in similar situations. The amounts to recover are EUR 20 - 30 million for each company. It also means that the companies can no longer continue to benefit from the advantageous tax treatment granted by these tax rulings.[36]

Moreover, recently the Commission has concluded that Ireland granted undue tax benefits of up to EUR 13 billion to Apple. However, this case will be subject to specific paper.

Furthermore, the Commission continues to pursue its inquiries into tax rulings practices in all Member States. It cannot prejudicate the opening of other formal investigations into tax rulings if it has indications that EU State Aid rules are not being complied with. Its existing formal investigations into tax rulings in Belgium (McDonald's) and Luxembourg (Amazon) are ongoing.

5 CONCLUSIONS

While the Commission has not yet reached a final decision with regard to the tax rulings in favour of Amazon and McDonald's, the Commission's preliminary view is that these rulings are again likely to constitute unlawful State aid under EU law. If the in-depth investigations confirm this view, the companies concerned will have to repay the aid received, plus interest, as already ruled in cases of Fiat, Starbucks and Apple. The Commission's decision seems likely to turn on the question of whether the benefits provided were "selective," or whether the same principles were applied to all companies.

Before opening these specific investigations, the Commission was already conducting a wider inquiry into certain tax practices by several Member States, an inquiry that the Commission has now broadened to include all Member States.[37] Through its (so far) five in-depth investigations, however, the Commission has made clear that it will not wait for the conclusions of its broader inquiry to pursue potential violations involving specific companies.

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35 Ibid.

36 http://europa.eu/rapid/press-release_IP-15-5880_en.htm or more in Decision of the Commission - SA.38375 http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_SA_38375
Decision of the Commission - SA.38374 http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_SA_38374

37 See more: http://www.nortonrosefulbright.com/knowledge/publications/120029/tax-rulings-on-transfer-pricing-may-violate-eu-state-aid-rules#autofootnote6 (online; 4/11/2016)

Companies that have benefited from these advantageous tax rulings or other special tax measures are advised to assess the possibility that tax benefits negotiated as part of their European tax planning may constitute unlawful State Aid. More generally, for the future, companies are reminded to take account not only of the applicable tax rules as part of their global tax planning and negotiation of tax rulings, but also of potential State Aid considerations.

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Decision of the Commission - SA.38374

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Contact Information:

Mgr. Kristína Považanová, PhD.
kristina.povazanova@flaw.uniba.sk
Comenius University in Bratislava, Faculty of Law
Šafárikovo nám. 6, P.O.BOX 313
810 00 Bratislava
Slovak Republic

JUDr. Hana Kováčiková, PhD.
hana.kovacikova@flaw.uniba.sk
Comenius University in Bratislava, Faculty of Law,
Department of the European Law
Šafárikovo nám. 6, P.O. BOX 313
810 00 Bratislava
Slovak Republic

DISCUSSION PAPERS

EU INTERNATIONAL FAMILY LAW AND THIRD STATES

Katarína Burdová[1]
Comenius University in Bratislava, Faculty of Law

Abstract: The aim of this contribution is to consider whether common provisions of the Brussels IIbis Regulation and of the Maintenance Regulation supersede the national rules only in so far as a given situation has substantial connections to the EU or in all situations irrespective of such connections. We will consider external effect (effect on extra-Union cross-border family cases) of the abovementioned Regulations on the basis of analysis of personal-territorial scope of their application.

Key words: EU international family law, personal-territorial scope, Brussels IIbis Regulation, Maintenance Regulation

1 INTRODUCTION

The European Union[2] (hereinafter referred to as "the EU"), through the exercise of internal and external competences[3], adopted several measures in the area of cross-border family law[4].

The aim of the EU acting at the EU level in the area of international family law is the unification of private international rules between the EU Member States[5] for the purpose of increasing decisional harmony in the EU. In this area, the EU adopted several regulations. The most important are the Brussels IIbis Regulation[6] and the Maintenance Regulation[7]. These Regulations have direct effect in the EU Member States; nevertheless, they are surely not mandatory nor applicable in third States.

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2 The EU has no competence in the sphere of pure domestic family law; however, the Union is tasked by the Treaties to develop judicial cooperation in family matters having cross-border implications.

3 Aude Fiorini states: "There are three main forms that the exercise of this (EU) competence can take.

First, the EU may (in accordance with the provisions of the Treaties) take EU-wide measures (Art. 81 TFEU). Second, the EU may authorise Member States, inter se, to establish family law measures (article 20). Third, it is also conceivable that this competence might be exercised through the participation of the EU in international family law instruments having a broader scope of application than the EU region (Art. 216 TFEU). In: Directorate-general for internal policies. Which Legal basis for Family law? The way forward.

Available at: http://www.europarl.europa.eu/RegData/etudes/note/join/2012/462498/IPOL-JURI_NT(2012)462498_EN.pdf

4 E.g. The Council Regulation (EU) No 1259/2010 of 20 December 2010 harmonised the law applicable to divorce and legal separation, but was adopted on the basis of enhanced cooperation; the EU has ratified the Hague Conference's Protocol of 23 November 2007 on the Law Applicable to Maintenance Obligations; the EU authorised the Member States to ratify, or accede to, the 1996 Hague Child Protection Convention etc.

5 Denmark, Ireland and the UK do not participate in any EU family law measures. However, the UK and Ireland may decide to take part.

6 The Council Regulation (EC) No 2201/2003 of 27 November 2003 concerning jurisdiction and the recognition and enforcement of judgments in matrimonial matters and the matters of parental responsibility, repealing Regulation (EC) No 1347/2000

7 The Council Regulation (EC) No 4/2009 of 18 December 2008 on jurisdiction, applicable law, recognition and enforcement of decisions and cooperation in matters relating to maintenance obligations

The Brussels IIbis Regulation involves rules of jurisdiction, rules of lis pendens and rules of recognition and enforcement of judgement in matrimonial matters (i.e. divorce, legal separation or marriage annulment) and matters of parental responsibility. The Maintenance Regulation covers rules of jurisdiction, rules of lis pendens and rules of recognition and enforcement of judgement in matters relating to maintenance obligations as well as applicable law by means of referring to the conflict of law rules as stipulated by the Hague Protocol[8].

The aim of this contribution is to consider whether common provisions of the Brussels IIbis Regulation and of the Maintenance Regulation supersede the national rules only in so far as a given situation has substantial connections to the EU or in all situations irrespective of such connections. We will consider external effect (effect on extra-Union cross-border family cases) of the abovementioned Regulations on the basis of analysis of their personal-territorial scope of application.

2 BRUSSELS IIBIS REGULATION AND THIRD STATES

The Brussels IIbis Regulation contains private international rules on matrimonial matters and on parental responsibility matters. While considering whether the application of unified rules under this Regulation is limited only to intra-Union situations, it is necessary to analyse separately rules concerning jurisdiction, rules concerning lis pendens as well as rules concerning recognition and enforcement of judgements.

Rules regarding lis pendens and dependent actions are contained in Article 19 of the Brussels IIbis Regulation. These provisions are applicable in cases where proceedings relating to divorce, legal separation or marriage annulment or proceedings relating to parental responsibility are brought before courts of different Member States of the EU. It is clear that the purpose of these rules is to distribute the competence to hear a dispute among courts of the EU Member States. In consequence, it may be concluded that the rules contained in Article 19 of the Brussels IIbis Regulation are applicable only to intra-Union situations. An intra-Union situation means that parallel proceedings are brought before courts of different Members States. Still, it does not mean that in a particular case, the dispute has no connection to a third State. Article 19 is applicable also in situations where courts of the Member States base their jurisdiction on national rules (on the basis of Article 7 or Article 14 of the Brussels IIbis Regulation) where e.g. a child has his/her habitual residence outside the EU but e.g. a parent is an EU Member State citizen or a plaintiff, a defendant or either of them has his/her habitual residence in an EU Member State etc.[9].

Article 19 of the Brussels IIbis Regulation is not applicable to coordination of the exercise of jurisdiction by courts of the Member States and courts of third States. The question whether a court of a Member State can decline jurisdiction under the Brussels IIbis Regulation on the basis of national lis pedens rules (or on the basis of forum non conveniens rules, or on the basis of cases where discretion to stay proceedings needs to be applied) in favour of a court of a third State has not been considered by the European Court of Justice ("the ECJ") till now. This question was answered by

8 The Hague Protocol of 23 November 2007 on the Law Applicable to Maintenance Obligations.

9 For more information on residual jurisdiction rules of the Member States under the Brussels II bis Regulation, consult NUYTS, A.: Study on residual jurisdiction. Review of the Member State´s Rules concerning the „Residual Jurisdiction" of their courts in Civil and Commercial Matters pursuant to the Brussels I and II Regulations.
Available at: http://www.ec.europa.eu/civiljustice/news/docs/study_residual_jurisdiction_en.pdf

the ECJ in the case Owusu which deals with the Brussels I Regulation[10]. In the case Owusu, the ECJ decided that national courts could not decline jurisdiction under Article 2 of Brussels I Regulation in favour of courts of non-Member States even if the jurisdiction of no other Member State is in issue or if the proceedings have no connecting factors to any other Member State.

Are the case Owusu conclusions applicable to the Brussels IIbis Regulation as well? In other words, if the common European rules of lis pendens under the Brussels IIbis Regulation are not applicable to the coordination of parallel proceedings in a Member State and in a third State, can national rules on lis pendens according to the lex fori of a Member State be applicable to such a situation? The answer to this question is not clear but, according to some interpretations, national rules are applicable to parallel proceedings in third States, but only if and to the extent that they do not impair nor impede the full effectiveness of the European regime on jurisdiction[11]. There is also a very interesting opinion that in parental responsibility disputes, "the combined effect of the habitual residence and lis pendens rules can cause significant injustice to litigants and harm the interests of their children. Given the fundamental nature of the child´s best interest principle (no doubt a jus cogens norm), the courts can justify the deferral of proceedings to a more suitable jurisdiction in violation of the possible prohibition in the Brussels IIbis in respect of deferrals and stays"[12].

According to the Chapter III of Brussels IIbis Regulation, common European rules on recognition or enforcement of foreign judgments are applicable only in an intra-Union situation where a judgment given in one EU Member State shall be recognized in the other EU Member States. Common European rules are not applicable on third State´s judgements recognition which is regulated by national law of the EU Member States. Despite the fact that the EU common rules are applicable only in a situation with significant connection to the EU, it does not mean that a judgment given in one Member State has no connection to third States. For instance, recognition of a divorce judgement given in a EU Member State concerning divorce of two nationals of a third State with the last common habitual residence outside the EU is governed by common EU rules on recognition in another EU Member States.

The Brussels IIbis Regulation contains two sets of rules of jurisdiction. First, the rules regulating jurisdiction in matrimonial matters (Articles 3 to 7 of Brussels IIbis Regulation) and, second, the rules of jurisdiction in the matters of parental responsibility (Articles 8 to 10 and Articles 12 to 15 of Brussels IIbis Regulation).

While considering the jurisdiction in matrimonial matters under the Brussels IIbis Regulation, it may seem that personal-territorial scope of these provisions is expressed in Article 6 of Brussels IIbis Regulation which states that there is no room for application of rules of national jurisdiction (residual jurisdiction) under Article 7 of the Brussels IIbis Regulation[13] if a respondent has his/her

[10] The Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters.

[11] MANGUS, U. – MANKOWSKI, P. (eds.): Brussels IIbis Regulation. European Commentaries on Private International law. Munich: Sellier European law publishers, 2012, p. 226.

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[13] Residual jurisdiction according to the Article 7 of the Brussels IIbis Regulation is a jurisdiction which shall be determined by national law (not by common European rules) of a Member State.

habitual residence in the territory of a EU Member State or is a national of a EU Member State or, in the case of the United Kingdom and Ireland, has his/her "domicile" in the territory of these States. According to some commentators, Article 6 refers to the distinction between Union disputes and extra-Union disputes[14]. It may appear that in Union disputes, common rules of jurisdiction according to Articles 3 to 5 are applicable and in extra-Union cases, where a respondent has his/her habitual residence in a third State or is a national of a third State, rules of national jurisdiction are applicable.

Nevertheless, according to the ECJ, such opinion is an erroneous interpretation. In the case Sundelind Lopez, the ECJ clarified that "Articles 6 and 7 of the Brussels IIbis Regulation are to be interpreted as meaning that where, in divorce proceedings, a respondent is not habitually resident in a Member State and is not a national of a Member State, the courts of a Member State cannot base their jurisdiction to hear the petition on their national law, if the courts of another Member State have jurisdiction under Article 3 of that Regulation". It means, inter alia, that Article 6 of Brussels IIbis Regulation is not a general scope rule. The fact that the Brussels IIbis Regulation does not contain a specific provision on the personal-territorial scope of its rules of jurisdiction in matrimonial matters means that common rules of jurisdiction (Articles 3 to 5) have to be considered in all cases despite the existence of substantial connection to third States. For example, in a situation where a marriage of two nationals of a non-Member State was concluded in a third State and they have common habitual residence in third States only, a Slovak court, in considering its jurisdiction, shall apply common European rules of jurisdiction and not national rules, if an applicant is a habitual resident in an EU Member State and if he/she resided there for at least a year immediately before the application was made.

To conclude this part, it can be stated that the application of common European rules of jurisdiction in matrimonial matters is not limited to intra-Union disputes but common rules are applicable also where a dispute has significant connection to a third State.

With regard to the rules on jurisdiction in matters on parental responsibility, the Brussels IIbis Regulation does not contain a provision on its personal-territorial scope and the Article 14 refers to "residual jurisdiction" that may be conferred by the national law within the forum of a EU Member State.

When we take into consideration the fact that "the fundamental principle of the jurisdiction rules in matters of parental responsibility is that the most appropriate forum is the relevant court of the Member State of the habitual residence of the child"[15] and given that the Articles 9, 10, 12 and 13 set out exceptions to the general rule, indicating where jurisdiction may lie with the courts of a Member State other than that in which the child is habitually resident[16], it may be concluded that common jurisdictional rules are applicable only in a situation where the child is a habitual resident within the EU, where the child´s habitual residence cannot be established or where the child is present within the EU and, in all other cases, rules of national jurisdiction of the lex fori of a EU Member State are applicable according to Article 14 of Brussels IIbis Regulation.

Having analysed the jurisdictional rules of the Brussels IIbis Regulation in more detail, we arrive at another conclusion. As Professor De Boer points out, Article 8 of Brussels IIbis Regulation is

14 MANGUS, U. – MANKOWSKI, P. (eds.): Brussels IIbis Regulation. European Commentaries on Private International law, p. 104.

15 European Commission: Practical Guide for the application of the Brussels IIa Regulation. Avaliable at: http://www.ec.europa.eu/justice/civil/files/brussels_ii_practice_guide_en.pdf p. 25.

16 European Commission: Practical Guide for the application of the Brussels IIa Regulation. Avaliable at: http://www.ec.europa.eu/justice/civil/files/brussels_ii_practice_guide_en.pdf p. 30.

applicable not only in a situation where the child is a habitual resident in a EU Member States, but also in a situation where the child subsequently moves to a third State. It is the consequence of the perpetuatio fori principle involved in Article 8 of Brussels IIbis Regulation[17]. Professor De Boer[18] also points to Article 12 of Brussels IIbis Regulation. For the needs of the application of Article 12(1), as well as Article 12(3) of Brussels II bis Regulation, neither habitual residence of a child nor his/her nationality are relevant. In particular, Article 12(3) of Brussels IIbis Regulation is potentially applicable in disputes with significant connection to a third State.

To conclude this part, it can be stated that the application of common European rules of jurisdiction in matters of parental responsibility is generally not limited to situations where the child has his/her habitual residence within the EU.

3 MAINTENANCE REGULATION AND THIRD STATES

Rules of jurisdiction laid by the Maintenance Regulation are unlimited in their territorial scope; therefore, the application of these provisions is direct and universal and is extended to persons living in third States. These common European jurisdictional rules leave no room for the application of rules of national jurisdiction.

Conversely, lis pendens rules as well as rules on recognition and enforcement of judgements are limited to an intra-Union situation, similarly to the Brussels IIbis Regulation provisions of lis pendens and recognition and enforcement. The fact that jurisdiction rules are universal but lis pendens rules are limited to intra-Union situations may give rise to the question whether national rules of lis pendens are applicable in a situation where a dispute has significant connection to third States. In other words, are the conclusion of the case Owusu applicable within the Maintenance Regulation regime? The answer to this question remains unclear and the ECJ will have to provide us with their position on the issue.

4 CONCLUSION

Universal personal-territorial scope of application of jurisdictional rules of the Brussels IIbis Regulation may be of confusing nature because it does not require an identification of intra-Union aspect of dispute as in the case of the Brussels I Regulation but "a three-step reasoning: does the court in the EU that is seized have jurisdiction according to the Brussels IIbis Regulation´s rules; if not, does another court in the EU have jurisdiction according to the Brussels IIbis Regulation´s rules; if not, a court may look at its domestic bases of jurisdiction"[19]. In contrast, the Maintenance Regulation, which also has a universal scope of jurisdictional rules, does not require such an assessment. These differences can cause problems for courts of the EU Member States, which often apply both Regulations in one procedure and confuse unskilled parties.

17 DE BOER, Th. M.: What we should not expect from a recast of the Brussels IIbis Regulation. In: NIPR, 2015, 1, p. 16.
18 Ibid., p. 13.
19 Kruger, T.: The Disorderly infiltration of EU law in Civil procedure. In: NILR, 2016, p. 7.

The extension of scope of application of jurisdictional rules in matters of parental responsibility under the Brussels IIbis Regulation to situations where the child has not habitual residence within the EU territory is criticised by Professor de Boer for, among other things, the likelihood that the court´s decision will not be recognized outside the EU, the problems regarding taking the evidence in the third States and the conflict between the Brussels IIbis Regulation and other sources like the 1996 Hague Convention.

In contrast, the limited scope of the common rules of recognition and enforcement of judgements of both Regulations and application of national rules for assessment of res iudicata effects of third States judgments in a Member State may lead to forum shopping. Adoption of a common provision on basic principles under which a third State judgement may be recognized and enforced in all Member States would be welcome but appears to be unlikely at present.

The existing multilateral treaty solution with third States achieved at the Hague Conference on Private International law currently remains a preferable and an appropriate solution.

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Contact information:

JUDr. Katarína Burdová, PhD.
katarina.burdova@flaw.uniba.sk
Comenius University in Bratislava
Šafárikovo námestie 1,
Bratislava
810 00
Slovakia

EU´S TRADE AGREEMENTS[1]

Hana Kováčiková, Kristína Považanová
Comenius University in Bratislava, Faculty of Law

Abstract: Conclusion of the Trade agreements between the European Union and the third countries is one of the displays of the EU´s sovereignty. At the same time, it is an effective tool for enhancement of the EU´s position within a globalised world of trade. The aim of the trade agreements is to create an easier business environment for (European) entrepreneurs, in particular by removing the customs, opening the public procurement, establishing the common technical standards, setting the rules of solving the disputes. At the same time, the trade agreements guarantee the achieved level of rights and interests protected by law of the European subjects. This leads to exterritorial application of the European law. This article is focused on brief analysis of concluded EU´s trade agreements and their application.

Key words: European Union, trade agreements, external relations, Europeanisation of non-European legal area

1 INTRODUCTION

Trade for all. This is a new strategy of the European Union in the area of the trade policy, which was adopted and presented in 2014[2]. According to this strategy, trade policy is focused on big companies, small companies, consumers, workers and therefore is supposed to become more responsible, more effective, and more transparent and will not only project our interests, but also our values[3]. These goals are in compliance with the general clause contained in the Article 3(5) of the Treaty on European Union (hereinafter known as "TEU")[4].

The common trade policy belongs among the exclusive competence of the EU, as stipulates the Article 3(1.e) of the Treaty on Functioning of the European Union (hereinafter referred as "TFEU")[5]. The European Union shall provide common trade policy on the basis of uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the trade aspects of intellectual property, foreign direct investment,

1 Príspevok bol spracovaný v rámci projektu APVV-0158-12 "Efektívnosť právnej úpravy ochrany hospodárskej súťaže v kontexte jej aplikácie a praxi".

2 Available at: http://trade.ec.europa.eu/doclib/docs/2015/october/tradoc_153846.pdf.

3 EUROPEAN COMMISSION: Trade for All. Towards a more responsible trade and investment policy, p. 5.

4 Article 3 (5) TEU: In its relations with the wider world, the Union shall uphold and promote its values and interests and contribute to the protection of its citizens. It shall contribute to peace, security the sustainable development of the Earth, solidarity and mutual respect among peoples, free and fair trade, eradication of poverty and the protection of human rights, in particular the rights of the child, as well as to the strict observance and the development of international law, including respect for the principle of the United Nations Charter.

5 This is the legal regime after the Lisbon Treaty. Common trade policy under the Treaty Establishing the European Communities belonged to mixed competences of the EC and the Member States.

the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies.

The common trade policy shall be conducted in the context of the **principles and objectives of the Union's external action**[6]. Article 205 of the TFEU[7] then referred to the use of Article 21 of the TEU, which guarantees implementation of principles as democracy, the rule of law, the universality and indivisibility of human rights and fundamental freedoms, respect for human dignity, the principles of equality and solidarity, and respect for the principles of the United Nations Charter and international law and promotion of objectives as encourage the integration of all countries into the world economy, including through the progressive abolition of restrictions on international trade and other.

The realisation of common trade policy by the EU is at the same time the most effective tool for spreading the European law to the third countries, as trade policy reinforces the functioning of the EU Internal Market linking its rules with the global trade system.

2 COMMON TRADE POLICY

Common trade policy can be defined as a complex of measures, which are capable to impact a trade between the EU and the third countries. Trade policy creates a legal framework for trading between the EU and its contractors[8].

EU trade policy aims to open new markets for European exporters, workers and investors through lifting barriers (tariff and non-tariff) to the markets of its trading partners. According to new Strategy, trade policy will effectively address issues that affect today's value chain-based economy, like services, digital trade and the movement of experts, senior managers and service providers. The new approach also involves using trade agreements and trade preference programmes as tools to promote values like sustainable development human rights, fair and ethical trade and the fight against corruption.

The EU realises its common trade policy through the unilateral acts of the EU[9], by membership in international organisations[10] and by concluding the international trade agreements.

Negotiations on trade agreement treaty belong exclusively to the EU, without participation of the Member States. The negotiation process starts at Commission´s initiative, which shall make recommendations to the Council. The Council than authorises the Commission to open the necessary negotiations. During the negotiations, the Commission consults with a special committee appointed by the Council and reports regularly to this committee and to the European Parliament

6 Article 207 (1) of the TFEU.

7 The Union's action on the international scene, pursuant to this Part, shall be guided by the principles, pursue the objectives and be conducted in accordance with the general provisions laid down in Chapter 1 of Title V of the Treaty on European Union.

8 BLAŽO, O.: Základy práva spoločnej obchodnej politiky Európskej Únie. Bratislava: Univerzita Komenského v Bratislave, Právnická fakulta, 2014, p. 7.

9 E.g. Council regulation (EC) No. 3285/94 on the common rules for imports and repealing Regulation (EC) Nov. 518/94/EC, Council regulation (EC) No 3295/94 of 22 December 1994 laying down measures to prohibit the release for free circulation, export, re-export or entry for a suspensive procedure of counterfeit and pirated goods.

10 E. g. World Trade Organisation.

on the achieved progress. At the end of negotiations, the Council upon the Commission´s recommendation authorises the signing of agreements and concludes them. As the common trade policy is governed by regular legislative procedure, the Council shall adopt a decision concluding the agreement after obtaining the consent of the European Parliament.[11]

The process of negotiations has been recently highly criticised because of the lack of transparency. There were a lot of protests in the Member States concerning the absence of information on CETA or TTIP agreements (later protests concerning their content followed). Therefore, the Commission introduced new methods of communication with the public, which shall reinforce the transparency (for example a commitment to publish key negotiating texts from all negotiations, public consultations, civil society dialogue, sustainability impact assessments, public debate, etc.)[12].

2.1 Trade agreements

Negotiations according to Articles 207 and 2018 of the TFEU can result in different types of the trade agreements: (i) **Partnership and Cooperation Agreements**, (ii) **Association Agreements**, (iii) **Stabilisation Agreements**, (iv) (*Deep and Comprehensive*) **Free Trade Agreements**, (v) (*Interim*) **Economic Partnership Agreements** and (vi) **Customs unions**. The type of the agreement often depends on the degree of economic development of the contractor or on the mutual political relations, too.

Partnership and Cooperation Agreements[13] *(PCAs)* provide a general framework for bilateral economic relation without eliminating or reducing custom tariffs. PCA establish the basic common objectives in the field of political dialogue, trade, energy, transport, environment, science and technology, justice and home affairs. In relation to business, they have non-preferential character.

Association Agreements[14] *(AAs), Stabilisation Agreements*[15] *(SAs), Free Trade Agreements*[16] *(FTAs) and Economic Partnership Agreements*[17] *(EPAs)* remove or reduce custom tariffs in bilateral case. The EU has concluded a number of important trade agreements with trading partners and is in the process of negotiating agreements with many more. FTA are designed to create opportunities by opening new markets for goods and services, increasing investment opportunities, making trade cheaper, by eliminating substantially all customs duties, making trade faster, by facilitating goods' transit through customs and setting common rules on technical and sanitary standards, making the policy environment more predictable, by taking joint commitments on areas that affect trade such as intellectual property rights, competition rules and the framework for public purchasing decisions.

Customs unions[18] *(CUs)* eliminate customs duties in bilateral trade and establish a joint customs tariff for foreign importers.

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11 The process of concluding the international trade agreements are specified in the Article 207 and Article 218 of the TFEU.

12 European Commission: Factsheet. Transparency in EU trade negotiations. Available at: http://trade.ec.europa.eu/doclib/docs/2013/june/tradoc_151381.pdf.

13 The EU has concluded PCAs for example with Russia (1997) and the Armenia (1999), Azerbaijan (1999), Kazakhstan (1999), Kyrgyzstan (1999), Uzbekistan (1999) and Tajikistan (2009).

14 The EU has concluded AAs for example with Ukraine (2014), Georgia (2016), Moldova (2016).

15 The EU has concluded SAs for example with Albania (2006), Bosnia and Herzegovina (2015).

16 The EU has concluded FTAs for example with South Korea (2015), CETA with Canada (2016- not yet applied).

17 The EU has concluded EPAs for example with Southern African Development Community (2016 – not yet applied).

18 The EU has concluded CUs for example with Andorra (1991) and Turkey (1995).

The European Union concludes above mentioned trade agreements with regards to its basic goals – to safeguard its values, fundamental interests, security, independence and integrity, consolidate and support democracy, the rule of law, human rights and the principles of international law, foster the sustainable economic, social and environmental development of developing countries, with the primary aim of eradicating poverty, encourage the integration of all countries into the world economy, including through the progressive abolition of restrictions on international trade, help develop international measures to preserve and improve the quality of the environment and the sustainable management of global natural resources, in order to ensure sustainable development[19]. Therefore, trade agreements can be considered to be a tool, through which the EU law is imported into legal systems of the third countries. We would like to demonstrate and confirm this statement on the example of Slovak Republic in the time before Membership in the EU.

2.2 Europeanisation of the Slovak law before Membership in the EU

Slovak republic had begun to autonomously adapt its legal order to European law nine years before it became a full member of the EU. The precondition of such behaviour was the conclusion of the **European Association Agreement** (EAA) on October 4th 1993, which came into effect on 1st of February 1995. This Agreement in its Preamble defined the Slovakia´s accession to the European Community as the final objective of the Agreement. In Article 69, both contracting parties confirmed that the ***approximation of existing and future Slovak legislation with the European one is the main condition for economic integration of the Slovak Republic to the Community***. The Slovak Republic pledged to make efforts to ensure the progressive compatibility of its legislation with the legislation of the Community.

Let´s see how it worked in the specific area of the public procurement (PP). At the time, the relevant PP rules were set in **Act No 263/1993 Coll. on public procurement of goods, services and public works (Public Procurement Act**). It was a minimalistic model of act, which contained only 27 paragraphs. The purpose of this act was to provide the forms and rules of the PP of goods, services and public works, which are paid from the public funds, with the aim to achieve their effective use, transparency of the process and increase the competition. When it came to procurement procedures, the act defined as a basic form of procurement the "public tender" and in the case, when this cannot be used, it presupposed restricted procedure, negotiated procedure and a direct award as an extraordinary tool. The offers were examined and evaluated by three-member commission. The independence of the members of the commission was to be guaranteed by their moral integrity, non-existence of employment or family relations to the tenderer or by the exclusion of the member from evaluation when he is a tenderer at the same time and in same tender. The only reason to exclude the tenderer from the PP was his corruptive behaviour towards the members of the commission. However, the essential condition for such exclusion was the admission of the corrupted commissioner. From brief assessment of this Act and taking into account the then legal situation in Slovakia, we can say that it was a rule that was not difficult to circumvent. To get an unfair advantage, the tenderer needed only to have in the evaluation commission a related person, who wasn´t his family or employee and who didn´t admit that he was corrupted. Also revisions of the PP processes were weak, ineffective and long-lasting.

[19] Article 21 (2) of the TEU.

According the Article 68 of the EAA, both parties had opened the access to their markets of public procurement[20]. Therefore, the reform of the PP rules in Slovakia was inevitable. Slovak Republic had met the harmonisation goal gradually in two main steps.

The first step was realised by adopting the (new) **Act No. 263/1999 Coll. on public procurement and on amendment of other acts** and its amendments[21].This new reglementation was inspired by the Council Directive 92/50/EEC of 18 June 1992 relating to the coordination of procedures for the award of public service contracts, Council Directive 93/36/EEC of 14 June 1993 coordinating procedures for the award of public supply contracts, Council Directive 93/37/EEC of 14 June 1993 concerning the coordination of procedures for the award of public works contracts and **Council Directive 89/665/EEC** of 21 December 1989 on the coordination of the laws, regulations and administrative provisions relating to the application of review procedures to the award of public supply and public works contracts.

The Slovak Act No. 263/1999 Coll. harmonised with above mentioned directives the personal scope of the PP, financial limits relevant for individual procedures, conditions for participation in PP, the criteria for the award. The most important asset was the creation of Public Procurement Office, carrying out the comprehensive competences in the field of PP, including the surveillance.

However, despite the aim of Slovak legislation to reach the European standards – transparency of the PP process, non-discrimination and efficiency in public spending, it succeeded only partially. There was still possible to bypass the transparency, for example during the process of opening the envelopes with offers, which was until 2001 undisclosed to public. The PP system was often abused the by the method of negotiated procedure without publication, where the award came directly to the selected company without any market research. The best tendered price was often dramatically increased by later amendments of the concluded contract, etc.

With the impending accession of the Slovakia to the European Union approximation efforts intensified. The Copenhagen criteria obliged the acceding states to fully implement the *acquis communautaire.* For Slovakia, that meant the obligation to complete ongoing harmonisation of PP law (and of course, the other areas of law, too) before 1st of May 2004. This goal was achieved by adopting the **Act No 530/2003 Coll. on public procurement and on the amendment of Act. No 575/2001 Coll. on the organisation of government activities and the state administration, as amended**, which came into force on 1st of January 2004. Explanatory Memorandum to this Act declared, that by adopting this Act, Slovakia achieved in PP law a full compliance with the European law.

By this example, we proved that the third countries, through the trade and its aspects, adopt the EU law even before they become its members.

3 CONCLUSION

Besides goods, services, intellectual property and other commodities European Union exports also the law. This is realised by the trade agreements, which always contain (more or less) parts of the ex-

[20] This regime was the asymmetric one, where the Slovak companies were allowed to participate on PP in the European market from the day of the validity of the Agreement. On the other side, the Slovak republic guaranteed to allow full access to its national PP for the companies from the Community within the 10-year transitional period.

[21] Act No. 557/2001 Coll. and Act No. 530/2002 Coll.

isting rules of the EU law. Therefore, we can confirm that Europeanisation of the non-European area is an existing process, with the effect on the Europeans (and the citizens of the third countries) too.

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Treaty Establishing the European Communities

Treaty on European Union

Treaty on the functioning of the European Union

Contact information:

JUDr. Hana Kováčiková, PhD.
hana.kovacikova@flaw.uniba.sk
Comenius University in Bratislava, Faculty of Law,
Department of the European Law
Šafárikovo nám. 6, P.O. BOX 313
810 00 Bratislava
Slovak Republic

Mgr. Kristína Považanová, PhD.
kristina.povazanova@flaw.uniba.sk
Comenius University in Bratislava, Faculty of Law
Šafárikovo nám. 6, P. O. BOX 313
810 00 Bratislava
Slovak Republic

LOCAL NEXUS IN MERGER CONTROL REGIMES[1]

Daniela Lukáčová
Antimonopoly Office of the Slovak Republic[2]

Abstract: Merger control is one of the competition law tools. While competition authorities in EU act primarily on the basis of national legislation, European Commission controls mergers with EU dimension. The jurisdictional tests relate only to the economic size of the parties and do not depend on the market shares of the parties or substantive impact of the transaction, or on whether the concentration will have any effects within the state. Globalization increases the number of multijurisdictional mergers that are subject to control of several competition authorities within or outside the EU. Differences in merger control proceedings in such cases with regard to the timeframe, or the result of the proceeding, could have a negative impact on the economy in another country. Parties to the concentration could decide to neglect the merger notification due to the timeframe, or complications connected with approving of multijurisdictional merger in other countries with jurisdiction. Therefore, the national authorities' effort to set in their legislation turnover criteria with local nexus could help to control concentrations with potential effect on competition in their country.

Key words: Local nexus, merger control, multijurisdictional mergers, globalization

1 INTRODUCTION

Merger control is one of the competition law enforcement tools. Competition authorities in EU act primarily on the basis of national legislation. European Commission controls mergers with EU dimension, a concept which depends on the respective turnovers of the undertakings concerned.[3] While definition of a merger transaction seeks to identify those transactions that result in a more durable combination of previously independent businesses or assets, notification thresholds are used to identify transactions that have a sufficiently material nexus to a given jurisdiction. The jurisdictional tests relate only to the economic size of the parties and do not depend on the market shares of the parties or substantive impact of the transaction, nor on whether the concentration will have any effects within the state.

Globalization increases the number of multijurisdictional mergers that are subject to control of several competition authorities within the European area but also outside it. Differences in merger control proceedings in case of global mergers with regard to the timeframe, or the result of the proceeding, could have a negative impact on the economy in another country. In such cases par-

[1] Tento projekt vznikol za podpory Agentúry na podporu výskumu a vývoja, grantu č. APVV-0158- 2 (Efektívnosť právnej úpravy ochrany hospodárskej súťaže v kontexte jej aplikácie v praxi) a Právnickej fakulty Univerzity Komenského v Bratislave. This paper was supported by the Grant APVV-0158- 2 The Effectiveness of Competition Law in the Context of its Application in Praxis.

[2] All views expressed in this paper are strictly personal and should not be construed as reflecting the opinion of the Antimonopoly Office of the Slovak Republic.

[3] ROSE, V. – ROTH, P.: European Community Law of Competition (Bellamy & Child). Oxford: Oxford University Press, 2009, p. 660.

ties to the concentration could decide to neglect the merger notification due to the timeframe, or complications connected with approving of global merger in countries with jurisdiction. Therefore, the national authorities' effort to set in their legislation turnover criteria with local nexus could help to aim control on concentrations with potential effect on competition in their country, in respect of which a reasonable likelihood of outcomes can be expected that conflict with the policy goals of a competition law regime.

2 LOCAL NEXUS

In establishing merger notification thresholds, each jurisdiction should seek to screen out transactions that are unlikely to result in appreciable competitive effects within its territory. Requiring merger notification as to such transactions imposes unnecessary transaction costs and commitment of competition agency resources without any corresponding enforcement benefit.

Merger notification thresholds should therefore incorporate appropriate standards of materiality as to the level of "local nexus" required, such as material sales or assets levels within the territory of the jurisdiction concerned. The "local nexus" thresholds should also be confined to the relevant entities or businesses that will be combined in the proposed transaction. In particular, the relevant sales and/or assets of the acquired party should generally be limited to the sales and/or assets of the business(es) being acquired.

This "local nexus" approach does not preclude the use of ancillary thresholds based on worldwide activities of the parties as an additional prerequisite, but worldwide revenues or assets should not be sufficient to trigger a merger notification requirement in the absence of a local nexus (e.g. revenues or assets in the jurisdiction concerned) exceeding appropriate materiality thresholds.[4]

2.1 Slovak Republic legislation reform

Merger control in Slovakia falls within the scope of the Antimonopoly Office of the Slovak Republic (hereinafter "AMO", "Office"), which is an independent central body of state administration of the Slovak Republic for the protection of competition. The competition legislation is to a great extent in line with the European law.

The AMO made substantive changes in relation to local nexus issues in 2011. Criteria for determining whether the concentration is subject to control by the Office were adjusted in new manner. These changes were adopted by amendment to the Act No. 136/2001 on Protection of Competition (hereinafter "Act on Protection of Competition"). The amendment newly setting the notification criteria regarded the relation to the domestic market, so called local nexus.

This process was prepared in order to arrange effective merger control system without imposing substantial cost on competition authority and merging parties.

Mergers meeting the turnover criteria set by the Article 10, par. 1, letter a) or b) Act on Protection of Competition are subject to ex ante mandatory notification – they fall under the control of the AMO.

[4] ICN Recommended Practices For Merger Notification Procedures, p. 1.

A concentration shall be subject to control by the Office if:

a) *the combined global turnover of the parties to the concentration is at least EUR 46,000,000 for the closed accounting period preceding the establishment of the concentration and at least two of the parties to the concentration attain a turnover of at least EUR 14,000,000 each in the Slovak Republic for the closed accounting period preceding the establishment of the concentration; or*
b) *at least one of the parties to the concentration attains a total turnover of at least EUR 19,000,000 in the Slovak Republic for the closed accounting period preceding the establishment of the concentration and at least one other party to the concentration attains a total global turnover of at least EUR 46,000,000 for the closed accounting period preceding the establishment of the concentration.*

Chart 1: ***Legislation before reform***

A concentration shall be subject to control by the Office if:

a) *the combined aggregate turnover of the parties to the concentration is at least EUR 46,000,000 attained for the accounting period preceding the establishment of the concentration in the Slovak Republic and at least two of the parties to the concentration attain a turnover of at least EUR 14,000,000 each in the Slovak Republic for the accounting period preceding the establishment of the concentration; or*
b) *combined turnover attained for the accounting period preceding the establishment of the concentration in the Slovak Republic*
    1. *if it is a matter of concentration pursuant to the article 9, par. 1, letter a) at least by one of the parties to the concentration is EUR 14,000,000 and simultaneously the global combined turnover for the accounting period preceding the establishment of the concentration attained by another party to the concentration is at least EUR 46,000,000,*
    2. *if it is a matter of concentration pursuant to the article 9, par. 1, letter b) by at least one party to the concentration that is being acquired or its part is being acquired is at least EUR 14,000,000 and simultaneously the global combined turnover for the accounting period preceding the establishment of the concentration attained by whichever other party to the concentration is at least EUR 46,000,000,*
    3. *if it is a matter of concentration pursuant to the article 9, par. 5 at least by one of the parties to the concentration creating jointly controlled enterprise is at least EUR 14,000,000 and simultaneously the global combined turnover for the accounting period preceding the establishment of the concentration attained by another party to the concentration is at least EUR 46,000,000.*

Chart 2: ***Legislation after reform***

The criteria determining whether a concentration is subject to control by the Office, were redefined with the goal to eliminate the mandatory notification of concentrations in cases which do not have any impact on markets in Slovakia but had to be notified due to the global turnover of undertakings concerned. Subject to merger review in the previous wording of the Act were also transactions, where the acquired company had not significant activities in Slovakia. Thus the AMO reviewed the amount of mergers without, or with minimal impact on the market in the Slovak Republic. Such mergers were reviewed due to the fact that the acquirer reached the set turnover threshold in the Slovak Republic and the acquired reached the set global turnover threshold. Before new legislation came into force, the AMO dealt with ca. 23 cases in 2011, around 25 % were cases without any potential impact on competition in the Slovak Republic.

2011 reform, including the process of setting thresholds, was based on the ICN principles, 2005 OECD Council Recommendation, examination of individual sectors in economy in Slovakia, the size of these industries and whole economy, the amount of sales achieved by companies in individual sectors, benchmark based on past experience as well as comparison with the notification criteria in countries with a GDP similar to that of the Slovak Republic. Also the results of the public consultation were taken into account in the process of adopting new legislation.

The criteria for mandatory notifications in cases of acquisitions have changed significantly. According to article 10, par. 1 point a) both the combined aggregate turnover of the undertakings concerned and the aggregate turnover of at least two of the undertakings concerned are linked to the turnover attained in the Slovak Republic and according to article 10, par. 1 point b) the entity which must attain the aggregate turnover in the Slovak Republic is determined according to the type of merger and the other undertaking concerned must attain worldwide aggregate turnover in a given amount.

Above shows that pursuant to the new wording the acquired company must attain the turnover in the Slovak Republic. The AMO assumption was that this could result in elimination of obligatory notification of mergers in which the acquired company had met only the criterion of worldwide turnover and had no significant participation in competition in the domestic market.

The AMO concluded that thresholds should be better targeted to result in a greater number of notifications of mergers with domestic reach without increasing the total number of notifications.

The goal of the notification criteria reform was to allow the Office to focus only on the most serious economic combinations of undertakings and to reduce the number of obligatory notified concentrations that even potentially could not have negative impact consisting in substantial lessening of competition in markets involving the Slovak Republic.

As a result of reforms, the number of notifications remained constant and almost all these cases had the local nexus in SR.

The AMO also complemented local nexus issue in 2011 and 2014 Amendments to the Act on Protection of Competition by other changes to determine costs and burdens of a merger control review system, such as a two phase process merger review, or short form of notification system.

2.2 Unsolved problems

Even though the criteria were changed with intention to set them at a level calculated to minimize the number of transactions that must be notified (that are unlikely to raise competitive concerns), without allowing transactions that raise concerns to fall outside the notification requirement, some questions remain open and unsolved.

In fact there is one type of mergers, within which, even under current notification system, we can find cases without any local nexus. These are cases notifiable under current notification system such as cases of joint ventures created by at least one parent company with activities in Slovakia (turnover threshold met in Slovakia) and by the other parent company, which fulfilled global turnover threshold and at the same time their JV is active/will be active solely abroad. The AMO dealt with approximately 4 such cases in 2012 - 2016.

Construction companies' case

Two construction companies created joint venture for the rental of construction equipment and maintenance work in Nordic countries. One of these parent companies was active in Slovakia, but the other

one was not, even this JV was not. But this concentration fell under AMO review according to Article 10, par. 1, letter b) 3 of the Act on Protection of Competition.

Publisher case

Two Swiss companies publishing newspapers and magazines created new joint venture for magazine publishing which had to be active only in France. These companies had also the joint venture in the Slovak Republic (turnover thresholds met in Slovakia), and they also fulfilled global turnover threshold, but the activity of JV was aimed at other local market. It fell under AMO review according to the same Article as the case above.

Airport Chile case

One airport services provider and one construction company created joint venture for providing airport reconstruction and airport operation in Chile. The construction company provided construction services with significant turnover also in Slovakia (Slovak turnover threshold), the other parent company fulfilled global turnover threshold and the activity of JV was solely outside the Slovak Republic.

Multifunctional objects/business centre case

One construction company, specialized in construction of business centres, and one financial institution, both Finnish companies, created joint venture for construction and operation of business centre in Nordic countries. Construction Company fulfilled Slovak turnover threshold, financial institution fulfilled global turnover threshold and again, the JV was intended to operate solely outside Slovakia. Both of these cases fell under AMO review according to the same Article as the case above.

Chart 3: ***JV cases***

This means that Act on Protection of Competition can apply to concentrations outside the Slovakia and regardless of the nationalities of the parties. As the control of concentrations in Slovakia is to a great extend modelled after the EU system with some procedural divergences, similar situation occurs also within the EU dimension.[5]

3 CONCLUSION

Above mentioned demonstrates that merger notification system revision is important in order to seek improvement, to achieve effective objective and convergence towards recognised best practices. Current setting namely contains some gaps. Above cases could serve as an example that sometimes notification criteria, upon which the local nexus is set, are insufficient.

It is possible to use some instruments that could help to make proceeding more effective in above JV cases under current legislation. Parties can use pre-notification contacts; short form CO with reduced information requirements, and the competition authority could issue decision in 1st phase proceeding without market investigation and detailed reasoning decision.

One of the possible solutions in future is to exclude the creation of joint ventures that will operate outside the Slovakia and have no impact on markets in Slovakia from the scope of AMO in the next Amendment to the Act on Protection of Competition. Such approach is also part of proposal

[5] High profile Phase II cases between non-European companies include Case M.619 Gencor/Lonrho, OJ 1997 L11/30, Case Boeing/McDonnell Douglas, OJ 1997L336/16, Case M.1069 Worldcom/MCI II OJ 1999 L116/1, Case M.2220 General Electric/Honeywell, OJ 2004 L48/1, Case M.3216 Oracle/PeopleSoft, OJ 2005 L218/6.

of the 2014 White Paper Towards more effective EU merger control[6], which covers these cases at the European level.

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Contact information:

Mgr. Daniela Lukáčová
daniela.lukacova@antimon.gov.sk
Antimonopoly Office of the Slovak Republic
Drieňová 24
82103
Slovak Republic

[6] EUROPEAN COMMISSION, White Paper Towards more effective EU merger control, COM (2014) 449, p. 77.